Pushing the Edges: Strategy and Survival in the Out-of-Court World

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PUSHING THE EDGES: STRATEGY AND SURVIVAL IN THE OUT-OF-COURT WORLD

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WHAT IS AN OUT-OF-COURT RESTRUCTURING?

Introduction

- "Out-of-court restructuring" is a catch-all term for various strategies a company and its stakeholders may employ to avoid formal, in-court bankruptcy or other insolvency proceedings, including:

  > Debt-for-equity exchanges or debt-for-debt exchanges
  > Amending and/or extending the terms of credit agreements or other debt instruments
  > Infusions of new capital
  > New financings or refinancings
  > Sales of assets
  > M&A transactions
  > Others

WHAT IS AN OUT-OF-COURT RESTRUCTURING?

Debt-for-Equity Exchanges

- **What**: Company offers equity (stock, preferred stock, convertible preferred stock, etc.) to a class/classes of lenders/debtholders in exchange for their existing debt in the company.

- **Why**: Debt-for-equity exchanges can quickly clear up a company's balance sheet and improve its cash flow, while providing debtholders with an upside stake in, and potentially more control over, the company's future.

- **When**:
  - In the bond context, such exchanges are generally feasible only when a large % of bondholders are willing to take a substantial equity position in the company. Exchanges are often conditioned upon a certain percentage of bondholders tendering their debt because of holdout risk.
  - In the syndicated lending context, debt-for-equity exchanges usually require 100% lender consent although work-arounds to effectuate exchanges may be possible.

WHAT IS AN OUT-OF-COURT RESTRUCTURING?

Debt-for-Debt Exchanges

- **What**: Company offers a new debt security to a class/classes of its lenders/ debtholders in exchange for their existing debt in the company.

  > The new debt will likely have terms advantageous to the company (extended maturity, revised covenants, PIK features, etc.) and the debtholders (new or additional security, higher pricing, fees, enhanced loan monitoring, etc.)

- **Why**: Debt exchanges may provide greater stability to the company through improved cash flow and extended maturity, while improving the exchanging lenders'/debtholders' pricing and position upon a default.

- **When**: Similar to debt-for-equity exchanges. Requires substantial agreement by bondholders and implicates 100% consent issues in the syndicated lending context.

WHAT IS AN OUT-OF-COURT RESTRUCTURING?

Amending and Extending the Terms of Credit Agreements

- **What**: Company and requisite percentage of lenders required by the credit agreement agree to amend terms, often by adding a new tranche of debt, extending the maturity date of some or all of the debt, modifying principal and interest payments, resetting covenants, etc.

- **Why**:
  - > Such transactions avoid much of the transaction costs and delay associated with debt/debt and debt/equity exchanges, and can often be accomplished efficiently with lender consent.
  - > Depending upon proposed amendments, required lender consent may be 50% or a super-majority (66 2/3%) rather than 100%.
  - > Amending lenders often also receive an up front fee for the amendment, and may be able to tighten financial covenants for additional protection.

- **When**: If the company needs relief short of full balance sheet restructuring, or to avoid upcoming maturity, amendment of the credit agreement with requisite lender consent is an efficient option.

WHAT IS AN OUT-OF-COURT RESTRUCTURING?

Issuance of New Equity

- **What**: Company issues new shares of equity as a means of raising capital. This may be effectuated in a variety of ways, including a rights offering to existing shareholders or through a direct cash contribution from a financial sponsor.

- **Why**: In addition to being a fast and cheap way for the company to obtain additional liquidity, the company's lenders'/debtholders' position will often improve from the additional liquidity.

- **When**: Two major hurdles for issuing new equity:
  - Interest – few parties may be interested in purchasing the stock of a financially distressed company.
  - Stockholder approval – legal requirements and the company's organizational documents may restrict the issuance of additional equity absent stockholder approval or consent (which may be a long process).

WHAT IS AN OUT-OF-COURT RESTRUCTURING?

New Financings or Refinancings

- **What**: Company issues new debt instruments or refinances old debt instruments (often those that are close to maturity or default or too expensive).

- **Why**:
  - > Provide short-term liquidity and help company avoid upcoming default by providing new liquidity to service existing debt or by paying off existing debt prior to default.
  - > Such financings can also be used to take advantage of low interest rates in the market.

