



PROGRAM MATERIALS
Program #30224
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Bankruptcy Code §363 Sales

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MODERATOR



Dr. Sharon Meit Abrahams
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Dr. Sharon Meit Abrahams is a legal talent development expert with over 25 years of experience in success coaching for attorneys and executing high impact programs for law firms. She has created and implemented firm wide initiatives that help attorneys maximize their productivity while maintaining engagement. When individuals produce, a firm increases its profitability. As a talent development leader, she has handled every aspect of an attorney's firm life from onboarding and integration, through mentoring and training to succession planning and exit interviews.

Dr. Abrahams has published three books with the American Bar Association and regularly publishes articles for Thomson Reuters and American Legal Media. Known for engaging and educational programs, Dr. Abrahams is a sought-after keynote speaker, program facilitator and law firm advisor.

SPEAKERS



Stephen B. Selbst
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Stephen Selbst is the co-chair of Herrick's Restructuring & Finance Litigation Group. He has more than 30 years of experience representing debtors, creditors, official committees, distressed investors and asset purchasers in bankruptcies and out-of-court restructurings.

Stephen advises clients from a wide range of industries, including financial services, telecommunications, government agencies and real estate. A skilled commercial litigator, Stephen also has significant experience in district and state courts, where he regularly represents clients in separate litigation arising out of bankruptcy. He also advises clients on structured finance and derivative transactions.



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Steven B. Smith focuses his practice on complex corporate restructuring, liquidations and bankruptcy litigation, including in-court Chapter 11 and Chapter 15 cases and out-of-court workouts. He has extensive experience representing distressed debt investors, bondholders, official and ad-hoc creditor committees, administrative and collateral agents, indenture trustees, stalking horse and other asset purchasers, trade and tort claimants, and other significant parties-in-interest in a variety of jurisdictions across the United States.

He is a frequent lecturer on bankruptcy and restructuring topics and has published articles and book chapters on bankruptcy-related topics. He has been frequently quoted in newspaper articles on insolvency related topics and has appeared on CNBC.



BANKRUPTCY CODE § 363 SALES— CARPE DIEM

SEPTEMBER 18, 2020

STEPHEN B. SELBST

STEVEN B. SMITH



AGENDA



- Section 363 Sales
 - What are they?
 - Why are they important today?
- Seizing the Day
 - Rules of engagement
 - Staying abreast of the market

363 SALES

OVERVIEW — WHAT ARE THEY?



- Bankruptcy Code § 363 provides a process for a debtor to sell assets with bankruptcy court approval, including in a public auction process
 - Common tool in bankruptcies
 - Potential assets include: real property, leases, companies, and personal property
- Advantages of the § 363 sale process:
 - Sale is prompt: Often completed within 75-90 days of bankruptcy commencement
 - Sale is transparent: Bankruptcy Court sets the rules for the auction and all participants have an equal chance
 - Buyer acquires the asset(s) free and clear of all liens, claims and encumbrances
- A Debtor's mandated goal is to obtain "highest and best" offer—to maximize value

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ROLE OF STALKING HORSE BIDDERS



- Debtors often enter into a commitment with a “stalking horse” buyer
 - The stalking horse sets a minimum floor for asset price
 - The stalking horse may compete in the auction, but may be outbid by others
 - If the stalking horse is outbid, it typically receives a “break-up fee” of 2%-4% of the amount of its initial bid and may recover its out-of-pocket expenses
- Bid Protections
 - Bid increment requirements
 - Break-up Fee
 - Bankruptcy Court approves amount of break-up fee and/or expense reimbursement as part of the bidding procedures motion
 - Reimbursement of Expenses

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BREAK-UP FEE DISPUTES



- Break-up fees sometimes get disputed
- Standards vary by jurisdiction:
 - Approach 1: Business Judgement Review (S.D.N.Y., generally):
 - Absent a “showing of bad faith, self-interest, or gross negligence,” these courts apply a three-prong approach, looking to (1) the relationship of the parties who negotiated the fee and whether such negotiations were tainted by self-dealing or manipulation, (2) the fee’s reasonableness in comparison to the total purchase price and (3) whether the fee chills or encourages bidding
 - Approach 2: Breakup Fees as Administrative Expenses (3d Cir., Del.):
 - Scrutinized under the standards of section 503(b) of the Bankruptcy Code
 - 3rd Circuit, for example, requires the stalking horse demonstrate the payments provided an actual benefit to the estate and were necessary to preserve the value of the estate assets
- Other scrutinized sales procedures include: marketing, diligence protocols and bidding increments

