

5 Tips For Bankrupt Cos. Looking To Sell Assets

By **Maria Chutchian**

Law360, New York (October 01, 2013, 4:32 PM ET) -- Chapter 11 filings across the U.S. are down, but bankruptcy experts say distressed companies are still utilizing asset sales under Section 363 of the U.S. Bankruptcy Code to protect the value of their businesses and avoid liquidation.

A 363 sale is a popular way for a company to save the value of its assets even as it struggles to keep its head above water and it offers the opportunity of keeping a business afloat, even if the company is taken over by new management. In these cases, a going-concern sale under Section 363 is the best way for many entities to steer clear of liquidating and is more efficient than marching into Chapter 11 with no clear plan.

"It's bad, in my experience, to file what's referred to as a free-fall bankruptcy, where you're going in knowing you have to sell but don't have anybody committed to buy," Jordi Guso of Berger Singerman LLP said. "It puts great stress on the process, management and stakeholders."

But struggling businesses need to carefully craft their approach to the sale to avoid being taken advantage of by lenders and interested buyers and to ensure that they are creating a situation that allows for a highly competitive bidding process that will maximize the value of their property, experts say. Otherwise, the company could end up being forced to switch gears and abandon the sale process after it already started, as biosolid recycling company Synagro Technologies Inc. found itself doing earlier this year after it already secured a stalking horse bid and court approval for bid procedures.

Here are five practices recommended by bankruptcy professionals for distressed companies considering a sale.

Get a Head Start Before Filing a Petition

Nothing will ruin a company's chances of securing the best value possible for its assets than a rushed sale process, experts say. To ensure that this doesn't happen, it's best to begin scouting out potential buyers long before stepping foot inside a bankruptcy court.

Beginning the process before filing for bankruptcy will boost competitive interest, attorneys say. It also allows interested buyers time to conduct due diligence and make themselves comfortable with the stakes.

"To accomplish the best result, debtors should be cognizant of the need to prepare detailed solicitation packages, disseminate those packages across a broad yet targeted group of potential strategic and financial bidders, create comprehensive data rooms ... and promote conversation between potential bidders and other key constituencies in the case, such as official creditors committees and lenders," Thomas Fawkes of Freeborn & Peters LLP said.

Find Bankers with Industry-Specific Expertise

To ensure that a company has reached out to every potential suitor, the help of an investment banker is crucial. Sellers need to hire someone with background in the industry of the distressed business, experts say.

"They should know who the players are for the assets and have the contact information for the universe of potential buyers," John Isbell of Thompson Hine LLP said.

Even if a company has its own list of potentially interested buyers, an investment banker can get the word out that the assets are up for sale and set up a thorough due diligence process. In certain instances, a potential buyer may pass on a prepetition opportunity only to come back after a stalking horse bid has been disclosed and drive up competition, Guso said.

Coughing up the funds for an expensive professional may be daunting to a cash-strapped businesses, but the investment will be worthwhile in the end. Investment bankers can attest to the integrity of the sale process down the road.

"Resources spent upfront will pay big dividends later when people come out of the woodwork to object to the sale, which almost always happens," Kathryn Coleman of Hughes Hubbard & Reed LLP said.

If the distressed company is small- or midmarket and simply can't afford an investment banker, it's up to the executives to determine who their competition is and who may be interested in buying their assets, Jan Hayden of Baker Donelson Bearman Caldwell & Berkowitz PC said. In many of those cases, buyers the debtor didn't know about will appear for the first time after the auction has been announced.

Pick a Safe Stalking Horse

Selecting a stalking horse bid, which serves as the minimum bid during an auction, is perhaps the most important part of the 363 sale process. After thoroughly surveying the field, debtors should pick a bidder that offers the best value with the fewest contingencies.

However, there are different things to consider. Coleman says a stalking horse bid should be the party with the most buy-ins from other constituencies, even if they aren't necessarily paying the most cash. Fawkes, on the other hand, recommends that sellers pick an all-cash offer, unless the buyer is a secured creditor with liens on the debtors' assets seeking to credit bid.

Either way, experts generally agree that, if possible, a company should avoid signing a no-solicitation agreement, which will stifle competition.

"You want to continue to market the assets prior to the auction to get more bidders interested in the assets," Isbell said.

Don't Fear the Breakup Fee

Protecting your selection for a stalking horse bid can be pricey, but experts say that shouldn't let the best deal fall through the cracks. Developing a competitive bidding process for the auction is important because it will result in greater recovery for creditors, even if it means agreeing to a hefty fee in the event that an offer better than the stalking horse comes along.

And even if no better offer presents itself, the company has simply gained the trust and confidence of its buyer.

"If I'm representing the seller, I'd be willing to trade paying a bona fide, well-capitalized, committed buyer a higher breakup fee to assure myself of that certainty and that I'm going hand in hand with a partner that I know will close," Guso said.

Furthermore, it's likely in just about any case that unsecured creditors will demand that the breakup fee be whittled down if they are going to agree to bid procedures, he added.

Smaller companies, on the other hand, will have to pay closer attention to the amount of the fee, especially if they don't have a broker to ensure that all interested parties have been contacted, Hayden said. If a debtor is left to itself to contact potential buyers, it is possible that it won't reach every party before it selects a stalking horse, and a better offer could present itself during the auction.

But in those smaller cases, judges are less inclined to approve a large fee, she said.

Cooperate with Lenders and Unsecured Creditors

General unsecured creditors always get the short end of the stick in a bankruptcy proceeding, but they also have the power to get in the way of a debtor's sale process, which can mean litigation. To corral their support, experts say debtors must be sure that something is set aside for them, no matter how few proceeds are available.

If the best offer doesn't provide enough to pay off, even partially, unsecured creditors' claims, companies will have to negotiate with lenders for a carveout that will provide the junior creditors some value, experts say. That should solidify the unsecured creditors' consent to the sale, according to Michael L. Gesas of Arnstein & Lehr LLP.

But in the event that there aren't enough resources to even set aside a carveout, debtors will have to convince unsecured creditors that the sale is necessary to ensure that the business can continue, which would allow it to use the unsecured creditors as vendors going forward. This situation occurs often in the automotive industry, Gesas said.

"Most vendors don't want to turn down new business," he said.

Open discussions with these stakeholders allow the seller to fully explain the sale's economic benefit to all parties and secure an easy approval. From the get-go, debtors should be looping both secured lenders and unsecured creditors in on sale talks. Transparency is key to a successful and uncontested outcome, attorneys say.

"It's really just explaining to each group why it's in their best interests to take the 363 sale," Hayden said.

--Editing by Katherine Rautenberg and Sarah Golin.

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