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Northwestern University Law Review Vol. 107, No. 4

BETTING ON THE UPSIDE: WHY AFFIRMING *RIVER ROAD* FAVORS DISTRESSED DEBT SPECULATORS OVER THE REHABILITATION OF BUSINESSES

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ABSTRACT—The Chapter 11 bankruptcy process demands a careful balance between protecting the creditors' rights to be repaid and allowing a failing entity the ability to restructure. The Supreme Court in *RadLAX Gateway Hotel* affirmed the Seventh Circuit's holding in *River Road* and interpreted the Bankruptcy Code in a way that improperly shifts this balance towards the most senior creditors at the expense of business. This Note will analyze the circuit disagreement over the cramdown provision in the Bankruptcy Code and the Supreme Court's ultimate resolution. It will argue that in light of recent trends in the credit markets—including highly liquid secondary markets for debt and aggressive lenders looking to speculate on restructuring businesses—the Supreme Court's current interpretation of the Bankruptcy Code supports improper policy. It will also argue that consistent interpretation between two provisions in the Bankruptcy Code—§§ 363 and 1129(b), focusing on balancing the needs of debtors to restructure with the rights of creditors to be repaid—suggests that the Supreme Court should have interpreted the cramdown provision to grant more flexibility in plan design. This Note argues that Congress, in light of the *RadLAX* decision, should amend the Bankruptcy Code to better suit the goals of the modern-day bankruptcy.

AUTHOR—J.D., Northwestern University School of Law, 2013. Many thanks to Professor Clinton Francis of Northwestern University School of Law for offering me a window into the practical realities of bankruptcy negotiation, and Jason Cairns of Northwestern University School of Law and the *Northwestern University Law Review* editors for providing invaluable feedback throughout the many drafts of this Note.

INTRODUCTION

In the fast-paced and high-volume world of bankruptcy, a small disagreement in statutory interpretation sealed the fate of billions of dollars of investment capital.[1] In April 2012, the Supreme Court resolved the split between the Third, Fifth, and Seventh Circuits over "[w]hether a debtor may pursue a chapter 11 plan that proposes to sell assets free of liens without allowing the secured creditor to credit bid, but instead providing it with the indubitable equivalent of its claim under Section 1129(b)(2)(A)(iii) of the Bankruptcy Code."[2] The Fifth Circuit in *Bank of New York Trust Co. v. Official Unsecured Creditors' Committee* (*In re The Pacific Lumber Co.*) and the Third Circuit in *In re Philadelphia*

[1] Vincent S.J. Buccola & Ashley C. Keller, *Credit Bidding and the Design of Bankruptcy Auctions*, 18 GEO. MASON L. REV. 99, 100 (2010) (noting that whether secured creditors are entitled to credit bid "likely holds tens of billions of dollars in the balance").

[2] Petition for Writ of Certiorari at i, RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065 (2012) (No. 11-166).

Newspapers, LLC held that a debtor *can* confirm an asset sale plan that restricts credit bidding under the indubitable equivalent standard of subsection (iii),[3] while the Seventh Circuit in *River Road Hotel Partners v. Amalgamated Bank* held that a debtor *cannot* confirm a plan in this manner; rather, any plan that proposes to sell assets free and clear of liens must presumptively permit credit bidding.[4] The Supreme Court affirmed the Seventh Circuit's holding in *River Road*, renamed *RadLAX Gateway Hotel, LLC v. Amalgamated Bank*,[5] in a brief opinion that unnecessarily restricts the cramdown options available to bankruptcy courts and fosters the continued use of aggressive lender strategies.

In re Philadelphia Newspapers and *River Road* are, above all, cases of statutory interpretation.[6] They analyzed § 1129(b)(2)(A) of the Bankruptcy Code, which permits a debtor to confirm a plan over the opposition of secured creditors if: (i) the secured creditors retain their liens on the collateral and receive deferred cash payments equal to the present value of their secured claim; (ii) subject to the secured creditors' right to credit bid, the debtors sell the collateral "free and clear of such liens" and such liens "attach to the proceeds of [the] sale"; or (iii) the plan provides the secured creditors with the indubitable equivalent of their claims.[7] The Third Circuit in *In re Philadelphia Newspapers* concluded that the three subprovisions of § 1129(b) are disjunctive, and that a plan may be confirmed under *any* subprovision,[8] while the Seventh Circuit in *River Road* concluded that what the plan *proposes* to accomplish governs the subprovision under which it must be confirmed.[9]

Focusing on the *impact* of the statutory interpretation will add clarity and context to the debate. The Third and Fifth Circuits held that the proponent of a plan, typically the debtor, may *choose* whether to restrict credit bidding at an auction sale.[10] The Seventh Circuit, on the other hand, enforced a functional classification for the plan: what the plan *proposes* to

[3] *In re* Phila. Newspapers, LLC, 599 F.3d 298, 301 (3d Cir. 2010); Bank of N.Y. Trust Co. v. Official Unsecured Creditors' Comm. (*In re* The Pac. Lumber Co.), 584 F.3d 229, 246 (5th Cir. 2009). Credit bidding is the practice of a creditor bidding at a bankruptcy auction sale of assets in credit up to the value of its claim.

[4] 651 F.3d 642, 652–53 (7th Cir. 2011), *aff'd sub nom.* RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065 (2012).

[5] For the duration of this Note, I will refer to the Seventh Circuit opinion as "*River Road*" and to the Supreme Court opinion as "*RadLAX Gateway Hotel*" or "*RadLAX*."

[6] *See River Rd.*, 651 F.3d at 647; *In re Phila. Newspapers*, 599 F.3d at 304.