- **When**:
  - > New financings are possible where the company's existing debt documents permit the incurrence of such debt (or can be modified to permit the new indebtedness).
  - > Refinancings may be an option where a class of lenders/debtholders is intent on being paid out at par.
  - > Refinancing of some debt may require the payment of a prepayment premium, which may make refinancing prohibitively expensive.

WHAT IS AN OUT-OF-COURT RESTRUCTURING?

Sale of Assets/M&A Transaction

- **What**: Company sells some or substantially all of its assets or engages in a merger transaction with another entity.

- **Why**:
  - > Sale may provide a company with additional liquidity for assets that it no longer requires or are highly valued in the market.
  - > Selling or merging the company as a going concern may be the best option to maximize value for all stockholders.

- **When**:
  - > Asset sales are possible where the company's existing debt documents permit such sales.
  - > Where requisite lender consent for a sale is possible, a sale of assets that are more valuable to a third party may shore up a company's balance sheet.
  - > Potential liabilities associated with such assets may make buyers wary of purchasing assets outside of bankruptcy.
  - > Legal and regulatory issues may be implicated by sale/merger of substantially all of the company.

WHY OUT-OF-COURT?

Considerations

- Several considerations come into play when determining whether to pursue an out-of-court restructuring and also whether consummation of an out-of-court restructuring is feasible, including:
  - > Timing
  - > Economics
  - > Tax Implications
  - > Liquidity Status
  - > Corporate Structure
  - > Contractual Restrictions
  - > Cooperation
  - > Others

WHY OUT-OF-COURT?

Out-of-Court Restructuring Advantages

- **More Efficient**
  - > Faster – Bankruptcy triggers a host of filing requirements and subjects many of the company's restructuring decisions to bankruptcy court approval and review by others.
  - > Cheaper – Bankruptcy filings can generate substantial administrative and professional costs.
  - > Fewer Parties
    - – Out-of-court restructurings can often be negotiated and effectuated by the primary stakeholders.
    - – Bankruptcy creates a forum for many others – US Trustee, Creditors Committee, other Committees, individual creditors, etc. – to potentially complicate and delay the restructuring process.

- **Confidential**
  - > Out-of-court restructurings can often be accomplished without advertising or disclosing that the company may be in financial distress.
  - > The company can avoid negative press and employee morale issues associated with filing for "bankruptcy."

- **Allows the Company to Remain in Control of its Business**
  - > Out of court restructurings avoid the need for bankruptcy court approval of company actions.
  - > Rights of creditors and other parties in interest are generally unaffected by out-of-court restructurings other than the rights expressly being modified.

WHY OUT-OF-COURT?

Out-of-Court Restructuring Disadvantages

- **Inability to Bind Third Parties**
  - > No automatic stay means that creditors may seek to collect on debts or foreclose on collateral.
  - > Not all required lenders or debtholders may consent to a restructuring transaction.
    - – Plan voting and "cram down" powers not available outside of bankruptcy.
    - – Holdouts may make out-of-court restructuring impossible or impractical.
- **Inability to Obtain Financing**
  - > Lenders may be unwilling to finance a company in distress without superpriority liens and claims that may only be available in bankruptcy.
- **Value Erosion**
  - > No ability to shed burdensome or obsolete assets, leases and contracts through sale, rejection or assignment.
- **Preference, Fraudulent Transfer and Litigation Risk**
  - > An out-of-court restructuring may be later attacked in bankruptcy as a preference or fraudulent transfer, or may be the subject of related litigation.

ISSUES IN OUT-OF-COURT RESTRUCTURINGS

Obstacles to Out-of-Court Restructurings

Contractual Restrictions

> Debt instruments may prohibit many restructuring options, such as sales of assets or incurring new financing.

> Amending debt instruments may be difficult:
- Most credit agreements and bond indentures require unanimous consent for amendments or waivers to many material provisions of the loan, such as extending maturity dates, reducing the principal amount, or releasing collateral or guarantees.
- Obtaining such consent may be difficult, especially with large lender or bondholder groups and where the debt has been actively traded.

> Security Agreements, however, typically only require some specified majority of lenders ("Required Lenders") to authorize the agent under the credit agreement to exercise (or forbear from exercising) remedies under various loan documents.

ISSUES IN OUT-OF-COURT RESTRUCTURINGS

Obstacles to Out-of-Court Restructurings

- **Competing Interests**

  > Lender interests may not be aligned:

  – Lenders may be wearing multiple hats and occupy different parts of the company's capital structure.

