

Minority First-Lien Lenders Rebuffed in Attempts to Hijack Bankruptcy Sales

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Bankruptcy courts in the District of Delaware and Southern District of New York recently approved major asset sales over challenges by minority first-lien lenders to the authority of administrative and collateral agents to credit-bid and consent to such sales. In *In re Chrysler LLC*,¹ minority first-lien lenders sought to derail the multi-billion dollar sale that was the core of the struggling carmaker's U.S. Treasury-supervised restructuring. The objecting lenders argued that the assets could not be sold free and clear of their first-priority liens because they did not consent, as required by §363(f) of the Bankruptcy Code, and the purported consent of the first-lien administrative agent on their behalf was unauthorized.² In *In re GWLS Holdings Inc. (Great Wide)*,³ and *In re Metaldyne Corp.*,⁴ lenders disputed the authority of administrative agents to credit-bid on substantially all of the debtors' assets.⁵

In each case, the dissenting lenders held less than 1 percent of the first-lien indebtedness.⁶ In *Great Wide*, the objecting lender held a mere \$1 million of \$337 million in senior debt.⁷ In *Metaldyne*, the lender held \$3.5 million of \$425 million prepetition term debt.⁸ In *Chrysler*, objecting lenders held \$42 million of \$6.9 billion in first-lien claims.⁹

¹ Case No. 09-50002 (AJG) (Bankr. S.D.N.Y.).

² *In re Chrysler LLC*, 405 B.R. 84, 100-01 (Bankr. S.D.N.Y. 2009). Objecting lenders and other parties in interest raised additional objections, asserting, among other things, that the asset sale and restructuring was a sub rosa plan and violated the absolute priority rule. *Id.* at 93.

³ Case No. 08-12430 (PJW) (Bankr. D. Del.).

⁴ Case No. 09-13412 (MG) (Bankr. S.D.N.Y.).

⁵ *In re GWLS Holdings Inc.*, 2009 Bankr. LEXIS 378, *4 (Bankr. D. Del. Feb. 23, 2009); *In re Metaldyne Corp.*, 2009 Bankr. LEXIS 2131, *8-11 (Bankr. S.D.N.Y. Aug. 12, 2009).

⁶ In a recent case in the District of Delaware, *In re Foamex International*, Case No. 09-10560 (KJC), Chief Bankruptcy Judge Kevin J. Carey approved the sale of substantially all of the debtors' assets to the first-lien lenders over the objections of dissenting minority lenders holding approximately \$100 million of approximately \$344 million in outstanding indebtedness. The dissenting first-lien lenders argued that even if a credit bid was authorized by credit and security documents, the minority lenders could choose not to participate and instead receive payment in full of their indebtedness. Citing *Great Wide* with approval in open court, Judge Carey approved the credit-bid and sale over the dissenting lenders' objections. The sale order provides that the first-lien lenders reserve their rights against the agent or any other lender under the first-lien credit and security documents, except for "any claims or causes of action relating to the ability of the agent to credit-bid the claims of all such lenders and the Sale and transfer of the Purchased Assets to the Purchaser in accordance with the Final APA." See Order (A) Authorizing and Approving the Sale of Purchased Assets Free and Clear of Liens, Claims, Encumbrances and Other Interests, (B) Authorizing and Approving the Assumption and Assignment of Executory Contracts and Unexpired Leases and (C) Granting Related Relief (Docket No. 483).

⁷ *In re GWLS Holdings Inc.*, 2009 Bankr. LEXIS 378 at *3.

⁸ *In re Metaldyne Corp.*, 2009 Bankr. LEXIS 2131 at *2.

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Each case demonstrates the potential for divergent interests among lenders in a syndicate under a common-credit agreement, especially in bankruptcy. The cases also highlight the need for borrowers, agents and lenders to reconsider routine language in credit agreements on the "front end" so as to anticipate the tactics of aggressive and hostile minority lenders in bankruptcy. In each case, the objecting first-lien lenders based arguments on,

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among other things, routine "amendment and waiver" provisions in the applicable credit agreement,¹⁰ which generally provide that an administrative agent, with the consent of "required lenders" (usually the holders of a simple majority, or more, of the principal indebtedness) may enter into an agreement that amends or modifies the credit agreement or waives rights, including with respect to a default.