[7] 11 U.S.C. § 1129(b)(2)(A) (2006).

[8] 599 F.3d at 305–06, 310.

[9] 651 F.3d at 652.

[10] *In re Phila. Newspapers*, 599 F.3d at 301; Bank of N.Y. Trust Co. v. Official Unsecured Creditors' Comm. (*In re* The Pac. Lumber Co.), 584 F.3d 229, 247 (5th Cir. 2009).

do governs how the plan will be classified.[11] According to the Seventh Circuit, a debtor does not have the choice to prohibit credit bidding for an asset sale plan. Thus, the statutory interpretation of § 1129(b) can be boiled down to proponent choice, on the one hand, and functional classification on the other.

This Note will discuss the Supreme Court's resolution of the circuit split formed by the three key cases. It will first explain how a plan can be crammed down within bankruptcy, highlighting additional procedural requirements incident to confirming a plan under the various subprovisions of § 1129(b). It will continue with a discussion of the three cases that formed this circuit split—*River Road*, *In re Philadelphia Newspapers*, and *In re The Pacific Lumber Co.*—highlighting the differences in their reasoning. It will then discuss the Supreme Court's brief opinion resolving the circuit split.

The Note will continue with an analysis of the recent trends in bankruptcy in which credit bidding is used as a tool to undermine the reorganizational goal of a Chapter 11 proceeding. Granting courts and debtors the choice to restrict credit bidding may offer a remedy to aggressive credit bidding tactics, benefitting debtors and increasing the likelihood of a productive rehabilitation of their businesses. Next, I will discuss the two-step analysis courts must apply in order to confirm a plan under the indubitable equivalent standard of § 1129(b) and show that the Supreme Court's failure to conduct this analysis led it to erroneously interpret the statute. First, I will argue that a plan that proposes to sell assets of the debtor free and clear of liens *may* be confirmed under the indubitable equivalent prong. Second, I maintain that an asset sale plan that restricts credit bidding will provide creditors with the indubitable equivalent of their claim if the creditors are paid, in full, the judicially determined value of their claim. In light of this, I argue that Congress should respond to the Supreme Court's opinion by revising the credit bidding provisions of the Bankruptcy Code.

I. THE CRAMDOWN REQUIREMENTS OF § 1129(B)

Central to the controversy at hand is the meaning of 11 U.S.C. § 1129(b): the cramdown provision of the Bankruptcy Code. This section will briefly discuss the cramdown provision, including its purpose and requirements. Because a full understanding of the cramdown provision requires additional knowledge of a bankruptcy proceeding, the following three subsections will discuss the concepts of indubitable equivalence, valuation, and credit bidding.

[11] *River Rd.*, 651 F.3d at 652.

Debtors choose to file a Chapter 11 reorganization instead of a Chapter 7 liquidation because they wish to continue operating as a reorganized business after the bankruptcy process.[12] In order to allow this outcome, Chapter 11 requires debtors to propose and confirm a plan of reorganization. This plan allows a debtor to restructure its assets, discharge its debts, and continue its operations.[13]

Section 1129 of the Bankruptcy Code provides the minimum requirements for confirming a plan.[14] In the majority of cases, a plan will have the support of all classes of creditors and be confirmed by consent.[15] In order for any plan to be confirmed via consent, the Code requires all impaired[16] classes of creditors to approve the plan.[17] However, if a plan does not have the support of all classes of creditors, § 1129(b) provides the means for a plan to be confirmed despite the objection by a class of creditors (known as a "cramdown").[18] If a proposed plan lacks unanimous support of all classes of impaired creditors, it may still be confirmed against dissenting creditors if "the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that . . . has not accepted[] the plan."[19]

The Code does not add clarity to what is meant by "does not discriminate unfairly." However, after analyzing the legislative history, Kenneth Klee notes: "In a nutshell, if the plan protects the legal rights of a dissenting class in a manner consistent with the treatment of other classes . . . then the plan does not discriminate unfairly with respect to the dissenting class."[20] The Code provides for a plan to be "fair and equitable with respect to a class" of creditors if it includes one of three

[12] *See* 1 COLLIER ON BANKRUPTCY ¶ 1.07[1][a], at 1-25 (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2012); 7 *id.* ¶ 1129.01, at 1129-11.

[13] 7 COLLIER, *supra* note 12, ¶ 1129.01, at 1129-11 to -13.

[14] *See* 11 U.S.C. § 1129(a)(1)–(6) (2006); *In re The Pac. Lumber Co.*, 584 F.3d at 245. See also Kenneth N. Klee, *All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code*, 53 AM. BANKR. L.J. 133, 136–37 (1979) for a summary of these provisions.

[15] Wayne Johnson, *In re* Bonner Mall Partnership*: The Ninth Circuit Embraces the New Value "Exception*,*"* 21 CAL. BANKR. J. 259, 259 n.8 (1993); Klee, *supra* note 14, at 133.

[16] 11 U.S.C. § 1124 defines when a class of claims or interests is unimpaired and, thus, does not have to vote to accept a plan under § 1129. Section 1124(1) dictates that a creditor is unimpaired when the plan "leaves unaltered the legal, equitable, and contractual rights" of the creditor. Under § 1124(2), a plan may also leave creditors unimpaired if it cures defaults, reinstates the maturity of the claim, compensates the holder for any damages, and does not otherwise alter any creditors' rights. *See* 7 COLLIER, *supra* note 12, ¶ 1124.01, at 1124-3. An impaired creditor is one that does not fit the characteristics of § 1124.

