



AMERICAN  
BANKRUPTCY  
INSTITUTE

# 2017 Central States Bankruptcy Workshop

## 363 Sales

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# AMERICAN BANKRUPTCY INSTITUTE CENTRAL STATES BANKRUPTCY WORKSHOP

## SECTION 363 SALES

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## TOPICS TO BE DISCUSSED

- OVERVIEW OF 363 SALES
- PROS & CONS OF A 363 SALE
- KEY PROVISIONS IN A BIDDING PROCEDURES ORDER
- HOT ISSUES:
  - Credit Bidding
  - Consigned Goods
  - Reopening the Auction
  - Sale of Customer Information
  - Successor Liability

## OVERVIEW OF 363 SALES

### 363 Sale Process with Stalking Horse

- Typical process will usually take about 45 days; can be done with or without a stalking horse although far more common to have a stalking horse.
- The debtor files motion seeking approval of proposed sale, including bidding procedures.
- Purchase Agreement finalized by this time or will be finalized prior to the hearing on the bidding procedures.
- Bidding procedures must balance interest of the debtor in having an auction process and interest of purchaser in acquiring the assets for the initial price.
- Generally at least two weeks' notice must be given to potential third parties to conduct due diligence and submit bids. This period will depend in large part on the marketing efforts prior to the filing of the motion, the complexity of the assets and any extenuating factors.

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## OVERVIEW OF 363 SALES

- Court determines appropriateness of bidding procedures and enters an order, usually within the first week to 10 days.
- Due diligence and marketing period for third parties, usually lasting for 3-4 weeks.
- Bid deadline – at the end of the due diligence period, about a month after the bid deadlines have been established.
- Auction, if necessary, normally conducted at the attorneys' offices, not in court – generally 2 – 5 days after bids have been submitted.
- Hearing to approve sale generally held within one or two days after auction.
- Depending on type of transaction (asset purchase or stock purchase), closing will occur shortly after approval unless governmental approvals are required.

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## OVERVIEW OF 363 SALES

- Burden of Proof/Standards
    - Sound Business Justification
  - Debtor's Burden
    - Proportionate value of the asset to the estate as a whole;
    - the amount of elapsed time since the filing;
    - the likelihood that a plan of reorganization will be proposed and confirmed in the near future;
    - the effect of the proposed disposition on future plans of reorganization; the proceeds to be obtained from the disposition vis-a-vis any appraisals of the property; and
    - whether the asset is increasing or decreasing in value.
- In re Lionel Corp.*, 722 F.2d 1063, 1071 (2d Cir. 1983)

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## PROS & CONS OF 363 SALE

### ADVANTAGES OF 363 SALE

- Ability to Bind Non-Consenting Constituencies
- Bankruptcy Protections Permit Organized Sale Process
- Expedited Review of Legal Issues and Disputes
- Reduction or Elimination of Risk of Liability
- Free and Clear of Liens, Claims and Interests
- Ability to “Cherry Pick” Assets
- Assignment of Favorable Contracts
- Potential to Maximize Value

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## PROS & CONS OF 363 SALE

### DISADVANTAGES OF 363 SALE

- Timing and Costs Associated with a Process
- Purchaser has Diminished Control
- Competitive Environment
- Heightened Scrutiny
- Public Process and Publicity

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### KEY PROVISIONS OF BIDDING PROCEDURES ORDER

- Bid deadline
- Minimum standards for qualified bidders and bids
  - financial capability
  - no financing contingency
  - no approval contingency
- Minimum overbids
- Deposit amounts
- Breakup fees and/or expense reimbursements
- Ability of secured creditor to credit bid
- Ability of bidders to bid on less than all assets being offered for sale