Such provisions often specify that unanimous lender consent is required only for amendments, modifications or waivers that effect certain material actions, such as an increase in lender commitments, a reduction in interest rates, waiver or delay of scheduled payments, extensions of maturity, changes to the definition of "required lenders" and a release of all or substantially all of the collateral. Minority lenders in *Chrysler*, *Great Wide* and *Metaldyne* argued that the proposed sales effected a release of substantially all of the collateral and required unanimous lender approval.¹¹

⁹ *In re Chrysler LLC*, 405 B.R. at 92.

¹⁰ *In re Chrysler LLC*, 405 B.R. at 102-03; *In re GWLS Holdings Inc.*, 2009 Bankr. LEXIS 378, at *4-5; *In re Metaldyne Corp.*, 2009 Bankr. LEXIS 2131 at *10-11.

The bankruptcy courts in each case—the Southern District of New York in *Chrysler* and *Metaldyne*, and the District of Delaware in *Great Wide*—held that amendment and waiver provisions were inapplicable, and that the actions of administrative and collateral agents were duly authorized under the plain language of credit and security agreements.¹² The courts rejected additional objecting lender arguments, including: in *Chrysler*, that the government had intimidated lenders into supporting an asset sale; in *Great Wide*, that an intercreditor agreement between first- and second-lien lenders somehow controlled the first-lien lender and agent's authority to credit-bid; and in *Metaldyne*, that a public-sale provision in the security agreement required each lender to credit-bid its own debt.¹³

Chrysler

The sale transaction at issue was a major component of Chrysler's

restructuring plan, which involved the establishment of a new Delaware LLC (New Chrysler), a nondebtor, to receive substantially all of Chrysler's assets and certain liabilities in exchange for a cash payment of \$2 billion.¹⁴

In an opinion dated May 31, 2009, the bankruptcy court approved the sale of substantially all of the debtors' assets free and clear of liens over the objection of the Indiana State Teachers Retirement Fund, Indiana State Police Pension Trust and Indiana Major Move Construction (collectively, the Indiana Funds).¹⁵ The Indiana Funds argued that the court could not approve Chrysler's sale of assets free and clear of the first

¹¹ *In re Chrysler LLC*, 405 B.R. at 102; *In re GWLS Holdings Inc.*, 2009 Bankr. LEXIS 378, at *11-12; *In re Metaldyne Corp.*, 2009 Bankr. LEXIS 2131 at *11.

¹² *In re Chrysler LLC*, 405 B.R. at 103; *In re GWLS Holdings Inc.*, 2009 Bankr. LEXIS 378, at *15; *In re Metaldyne Corp.*, 2009 Bankr. LEXIS 2131 at *18.

¹³ *In re Chrysler LLC*, 405 B.R. at 103-04; *In re GWLS Holdings Inc.*, 2009 Bankr. LEXIS 378, at *14-15; *In re Metaldyne Corp.*, 2009 Bankr. LEXIS 2131 at *21-22.

¹⁴ The restructuring plan included a joint venture with Fiat SpA, as well as settlements and agreements with unions with respect to a going-forward wage structure and the treatment of legacy obligations. *In re Chrysler LLC*, 405 B.R. at 92.

¹⁵ *Id.* at 112.

continued on page 76

Minority First-Lien Lenders Rebuffed in Attempts to Hijack Bankruptcy Sales

from page 30

liens because the Indiana Funds were a party in interest and did not provide the consent required under §363(f).¹⁶ The court overruled the objection, finding that the Indiana Funds were bound by the consent of the administrative agent and the collateral trustee.¹⁷

The court reasoned that under the first-lien credit agreement, the Indiana Funds “irrevocably designated” JPMorgan Chase Bank NA as the administrative agent and agreed to be bound by its exercise of properly-delegated authority, including actions taken at the request of lenders holding a majority of the first-lien indebtedness. Where the administrative agent received the support of 92.5 percent of the outstanding principal amount of the loans, the Indiana Funds were bound by the administrative agent’s direction to the collateral trustee, Wilmington Trust Co., to consent to the sale of assets free and clear of the liens of the first-lien lenders.¹⁸

The court rejected the Indiana Funds’ argument that the amendment and waiver section of the first-lien credit agreement required unanimous lender consent to sell substantially all of the collateral free and clear of the first liens. Citing *Great Wide*, the court stated that “[t]he transfer of the purchased assets to New Chrysler pursuant to §363...does not require any amendment, supplement or modification to the loan documents.”¹⁹

