

## ASK THE EXPERT

# Finding gold amidst the ashes: Navigating bankruptcy asset sales with experienced counsel

**W**hen you're looking to acquire business assets at a steep discount, a bankruptcy sale can be an ideal option. Despite creditors' interest in recovering as much as they can from the liquidation of bankruptcy assets, these assets are often available at prices far below their true value.

The rules regulating these sales ensure an orderly and transparent process for bidders, creditors and other stakeholders that can make bankruptcy sales a slow-moving process. Prospective buyers should understand relevant sections of the Bankruptcy Code and consider enlisting the help of experienced bankruptcy counsel to compete with seasoned bidders.

To learn what kinds of opportunities bankruptcy sales can offer and what buyers need to know to avoid pitfalls in the process, **Crain's Content Studio** posed questions to an expert in the field: James Sullivan, a partner at Windels Marx.



James Sullivan, a partner at Windels Marx.

estate, equipment, receivables, inventory, vehicles, intellectual property (patents, copyrights and trademarks), below-market leases and contract rights. In addition, businesses are often sold as a going concern in bankruptcy, including businesses in real estate, health care, retail, hospitality, entertainment, automotive, manufacturing, energy, aviation, telecommunication and mining.

**CRAIN'S: What's the difference between buying assets through a confirmed Chapter 11 plan rather than prior to plan confirmation or outside of a plan?**

**SULLIVAN:** There are a few advantages to purchasing assets pursuant to a confirmed Chapter 11 plan rather than prior to or outside of a plan. First, a sale under a plan need not be subjected to a competitive auction process so long as the plan satisfies all of the statutory criteria for approval of the plan. Therefore, buyers of a business or assets who wish to avoid an auction process should request that the assets be sold to them through a plan. Second, Section 1146(a) of the Bankruptcy

adequate prior notice of the sale and that explicit language is included in the sale motion, the sale agreement and the sale order providing that the sale is free and clear of all liens, claims and interests.

Further, including clear "free and clear" language in the sale order requires that creditors object to the sale to avoid the free and clear provision of the sale order. Another effective technique is to request that language be included in the sale order enjoining any efforts by creditors to pursue remedies against the buyer or the purchased assets and providing that the bankruptcy court shall retain exclusive jurisdiction to enforce the injunction even after the bankruptcy case is closed.

**CRAIN'S: What are the advantages to being the "stalking horse" bidder? Are there disadvantages?**

**SULLIVAN:** There are a number of advantages to being the "stalking horse" bidder (the initial bid against which all other bidders must compete). First, the stalking horse can draft a form of purchase agreement that is customized to the needs of the stalking horse. Competing bidders may find it difficult to submit a competing offer that materially differs from the stalking horse agreement. Second, the stalking horse bidder can obtain a number of special bidder protections, including a breakup fee (from 3% to 5% of the purchase price is typical) and expense reimbursement, if the stalking horse is outbid. Thus, unlike other bidders, the stalking horse is compensated for its time and expenses related to the sale process.

The primary disadvantage to being the stalking horse is that you must set the market by bidding against yourself.

In other words, it is possible that you will miss out on an opportunity to pay less if no stalking horse comes forward.

However, stalking horse agreements typically include very buyer-friendly terms, including with respect to price. Thus, this "disadvantage" is usually materially outweighed by the many significant advantages to being named the stalking horse.

**CRAIN'S: How do buyers position themselves as the stalking horse?**

**SULLIVAN:** A bidder can help position himself or herself as the stalking horse by offering to make a first-priority debtor-in-possession loan to the debtor and then make selection as the stalking horse a condition to making the loan. The bidder can also establish other

loan milestones that move the case in a direction friendly to the lender-bidder. Similarly, a potential bidder could attempt to purchase secured debt of the debtor (preferably at a discount) to use as leverage so as to be named the stalking horse. In addition, the bidder can approach the debtor early in the bankruptcy case (or even before the bankruptcy case is filed) before other bidders come forward. Finally, the bidder can try to offer the debtor something that other bidders may be unable to offer, such as an agreement to continue the business, keep key management and-or employees in place or assume certain key contracts or liabilities. ■

**CRAIN'S: Besides price, what are the advantages of buying assets out of bankruptcy? What kinds of assets can be acquired this way?**

**JAMES SULLIVAN:** Bankruptcy sales offer some significant advantages not available in a non-bankruptcy sale, including the ability to obtain trustworthy information about the business and the assets. There's also the ability to acquire lease and contract rights over the objection of a lease or contract counterparty (the

**"The best way to ensure that buyers are acquiring purchased assets free and clear of liens, claims or other interests is to ensure that any impacted creditor receives adequate prior notice of the sale."**


Bankruptcy Code renders unenforceable most contractual anti-assignment provisions); the ability to acquire assets free and clear of liens and other interests despite creditor objection; the ability to avoid payment of stamp and transfer taxes, such as real estate transfer and mortgage taxes; and the ability to avoid successor liability claims from the debtor's creditors.

Virtually any type of business or asset can be purchased out of bankruptcy. Assets commonly sold through bankruptcy include commercial and residential real


Code exempts sales under a confirmed Chapter 11 plan from the payment of stamp or other transfer taxes. For certain sale transactions, the amount saved from avoiding such taxes can outweigh the cost of the entire bankruptcy process.


**CRAIN'S: How can buyers be sure they are acquiring the assets free and clear?**

**SULLIVAN:** The best way to ensure that buyers are acquiring purchased assets free and clear of liens, claims or other interests is to ensure that any impacted creditor receives



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**James M. Sullivan**  
Partner  
212.237.1170  
jsullivan@windelsmarx.com

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