[17] § 1129(a)(8).

[18] *Id.* § 1129(b).

[19] *Id.* § 1129(b)(1).

[20] Klee, *supra* note 14, at 142.

requirements.[21] First, the plan may provide for a creditor to retain liens and receive deferred cash payments totaling the present value of the claim as of the date of the plan.[22] Second, the plan may instead provide for a sale of the debtor's assets free and clear of liens, subject to § 363(k) of the Code granting the debtors the presumptive right to credit bid, with the liens attaching to the proceeds of the sale.[23]

The third option dictates that the plan may provide for the creditors to receive the "indubitable equivalent" of their claim.[24] The phrase "indubitable equivalence" was first coined by Judge Learned Hand in *Metropolitan Life Insurance Co. v. Murel Holding Corp.* (*In re Murel Holding Corp.*) as a means of cramming down a plan of reorganization under the prior Bankruptcy Code.[25] This provision allows a bankruptcy court to support alternative means of plan reorganization proposed by the debtor, so long as the creditor receives the benefit of its bargain: the undeniable equivalent of the value of its claim.[26] The legislative history surrounding this subprovision is brief, but provides two examples of what could qualify as indubitable equivalence: abandoning the collateral to the class of creditors, or granting the creditors a replacement lien on similar collateral.[27] In both instances, the creditor is realizing the value of its secured claim.

Central to the circuit split is the nature of these three cramdown subprovisions. The Fifth and Third Circuits held that the three alternatives Congress provided in § 1129(b)(2)(A)(i)–(iii) are nonexclusive requirements.[28] A debtor may satisfy any one of them, or be granted any other reasonable means of "fair and equitable" treatment.[29] However, the Seventh Circuit held that a plan may only be crammed down under the indubitable equivalent standard of subsection (iii) if the plan does not provide for treatment similar to that found in options (i) or (ii).[30] The Supreme Court upheld the Seventh Circuit's logic, affirming that how a plan is structured will dictate under which provision it must be confirmed.[31]

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21 § 1129(b)(2).

22 *Id.* § 1129(b)(2)(A)(i).

23 *Id.* § 1129(b)(2)(A)(ii).

24 *Id.* § 1129(b)(2)(A)(iii).

25 *In re* Phila. Newspapers, LLC, 599 F.3d 298, 310 (3d Cir. 2010); Metro. Life Ins. Co. v. Murel Holding Corp. (*In re* Murel Holding Corp.), 75 F.2d 941, 942 (2d Cir. 1935).

26 *In re Murel Holding Corp.*, 75 F.2d at 942.

27 124 CONG. REC. 32,407 (1978).

28 *In re Phila. Newspapers*, 599 F.3d at 305–06; Bank of N.Y. Trust Co. v. Official Unsecured Creditors' Comm. (*In re* The Pac. Lumber Co.), 584 F.3d 229, 245 (5th Cir. 2009).

29 *In re Phila. Newspapers*, 599 F.3d at 309–10; *In re The Pac. Lumber Co*., 584 F.3d at 245.

30 River Rd. Hotel Partners v. Amalgamated Bank, 651 F.3d 642, 652 (7th Cir. 2011), *aff'd sub nom.* RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065 (2012).

31 *RadLAX*, 132 S. Ct. at 2072–73.

A. The Indubitable Equivalent Standard

An understanding of the cramdown provision of the Bankruptcy Code would be incomplete without a discussion of what the Code means by indubitable equivalence. In order for a plan to be confirmed under subsection (iii) of § 1129(b), the plan must provide for the creditor to realize the "indubitable equivalent" of its claim.[32] The Bankruptcy Code does not define indubitable equivalence, but uses the term in both § 1129(b)—allowing confirmation of a plan over the objection of a class of creditors[33]—and in § 361—providing adequate protection to secured creditors during a Chapter 11 case.[34] The legislative history for § 1129 dictates that "[t]he indubitable equivalent language is intended to follow the strict approach taken by Judge Learned Hand in *In Re Murel Holding Corp*."[35]

In *In re Murel Holding Corp.*, the debtors, who owned a residential apartment building in which Metropolitan Life Insurance Co. held a security interest, proposed a plan of reorganization pursuant to § 77(B) of the former Bankruptcy Code.[36] According to this plan, the debtors would remodel the apartment complex and repay Metropolitan Life Insurance Co. over a ten-year period with the proceeds.[37] Metropolitan Life Insurance Co. refused to consent to this plan and requested that the district court vacate the stay of its foreclosure proceedings against the debtors; however, the district court denied the motion.[38]

On appeal to the Second Circuit, Judge Hand held that the district court was not entitled to grant a stay against foreclosure.[39] Judge Hand reasoned that unwilling creditors could only be forced to accept a plan of reorganization if the plan "provide[d] adequate protection for the realization . . . of the full value of their interest, claims, or liens."[40] Judge Hand then elaborated on what constitutes "adequate protection":

> It is plain that "adequate protection" must be completely compensatory; and that payment ten years hence is not generally the equivalent of payment now. Interest is indeed the common measure of the difference, but a creditor who fears the safety of his principal will scarcely be content with that; he wishes to

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[32] 11 U.S.C. § 1129(b)(2)(A)(iii) (2006).

[33] *Id.* § 1129(b).

[34] *Id.* § 361 (providing a list of potential ways to provide adequate protection when required under §§ 362, 363, or 364).

[35] S. REP. NO. 95-989, at 127 (1978).

[36] Metro. Life Ins. Co. v. Murel Holding Corp. (*In re* Murel Holding Corp.), 75 F.2d 941, 941–42 (2d Cir. 1935).