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## KEY PROVISIONS OF BIDDING PROCEDURES ORDER

- Permissible deviations from asset purchase agreement
- Need to sign confidentiality agreement
- List of contracts and leases to be assumed
  - evidence of adequate assurance of future performance under contracts and leases to be assumed
- Need to keep back-up bid open until a date certain
- Full disclosure of bidder identity and relationship to debtor and its principals
- Certification of no collusion
- Need for debtor to consult with secured creditor and/or creditors committee regarding qualified bids, changes in sale terms and which bid is best

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## HOT ISSUES IN 363 SALES: CREDIT BIDDING

- Credit bidding allows a secured creditor to bid for its collateral using the debt it is owed to offset the purchase price.
- Section 363(k) provides for credit bidding, “unless the court for cause orders otherwise.”
- Cause is not defined in the Bankruptcy Code.
- Therefore it is left to the court to determine whether cause exists on a case-by-case basis.

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## HOT ISSUES IN 363 SALES: CREDIT BIDDING

*In re Fisker Automotive Holdings, Inc.*,  
510 B.R. 55 (Bankr. D. Del 2014)

Filing of Case: Fisker produced hybrid electric cars.

Purchase of Secured Debt: Shortly before the filing, Hybrid had purchased for \$25 million from the U.S. Department of Energy \$165 million of secured notes issued by Fisker.

Credit Bid: Debtors entered into an APA pursuant to which Hybrid would acquire substantially all of the Debtors' assets for consideration that included a \$75 million credit bid.

Private Sale: Debtors supported a private sale to Hybrid (no further marketing or auction would occur) because auction process unlikely to generate greater value for the estate with ability to credit bid full \$168.5 million.

Committee Bidding Procedures Motion: Committee opposed a private sale and filed a bidding procedures motion to hold an auction that would include Wanxiang America Corporation ("WAC").

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## HOT ISSUES IN 363 SALES: CREDIT BIDDING

*In re Fisker Automotive* (cont'd)

WAC's Offer: Prior to the bidding procedures hearing, WAC had made an extremely attractive offer that it was prepared to increase at an auction. WAC was a strategic buyer that had just purchased the assets of A123 Systems for \$300 million, assets that included the lithium ion battery, a key component for the Fisker cars.

### Debtors/Committee Stipulation

- No Credit Bid/Capped - If the credit bid capped or not allowed there is strong likelihood auction would create material value for estate. If not capped at \$25 million, WAC will not participate in auction and highly unlikely anyone else will either. Auction would be futile.
- Validity of Liens - Hybrid did not have a properly perfected lien on certain assets that would be sold.

Bankruptcy Court Ruling: Hybrid was allowed to credit bid but its bid would be limited to \$25 million, the price it paid for the DOE notes.

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## HOT ISSUES IN 363 SALES: CREDIT BIDDING

*In re Fisker Automotive* (cont'd)

Bankruptcy Court's Reasoning:

- Bidding will be Frozen- Cause exists because bidding will not only be chilled without the cap, bidding will be frozen. Without cap, Wanxiang would not bid.
- Problematic Conduct - "Hybrid's rush to purchase and to persist in such an effort is inconsistent with the notions of fairness in the bankruptcy process."
  - Case filed 3 business days before Thanksgiving and Debtors/Hybrid insisted sale hearing and confirmation occur by Jan. 3. No basis for the rushed timeline was provided. Judge would not allow such tactics to "short circuit the bankruptcy process."
- Validity of a Creditor's Lien - Debtors stipulated that Hybrid's claim was partially secured, partially unsecured and/or uncertain status for remainder.

The Court specifically rejected Hybrid's argument that "for cause" under §363(k) is limited to inequitable conduct, finding no basis in the statute.

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## HOT ISSUES IN 363 SALES: CREDIT BIDDING

*In re The Free Lance-Star Publishing Co.*  
(Bankr. E.D. Va 2014)

Acquisition of Debt: DSP Acquisition LLC ("DSP") purchased the debtor's bank debt.

Lien Issues: After it acquired the debt, but before the bankruptcy filing, DSP discovered that the bank did not hold perfected liens on the debtor's tower assets or tower parcel, which were critical to the value of its radio operations. Following the debtor's refusal to grant the liens, DSP recorded financing statements and fixture filings despite the knowledge that it did not hold valid liens.