  – Lenders may have acquired debt at different prices and at different times in the restructuring process.

  – Lenders may have different goals in any restructuring (such as protecting other investments in the debtor) or may actually prefer bankruptcy proceedings to further their strategic goals (e.g., to obtain majority ownership of the company or to collect on credit default swaps).

ISSUES IN OUT-OF-COURT RESTRUCTURINGS

Obstacles to Out-of-Court Restructurings

- Trust Indenture Act ("TIA") may prevent certain out-of-court restructurings
  - Section 316(b) of the TIA provides in relevant part:
    - "Notwithstanding any other provision of the indenture to be qualified, **the right of any holder of any indenture security to receive payment of the principal of and interest** on such indenture security, on or after the respective due dates expressed in such indenture security, or to institute suit for the enforcement of any such payment on or after such respective dates, **shall not be impaired or affected without the consent of such holder** . . . ."
  - Notes covered by the TIA, therefore, require unanimous consent to amend payment terms.
  - Recent decisions in *EDMC* and *Caesars* have gone further and held that even the *practical ability* to receive payment may not be impaired (even if the payment terms are not actually amended).
    - *EDMC* and *Caesars* will be discussed at a separate panel later today.

WHAT CAN BE IMPACTED THROUGH OUT-OF-COURT RESTRUCTURINGS

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Introduction

- Many out-of-court restructuring options require approval from Required Lenders to permit the proposed restructuring.

  > "Required Lenders" is customarily defined as lenders holding 50% or more of the commitments under a credit agreement.
  > Certain credit agreements also utilize the concept of Supermajority Lenders, which often requires the consent of lenders holding 66 2/3% or more of the commitments under the credit agreement in order to take action.

- Required Lenders (or Supermajority Lenders) can be used to influence and effectuate various forms of out-of-court restructurings in both creative and sometimes controversial ways that push the edges of what can be effectuated through an out-of court restructuring:

  > Forbearance Agreements
  > Sale Process
  > Restructuring Support Agreements
  > Priming Facilities
  > Modification of Payment Waterfalls
  > Modification of Pro Rata Treatment and Sharing Provisions
  > Unequal Treatment of Majority and Minority Lenders

WHAT CAN BE IMPACTED THROUGH OUT-OF-COURT RESTRUCTURINGS

Forbearance Agreements

- Forbearance agreements are agreements among lenders, the borrower and certain other parties pursuant to which the lenders agree to forbear from exercising rights and remedies (with certain limited exceptions) under the loan documents that they would otherwise have the right to take in the absence of such agreement.

- Many debt documents implicitly permit such agreements.
  - Before any remedies can be exercised by an agent upon a default, many debt documents either require Required Lenders to affirmatively request that the agent call a default, or permit Required Lenders to instruct the agent to refrain from exercising remedies.

Forbearance Agreements: Why Use Them?

- **Usefulness to Borrowers**
  - > Reprieve from acceleration and exercise of remedies.
    - – Lenders may allow interest to go unpaid or be PIK'd.
    - – Lenders may relax covenants.
  - > Opportunity to restructure outside of bankruptcy court and avoid the stigma, time and expense associated with reorganizing in bankruptcy court.
  - > Opportunity to complete an amendment to a credit agreement.
  - > Affords borrower opportunity to obtain a clean audit or meet other covenants.
  - > Short period for borrower to cure one time occurrence of Default or Event of Default (overall credit facility is not distressed).

- **Usefulness to Lenders**
  - > Lenders can receive significant consideration, financial and otherwise.
    - – More control over the restructuring process.
    - – Opportunity to amend the credit agreement and add additional provisions.
    - – Receive amendment/forbearance/advisor fees.

WHAT CAN BE IMPACTED THROUGH OUT-OF-COURT RESTRUCTURINGS

Forbearance Agreements: What They Can Do

- Forbearance agreements can provide a number of advantages to forbearing lenders including:

  > Forcing a change in the board through the appointment of independent directors.
  - Appoint independent directors as part of the forbearance agreement whose votes are required for any major board decision.
  - "Exploding Board": upon default under the forbearance agreement, the board automatically increases to include sufficient independent directors to constitute a majority.

  > Releases for lenders/agents for any borrower claims.

  > Clean up definitions and "holes" in collateral.