[37] *Id.* at 942.

[38] *Id.* at 941–42.

[39] *Id.* at 943.

[40] *Id.* at 942.

> get his money or at least the property. We see no reason to suppose that the statute was intended to deprive him of that in the interest of junior holders, unless by a substitute of the most indubitable equivalence.[41]

Importantly, Judge Hand outlined four ways in which a creditor could receive adequate protection: (1) the liens could be maintained; (2) the property could be sold free of the liens with the liens attaching to the proceeds; (3) "[t]he value of the liens" could be appraised and paid by the creditor; or (4) the judge may "equitably and fairly . . . provide such protection, that is, adequate protection, when the other methods are not chosen."[42] These four options for providing adequate protection in the cramdown context still appear in Chapter 11 of the Bankruptcy Code. If a creditor's liens are maintained, the creditor is classified as "unimpaired" and by definition will receive the full value of its bargain. Unimpaired creditors do not need to consent to any plan confirmation.[43] The remaining three options appear as the cramdown provisions in § 1129(b)(2)(A). Selling the property free and clear of liens is codified in § 1129(b)(2)(A)(ii), appraising the value of the liens and having them paid by the creditor is codified in § 1129(b)(2)(A)(i), and Judge Hand's indubitable equivalent standard appears in § 1129(b)(2)(A)(iii).[44] Since Judge Hand's opinion heavily influenced the cramdown provisions in the Bankruptcy Code,[45] the provisions themselves should be understood with *In re Murel Holding Corp.*'s reasoning in mind.

The indubitable equivalent standard Judge Hand established in *In re Murel Holding Corp.* also appears in § 361 of the Bankruptcy Code. Section 361 provides the means a court may use to grant adequate protection to a creditor during the bankruptcy process.[46] During a Chapter 11 proceeding, creditors are prohibited from foreclosing on their collateral without judicial permission, and debtors are permitted to cease all maintenance payments to creditors under a provision called the "automatic stay."[47] Because of this, a creditor may fear its collateral will decline in value over time and petition for relief from the automatic stay in order to remove its collateral.[48] The court must grant the petition if the debtor does

41 *Id.*

42 *Id.* (citing and quoting 11 U.S.C. § 207(b)(5) (1935) (current version at 11 U.S.C. § 1129(b) (2006))) (internal quotation marks omitted).

43 § 1124. *See also supra* note 16 (discussing unimpaired creditors).

44 § 1129(b)(2)(A)(i)–(iii).

45 *See supra* note 35 and accompanying text.

46 § 361.

47 *Id.* § 362(a); *see also* 1 COLLIER, *supra* note 12, ¶ 1.05[1], at 1-19 to -20.

48 3 COLLIER, *supra* note 12, ¶ 362.07, at 362-104 to -105. See also *id.* ¶ 362.08 for a discussion of the procedures for seeking relief from a stay.

not provide adequate protection[49] to ensure that the creditor's property rights in its collateral are not compromised.[50]

Cases addressing whether a creditor is realizing the indubitable equivalent of its claim focus their analysis on Judge Hand's two-prong approach of *value* and *risk*: the plan must adequately compensate the creditor for the current value of its claim—including principal and interest—and for the risk that the principal will not be repaid.[51] Despite this test's stringency, the indubitable equivalent standard gives bankruptcy judges sufficient flexibility to craft reorganization plans to fit the facts and circumstances of a given case.[52]

B. Valuation of a Creditor's Claim

Valuation of a creditor's claim by a bankruptcy court is another essential factor in § 1129 cramdown proceedings. In order for a plan to be confirmed under § 1129(b)(2)(A)(i)(II)—providing for deferred cash payments totaling the present value of the claim—a claim must first be valued.[53] In addition, valuing a claim is necessary to ensure that a creditor receives the indubitable equivalent of its claim under subsection (iii).

Section 1129 requires a secured creditor to be compensated in the "allowed amount" of its claim.[54] Chapter 11 calls for either the bankruptcy trustee[55] or the debtor[56] to file schedules of claims at the commencement of the case. Any filed claim is presumptively allowed unless an interested party objects.[57] If an objection arises, the claim is evaluated both for

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[49] One form of adequate protection granted by courts is periodic cash payments from the debtor to the creditor in order to compensate the creditor for the decline in collateral value during the automatic stay. *Id.* ¶ 362.07[3][b][i]. Other means include requiring the debtor to insure the property and requiring the debtor to pay any taxes on the property. *Id.* ¶ 362.07[3][f], at 362-117.

[50] *Id.* ¶ 362.07[3], at 362-106.

[51] *See* Metro. Life Ins. Co. v. Murel Holding Corp. (*In re* Murel Holding Corp.), 75 F.2d 941, 942–43 (2d Cir. 1935); *see also* Brite v. Sun Country Dev., Inc. (*In re* Sun Country Dev., Inc.), 764 F.2d 406, 409 (5th Cir. 1985) (discussing the value and risk of replacement liens).

[52] *See, e.g.*, *In re Sun Country Dev., Inc.*, 764 F.2d at 409 (finding the indubitable equivalent standard met when the debtor substituted one lien on 200 acres of land for twenty-one separate liens on twenty-one individual lots); Woods v. Pine Mountain, Ltd. (*In re* Pine Mountain, Ltd.), 80 B.R. 171, 174–75 (B.A.P. 9th Cir. 1987) (holding that the indubitable equivalent standard could be satisfied with a subordinated note that provided enough equity cushion on the prime note); *In re* May, 174 B.R. 832, 840 (Bankr. S.D. Ga. 1994) (agreeing to confirm a plan if the debtors amended it to surrender a portion of the creditor's collateral).

