June 4, 2012

# Supreme Court Holds Secured Creditor Has Absolute Right to Credit Bid at a Plan Sale

Whether a secured creditor has an absolute right to credit bid at a sale under a chapter 11 plan has been the subject of conflicting decisions rendered by the Third, Fifth and Seventh Circuits.[1] The United States Supreme Court has resolved these inconsistent rulings with its decision in *RadLAX Gateway Hotel, LLC, et al.*, v. *Amalgamated Bank*, [2] which affirmed the Seventh Circuit's holding that a secured creditor has an absolute right to credit bid in a sale under a chapter 11 plan. Writing for the unanimous Court, Justice Scalia held that when a plan provides for a sale of collateral free and clear of a secured creditor's liens, the secured creditor must be permitted to credit bid; a plan proponent cannot satisfy the confirmation requirements of section 1129(b) of the Bankruptcy Code by providing a secured creditor with the "indubitable equivalent" of its claim when the creditor's collateral is to be sold.

In 2007, RadLAX Gateway Hotel, LLC, and RadLAX Gateway Deck, LLC (the "Debtors") acquired the Radisson Hotel at Los Angeles International Airport and related properties with the proceeds of a $142 million loan secured by substantially all of the Debtors' assets. The Debtors did not have sufficient capital to complete renovation of the property and filed for chapter 11 protection in 2009. In 2010, the Debtors proposed a chapter 11 plan premised on a sale of substantially all of their assets to a stalking horse bidder offering $47.5 million. The auction procedures did not permit the secured creditor to credit bid; instead, it would have to pay cash if it were not satisfied with the stalking horse bid and wanted to acquire the property itself. The Debtors sought confirmation of their plan under section 1129(b)(2)(A)(iii), contending that payment of the sales proceeds constituted the "indubitable equivalent" of the secured creditor's claims.

Section 1129(b)(2)(A) provides for confirmation of a plan over the objection of a class of secured creditors – a "cramdown" plan -- provided the plan does not discriminate unfairly and is "fair and equitable." The "fair and equitable" requirements for secured creditors include (i) retention of liens and receipt of deferred cash payments equal to the present value of the collateral; (ii) sale of assets free and clear, subject to a secured creditor's right to credit bid; or (iii) realization of a secured creditor's claim by any means that constitutes the "indubitable equivalent" of its claims.

Amalgamated Bank, the trustee for the secured creditor, objected to the auction procedures and the plan, arguing that a sale of its collateral free of liens required that it be allowed to credit bid pursuant to section 1129(b)(2)(A)(ii). The Bankruptcy Court denied approval of the



[1] *See River Road Hotel Partners, LLC* v. *Amalgamated Bank*, 651 F.3d 642 (7th Cir. 2011); *In re Philadelphia Newspapers, LLC*, 599 F.3d 298 (3d Cir. 2010); *Scotia Pac. Co., LLC* v. *Official Unsecured Creditors' Comm. (In re Pacific Lumber Co.)*, 584 F.3d 229 (5th Cir. 2009).

[2] No. 11-166, 2012 WL 1912197 (May 29, 2012) (Scalia, J.) (Kennedy, J. recused).

Debtors' proposed auction procedures for failure to comply with such provision. The Debtors appealed and the Seventh Circuit affirmed. The Debtors then appealed to the Supreme Court.

The Court affirmed the Seventh Circuit, rejecting the Debtors' argument that by providing a secured creditor with the "indubitable equivalent" under section 1129(b)(2)(A)(iii) a chapter 11 debtor need not satisfy section 1129(b)(2)(A)(ii), which specifically provides for credit bidding. The Court concluded that the Debtors' reading of section 1129(b)(2)(A) was "hyperliteral and contrary to common sense," running afoul of the well-established cannon of statutory interpretation that "the specific governs the general" -- a specific statutory authority will be construed as an exception to general statutory authority. *Id.* at *4. The open-ended "indubitable equivalent" language in section 1129(b)(2)(A)(iii) should not be held to apply to proposed asset sales and accompanying bid procedures under a plan, which are matters specifically dealt with in section 1129(b)(2)(A)(ii). The Court further stated that the Bankruptcy Code "standardizes an expansive (and sometimes unruly) area of law, and it is our obligation to interpret the Code clearly and predictably using well established principles of statutory construction." Accordingly, the Court deemed the matter before it "an easy case." *Id.* at *6.

While the conclusion reached in *RadLAX* will be viewed by many restructuring professionals as correct, the Court's brief opinion notably omits any explanation of why credit bidding serves as the cornerstone of "fair and equitable" treatment in the context of a plan-based sale of a secured creditor's collateral. Nor is there any discussion of how such treatment is consistent with the various provisions of the Bankruptcy Code designed to protect the interests of secured creditors.

While lenders and restructuring professionals may question why the Court did not delve into the more substantive debate addressed by the prior Circuit Court decisions on this topic, the Court's definitive resolution of a secured creditor's right to credit bid at a plan sale will bring much needed certainty to the confirmation process and a correction in the debtor/secured creditor dynamic.

* * * *

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Alan W. Kornberg
212-373-3109
akornberg@paulweiss.com

Stephen J. Shimshak
212-373-3313
sshimshak@paulweiss.com

Alice Belisle Eaton
212-373-3125
aeaton@paulweiss.com

**NEW YORK**
1285 Avenue of the Americas
New York, NY 10019-6064
+1-212-373-3000

**BEIJING**
Unit 3601, Fortune Plaza Office
Tower A
No. 7 Dong Sanhuan Zhonglu
Chao Yang District, Beijing 100020
People's Republic of China
+86-10-5828-6300

**HONG KONG**
12th Fl., Hong Kong Club Building
3A Chater Road
Central Hong Kong
+852-2846-0300

**LONDON**
Alder Castle, 10 Noble Street
London EC2V 7JU
United Kingdom
+44-20-7367-1600

**TOKYO**
Fukoku Seimei Building, 2nd Floor
2-2, Uchisaiwaicho 2-chome
Chiyoda-ku, Tokyo 100-0011
Japan
+81-3-3597-8101

**TORONTO**
Toronto-Dominion Centre
77 King Street West, Suite 3100
P.O. Box 226
Toronto, ON M5K 1J3
Canada
+1-416-504-0520

**WASHINGTON, D.C.**
2001 K Street NW
Washington, DC 20006-1047
+1-202-223-7300

**WILMINGTON**
500 Delaware Avenue, Suite 200
Post Office Box 32
Wilmington, DE 19899-0032
+1-302-655-4410