



LENDING & RESTRUCTURING ALERT

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Supreme Court Clarifies Lenders' Right to Credit Bid

In *Radlax Gateway Hotel, LLC v. Amalgamated Bank*, the United States Supreme Court on May 29th resolved a dispute among federal appeals courts by confirming the right of secured lenders to credit bid when debtors propose to sell assets under a reorganization plan. This ensures that debtors cannot confirm “cramdown” plans that cash out lenders at their collateral’s appraised value. In what it called an “easy case,” the Court unanimously held that the debtor could not sell its assets under a reorganization plan without giving the lender the right to credit bid its claim. As we reported to you in previous Alerts, two federal appellate courts (the Third and Fifth Circuits) had held otherwise, allowing the debtors to evade the Bankruptcy Code’s credit-bidding requirement to the dismay of lenders. But the Supreme Court effectively overruled the decisions of those appellate courts by unequivocally stating that the “debtors may not obtain confirmation of a Chapter 11 cramdown plan that provides for the sale of collateral free of the Bank’s lien, but does not permit the Bank to credit-bid at the sale.”

Pursuant to the “cramdown” provision of the Bankruptcy Code, a debtor can only confirm a plan over the objection of the secured lender if the plan provides one of the following treatments for the lender’s claim: (i) the lender retains its lien and receives deferred cash payments; (ii) the debtor sells the property free and clear of the lien, but allows the lender the right to credit bid at the sale (unless the debtor shows “cause” to deny the right to credit bid); or (iii) the plan provides for the secured creditor to realize the “indubitable equivalent” of its claim.

In *Radlax*, the debtor sought to sell its assets to a “stalking horse” bidder without giving the lender the right to credit bid the value of its debt. Relying on the Third and Fifth Circuits’ decisions, the debtor argued that it complied with the “indubitable equivalent” cramdown option by paying the sale proceeds to the lender, and therefore claimed it did not have to permit the lender to credit bid. Both the bankruptcy court and the Seventh Circuit Court of Appeals rejected the debtor’s argument, disagreeing with the Third and Fifth Circuits’ approach, which set up a showdown at the Supreme Court.

In its decision, the Supreme Court emphasized the need for predictability in bankruptcy court litigation. It also acknowledged that the purpose of credit bidding is to protect creditors against a sale of their collateral at an artificially depressed price.

Lenders now know that a debtor cannot deprive them of their right to credit bid unless the debtor meets the extremely difficult, rarely satisfied requirement of showing “cause” to do so.

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