[53] 11 U.S.C. § 1129(b)(2)(A)(i)(II) (2006).

[54] *Id.*

[55] *Id.* § 1106(a)(2) (explaining that the duties of a trustee include filing of the schedule of claims "if the debtor has not done so").

[56] *Id.* § 521(a)(1).

[57] *Id.* § 502(a). Any creditor, indenture trustee, or equity security holder may file a proof of claim or interest in the estate. *Id.* § 501(a).

allowance and for valuation as of the date of the petition.[58] This process determines the allowed amount of claim compensation for purposes of § 1129.[59]

The value of a claim may be determined judicially or by sale at auction.[60] In order to establish the dollar value of a claim, the court must determine the current market value of the collateral (if any) securing the loan. A judicial determination of collateral takes place at a hearing, pursuant to § 506(a)(1).[61] Judicially determining the value of a claim can be a very complex process. Section 506(a)(1) directs valuation to be made "in light of the purpose of the valuation and of the proposed disposition or use of such property";[62] however, it does not provide additional guidance. When addressing this flexibility, the Supreme Court in *Associates Commercial Corp. v. Rash* was careful not to prescribe an overly particular valuation standard for the bankruptcy courts, noting that facts and circumstances should govern each individual decision: "Our recognition that the replacement-value standard, not the foreclosure-value standard, governs in cram down cases leaves to bankruptcy courts, as triers of fact, identification of the best way of ascertaining replacement value on the basis of the evidence presented."[63]

A bankruptcy court can also value a claim through an auction sale of the collateral. A debtor may sell its assets with judicial approval outside of the ordinary course of business pursuant to § 363(b), or may sell its assets as part of a plan of reorganization pursuant to § 1129(b)(2)(A)(ii).[64] If the collateral is to be sold during a liquidation sale of the debtor's assets or as a part of a reorganization plan, the value of the collateral should be substantially equivalent to the consideration received by the estate at the

[58] *See id.* § 502(b) (providing that "the court, after notice and a hearing, shall determine the amount of such claim in lawful currency of the United States as of the date of the filing of the petition").

[59] *Id.* This section provides nine reasons why a claim may be disallowed, including claims that are unenforceable, claims for insiders, and claims that were not timely filed. *Id.* All other properly filed claims of creditors will be allowed. These include claims secured by a lien and properly recorded pursuant to the UCC (for example, a mortgage or lien on inventory or other property); unsecured claims that are protected by statute (for example, labor wage claims, claims for retirement benefits, or claims for payment for services); or any other claims to ownership of the business (for example, bondholders or shareholders).

[60] River Rd. Hotel Partners v. Amalgamated Bank, 651 F.3d 642, 650 (7th Cir. 2011), *aff'd sub nom.* RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065 (2012).

[61] § 506(a)(1); *see also* 4 COLLIER, *supra* note 12, ¶ 506.03[4][a], at 506-22 to -23.

[62] § 506(a)(1).

[63] 520 U.S. 953, 965 n.6 (1997).

[64] § 363(b)(1) ("The trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate . . . ."); *id.* § 1129(b)(2)(A)(ii) ("[The plan provides] for the sale, subject to section 363(k) of this title, of any property that is subject to the liens securing such claims, free and clear of such liens . . . .").

sale.[65] Many bankruptcy courts have noted that as long as the sale conditions are fair, and the transaction took place at arm's length, the consideration received through a sale is a better indicator of collateral value than an appraiser's estimate.[66]

Secured claims that are allowed by the bankruptcy court receive special attention by the Code. Oversecured claims—claims in which the face value of the claim is less than the current market value of the collateral—are allowed to the full amount of the debt.[67] On the other hand, undersecured claims—where the claim's face value is greater than the current market value of the collateral—are bifurcated.[68] These claims are divided into a secured claim to the extent of the current market value of the collateral securing the claim and an unsecured claim for the balance.[69]

A creditor may avoid the bifurcation process of § 506(a) by election and treat the entire face value of its claim as secured under § 1111(b)(2).[70] A creditor may not make a § 1111(b) election if its interest in the collateral is of "inconsequential value," or if the creditor "has recourse against the debtor" and the collateral is to be sold pursuant to § 363 or under a plan of reorganization.[71] This election is attractive to creditors who are retaining liens on the collateral through reorganization and believe both that their collateral is undervalued and that the debtor is likely to reenter bankruptcy before satisfying the creditor's claim.[72] The risk of a restructured entity filing for bankruptcy again is substantial, occurring between 25% and 33%

65 4 COLLIER, *supra* note 12, ¶ 506.03[6][b], at 506-37.

66 Romley v. Sun Nat'l Bank (*In re* The Two "S" Corp.), 875 F.2d 240, 244 (9th Cir. 1989) ("Evidence of other appraised values is also irrelevant, because the sale price is a better indicator of the asset's value than any estimate of value given prior to sale."). *See also* Takisaki v. Alpine Grp., Inc. (*In re* Alpine Grp., Inc.), 151 B.R. 931, 935 (B.A.P. 9th Cir. 1993) ("The offered price . . . is conclusive evidence of the property's value."). Conversely, evidence of value obtained by an offer to purchase the collateral may not be persuasive if the terms of the offer are not acceptable to the debtor and the offer is rejected. *See In re* Smith, 42 B.R. 198, 200 (Bankr. N.D. Ga. 1984).

