

SECURED CREDITORS

The US Court of Appeals for the Third Circuit recently ruled that a Chapter 11 POR may provide for a sale of assets subject to a secured creditor's lien **without** affording the secured creditor the opportunity to credit bid its debt *In re Philadelphia Newspapers, LLC*, No. 09-4266, slip op. (3d Cir. March 22, 2010). Note that Delaware is in the Third Circuit.

Debtors proposed a POR under which their assets would be sold free of liens at a public auction and the Debtors contemporaneously entered into an asset purchase agreement with a group of insiders who proposed to acquire the Debtors' assets for cash in an amount substantially below the amount of the lenders' claim secured by those assets. In addition, the Debtors proposed bidding procedures designating the insider group as the stalking horse bid and requiring any competing bid to be in cash.

The secured lenders objected, arguing that the procedures unlawfully deprived them of the opportunity to credit bid.

The Third Circuit rejected the secured lenders' challenge to the procedures.

Section 1129(b)(A) permits cramdown of an impaired class that votes against a POR if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the POR

Section 1129(b)(2)(A) sets out alternative means by which a Chapter 11 POR may be crammed down as "fair and equitable":

1129(b)(2) For the purpose of this subsection, the condition that a plan be fair and equitable with respect to a class includes the following requirements:

(A) With respect to a class of secured claims, the plan provides -

(i)(I) that the holders of such claims retain the liens securing such claims, whether the property subject to such liens is retained by the debtor or transferred to another entity, to the extent of the allowed amount of such claims; and

(II) that each holder of a claim of such class receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property;

(ii) for the sale, subject to Section 363(k) of this title, of any property that is subject to the liens securing such claims, free and clear of such liens, with such liens to attach to the proceeds of such sale, and the treatment of such liens on proceeds under clause (i) or (iii) of this subparagraph; or

(iii) for the realization by such holders of the indubitable equivalent of such claims

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Analyzing Section 1129(b)(2)(A) of the Bankruptcy Code, the majority held that a sale without the opportunity to credit bid could be approved so long as the plan ultimately provided the secured creditor with the "indubitable equivalent" of its of its secured claim. The majority reasoned that although one provision of Section 1129(b)(2)(A) expressly conditioned secured creditor cramdown on an opportunity to credit bid, the "indubitable equivalent" test in the same section did not, with the result that a secured creditor can be crammed down by a Chapter 11 POR providing for a sale free and clear of liens without credit bidding if the POR satisfies the indubitable equivalent standard.

Implications:

Debtors may use *Philadelphia Newspapers* to preclude the use of credit bidding as a safeguard against low-value acquisitions of collateral under a POR

Secured creditors may still compete with cash bids of their own, but this is often difficult for large creditors to do, particularly when they include CLOs or other entities that are unable to advance funds

Philadelphia Newspapers also undercuts other recent decisions affirming the ability of the required lenders to instruct the agent to credit bid, when the Credit Agreement so permits, thereby "dragging along" the remainder of the lenders in the group

Creditor groups will have to design mechanisms for cash bids, knowing that any cash advances will be round-tripped. Secured creditors may also want to condition any use of cash collateral or DIP financing on permitting credit bidding.

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