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RECENT EXAMPLES



- Toys R Us (Sept. 18, 2017 filing)
 - Operated approximately 750 US stores
 - Utilize a 363 sales process as part of an orderly liquidation
 - Bid procedures gave Debtors discretion on marketing assets
 - The Debtors could sell them singly or in groups
 - Could reject an individual bid if placing property in a group would increase overall value
 - Approx. \$575m in aggregate value raised from properties sold
- Fairway Markets (Jan. 23, 2020 filing)
 - Stalking horse bidder for five stores and a distribution center, with option to purchase additional stores
 - All assets up for sale
 - Competing bidder (Food Bazaar), seeking stalking horse bid assets, plus additional store
 - Stalking horse increased bid and won
 - Two other bidders won additional assets/stores
 - Aggregate \$82.5million from the auction

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RECENT EXAMPLES (CONT.)



- John Varvatos—Men’s Retailer (May 6, 2020 filing)
 - Operates 27 retail stores, plus wholesale/online sales
 - Reached agreement with existing investor to sell as a going concern
 - Investor provided DIP financing, permitting company to operate during case
 - Investor designated stalking horse, with ability to **credit bid** at 363 auction
 - Seeking to hold auction on June 10 **virtually**
 - All operating assets to be sold, with investor acting as stalking horse with \$76m credit bid

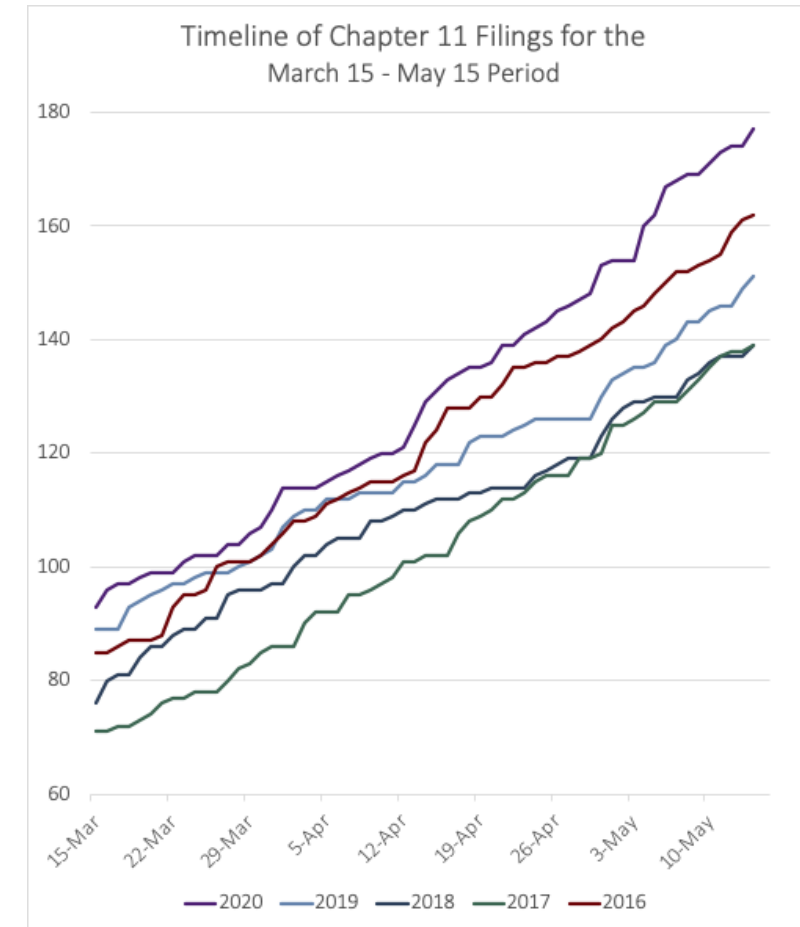
- Haight Street (June 2019 **involuntary** filing)
 - Single Asset: real property in Flushing – 40 residential units and 10 commercial units
 - Secured debt of ~\$17m
 - Ch. 11 Trustee appointed, obtained financing and completed construction, and began to market
 - Stalking horse emerged during lead up to auction (no credit bid), lender consented to terms
 - New stalking horse emerged with lowered bid (\$27.3m) after Covid led original stalking horse unable to pay deposit
 - Virtual auction held on May 12, no competing bids

2020'S FILING EXPECTATIONS

WAVE OF BANKRUPTCIES EXPECTED



- Chapter 11 filings are on the rise in 2020, with increased pace expected
- 20 filings so far by debtors with more than \$1b in liabilities
- 240 + major filers (>\$10m in liabilities) so far in 2020