67 § 506(a)(1) ("An allowed claim of a creditor secured by a lien on property in which the estate has an interest . . . is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property . . . ."). The Code defines the concept of "collateral" as the "creditor's interest in the estate's interest in such property." *Id.* The Supreme Court has confirmed that this phrase should be interpreted as the common notion of "collateral." United Sav. Ass'n of Tex. v. Timbers of Inwood Forest Assocs., Ltd., 484 U.S. 365, 372 (1988).

68 4 COLLIER, *supra* note 12, ¶ 506.03[4], at 506-20.

69 § 506(a)(1); *see also* 4 COLLIER, *supra* note 12, ¶ 506.03[4], at 506-20 & n.57.

70 *See, e.g.*, *In re* River E. Plaza, LLC, 669 F.3d 826, 829, 831, 833 (7th Cir. 2012); 680 Fifth Ave. Assocs. v. Mut. Benefit Life Ins. Co. in Rehab. (*In re* 680 Fifth Ave. Assocs.), 29 F.3d 95, 97 (2d Cir. 1994) ("Section 1111(b) allows an undersecured creditor either to elect to have its entire claim treated as secured, or to have the claim bifurcated into secured and unsecured portions, notwithstanding the fact that under 11 U.S.C. § 502(b)(1), the nonrecourse nature of the loan would otherwise bar a deficiency claim for the unsecured portion of the loan.").

71 § 1111(b)(1)(B).

72 *In re River E. Plaza*, 669 F.3d at 830.

of the time.[73] By making this election, a creditor foregoes the right to an immediate payment of the secured claim in exchange for maintaining a lien over the property, with the expectation that it will either be paid by the debtor over time or yield greater proceeds from a later foreclosure sale of the recovered collateral.[74]

C. Credit Bidding During a Sale of Assets Free and Clear of Liens

The final critical topic for understanding § 1129 cramdown proceedings is the credit bidding process. In order for a plan to be confirmed under § 1129(b)(ii), a sale of the debtor's assets must be conducted subject to § 363(k).[75] Section 363(k) permits a creditor with an allowed claim to bid for the debtor's assets at auction and, "unless the court for cause orders otherwise," to offset the value of its lien "against the purchase price of [the] property."[76] This practice is commonly referred to as "credit bidding," and was recognized under bankruptcy law prior to the current Code.[77] In practice, credit bidding authorizes a creditor with an allowed claim[78] to bid on credit at an auction sale up to the full face value of its claim.[79] This is true even if the creditor's claim is

[73] *Id.*; *see also* Stuart C. Gilson, *Transactions Costs and Capital Structure Choice: Evidence from Financially Distressed Firms*, 52 J. FIN. 161, 162 (1997); Edith Shwalb Hotchkiss, *Postbankruptcy Performance and Management Turnover*, 50 J. FIN. 3, 15 (1995); Lynn M. LoPucki & William C. Whitford, *Patterns in the Bankruptcy Reorganization of Large, Publicly Held Companies*, 78 CORNELL L. REV. 597, 608 (1993); Harvey R. Miller & Shai Y. Waisman, *Does Chapter 11 Reorganization Remain a Viable Option for Distressed Businesses for the Twenty-First Century?*, 78 AM. BANKR. L.J. 153, 188 (2004).

[74] *In re River E. Plaza*, 669 F.3d at 830. In order to better illustrate this provision, imagine a lender holds a $100 million secured interest in a piece of property, the value of which has declined to $50 million. Traditional bifurcation would allow for a $50 million secured loan that would receive priority repayment in the plan, and a $50 million unsecured claim that in most cases is unlikely to be repaid. If the lender would prefer to terminate its relationship with the debtor, is not confident that the company will survive reorganization, or is concerned that the collateral will continue to decrease in value, it might prefer to take the current value in bifurcation. However, if the lender believes that the value of the property will increase or that the debtor will be capable of making payments once reorganized, the creditor may prefer to make a § 1111(b) election and retain a secured lien for the original $100 million value. The creditor could then negotiate structured payments over a period of time (for example, five years) in order to repay the $100 million loan.

[75] § 1129(b)(2)(A)(ii).

[76] *Id.* § 363(k).

[77] *See, e.g.*, Morgan v. Blieden (*In re* Mun. Gas Co.), 107 F.2d 133, 134 (8th Cir. 1939); Miners Sav. Bank of Pittston, Pa. v. Joyce, 97 F.2d 973, 975 (3d Cir. 1938).

[78] *See* Nat'l Bank of Commerce of El Dorado v. McMullan (*In re* McMullan), 196 B.R. 818, 835 (Bankr. W.D. Ark. 1996) (holding that a creditor may not bid on a lien that has not yet been determined to be valid).

[79] 3 COLLIER, *supra* note 12, ¶ 363.09, at 363-79. *See also* 4 *id.* ¶ 506.02, at 506-8 to -9 (summarizing provisions within the Bankruptcy Code that protect the holders of secured claims).

undersecured—meaning the present market value of the collateral securing the claim is less than the face value of the claim.[80]

To illustrate this concept by example, suppose Debtor borrowed $100 million from Creditor secured by Debtor's rental apartment complex. Later, when the apartment complex is only worth $50 million, Debtor files for bankruptcy. In the plan of reorganization, Debtor wishes to sell the apartment complex at auction and use the proceeds to pay Creditor's claim. At the auction, Creditor may "bid" up to $100 million—the face value of Creditor's claim. Because the apartment complex has a current market value of $50 million, Creditor may easily become the highest bidder at auction without using any additional cash.