  > Milestones for a restructuring, including a path to a restructuring support agreement.

WHAT CAN BE IMPACTED THROUGH OUT-OF-COURT RESTRUCTURINGS

Sale of Company or Company Assets

- **Typical Process**
  - > Borrower agrees to market and sell the assets of the company as a going concern.
  - > Forbearance agreement lays out sale related covenants (all acceptable to the agent in its discretion) including:
    - – Retention of investment banker.
    - – Establishment of sale timeline including distribution of marketing materials, bid deadlines, bid selection and negotiation and consummation of transaction.
    - – Proceeds of sale paid over directly to agent for application in accordance with the credit agreement and loan documents.
    - – Failure to meet covenants and sale process milestones results in forbearance default and ability to exercise rights and remedies.

- Sales often effectively result in a change in ownership (unlike many other forms of out-of-court restructuring).

WHAT CAN BE IMPACTED THROUGH OUT-OF-COURT RESTRUCTURINGS

Restructuring Support Agreements

- Restructuring Support Agreements ("RSAs") are agreements by a company and its primary creditor constituencies to support and vote in favor of a restructuring in bankruptcy.

  > RSAs provide an additional mechanism for majority creditors to effect a restructuring over minority dissent.

  > RSAs typically provide:

    – The material terms of a plan of reorganization (or liquidation).
    – Parties will vote to accept the plan.

  > RSAs may also provide for:

    – Milestones similar to those in a forbearance agreement.
    – Limitations on company actions, such as the use of cash collateral or on obtaining DIP financing in bankruptcy.

  > RSAs may be entered into prepetition or postpetition.

WHAT CAN BE IMPACTED THROUGH OUT-OF-COURT RESTRUCTURINGS

Restructuring Support Agreement Issues

- **Trading Restrictions**
  - > Pre-negotiating the terms of a plan often involves the receipt of material non-public information which may restrict the freedom creditors to trade their debt – creating disincentives to support a restructuring.
  - > Creditor constituencies may create steering committees, so a subset of a class of creditors can negotiate a plan, while other creditors are free to trade.

- **Prepetition vs. Postpetition**
  - > Prepetition RSAs, like prepackaged plans, are commonly approved in bankruptcy after notice and a hearing.
  - > Postpetition RSAs, however, are often challenged as improper solicitation of votes on a plan.
    - – Section 1125(b) of the Bankruptcy Code provides that "[a]n acceptance or rejection of a plan may not be solicited after the commencement of the case under this title from a holder of a claim or interest" unless a disclosure statement has been approved by the bankruptcy court.
    - – Violations may result in the disqualification of improperly solicited votes.

WHAT CAN BE IMPACTED THROUGH OUT-OF-COURT RESTRUCTURINGS

Priming Facilities

- Priming facilities are a form of new financing that a company may pursue in an out-of-court restructuring.

- Assuming that current lenders want to continue to fund the company:

  > Lenders may be able to create a priming facility if permitted by the existing loan documents.
    - This requires a review of whether amendments can be made with Required Lender support only, as opposed to 100% lender support.

  > Actions typically requiring 100% lender support (often referred to as "sacred rights") include:
    - Reducing principal or interest payments
    - Extending maturity dates
    - Reducing the requisite % for Required Lenders
    - Releasing collateral

WHAT CAN BE IMPACTED THROUGH OUT-OF-COURT RESTRUCTURINGS

Priming Facilities

- **Easy Way**: Debt documents permit the incurrence of senior debt.
  - > Will require an intercreditor agreement to govern the relationship between the priming facility and the existing credit agreement.
- **Required Lender Way**: If senior debt is not permitted, amendments to the debt documents may often be made to permit (or effectively permit) such debt.
  - > Amend permitted indebtedness basket (with Required Lender support) to allow for the incurrence of a new type of debt (the priming facility); and
  - > Amend permitted lien basket (with Required Lender support) to allow for the incurrence of priming liens, to secure the priming facility.

WHAT CAN BE IMPACTED THROUGH OUT-OF-COURT RESTRUCTURINGS

Pushing the Edges with Required Lenders

- **Amending Payment Waterfall.** Payment waterfalls often may be amended by Required Lenders.
  - > Amend the existing payment waterfall by creating new tranches of debt within existing security with higher priority for lenders willing to consent to restructuring.
    - – In such transaction, Required Lenders are free to alter their rights (with 100% of their consent), while other lenders' rights will remain unchanged.
    - – While a credit agreement may specify a waterfall upon default, a default often requires the instruction by Required Lenders to call a default and apply such waterfall. A credit agreement could be restated to provide for an alternative waterfall upon a default.
    - – Results in effective modification of repayment schedule -- commonly assumed and understood to require 100% lender approval -- with a simple majority of lenders.

