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Alert

Fisker Part II: Delaware District Court Refuses to Hear Appeal of Controversial Bankruptcy Court Decision Capping Credit Bid

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We recently wrote about the highly controversial decision of the Delaware Bankruptcy Court in *In re Fisker Automotive* capping a secured creditor's right to credit bid its $168 million claim at $25 million.[1] The secured creditor immediately appealed to the District Court.[2] As a procedural matter, the secured creditor had an absolute right to have its appeal heard only if the Bankruptcy Court's ruling was considered a "final order." If it was not a "final order," then the District Court had discretion on whether to hear the merits of the appeal. On Feb. 7, 2014, the District Court determined that the Bankruptcy Court order was not final and declined to hear the appeal. The District Court's 11-page opinion is just as controversial as the Bankruptcy Court's order.[3]

The District Court found that there was no "controlling question of law as to which there exists substantial grounds for a difference of opinion" because the Bankruptcy Court's controversial ruling was supported by the "plain text of 363(k)" (which permits a bankruptcy court to limit credit bidding for "cause") and "relevant legal precedent." The District Court effectively adopted the Bankruptcy Court's rationale that "cause" to cap a credit bid incudes "foster[ing] a competitive bidding environment." The Bankruptcy Court and District Court both cite a footnote in the Third Circuit's *Philadelphia Newspapers*[4] decision to support their reasoning. The secured creditor argued that the footnote is not controlling law because two of the three judges in that case declined to adopt the portion of the opinion with the footnote. Thus, the creditor argued the premise that a court can limit a credit bid to foster competitive bidding is mere *dicta*. Furthermore, the *Philadelphia Newspapers* decision (which affirmed the denial of a right to credit bid for a sale of assets under plan, as opposed to a sale under Section 363) was later overruled by the United States Supreme Court. *See RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 132 S. Ct. 2065 (2012). The District Court did not address these issues in its decision.

The District Court also dismissed the secured creditor's argument that it would be without a remedy if the auction occurred while its credit bid was capped at $25 million. The District Court noted that the secured creditor could credit bid $25 million and continue bidding with cash. In that context, the secured creditor could receive either a cash return of the difference between a full credit bid and the

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[1] Click here for our prior *Alert*.

[2] The secured creditor also sought a direct appeal to the Third Circuit.

[3] Click here for the District Court's decision.

[4] *Philadelphia Newspapers* 599 F.3d 298, 315-16 fn. 14 (3d Cir. 2010).

$25 million cap on its credit bid were the Bankruptcy Court to conclude it was so entitled. If a third-party bidder won the auction, the secured creditor would receive its entitlement from the sale proceeds.

Observations

The Bankruptcy Court's order purports to be "non-precedential" and the District Court's ruling was not a decision on the merits, but rather a decision on the right to prosecute an appeal. Nevertheless, we expect that out-of-the-money constituents and potential bidders will in the future seek to rely on these decisions to challenge and/or cap credit bids. There are significant concerns about the correctness of these decisions, but market participants likely will have to endure a wave of litigation and wait until the issue is resolved (in this case or in other cases) by the Courts of Appeals.

Authored by Adam C. Harris, David M. Hillman and James T. Bentley.

If you have any questions concerning this *Alert*, please contact your attorney at Schulte Roth & Zabel or one of the authors.

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New York | Washington DC | London
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