Source: Reorg.com

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RULES OF THE ROAD



- Begins with Debtors' sale procedures motion
 - Due diligence—duration and process
 - Deadlines: indications of interest, stalking horse bidder designations, auction, court approval
 - Qualified bidder requirements, down payments, bidding increments
 - Stalking horse break-up fees and/or expense reimbursement
- Court must approve bid procedures prior to auction
- Diligence Process
 - Prospective bidders sign NDAs and gain access to electronic data room
 - Prospective bidders can ask for additional information and may interview management
 - No bidder is to be favored or discriminated against
 - Debtors are to seek a “robust auction”

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RULES OF THE ROAD (CONT.)



- Only “qualified bidders” may participate in the auction
 - Debtor determines, usually in conjunction with secured lender(s) and creditors committee
 - Debtors should seek to have numerous qualified bidders and a competitive auction
 - Qualified bidder must demonstrate financial capability, either in cash or committed financing
 - Down payment of 5-10% of initial bid amount commonly required
- Auctions
 - Typically held in offices of a debtor’s counsel and led by debtor’s financial advisor
 - Virtual auctions are possible and more common
 - All bids and statements of position are “on the record” (court reporter present)
 - After a new topping bid, remaining bidders generally given time to caucus and determine whether to submit topping bid
 - Debtor has flexibility to change auction rules in process to maximize value

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RULES OF THE ROAD (CONT.)



- Winning Bidders

- Auction continues until Debtor determines “highest and best” bid
 - Typically consults with secured lender(s) and creditors’ committee
 - Purchase agreements are “hard” – with limited reps and warranties or indemnity provisions

- Court Approval

- Debtor seeks Court approval following auction
 - Usually 1-3 days after auction
- Disappointed bidders sometimes challenge the auction
 - Rarely successful post auction
 - If successful, likely outcome is reopening of auction

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IDENTIFYING & CAPITALIZING ON OPPORTUNITIES



- Importance of Counsel
 - Access to Debtor’s advisors
 - Qualifying as bidder
 - Ensuring even playing field
 - Avoiding “foot-faults”
- Using Financial Advisors
 - Diligence of the debtor’s assets and cap structure
 - Assessing stalking horse and competing bids, and bidding strategies
 - Access to Debtor’s advisors
- Resources
 - Reorg Research
 - *The Real Deal, Crain’s*
 - Counsel and Advisors
- Herrick Reporting
 - We are building out a regularly-distributed email discussing 363 opportunities for our clients – email HerrickNews@herrick.com to get added



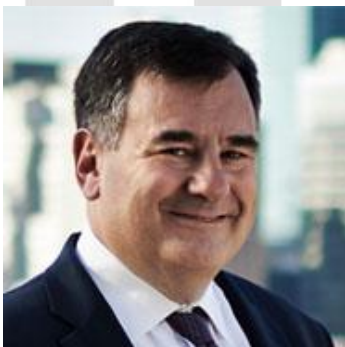
HERRICK'S RESTRUCTURING & FINANCE LITIGATION GROUP

RESTRUCTURING & FINANCE LITIGATION



- We focus on corporate, real estate, and capital markets related litigation in addition to bankruptcy and restructuring matters
- Our scope of work covers a broad range of litigation involving corporate finance, M&A litigation, valuation disputes, capital markets, bondholder rights, lender disputes, complex financial and various real estate investment matters
- We capitalize on the Herrick's relatively small size—compared with other firms that practice in the distressed space—to develop a niche litigation practice, offering sophisticated litigation expertise without being burdened by the extensive conflicts that often accompany big law firms
- Our group has extensive experience representing creditors and debtors in all phases of complex chapter 11 bankruptcy cases and out-of-court restructurings—including distressed debt investing, restructuring-related litigation, and real estate workouts
- Our clients include official and ad hoc creditor committees, hedge funds, mortgage lenders, real estate project owners, private equity funds, distressed debt investors, bondholders, financial institutions, and corporate debtors
- *Regional Roots, National Reach:* While Herrick has deep roots in the New York and New Jersey courts, its Restructuring and Finance Litigation team practices throughout the country, including Delaware, Texas, Florida, Illinois, Oklahoma, North Carolina, and California, as well as in international cross-border cases.

HERRICK, FEINSTEIN BANKRUPTCY PARTNERS



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Steve is also experienced in the analysis of true sale, non-consolidation, and bankruptcy remoteness principles in opinion and related contexts and has lectured on the topic on numerous occasions.