

## Bankruptcy court can be safe place to buy troubled company's assets

by Thomas Messana

A bankruptcy sale is a combination of a Middle Eastern bazaar, a used car lot and a political speech all rolled into one. It combines the best of law and economics with the goal of returning assets to productive use. Through it one may acquire the proverbial diamond in the rough...or, glass. Opportunity abounds, for the strong of nerve.

First and foremost, one needs the assistance of an experienced guide—a bankruptcy lawyer well versed in all methods of distressed sales. There are two primary methods of selling bankruptcy assets: “pursuant to a plan” and “through a 363 sale.”

Typically, sales pursuant to a plan of reorganization are coupled with other substantive changes in the debtor's business operations. While often more expensive and less expedient than a 363 sale, strategically, a potential bidder may prefer to effectuate the sale pursuant to a plan of reorganization, because it may be possible to “lock out” other potential bidders. Sales pursuant to a plan do not provide, as 363 sales do, an easy procedural mechanism by which non-creditors may participate.

Most buyers prefer 363 bankruptcy sales because, on 20-days notice, that section of the Bankruptcy Code permits the transfer of assets free and clear of all liens, claims and encumbrances, even if the holders of such claims do not consent to the sale. But almost anything can happen.

Typically, in large or “mega-cases,” the sale process involves large assets and is far more likely to be regulated and predictable. In such cases, the bankruptcy court normally establishes a set of bidding procedures to govern the sale. For example, there are often minimum deposits required from all bidders and overbid increments. In large bankruptcy sales, procedure is key and notice is wide and far.

One legitimate bidder often encourages other bidders into the process, but it can be difficult to get that “first” buyer to the table. Understanding this, courts have approved incentives to induce a potential buyer to “go first.” Denominated “the stalking horse,” the bankruptcy court often authorizes the payment of a break-up fee to mitigate the risk of going first if the stalking horse bidder is not the successful bidder at the 363 sale. The break-up fee is usually tied to the due diligence costs the initial bidder must expend in order to go first.

In medium and smaller cases, typically the procedure is far less formal. Notice of the sale is far more limited, usually only to creditors. But *all* bankruptcy sales are subject to “higher and better offers.” Therefore, the best objection to a bankruptcy sale is that the price is inadequate and that the objecting party is willing to pay the bid price plus some increased sum. Often times a hearing on a proposed sale will yield spontaneous results. In such situations, a bankruptcy court may order the parties to the hallway to conduct an auction on the spot or,

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in some circumstances, conduct an auction itself. Whatever the method, the court tries to force competing bidders to fashion their bids as mirror images, except for price. Obligated to this structure apples are being bid against apples, oranges against oranges.

Bankruptcy courts are courts of equity with broad powers to hear and rule on matters in furtherance of their jurisdictions. Sale of assets of debtors appearing before them is within a bankruptcy court's jurisdiction. Hence, one of the best aspects of a bankruptcy sale is, given an arms-length transaction on proper notice to creditors, a *federal court order* blessing the transaction. A bankruptcy sale is usually free and clear of all liens, claims and encumbrances. Simply put, there is minimal risk to the purchasers of successor liability or of unknown claims surfacing after the sale price has been paid. Additionally, unlike most legal issues, effective appeal of the sale order can be essentially eliminated.

Buy low and sell high is the mantra of successful business everywhere. Bankruptcy courts are clearly full of distressed assets. Whether that is a proper valuation or a temporary market aberration is the judgment upon which fortunes are made and lost. A bankruptcy attorney for a prospective purchaser must make his or her client aware of these distinctions. Find a good one and see for yourself. The fortune you create may be your own!

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