DSP Actions:

- Pressured the debtor to file for bankruptcy more than 90 days after the UCC fixture filing;
- discouraged the debtor from marketing its assets to others;
- insisted any marketing materials caution buyers that DSP had the right to credit bid up to \$39 million; and
- insisted that the sale close within 6 weeks of the petition date.

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## HOT ISSUES IN 363 SALES: CREDIT BIDDING

*In re Free Lance (cont'd)*

Bankruptcy Court Ruling: Ultimately, DSP's credit bid was limited to \$13.9 million (as opposed to the \$39 million that DSP had stated it was entitled to).

Bankruptcy Court's Reasoning:

- Validity of Liens: DSP did not have valid, properly perfected liens on the tower and other assets and was not entitled to credit bid the economic value of its claim against assets in which it held no security interest.
- Inequitable Conduct: DSP engaged in inequitable conduct by improperly recording purported liens and failing to disclose its conduct to the bankruptcy court (and in fact filing a false declaration with the Court about the extent and priority of its liens) .
- Aggressive Tactics: Aggressive loan-to-own tactics by DSP -- attempting to depress the sale price by forcing the debtor to rush to sale.

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## HOT ISSUES IN 363 SALES: CREDIT BIDDING

*In re Aéropostale, Inc.*

(Bankr. S.D.N.Y. Aug. 26, 2016)

Facts: Debtor sought to prohibit the Lender from credit bidding.

Court: Distinguishing *Fisker* and *Free Lance*, Court held that the Lender was entitled to credit bid.

No Inappropriate Conduct: Unlike *Free Lance*, no evidence of inappropriate behavior by the Lender: no allegations of collusion, undisclosed agreements or any other actions designed to chill the bidding or unfairly distort the sale process.

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## HOT ISSUES IN 363 SALES: CREDIT BIDDING

### Take Away

- Need more than just chilled bidding.
- The ABI Commission to Study the Reform of Chapter 11 recently released its Final Report and Recommendations in which it noted "the fundamental role of credit bidding under state law and [section 363\(k\)](#)" and that "all credit bidding chills an auction process to some extent." The Commission "did not believe that the chilling effect of credit bids alone should suffice as cause under [section 363\(k\)](#)."

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## HOT ISSUES IN 363 SALES: CONSIGNED GOODS

### *In re Whitehall Jewelers, Inc.*

(Bankr. D. Del. 2008)

Facts: The Debtors sought to sell inventory from 124 consignment vendors valued at \$63 million. The proposed purchasers were a group of liquidators that intended to conduct going-out-of-business sales at Whitehall's stores. The proposed purchase price was approximately 50% of the cost value of the goods.

- Consigned vendors opposed the GOB motion, arguing that the consigned goods were not "property of the estate" and could not be sold by the Debtors.
- The Debtors argued that they could sell the consigned goods because there was a "bona fide dispute" under section 363(f)(4) with respect to the consigned goods. The consigned vendors had not taken the necessary steps to assert priority of their interests, i.e. vendors hadn't filed UCC statements, had filed deficient UCC statements, etc.

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## HOT ISSUES IN 363 SALES: CONSIGNED GOODS

### *In re Whitehall (cont'd)*

Holding: The Debtors had to first demonstrate that the consigned goods were property of the estate. The Debtors failed to meet this burden.

Evidence: Consigned goods were not property of the estate:

- The relationship between the Debtors and each Consignment Vendor was governed by a Vendor Trading Agreement which stated that the goods were consigned; and
- Debtors' filing with the Securities and Exchange Commission disclaimed Debtors' ownership in the consigned goods.

Adversary Proceeding: The Court also ruled that it would not decide the issue in the context of a contested matter. Rather, Third Circuit precedent required Whitehall to commence an adversary proceeding against each of the 124 consignment creditors to determine ownership of the consigned goods.

