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Secured lenders have a right to credit bid in bankruptcy -- at least in the Seventh Circuit

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Breaking with the Third Circuit and the Fifth Circuit, on June 28, 2011, the Seventh Circuit held that a debtor's plan of reorganization that provides for the sale of the debtor's assets free and clear of an existing security interest may only be confirmed over the objection of its secured creditor if the plan's sale procedure permits the secured creditor to credit bid its secured debt for the assets being sold. *River Road Hotel Partners, LLC v. Amalgamated Bank*, -- F.3d --, Nos. 10-3597 & 10-3598 (7th Cir. June 28, 2011).

The circuit split centers on the Bankruptcy Code's provisions that only permit the confirmation of a plan of reorganization over the objection of a creditor class (a so called "cram down") where the plan's treatment of such class is "fair and equitable." When the objecting class consists of secured creditors, the Bankruptcy Code requires that such fair and equitable treatment include provisions whereby either: (A) the secured creditor retains its liens in its collateral whether such collateral is retained by the debtor or transferred to another party and the secured creditor receives a specified level of cash payments under the plan, 11 U.S.C. § 1129(b)(2)(A)(i); (B) the secured creditor "realiz[es] ... the indubitable equivalent" of its claim, id. § 1129(b)(2)(A)(iii); or (C) the secured creditor's collateral is sold subject to the secured creditor's right to credit bid for such property, the secured creditor retains a lien in the proceeds of the sale and the treatment of this new lien is in accordance with (A) or (B) above. Id. § 1129(b)(2)(A)(iii). Because the Bankruptcy Code does not define "indubitable equivalent" the courts, in providing their own definition have struggled over whether these three alternative "fair and equitable" treatments are mutually exclusive such that the only method for selling property free and clear is in an auction that permits credit bidding, or whether indubitable equivalent alternative is broad enough to encompass a free and clear sale that would not otherwise be "fair and equitable" because it did not honor credit bidding.

Both the Fifth Circuit and the Third Circuit have interpreted the fair and equitable option broadly. In the 2009 *Pacific Lumber* opinion, (*In re Pacific Lumber, Co.*, 584 F.3d 229, 246 (5th Cir. 2009) the Fifth Circuit held that a plan that proposed the sale of the debtor's encumbered assets to a specified purchaser with the secured lender receiving cash in the amount of the judicially determined value of the collateral but absent any right to credit bid qualified as indubitable equivalent treatment. In the 2010 *Philadelphia Newspapers* opinion, (*In re Philadelphia Newspapers*, 599 F.3d 298 (3d Cir. 2010) the Third Circuit held, in a 2-1 decision, that a plan that proposed selling the debtor's encumbered assets free and clear of liens in an auction that prohibited credit bidding could qualify as indubitable equivalent treatment where the secured creditor was entitled to the proceeds of such sale.

Breaking with such precedents, the Seventh Circuit, in the *River Road* bankruptcy, rejected such a broad interpretation of "indubitable equivalents" reasoning that, if such an interpretation were adopted, this option of achieving fair and equitable treatment would eliminate the need for the other two more specific options. Thus, adopting a narrow interpretation where the indubitable equivalent option does

not encompass free and clear sales, the Seventh Circuit held that to be confirmed over the objection of a secured creditor, a plan may only provide for a free and clear sale of the creditor's collateral if it honors the creditor's right to credit bid.

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