WHAT CAN BE IMPACTED THROUGH OUT-OF-COURT RESTRUCTURINGS

Pushing the Edges with Required Lenders

- **Amending *Pro Rata* Treatment and Sharing Provisions**
  - *Pro rata* treatment and sharing provisions are intended to insure that:
    - (i) all lenders of a particular tranche are treated on a *pro rata* ratable basis; and
    - (ii) a lender that receives more than its *pro rata* share must share proceeds of its excess non-ratable payout with other lenders so the benefit of all such payments are shared ratably.

- In some instances -- and in some credit agreements – *pro rata* treatment and sharing provisions can be amended by Required Lenders.

- Modification of *pro rata* treatment and sharing provisions can create disproportionate treatment of majority and minority lenders resulting from an out-of-court restructuring.

WHAT CAN BE IMPACTED THROUGH OUT-OF-COURT RESTRUCTURINGS

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Pushing the Edges with Required Lenders

- **Unequal Treatment of Majority and Minority Lenders**

  > Out-of-court restructurings where lenders can modify payment waterfalls and pro rata treatment and sharing provisions with Required Lenders consent can create fundamental differences in treatment of loans.

  > Required Lenders may receive the benefit of higher priority, improved economics, enhanced and additional fees, reset covenants, etc., while minority lenders are effectively "left behind".

  > Proposed different treatment between majority and minority lenders used as leverage to force non-consenting lenders to support out-of-court restructuring.

  > Recent trend has witnessed Required Lenders denying minority lenders the opportunity to even participate in out-of-court restructurings that provide majority lenders with favorable and unequal treatment – Required Lenders have sought to monopolize the benefits of the out-of-court restructuring.

  > Implicates a host of legal and policy implications.

CASE LAW

Introduction

- As described above, many out-of-court restructurings can be effected through the consent of Required Lenders. However, such actions are often taken *against* the will of one or more minority lenders.

- Fault lines arise when and where there are disputes concerning whether Required Lenders are authorized under the loan documents and applicable law to take certain actions.

- Where Required Lenders take actions that impact minority lender rights, minority lenders may bring suit to enforce their rights.

- Case law involving disputes between majority and minority lenders has arisen in multiple contexts:
  - RSAs
  - Exercise of remedies
  - Credit bidding
  - Payment modification
  - Unequal treatment

CASE LAW

Introduction

- Bankruptcy courts have generally focused on the provisions contained in the relevant loan documents to determine whether the particular actions taken by Required Lenders are permissible.
- Bankruptcy courts have been reluctant to go further because they are hesitant to intrude on intercreditor disputes.
- Consequently, bankruptcy courts have declined to adjudicate majority/minority litigation concerning breach of contract and breach of duty claims, deferring such litigation to state court or other federal court forums.
- Some relevant case law examples follow.

CASE LAW

RSAs: *In re Indianapolis Downs,* 486 B.R. 286 (Bankr. D. Del. 2013)

- **Issue:** May a debtor bind creditors to support a plan through a postpetition RSA without violating Section 1125(b) of the Bankruptcy Code?

- **Background:**

  > Debtors and major bondholder constituencies entered into a postpetition RSA to support a sale process potentially followed by a standalone plan, if the sale process did not result in a sufficient bid.

  > Bondholders were bound by the RSA to vote in favor of the plan.
  – Debtors could enforce the RSA by specific performance.

  > Debtors received approval of the RSA and disclosure statement simultaneously.

  > Certain creditors objected and sought to designate votes obtained pursuant to the RSA (which would prevent confirmation).

  > Two recent Delaware bankruptcy court cases (*In re Stations Holding Co., Inc.* and *In re NII Holdings, Inc.*) had concluded that Section 1125(b) is a "bright-line rule" that prohibits any RSA executed after the petition date.

