

# Pratt's Journal of Bankruptcy Law

LEXISNEXIS® A.S. PRATT™

JULY/AUGUST 2015

**EDITOR'S NOTE: ON THE DOCKETS**

Steven A. Meyerowitz

**THE DEBTOR'S REJECTION POWER: HOW IS IT CONSTRAINED AND CAN A COUNTERPARTY CONSTRAIN IT?**

James A. Croft

**U.S. SUPREME COURT PRESERVES BANKRUPTCY COURT POWER TO HEAR DISPUTES**

Michael L. Cook, Lawrence V. Gelber, and David M. Hillman

**FIFTH CIRCUIT FINDS UNDERSECURED CREDITOR WAIVED RIGHT TO CREDIT BID**

Michael L. Cook

**DELAWARE COURT OF CHANCERY DECISION CLARIFIES FIDUCIARY ISSUES IN INSOLVENT COMPANY CONTEXT**

Mark S. Chehi, John K. Lyons, and Ana Lucía Hurtado

***OAK ROCK FINANCIAL* DISTRICT COURT ADDRESSES THE APPLICABLE LEGAL STANDARD FOR TRUE PARTICIPATION AGREEMENTS**

Jason W. Harbour and Shannon E. Daily

**S.D.N.Y. AFFIRMS *MPM SILICONES*' "PRIME PLUS" FORMULA FOR CRAMDOWN INTEREST RATES, LIKELY HARMING CREDITOR RECOVERIES**

Craig M. Price, Michael Friedman, and Franklin H. Top, III

**THE *ENERGY FUTURE HOLDING CORP.* DECISION: VALIDATING TENDER OFFERS AND LIMITING THE APPLICATION OF CONFIRMATION REQUIREMENTS IN BANKRUPTCY SETTLEMENTS**

Andrew I. Silfen, Jeffrey N. Rothleder, and Ronni N. Arnold

**INSURANCE COVERAGE CLAIMS ARE "NON-CORE," NEW JERSEY BANKRUPTCY COURT CONFIRMS**

Stuart I. Gordon and Frank Misiti

**THE 2014/2015 GRADUAL REFORM OF THE SPANISH INSOLVENCY ACT: HOW IT AFFECTS THE BUSINESS OF INVESTORS IN DISTRESSED DEBT**

Jesús Varela, Julio Parrilla, and Antonio García



LexisNexis

**QUESTIONS ABOUT THIS PUBLICATION?**

---

For questions about the **Editorial Content** appearing in these volumes or reprint permission, please call:

Kent K. B. Hanson, J.D. at ..... 1-800-424-0651 ext. 3207

Email: ..... kent.hanson@lexisnexis.com

For assistance with replacement pages, shipments, billing or other customer service matters, please call:

Customer Services Department at ..... (800) 833-9844

Outside the United States and Canada, please call ..... (518) 487-3000

Fax Number ..... (518) 487-3584

Customer Service Web site ..... <http://www.lexisnexis.com/custserv/>

For information on other Matthew Bender publications, please call

Your account manager or ..... (800) 223-1940

Outside the United States and Canada, please call ..... (518) 487-3000

---

Library of Congress Card Number: 80-68780

ISBN: 978-0-7698-7846-1 (print)

ISBN: 978-0-7698-7988-8 (eBook)

Cite this publication as:

[author name], [*article title*], [vol. no.] PRATT’S JOURNAL OF BANKRUPTCY LAW [page number] ([year])

**Example:** Patrick E. Mears, *The Winds of Change Intensify over Europe: Recent European Union Actions Firmly Embrace the “Rescue and Recovery” Culture for Business Recovery*, 10 PRATT’S JOURNAL OF BANKRUPTCY LAW 349 (2014)

This publication is sold with the understanding that the publisher is not engaged in rendering legal, accounting, or other professional services. If legal advice or other expert assistance is required, the services of a competent professional should be sought.