### Global Settlement

- A global settlement was reached – all consigned goods would be returned to vendors who were part of the settlement and the Debtors had to pay the vendors in full for the cost of any of their consigned goods that had been sold.

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## HOT ISSUES IN 363 SALES: CONSIGNED GOODS

### *The Sports Authority, Inc.*

(Bankr. D. Del. 2016)

### Facts:

- At the time of its bankruptcy filing, Sports Authority was in possession of 8.5 million units of consigned goods, at a cost of \$84.8 million, from 170 consignors.
- Sports Authority typically entered into its standard form of consignment agreement with each of its consignors. Under the agreements, Sports Authority was required to remit the agreed-upon invoice price to the consignor within a specified timeframe following the sale of the consigned goods.
- The Debtors sought to sell consigned goods at a discount, proposing to escrow the sale proceeds.
- The lender alleged that many consignors filed UCC statements in the preference period or not at all and that therefore its blanket lien was superior.
- The consignors objected to the sale of their goods, citing Whitehall Jewelers.
- The Debtors filed 160 adversary complaints and argued that the filing of the complaints created a bona fide dispute for purposes of §363(f).

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## HOT ISSUES IN 363 SALES: CONSIGNED GOODS

### *The Sports Authority (cont'd)*

Court Ruling: Debtors had three options:

- Stop selling the consigned goods;
  - Settle with the consignors; or
  - Sell the consigned goods pursuant to the terms of the consignment agreements, including not placing sale proceeds in escrow and complying with all discounting limitations held by vendors.
- Debtors choose the third option and over the next four months intense litigation went on with the lender and Debtors filing appeals from the Court's orders and unsuccessfully trying to obtain stays of the orders from both the bankruptcy court and the district court.
  - The Court had denied the lender's request that the sale proceeds be escrowed pending adjudication of the lawsuits and instead ruled that the lender could seek recovery of the sale proceeds from the consignors if it was determined that the lender's rights were superior.

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## HOT ISSUES IN 363 SALES: CONSIGNED GOODS

### *The Sports Authority (cont'd)*

#### The Settlement

- A deal was reached in July after 4 months of intense litigation between the consigned vendors and the lenders.
- Under the deal, 70 of the 160 consigned vendors would receive various percentages from the proceeds of their consigned goods (between 25% to 50%).
- The settlement included a waiver of preference claims against the consigned vendors. The Committee opposed this on the grounds that no analysis had been done with respect to defenses. The Court overruled the objection.

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## HOT ISSUES IN 363 SALES: REOPENING THE AUCTION

Goal of an Auction: Maximize value for creditors.

Bidding Procedures: Lay out detailed rules and procedures for conduct at the auction, which are then approved by the Court.

Business Judgment: At the conclusion of the auction, the debtor/trustee must determine in the exercise of its business judgment which offer represents the highest or best bid for the assets.

Announcement at Auction: Debtor/Trustee will announce at the auction who is the successful bidder, subject to Court approval, and close the auction.

Reopening the Auction: What happens when someone makes a bid after the auction has closed?

Courts have to balance the integrity and finality of auctions with the best interests of all creditors.

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## HOT ISSUES IN 363 SALES: REOPENING THE AUCTION

*In re Allied System Holdings*  
(Bankr. D. Del 2012)

At the Auction: The Debtor conducted a two day auction to sell substantially all of its assets. There were two bidders -- the Debtor's lender and Jack Cooper Holdings. Ultimately, the Debtor declared the lender's bid of \$105 million -- \$40.5 million (cash) and \$64.5 million (credit bid) the highest. Jack Cooper's last bid had been \$100 million in cash.

After the Auction:

Jack Cooper objected to the sale and requested that the auction be reopened, claiming:

- Auction a "sham."
- Forced to bid against a "phantom transaction" that was not documented.
- Debtors repeatedly and impermissibly ignored, waived or modified the bidding procedures for the sole benefit of the lender.
- Increased bid to \$135 million (\$125 million cash and \$10 million secured note).