CASE LAW

RSAs: *In re Indianapolis Downs*

- **Court:** Plan confirmed. The term "solicitation" must be interpreted narrowly.
  - > Consistent with the Third Circuit's ruling in *Century Glove, Inc. v. First American Bank,* Section 1125(b) should not be read in a way that "chills or hamstrings the negotiation process."
  - > RSA parties were sophisticated and sufficiently informed about the Debtors' business.
    - "It would grossly elevate form over substance to contend that § 1125(b) requires designation of their votes" because they had not reviewed a court-approved disclosure statement prior to reaching agreement with the debtor to support a plan.
  - > Court distinguished *In re Stations Holding Co., Inc.* and *In re NII Holdings, Inc.* because those cases involved pre-packaged cases in markedly different factual and procedural contexts than the case at bar.
    - The court also noted that the orders in those cases had limited precedential value.

CASE LAW

Forbearance of Remedies: Beal Sav. Bank v. Sommer, 8 N.Y.3d 318 (N.Y. 2007)

- **Issue**: Does a minority lender to a credit agreement have the right to exercise remedies under the credit agreement if Required Lenders opt to forbear from exercising remedies?

- **Background**: Borrower was party to a credit agreement (the "CA") with dozens of lenders that was accompanied by a "Keep-Well Agreement" between Borrower's parent and the lenders which, among other things, guaranteed the payment of any accelerated debt under the CA.
  - > Borrower filed for bankruptcy (thereby defaulting on the CA).
  - > Thereafter, Required Lenders and the parent reached a Settlement Agreement pursuant to which Required Lenders would agree to forbear from exercising remedies under the CA (including acceleration of the debt), but would receive $6.5M in the aggregate.
    - – The CA also authorized the agent to collect payments from Borrower on behalf of the Lenders.
  - > The CA was silent as to individual lender rights to enforce the CA.
  - > Plaintiff, the only non-consenting lender, brought suit to enforce the guaranty or, in the alternative, pay the plaintiff its pro-rata share of such proceeds.

CASE LAW

Forbearance of Remedies: Beal Sav. Bank v. Sommer

- **The Loan Documents:**
  - > Section 18(a) of the Keep-Well Agreement stated that it is to be construed in accordance with the CA.
  - > Section 18(b) of the Keep-Well Agreement, stated that it is enforceable "by the Administrative Agent and each Lender."
  - > Section 8.3 of the CA provides that the debt may only be accelerated where the Administrative Agent acts at the direction of "Required Lenders" (66 2/3% of the outstanding principal balance).
  - > Section 9.1 of the CA authorized the Administrative Agent to use its authority granted in the CA to act on the lenders' behalf.
  - > Section 10.20 of the CA provided that the remedies under the CA are "cumulative, not exclusive."
  - > Section 4.8 of the CA was a *pro rata* sharing provision.

CASE LAW

Forbearance of Remedies: Beal Sav. Bank v. Sommer

- **Plaintiff Arguments**:
  - The parent guarantee in the Keep-Well Agreement is enforceable by individual lenders given that nothing in the CA or Keep-Well Agreement "precluded a Lender from otherwise proceeding individually."

- **Defendant Arguments**:
  - Plaintiff lacked standing because Section 8.3 of the CA provides that the debt may only be accelerated where the Administrative Agent acts at the direction of "Required Lenders" (66 2/3% of the outstanding principal balance).
    - Because Required Lenders did not exercise such remedies, no acceleration can occur.

CASE LAW

Forbearance of Remedies: Beal Sav. Bank v. Sommer

- **Court:** Plaintiff has no independent right to sue under either agreement.
  - > Events of default are only discussed in Section 8.3 of the CA, which states "it is the Administrative Agent [rather than individual lenders] that, upon direction of the Required Lenders, may exercise any or all rights and remedies as the Lenders elect."
    - – Section 18(b) of the Keep-Well Agreement, which states that it is enforceable "by the Administrative Agent and each Lender," does not override the more specific language of Section 8.3.
    - – This interpretation would "render section 8.3 meaningless because there would be no reason to provide that the Required Lenders could enforce the agreements by a supermajority directing the Administrative Agent to act."
  - > The CA provides that "[e]ach Lender authorize[d] the Administrative Agent to act on behalf of such Lender," which demonstrates that the "Lenders contemplated unified action by the Administrative Agent."
  - > Cumulative remedy provisions "do not provide to each Lender express grants of enforcement in the event of default."
  - > The Settlement Agreement did not have the effect of releasing the parent's guarantee in violation of Section 7 of the Keep-Well Agreement.
    - – Even if it did, Required Lenders properly exercised their rights to restructure the CA.