A bankruptcy auction determines the market value of the collateral—the value of the *secured* claim—but a creditor's claim may be bifurcated into a secured portion and an unsecured portion. If Creditor with a $100 million face-value claim bids $50 million on the property (the current market value) and wins, Creditor still retains an *unsecured* $50 million claim on the estate for the difference. If, however, it takes an $80 million credit bid to guarantee a win at auction, Creditor only retains a $20 million unsecured claim against the estate. This is of little import, however, as unsecured claims are rarely paid, and when they are it is for mere pennies on the dollar.[81] To a creditor, the value of its claim is the value of the *secured* portion of its claim.

The presumptive right to credit bid provides many advantages to creditors. It is often seen as a check against low valuation of collateral at an auction sale.[82] Alternatively, some view credit bidding as granting secured lenders the right to ensure collateral is not sold at a value below a price to which they would consent.[83] Most importantly, if a lender cannot obtain the requisite cash to bid in an auction, credit bidding may be the only way a lender is able to attend. One of the best ways to increase the amount realized at auction is to increase the quantity of interested bidders.[84] Credit bidding may be a double-edged sword, however, as debtors frequently

[80] *See, e.g.*, Cohen v. KB Mezzanine Fund II, LP (*In re* SubMicron Sys. Corp.), 432 F.3d 448, 460–61 (3d Cir. 2006) (holding that a creditor's bid sets the creditor's allowed secured claim under 11 U.S.C. § 506(a)); *In re* Morgan House Gen. P'ship, 1997 U.S. Dist. LEXIS 1306, at *3 (E.D. Pa. Feb. 7, 1997); *In re* Realty Invs., Ltd., 72 B.R. 143, 146 (Bankr. C.D. Cal. 1987); S. REP. NO. 95-989, at 56 (1978) ("No prior valuation under section 506(a) would limit this bidding right, since the bid at the sale would be determinative of value.").

[81] Douglas Baird et al., *The Dynamics of Large and Small Chapter 11 Cases: An Empirical Study* 19, 21–23 (Yale Int'l Ctr. for Fin., Working Paper No. 05-29, 2007), *available at* http://ssrn.com/abstract=866865.

[82] *In re* Phila. Newspapers, LLC, 599 F.3d 298, 334 (3d Cir. 2010) (Ambro, J., dissenting).

[83] *Id.*

[84] *See* Buccola & Keller, *supra* note 1, at 119–20 (discussing the dynamics of a bankruptcy auction and the impact of credit bidding).

argue that credit bidding "chill[s]" auctions.[85] When prospective bidders find themselves in competition with a credit bidder who has resources far in excess of the current market value of the assets, the prospective bidders may deem the cost of entering the auction not worth the substantial likelihood of being outbid.[86]

II. THE CIRCUIT SPLIT

The Supreme Court has recently resolved the split between the circuits on the means by which a plan can be confirmed under § 1129 of the Bankruptcy Code.[87] The Seventh Circuit mandated a functional classification of a plan in which the debtor may not restrict credit bidding during an asset sale. It held that a plan that proposes to sell substantially all of the debtor's assets free of liens may not be confirmed under the indubitable equivalent standard of § 1129(b)(2)(A)(iii) without granting the creditors the right to credit bid.[88] The Fifth Circuit and Third Circuit granted the debtor the choice of restricting credit bidding during an asset sale. They maintained that a plan that proposes to sell the debtor's assets may be confirmed under the indubitable equivalent standard without credit bidding if the plan ensures the creditors will receive the indubitable equivalent of their claim.[89] The Supreme Court in *RadLAX Gateway Hotel* affirmed the Seventh Circuit, holding that a plan that proposes to sell assets free and clear of liens *must* be crammed down under subprovision (ii) and presumptively permit credit bidding.[90] This section will discuss the cases that formed this split and how the judges involved are simultaneously trying to adhere to the true meaning of § 1129(b), as well as provide guidance that agrees with the commercial realities of a bankruptcy proceeding.

A. In re The Pacific Lumber Co.

In re The Pacific Lumber Co.[91] was the first case to hold that a plan could be confirmed under § 1129 as fair and equitable with respect to a

[85] Adam D. Marshall, *Shifting Strategies for Secured Creditors: Credit Bidding as a Continuing Strategic Option in Chapter 11 Cases*, ASPATORE (Jan. 2011), 2011 WL 190431, at *3; *see also* Daniel P. Winikka & Debra K. Simpson, *Will Bankruptcy Courts Limit the Right to Credit Bid?*, 17 NORTON J. BANKR. L. & PRAC. 921, 924 (2008).

[86] For further discussion on courts' responses to the argument that credit bidding chills auctions, and for a real case example demonstrating the chilling phenomenon, see *infra* Part III.A.

[87] RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065, 2072 (2012), *aff'g* River Rd. Hotel Partners v. Amalgamated Bank, 651 F.3d 642 (7th Cir. 2011).

[88] *River Rd.*, 651 F.3d at 651.

[89] *In re* Phila. Newspapers, LLC, 599 F.3d 298, 311 (3d Cir. 2010); Bank of N.Y. Trust Co. v. Official Unsecured Creditors' Comm. (*In re* The Pac. Lumber Co.), 584 F.3d 229, 247 (5th Cir. 2009).

[90] *RadLAX*, 132 S. Ct. at 2073.

