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WHAT IS CREDIT BIDDING IN BANKRUPTCY?

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Posted at 13:33h in Chapter 11 Bankruptcy by Nicholas Ortiz, Boston Bankruptcy Attorney • 0 Comments • Share

Credit bidding is a right that secured creditors have in bankruptcy sales allowing them to control the sale of their collateral. When collateral that secures a lien is proposed to be sold at a bankruptcy auction, a secured creditor is allowed to bid the amount of its debt as a credit bid, i.e. not a cash bid. This means that the secured creditor can compete with cash bidders with just a pen stroke. The right to credit bid, which is found principally in Section 363 of the Bankruptcy Code, gives undersecured creditors the ability to control their collateral when it it worth less than the face amount of their claims. For example, if some real estate worth $500,000 and collateral for a bank loan of $750,000 was proposed to be sold, a debtor would find it difficult to sell the property over the objection of its mortgagee in a bankruptcy sale for its value. This is because the secured lender would have the ability to bid the full amount of its claim of $750,000 without offering any cash. Credit bidding is seen as one of the chief rights of secured creditors in bankruptcy.

Although credit bidding has traditionally been seen as available in all bankruptcy sales, this notion has been partially eroded. In the seminal case of In re Philadelphia Newspapers, LLC, 599 F. 3d 298 (3rd Cir. 2010) the influential Third Circuit Court of Appeals upheld bid procedures that barred a secured lender from credit bidding at a bankruptcy sale. The key point of this case was that the sale was a plan sale and not a Section 363 sale. Consequently, the panel held that the debtor had the right to give the lender what is known as the "indubitable equivalent" of its claim, and that there was no statutory right to credit bid under the circumstances. The panel left open the option of the lender to contest whether it had really received indubitable equivalent value at the plan confirmation stage. Philadelphia Newspapers offers an intriguing alternative to attempt a cramdown of a secured claim through a bankruptcy sale.

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