The court also noted that the amendment and waiver section provided an exception for actions that were otherwise authorized by the loan documents.²⁰ The collateral agent was authorized to sell any or all collateral under the collateral-trust agreement, which provided the collateral agent with authority to consent to the sale in bankruptcy “without the need to amend or modify the loan documents.”²¹ The

court further held that the sale under §363 was not a “release” of collateral “because the lien attaches to the proceeds of the sale, which remains as collateral to secure the loan made by the Lenders.”²² The court concluded that the credit and collateral documents allowed the administrative agent and collateral trustee to act for the good of the lender group as a whole and to prevent a minority of lenders from asserting undue leverage.²³

The Indiana Funds made the additional—and unusual—argument that the consent provided by the majority of first-lien lenders should be voided because it was the result of “undue pressure” from the federal government. It suggested that the first-lien lenders that received funds under the government’s Trouble Asset Relief Program (TARP) were intimidated by the government to support the Chrysler asset sale.²⁴ The court dismissed the allegations as “mere speculation... without merit” and noted that “it is not clear that this Court would even have jurisdiction over this inter-creditor dispute.”²⁵ Following the opinions of the bankruptcy court, the Second Circuit Court of Appeals affirmed the sale order,²⁶ and the Supreme Court, after a one-day temporary stay, denied a petition by the Indiana Funds to stay the sale.²⁷

Great Wide

In *Great Wide*, the court approved the first-lien agent’s credit bid of the full amount outstanding under the first-lien facility (approximately \$337 million)²⁸ over the objections of Grace Bay Holdings II LLC, which held a mere \$1 million of the first-lien debt. As the Indiana Funds argued in *Chrysler*, Grace Bay asserted that the credit-bid required unanimous lender consent since, under the amendment and waiver section of the first-lien credit agreement, unanimous lender consent was required for modifications that released all or substantially all of the collateral securing the first-lien

facility.²⁹ Grace Bay also pointed to language in the intercreditor agreement between the first- and second-lien lenders that provided that so long as the first-lien obligations are outstanding:

[T]he First Lien Collateral Agent and the First Lien Secured Parties shall have the exclusive right to enforce rights, exercise remedies (including setoff and the right to credit-bid debt) and make determinations regarding the release of, disposition, or restrictions with respect to the Collateral without any consultation with or the consent of the Second Lien Collateral Agent or any Second Lien Secured Party.³⁰

The court approved the sale to the first-lien lenders, but the sale order, dated Jan. 23, 2009, expressly stated that the purchased assets remained subject to a \$1 million lien in favor of Grace Bay, pending further order of the court.³¹ In its opinion dated Feb. 23, 2009, the court held that the credit bid was not an amendment or modification to the loan documents.³²

Further, the court found Grace Bay’s assertion that the intercreditor agreement evidenced the need for unanimous lender consent to a credit bid to be “strained and unpersuasive.”³³ It correctly found that the intercreditor agreement governed the rights of the first-lien lenders and agent in relation to the second-lien lenders and agent, and did not address first-lien lender consent to action by the first-lien agent.³⁴ The court found clear authority for the credit-bid in §10.1 of the first-lien credit agreement, which authorized the first-lien agent to exercise any powers delegated by the credit agreement and the collateral agreement, and §6.6 of the first-lien collateral agreement, which provided that during an event of default the collateral agent could “exercise... all rights and remedies of a secured party under the New York UCC or any other applicable law” including the sale of collateral.³⁵ The court held that the reference to “other applicable law” included the Code, including

¹⁶ *Id.* at 100-01. Section 363(f) provides that a debtor may sell property “free and clear of any interest in such property” if –

(1) applicable nonbankruptcy law permits sale of such property free and clear of such interest;

(2) such entity consents;

(3) such interest is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property;

(4) such interest is in bona fide dispute; or

(5) such entity could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest.

The debtors in *Chrysler* asserted that a sale free and clear of “interests,” including liens and other encumbrances, was proper under §363(f)(2) based on the consent of first-lien agents. *Id.* In *Great Wide*, at issue was authority of a first-lien agent to credit-bid under §363(k). *In re GWLS Holdings Inc.*, 2009 Bankr. LEXIS 378, at *11-16.

¹⁷ *Id.* at 102.

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ *Id.* at 103.

²¹ *Id.*

²² *Id.*

²³ *Id.*

²⁴ *Id.*

²⁵ *Id.* at 104.

²⁶ *In re Chrysler LLC*, 2009 U.S. App. LEXIS 17441, *28-32 (2d Cir. Aug. 5, 2009).