LexisNexis and the Knowledge Burst logo are registered trademarks of Reed Elsevier Properties Inc., used under license. A.S. Pratt is a registered trademark of Reed Elsevier Properties SA, used under license.

Copyright © 2015 Reed Elsevier Properties SA, used under license by Matthew Bender & Company, Inc. All Rights Reserved.

No copyright is claimed by LexisNexis, Matthew Bender & Company, Inc., or Reed Elsevier Properties SA, in the text of statutes, regulations, and excerpts from court opinions quoted within this work. Permission to copy material may be licensed for a fee from the Copyright Clearance Center, 222 Rosewood Drive, Danvers, Mass. 01923, telephone (978) 750-8400.

*An A.S. Pratt® Publication*

Editorial Offices  
630 Central Ave., New Providence, NJ 07974 (908) 464-6800  
201 Mission St., San Francisco, CA 94105-1831 (415) 908-3200  
[www.lexisnexis.com](http://www.lexisnexis.com)

MATTHEW  BENDER

# *Editor-in-Chief, Editor & Board of Editors*

---

## **EDITOR-IN-CHIEF**

**STEVEN A. MEYEROWITZ**

*President, Meyerowitz Communications Inc.*

## **EDITOR**

**VICTORIA PRUSSEN SPEARS**

*Senior Vice President, Meyerowitz Communications Inc.*

## **BOARD OF EDITORS**

**Scott L. Baena**

*Bilzin Sumberg Baena  
Price & Axelrod LLP*

**Thomas W. Coffey**

*Tucker Ellis & West LLP*

**Matthew W. Levin**

*Alston & Bird LLP*

**Leslie A. Berkoff**

*Moritt Hock & Hamroff  
LLP*

**Michael L. Cook**

*Schulte Roth & Zabel LLP*

**Patrick E. Mears**

*Barnes & Thornburg LLP*

**Ted A. Berkowitz**

*Farrell Fritz, P.C.*

**Mark G. Douglas**

*Jones Day*

**Alec P. Ostrow**

*Stevens & Lee P.C.*

**Michael L. Bernstein**

*Arnold & Porter LLP*

**Timothy P. Duggan**

*Stark & Stark*

**Deryck A. Palmer**

*Pillsbury Winthrop Shaw  
Pittman LLP*

**Andrew P. Brozman**

*Clifford Chance US LLP*

**Gregg M. Ficks**

*Coblentz, Patch, Duffy &  
Bass LLP*

**N. Theodore Zink, Jr.**

*Chadbourne & Parke LLP*

**Kevin H. Buraks**

*Portnoff Law Associates,  
Ltd.*

**Mark J. Friedman**

*DLA Piper*

**Peter S. Clark II**

*Reed Smith LLP*

**Robin E. Keller**

*Lovells*

PRATT'S JOURNAL OF BANKRUPTCY LAW is published eight times a year by Matthew Bender & Company., Inc. Copyright 2015 Reed Elsevier Properties SA., used under license by Matthew Bender & Company, Inc. All rights reserved. No part of this journal may be reproduced in any form—by microfilm, xerography, or otherwise—or incorporated into any information retrieval system without the written permission of the copyright owner. For permission to photocopy or use material electronically from *Pratt's Journal of Bankruptcy Law*, please access

www.copyright.com or contact the Copyright Clearance Center, Inc. (CCC), 222 Rosewood Drive, Danvers, MA 01923, 978-750-8400. CCC is a not-for-profit organization that provides licenses and registration for a variety of users. For subscription information and customer service, call 1-800-833-9844.

Direct any editorial inquires and send any material for publication to Steven A. Meyerowitz, Editor-in-Chief, Meyerowitz Communications Inc., 26910 Grand Central Parkway, No. 18R, Floral Park, NY 11005, smeyerowitz@meyerowitzcommunications.com, 718.224.2258. Material for publication is welcomed—articles, decisions, or other items of interest to bankers, officers of financial institutions, and their attorneys. This publication is designed to be accurate and authoritative, but neither the publisher nor the authors are rendering legal, accounting, or other professional services in this publication. If legal or other expert advice is desired, retain the services of an appropriate professional. The articles and columns reflect only the present considerations and views of the authors and do not necessarily reflect those of the firms or organizations with which they are affiliated, any of the former or present clients of the authors or their firms or organizations, or the editors or publisher. POSTMASTER: Send address changes to *Pratt's Journal of Bankruptcy Law*, LexisNexis Matthew Bender, 630 Central Avenue, New Providence, NJ 07974.