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## HOT ISSUES IN 363 SALES: REOPENING THE AUCTION

### *Allied System Holdings (cont'd)*

#### Committee objected to the sale:

- The auction was not fair and open, noting that that the Debtors were “willing to waive and/or disregard the bid procedures in order to acquiesce to the ghost bidding” of the lender.
- Lender bid not the highest and best -- the deal was structured as a way to liquidate the company rather than keep its assets operating.

#### Debtor Response:

- Argued ran a full, fair and open sale process;
- Was prepared to go forward with the sale to the lender until the materially increased bid by Jack Cooper. Substantial increase in recoveries; and
- Believed that reopening the auction would avoid a highly contested sale hearing.

Hearing to Reopen Auction - The Court noted that it was hesitant to reopen the auction where the losing bidder had a full and fair opportunity to participate in the auction. Nevertheless the Court agreed to reopen the auction. The Court placed substantial weight on the fact that the Debtor supported reopening the auction.

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## HOT ISSUES IN 363 SALES – REOPENING THE AUCTION

### *In re RadioShack (Bankr. D. Del 2015)*

At the Auction: The bidding started at \$12 million and was up to \$18 million. The Debtors called for final sealed bids from potential buyers. The Debtors then declared General Wireless the winner with a bid of \$26.2 million for the Debtors’ intellectual property including trademarks and customer data on approximately 67 million customers. General Wireless had previously acquired (through a separate sale) approximately 1,740 RadioShack stores.

After the Auction: After the auction was closed, Wonderland Investment Group offered \$30 million for the IP and asked that the auction be reopened. Wonderland argued that the changed form -- open bidding to sealed bidding -- was in violation of the bidding procedures approved by the Court. Both the Committee and Salus Capital Partners, a lender with liens on the IP, supported reopening the auction.

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## HOT ISSUES IN 363 SALES – REOPENING THE AUCTION

### *In re RadioShack* (cont'd)

#### Hearing to Reopen Auction - Request to Reopen Auction Denied.

- Change was permitted per Bidding Procedures Order - The Court cited language in the bidding procedures order that allowed the Debtor, after consultation with interested parties, to adopt appropriate auction rules.
- Upset Settlement Agreement - The Court also noted concerns that reopening the bidding could have upset a settlement agreement reached between General Wireless and approximately 35 state attorney generals regarding the protection of customer information.
  - RadioShack agreed to sell only a few categories of its customer data, including names, mailing addresses, email addresses active within the past two years and limited transaction data such as purchase price, product information and store location.
  - There would be no transfer of credit card information, SS numbers, birth dates or phone numbers.

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## HOT ISSUES IN 363 SALES – REOPENING THE AUCTION

### Take Away

- Unusual to reopen an auction but it does happen.
- Decision to reopen auction sale is committed to court's discretion.
- Court more likely to reopen the auction if the overbid is substantially better offer but this factor alone is not enough.
- Court more likely to reopen the auction if a bidder can demonstrate flaws in the auction process or material deviation from Court-approved procedures.
- Most importantly, Court more likely to reopen the auction if the potential bidder has support of other key parties in interest, especially the Debtor.
- If these factors aren't met, a Court is unlikely to order that an auction be reopened because the only way to get the highest price is for bidders to know with certainty that the results of auction will be final.

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## HOT ISSUES IN 363 SALES – REOPENING THE AUCTION

### ABI Report

- Proposes to prohibit courts from reopening an auction “unless the court finds extraordinary circumstances or material procedural impediments (such as the lack of adequate notice or an improperly conducted sale process) to the auction process that may have had a material effect on the sale results.”
- A higher purchase price should not, alone, constitute extraordinary circumstances sufficient to overturn an otherwise final auction.