²⁷ *Indiana State Police Pension Trust v. Chrysler LLC*, 129 S.Ct. 2275 (U.S. 2009).

²⁸ *In re GWLS Holdings Inc.*, 2009 Bankr. LEXIS 378, at *3.

²⁹ *Id.* at *3-4.

³⁰ *Id.* at *5.

³¹ *Id.* at *8.

³² *Id.* at *12.

³³ *Id.* at *14.

³⁴ *Id.* at *14-15.

³⁵ *Id.* at *13.

§363(k), under which the first-lien agent submitted the credit bid.³⁶

Following entry of the sale order that carved out resolution of Grace Bay's lien, Grace Bay—for the first time—raised the argument that the court lacked jurisdiction. The court observed that “Grace Bay did not object to the Court resolving Grace Bay's objections at the hearing regarding the Sale Order, did not make any reservations regarding the instant contract interpretation issue, and did not file an appeal to the Sale Order.”³⁷ “In short,” Judge **Peter J. Walsh** held that “Grace Bay has submitted to this Court's jurisdiction.” The court also noted that the credit bid was an “integral part” of the sale of assets, which was a “core” bankruptcy matter.³⁸ Grace Bay appealed the court's ruling to the Delaware district court,³⁹ and on Aug. 12, 2009, the debtors filed a stipulation of dismissal that attached a settlement stipulation that provided for the payment in full of Grace Bay's claim.

Metaldyne

In *Metaldyne*, the court approved the sale of substantially all of the debtors' assets to a consortium that included the debtors' prepetition senior term lenders. The consideration was a mixture of cash, assumption of liabilities and a credit bid of the entire \$425 million in senior term debt.⁴⁰ Minority lender BDC Finance LLC objected that under the credit

agreement and security agreement the term lenders' agent, JPMorgan Chase NA, could not properly credit-bid BDC's debt or release liens on collateral without BDC's consent.⁴¹ BDC argued that unanimous lender consent was required for the release of collateral under the amendment and waiver provision of the credit agreement.⁴²

There appears to be no shortage of prepetition lenders with minority positions willing to assert creative arguments to obtain leverage in bankruptcy sales.

In an opinion dated Aug. 12, 2009, the court held that the credit bid did not implicate the amendment and waiver provision of the credit agreement.⁴³ The court relied on *Chrysler* and *Great Wide*, stating that “the sale through a credit-bid does not involve or require amendment or modification of the loan documents.”⁴⁴ As in *Chrysler* and *Great Wide*, the court found that the lenders' delegation of authority, in the agency provisions of the credit agreement, was sufficient to bind the minority lender in a credit-bid on collateral that was supported by holders of a majority of the outstanding indebtedness.⁴⁵

BDC also relied on a public-sale provision in the security agreement that provided that “any secured party” could purchase by way of a credit-bid collateral free of the grantor's rights of redemption and similar encumbrances. BDC argued that because that section spoke in terms of “any secured party,” the agent was precluded from credit-bidding any secured party's debt.⁴⁶ The court held that the public-sale provision applied to sales under the New York UCC and not §363 of the Bankruptcy Code.⁴⁷ The court also noted that the definition of “secured party” in the security agreement included the administrative agent.⁴⁸

Conclusion

There appears to be no shortage of prepetition lenders with minority positions willing to assert creative arguments to obtain leverage in bankruptcy sales. In each discussed case, the objecting first-lien lenders based arguments on language in routine “amendment and waiver” provisions in applicable credit agreements. While *Chrysler*, *Great Wide* and *Metaldyne* provide authority against a minority lender raising such an argument, borrowers, lenders and agents may benefit from language in credit and security documents that clarifies the application (or nonapplicability) of these sections in connection with dispositions of collateral in bankruptcy. ■

³⁶ *Id.*

³⁷ *Id.* at *10.

³⁸ *Id.*

³⁹ 09-cv-00214 (D. Del.).

⁴⁰ *In re Metaldyne Corp.*, 2009 Bankr. LEXIS 2131 at *6-7.

⁴¹ *Id.* at *9-10.

⁴² *Id.*

⁴³ *Id.* at *18-19.

⁴⁴ *Id.* at *18.

⁴⁵ *Id.* at *20-21. Lenders supporting the credit bid and sale held 97 percent of the outstanding indebtedness.

⁴⁶ *Id.* at *10.

⁴⁷ *Id.* at *21.

⁴⁸ *Id.* at *22.

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