# Fifth Circuit Finds Undersecured Creditor Waived Right to Credit Bid

*Michael L. Cook\**

*The author of this article discusses a recent U.S. Court of Appeals for the Fifth Circuit decision holding that an undersecured creditor intending to credit bid at a sale of the debtor's unencumbered property must give "notice" of its intent to the bankruptcy trustee.*

An undersecured creditor ("C") intending to credit bid at a sale of the debtor's unencumbered property must give "notice" of its intent to the bankruptcy trustee, held the U.S. Court of Appeals for the Fifth Circuit on April 23, 2015.<sup>1</sup> Affirming the bankruptcy and district courts' denials of C's belated request, the Fifth Circuit held that C "failed to exercise" its right to credit bid at a sale of its collateral. As discussed in this article, however, the case really dealt with a secured creditor's right under Bankruptcy Code ("Code") Section 1111(b) to "elect" a nominally large secured claim in exchange for waiving its unsecured deficiency claim.

## FACTS

The reorganization plan in this case provided for the sale of the debtor's mineral leases and several wells to a third party for cash. The plan recognized C's "lien on four of these mineral leases and one well," but "[f]our other creditors [also had] secured interests in the . . . well."<sup>2</sup> C was essentially in the position "of a third lien creditor on real property."<sup>3</sup> Despite C's electing "to promote its unsecured claim to secured status" under Code Section 1111(b),<sup>4</sup> the Fifth Circuit agreed with the lower courts' rejection of C's election because the encumbered property was being "sold under the plan"—an explicit statutory exclusion from Section 1111(b) election rights.<sup>5</sup>

C never opposed confirmation of the plan, never appeared at the confirma-

---

\* Michael L. Cook, a member of the Board of Editors of *Pratt's Journal of Bankruptcy Law*, is a partner in the Business Reorganization Group at Schulte Roth & Zabel LLP and the chairman of the American College of Bankruptcy. He may be contacted at michael.cook@srz.com.

<sup>1</sup> *In re R.L. Adkins Corp.*, No. 14-10768 (5th Cir. Apr. 23, 2015).

<sup>2</sup> *Id.*

<sup>3</sup> *Id.*

<sup>4</sup> *Id.*

<sup>5</sup> 11 U.S.C. § 1111(b)(1)(B)(ii).

tion hearing and never appealed from the order confirming the plan. Because the plan recited that the asset sale was being done under Code Section 363 with an opportunity for secured creditors like C to credit bid, in the court's view, C had effectively waived not only its right to credit bid but also to obtain a ruling on its purported right to make the Section 1111(b)(2) election. It was only after the bankruptcy court had confirmed the reorganization plan that C asserted a lien on the property held by the asset purchaser.

### RELEVANCE OF THE DECISION: SECTION 1111(B) ELECTION OR CREDIT BID AS SECURED LENDER PROTECTIONS

The *Adkins* decision is noteworthy for at least two reasons. First, the asset purchaser correctly argued that the trustee's sale of the debtor's property "under § 363 . . . or . . . under the Plan . . . preclude[d] an undersecured lender from making the § 1111(b) election."<sup>6</sup>

The concurring judge in *Adkins* explained that C's "practical position seems at odds with its claim to having been 'denied' a right to credit bid. Given the nature of [C's] liens, exercising a credit bid . . . would not have been feasible . . . [C] might theoretically credit bid . . . but [was] unlikely to do so because [it] would have to pay off the senior liens before [it] could take possession . . . [C is apparently] trying to take advantage of the bankruptcy court's error in failing to rule on the § 1111(b) election before it confirmed the Chapter 11 Plan."<sup>7</sup> In the concurring judge's view, the "argument that [C] waived its § 1111(b) election by failing to pursue it at the confirmation hearing is persuasive"<sup>8</sup>