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## HOT ISSUES IN 363 SALES: SALE OF CUSTOMER INFORMATION

### **Statutory Framework**

- “Personally Identifiable Information” - 11 U.S.C. § 101(41A)
- Appointment of Consumer Privacy Ombudsman” - 11 U.S.C. § 332
- Restrictions on dispositions of Customer Data - 11 U.S.C. § 363(b)(1)
  - A. sale must be consistent with debtor’s privacy policy;or
  - B. sale is approved by court after appointment of consumer privacy ombudsmen

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## HOT ISSUES IN 363 SALES: SALE OF CUSTOMER INFORMATION

### Key Cases

- *Toysmart.com* - sale (a) permitted only to a “qualified buyer” in a related market, (b) required buyer to abide by debtor’s privacy policy, and (c) affirmative consent (i.e. opt-in) required before material changes to privacy policy could be made.
- *Borders Bookstore* - customers were permitted opportunity to opt out of the transfer of the customer data.
- *RadioShack* - sale included opt-out option to consumers prior to transfer and other limitations.
- *Sports Authority* - “We may transfer your personal information in the event of a corporate sale, merger, acquisition, dissolution or similar event.”

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## HOT ISSUES IN 363 SALES: SALE OF CUSTOMER INFORMATION

### Takeaways

- United States Trustees, the Federal Trade Commission, State Attorney General’s Office and other Government Agencies may get involved to protect privacy rights.
- Language in privacy policies must be strong and clear to permit the transfer of customer data.
- Restrictions in debtor’s privacy policy may limit the pool of purchasers and value of customer lists and related assets.

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## HOT ISSUES IN 363 SALES: SUCCESSOR LIABILITY

- Recent cases challenging scope of “free and clear” sale orders in relation to successor liability:
  - *In re Motors Liquidation Company*, 829 F. 3d 135 (2d Cir. 2016) (*cert. denied*)
  - *In re Elk Grove Village*, 562 B.R. 708 (Bankr. N.D. Ill. 2016) (*appeal pending*)
  - *In re Naperville Theater*, 2016 WL 930659 (N.D. Ill. 2016) (*appeal from remand proceedings*)
- Implications for Debtors and Trustees:
  - Price
  - Due diligence
  - Notice to potential claimants
  - Disclosure obligations to potential purchasers

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## HOT ISSUES IN 363 SALES: SUCCESSOR LIABILITY

- Implications for Purchasers:
  - Price
  - Due diligence
  - Holdback escrows
  - Ensuring proper notice to potential claimants
- Implications for Secured Creditors
- Implications for Potential Claimants under various successor liability theories

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## HOT ISSUES IN 363 SALES: SUCCESSOR LIABILITY

*In Matter of Motors Liquidation Co.*,  
829 F.3d 135 (2d Cir. 2016),  
Petition for Cert Docketed (Dec. 15, 2016), cert. denied

- Court had jurisdiction to interpret and enforce its sale order.
- The Code permits a debtor to sell substantially all of its assets to a successor corporation through a §363 sale, outside of the normal reorganization process.
- A bankruptcy court may approve a sale “free and clear” of successor liability claims if those claims flow from Chapter 11 debtor's ownership of the sold assets, if the claims arose from a right to payment that arose prepetition or resulted from prepetition conduct fairly giving rise to the claims, and if there was some contact or relationship between debtor and claimant such that claimant is identifiable.

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## HOT ISSUES IN 363 SALES: SUCCESSOR LIABILITY

*In Matter of Motors Liquidation Co.* (cont'd)

- The sale order covered pre-closing accident claims and economic loss claims arising from the ignition switch defect or other defects, but not independent claims relating only to successor's conduct and used car purchasers' claims.
- As a matter of procedural due process, creditors with ignition switch claims were entitled to notice by direct mail or some equivalent, not mere publication notice.