CASE LAW

Credit Bidding: *In re Metaldyne Corp.*, 409 B.R. 671 (Bankr. S.D.N.Y. 2009)

- **Issue**: May an agent, at the direction of the Required Lenders, credit bid the secured debt of all of the lenders?

- **Background**:

  > Borrower and lenders were parties to a Credit Agreement (the "CA").

  > Borrower filed for bankruptcy and placed its assets up for auction.

  > A consortium made up of holders of approximately 97% of Borrower's secured debt purchased substantially all of Borrower's assets by directing the agent to credit bid the entire amount of the secured debt and releasing the lenders' liens on all of Borrower's remaining collateral.
    – It was not known what consideration minority lenders would receive.

  > Minority lenders objected to the Agent's credit bid, arguing that it was not authorized to do so under the CA.

CASE LAW

Credit Bidding: *In re Metaldyne Corp.*

- **The Loan Documents:**

  > Any lender may credit bid its claims in any public sale of Borrower's collateral.

  > Amendments to the CA may not "release all or substantially all of the Collateral from the Liens" without unanimous lender consent.

  > Any recoveries under the CA must be shared pro-rata among the lenders.

  > Agent was "irrevocably appoint[ed]" by the lenders to "exercise any and all rights afforded to a secured party" including "to sell or otherwise dispose of all or any part of the Collateral."

CASE LAW

Credit Bidding: *In re Metaldyne Corp.*

- **Court:** Sale approved.

  > Nothing in the loan documents prohibited the agent from credit bidding.
    - A lender's right to credit bid its claims does not limit the agent's power.
    - Credit bidding is not an amendment to the loan documents, but rather, an authorized exercise of remedies by the agent.
    - Releasing liens in the exercise of such remedies is permissible.

  > Disputes over *pro* rata sharing of the proceeds of the sale are intercreditor or lender-agent disputes "neither of which is properly before this Court."
    - The court declined to consider whether there was any impropriety in the fact that a new company formed by Required Lenders was the purchaser, even though the entire amount of the debt was credit bid.

CASE LAW

Credit Bidding: *In re GSC, Inc.*, 453 B.R. 132 (Bankr. S.D.N.Y. 2011)

- **Issue:** May an agent pair its credit bid with a cash bid, and allocate the assets that it purchases among the two?

- **Background**:
  - > A single investor purchased a 51.1% share (sufficient to be a Required Lender) in Borrower's $240M credit facility secured by substantially all of Borrower's assets.
  - > After Borrower filed for bankruptcy, it placed its assets up for auction.
  - > Required Lender won the auction by credit bidding the secured debt plus $11M in cash and notes.
  - > Required Lender then *allocated* its bid between the credit bid and the cash/notes purchase price.
    - – The "Credit Bid Allocable Items" were valued at approximately $5M.
    - – The "Cash Bid Allocable Items" were valued at over $126M.
  - > The loan documents expressly prohibited individual enforcement of remedies, but provided that the agent must exercise remedies "for the benefit of the [lenders]."
  - > Minority lenders objected to the allocation of the bid, which effectively wiped out their security and limited their recovery.

CASE LAW

Credit Bidding: *In re GSC, Inc.*

- **Court:** Sale approved.
  - > The court noted that allocation issues were "not properly before this court."
    - – Allocation issues "constitute[] a dispute between the Agent, the [minority] Lenders, and [Required Lender], not with the credit bid itself."
  - > As with *Metaldyne*, the court's decision rested largely on the fact that the loan documents authorized the agent to exercise remedies at the direction of Required Lender.

- The minority lenders simultaneously brought state court actions for, among other things, breach of contract, against Required Lender, the agent, and certain related parties.
  - > The case was filed in 2010, and is still pending.

LEGAL AND POLICY CONSIDERATIONS

Balancing Competing Legal and Policy Interests

- Bankruptcy process vs. out-of-court restructuring.
- Required Lender flexibility vs. protection of "sacred rights."
- Lender expectations vs contractual and legal authority.
- Holdout behavior – protection of economic rights vs. obstruction/ opportunistic behavior.
- Due process/notice considerations.
- Role of bankruptcy courts and judges.
- Freedom of contract vs. bankruptcy policy and principles.
- Role of equity, fairness and market certainty.