Why did C seek to make the Section 1111(b) election? An undersecured creditor such as C has the opportunity under Section 1111(b)(2) to have its "entire secured claim treated as an allowed secured claim," regardless of the collateral's value, when there is *no* sale of the debtor's property.<sup>9</sup> But the "quid pro quo for making the election" is that "the undersecured creditor must give up its unsecured [deficiency] claim."<sup>10</sup> Had C been able to elect Section 1111(b)(2) treatment in *Adkins*, its allowed secured claim would have been \$321,506, instead of the trustee's \$38,753 valuation of C's collateral. The practical effect of this election, had it been available, would be to protect C

---

<sup>6</sup> *In re R.L. Adkins Corp.*, No. 14-10768.

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> CHAS. J. TABB, *THE LAW OF BANKRUPTCY* § 11.32, at 1162 (2d ed. 2009).

<sup>10</sup> *Id.*

against the risk that the trustee would cram down its secured claim at a low valuation. For purposes of cramdown under Code Section 1129(b)(2)(A)(i)(II), C would also have an allowed secured claim with the face amount of \$321,506, requiring the reorganized debtor to pay C the full \$321,506.28 over time. The Section 1111(b) election “ensures essentially that the debtor must resolve the secured claim for the maximum value from the collateral.”<sup>11</sup> Code Section 1129(b)(2)(A), though, requires only that the *present value* of these deferred cash payments “as of the effective date of the plan” equal the judicially determined value of the lender’s collateral, presumably \$38,753 in the *Adkins* case. But C’s secured claim would still be secured by a *lien* of \$321,506. C could thus benefit if the debtor later defaulted or sold the property. As noted, however, under Code Section 1111(b)(1)(B)(ii), the trustee’s sale of C’s collateral precluded any election right C might have had.

Second, and more important, C’s right to credit bid provided an alternative protection when it could not make the Section 1111(b) election. A recourse secured creditor like C can “bid in its claim when the collateral is [to be] sold” and “offset his full allowed claim against the purchase price.”<sup>12</sup> In *Adkins*, the Fifth Circuit recognized the U.S. Supreme Court’s holding that “debtors may not sell their property free of liens without allowing a lienholder to credit bid.”<sup>13</sup> As the concurring opinion in *Adkins* noted, “secured creditors are [thus] assured of being able to credit bid for their collateral and retain the benefit of their bargain . . . .”<sup>14</sup> C, however, failed to timely exercise its credit-bidding rights.

## PRACTICAL ADVICE FOR SECURED LENDERS

- *Promptly Assert Section 1111(b) Election Right and Obtain Ruling Before Plan Confirmation Hearing*
  - “The court’s decision will, after all, decisively affect the valuation [of the] creditor’s secured claim and . . . the requisites for plan confirmation . . . .”<sup>15</sup>
- *Insist on Section 1111(b) Election Rights If Sale Is Uncertain*

<sup>11</sup> *In re R.L. Adkins Corp.*, No. 14-10768.

<sup>12</sup> K. Klee, *All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code*, 53 AM. BANKR. L.J. 133, 153 and n.127 (1979), citing 11 U.S.C. § 1129(b)(2)(A)(ii).

<sup>13</sup> *In re R.L. Adkins Corp.*, citing *RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 132 S. Ct. 2065 (2012).

<sup>14</sup> *Id.*

<sup>15</sup> *Id.*

- Only when the estate actually sells collateral under Code Section 363(b) or “under the plan” will a lender be precluded from the Section 1111(b) election.
- *Seek Transparent, Public Auction and Ensure Right to Credit Bid*
  - Review bidding and notice procedures to ensure credit bidding protection and testing of “market for valuations.”<sup>16</sup>

---

<sup>16</sup> *Id.*