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## HOT ISSUES IN 363 SALES: SUCCESSOR LIABILITY

*In re Elk Grove Village,*

562 B.R. 708 (Bankr. N.D. Ill. 2016) (appeal pending)

Facts: Trustee sold assets in “free and clear” bankruptcy sale per Section 363. Pre-petition, debtor owed substantial taxes to Illinois Department of Revenue (IDOR) but also to a secured creditor. Lender’s liens were substantially undersecured and were filed before IDOR’s liens against the same assets of the debtor. Illinois bulk sales and tax statutes gave IDOR the right to hold purchaser personally liable for debtor’s unpaid taxes up to the value of the assets transferred (IDOR’s “Successor Liability Interest”). Bankruptcy court sale order extinguished interests of secured lender and IDOR in the debtor’s assets and against purchaser, extending those interests instead to sale proceeds as adequate protection.

Issue: Whether IDOR’s Successor Liability Interest took priority over the secured lender’s interest in the sale proceeds.

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## HOT ISSUES IN 363 SALES: SUCCESSOR LIABILITY

*In re Elk Grove Village (cont’d)*

Bankruptcy Court First Opinion (510 B.R. 594): While IDOR Successor Liability Interest is an “interest” that may be extinguished under Section 363(f), and theoretically entitled to adequate protection per Section 363(e), secured lender’s interest in sale proceeds took priority over IDOR’s Successor Liability Interest since secured creditor (having filed first) could otherwise have enforced its unsatisfied lien against assets in hands of purchaser ahead of IDOR under the UCC. IDOR’s subordinate position, being “out of the money”, did not experience decline in value worthy of adequate protection.

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## HOT ISSUES IN 363 SALES: SUCCESSOR LIABILITY

*In re Elk Grove Village* (cont'd)

District Court (541 B.R. 673): Bankruptcy court did not apply proper test to determine value of extinguished IDOR's Successor Liability Interest, which should be comparing two dollar amounts: (1) creditor's recovery in bankruptcy where Section 363(f) has extinguished its interest in the sold property, with (2) creditor's recovery had its interest in the sold property not been extinguished by Section 363(f). If value in (2) exceeds value in (1), then creditor (IDOR) has suffered decline in value in its interest in sold property, a monetary loss requiring adequate protection.

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## HOT ISSUES IN 363 SALES: SUCCESSOR LIABILITY

*In re Elk Grove Village* (cont'd)

Bankruptcy Court Remand Opinion (562 B.R. 708): IDOR's Successor Liability Interest, while having *calculable value* (the amount of unpaid tax up to the value of the assets transferred), nonetheless had no *realizable value* (per part (2) of District Court ruling) because absent extinguishment in a 363 sale (i) purchaser would have withheld part of purchase price to pay the tax, but (ii) those same withheld amounts would still have been proceeds of sale subject to superior lien rights of lender who, being undersecured, would have been entitled to take all of such withheld proceeds ahead of IDOR under the UCC. With no realizable value, IDOR's Successor Liability Interest did not entitle it to any share of sale proceeds ahead of secured lender. IDOR never sought forms of adequate protection other than access to sale proceeds, so its claim for adequate protection must fail.

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## HOT ISSUES IN 363 SALES: SUCCESSOR LIABILITY

*In re Elk Grove Village* (cont'd)

Implications for Bankruptcy Sales (depending on outcome of appeal to 7<sup>th</sup> Circuit):

- Holders of successor liability interests, including tax authorities, may press for more aggressive forms of adequate protection, in sales where priority secured creditor is undersecured (*dicta* in bankruptcy court remand opinion, 562 B.R. at 721-722)
- In cases with large pre-petition debtor tax liabilities, if law remains unsettled (or 7<sup>th</sup> Circuit reverses), posing risks to sale proceeds, secured creditors may prefer to forego bankruptcy sales and instead lift the stay to take advantage of state laws that circumvent bulk sales statutes (District Court: “Had UCB [secured lender] chosen to foreclose instead of consenting to a Section 363 sale in bankruptcy, then the parties do not dispute that the Bulk Sales Acts would not have applied and that the IDOR could not have collected the unpaid taxes.”) (541 B.R. at 680).