[91] 584 F.3d at 247, 249.

dissenting class of creditors even if a sale of the creditor's collateral did not afford the opportunity to credit bid. This Chapter 11 proceeding concerned a plan to restructure six affiliated entities all involved in the timber business in California.[92] After the restructuring, the principal creditor and a key competitor would pay $580 million to satisfy the other creditors and would own all of the assets of the business.[93] All but two classes of creditors approved the plan.[94]

To confirm the plan, the bankruptcy court proceeded to "cram down" the plan on the dissenting creditors in accordance with § 1129(b).[95] Proving that the plan was fair and equitable required the court to value the assets securing their claim. The bankruptcy court conducted a judicial valuation, hearing "extensive valuation testimony over several days," and concluded the assets were worth "not more than $510 million."[96] The bankruptcy court held that the valuation of $510 million in cash was the "indubitable equivalent" of the creditors' secured claim according to § 1129(b).[97]

The creditors appealed the bankruptcy court's decision to the Fifth Circuit, challenging that the plan was "not 'fair and equitable' because the plan sold the [assets] without providing the [creditors] a right to credit bid."[98] The creditors contended that since the plan proposed to sell the assets, the plan must conform with the requirements of § 1129(b)(2)(A)(ii), granting the creditors the right to credit bid pursuant to § 363(k).[99] The creditors insisted that the ability to credit bid would protect them against what they perceived to be an undervaluation of their collateral.[100]

In response, the Fifth Circuit reasoned that a reorganization plan may be fair and equitable to a class of dissenting creditors if it provides the creditors with the "indubitable equivalent" of their claim by any means.[101] The court first determined the asset transfer was a sale, but held that "because the three subsections of § 1129(b)(2)(A) are joined by the disjunctive 'or,' they are alternatives," and thus compliance with any one of the subsections may permit a finding of "fair and equitable."[102] The court also noted that the word "includes" in § 1129(b)(2) shows that the three alternatives proposed for plan confirmation are not exhaustive and

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92 *Id.* at 236–37.
93 *Id.*
94 *Id.* at 238.
95 *Id.*
96 *Id.*
97 *Id.*
98 *Id.* at 239.
99 *Id.* at 245.
100 *Id.* at 244.
101 *Id.* at 246.
102 *Id.* at 245.

reiterated that "[e]ven a plan compliant with these alternative minimum standards is not necessarily fair and equitable."[103] The court concluded that confirming an asset sale under indubitable equivalence does not render options (i) and (ii) superfluous as the standard of indubitable equivalence is "no less demanding a standard than its companions."[104] The Fifth Circuit scrutinized the valuation proceedings and determined they were not clearly erroneous and represented a fair value of the creditor's secured claim.[105] Thus, according to the Fifth Circuit, § 1129 does not require the opportunity to credit bid.

B. In re Philadelphia Newspapers, LLC

The Third Circuit was the next to confront this issue in *In re Philadelphia Newspapers, LLC*.[106] This case presented a similar situation in which a proposed plan for the sale of assets free and clear of liens prohibited the creditors from credit bidding at auction.[107] Unlike *In re The Pacific Lumber Co.*, this plan proposed that the value of the debtors' assets be determined at the auction sale, rather than via a judicial process.[108]

Philadelphia Newspapers, LLC, a publishing company, filed for Chapter 11 protection after defaulting on a $318 million loan secured by substantially all of its assets.[109] The debtors proposed a reorganization plan whereby their assets would be sold free of liens at an all-cash public auction, precluding the creditors from credit bidding.[110] As proposed, the plan would generate "$37 million in cash for the [l]enders," plus the lenders would receive a property "valued at $29.5 million, subject to a two-year rent free lease."[111] If additional cash were raised at the auction, the lenders would receive these proceeds.[112]

The lenders objected to the bid procedures, prompting the bankruptcy court to issue an order refusing to restrict credit bidding at the auction.[113] The bankruptcy court reasoned that although the plan was proceeding under the § 1129(b)(2)(A)(iii) option of plan confirmation—the indubitable equivalent prong—the plan was structured as a sale free and clear of liens under § 1129(b)(2)(A)(ii) in every way except for the prohibition on credit

103 *Id.*
104 *Id.* at 246.
105 *Id.* at 248–49.
106 599 F.3d 298, 301 (3d Cir. 2010).
107 *Id.*
108 *Id.*
109 *Id.*
110 *Id.* at 302.
111 *Id.*
112 *Id.*
113 *Id.*

bidding.[114] According to the court, structuring the plan as a sale free and clear of liens required it to proceed under § 1129(b)(2)(A)(ii).[115] The bankruptcy court then modified the plan to permit credit bidding and the debtors appealed to the district court, which reversed.[116]

On appeal, the Third Circuit affirmed the district court, holding that § 1129(b) permits a bankruptcy court to confirm a plan so long as the creditor will receive the "indubitable equivalent" of its claim.[117] The Third Circuit opined that the plain meaning of § 1129(b) is unambiguous, and as a result the court must follow the statute's language.[118] The statute purposefully employs the word "or," which is defined in § 102(5) of the Code.[119] The Code defines "or" as nonexclusive, and a statutory note dictates that "if a party 'may do (a) or (b)', then the party may do either or both."[120] "The party is not limited to a mutually exclusive choice between the two alternatives."[121]

The Third Circuit further concluded that the specific method of confirming a plan in § 1129(b)(2)(A)(ii) does not operate to limit the broader language of (iii), and thus the canon of construction that the "specific governs the general" is not applicable.[122] Unlike *In re The Pacific Lumber Co.*, the Third Circuit did not analyze whether the debtors' proposed plan satisfied indubitable equivalence, but merely said that a plan proposing to sell collateral free and clear of liens at an all-cash auction *could* satisfy the indubitable equivalent standard.[123] The *In re Philadelphia Newspapers* debtors proceeded with their plan of an all-cash auction and yielded a significant financial benefit from restricting credit bidding.[124]

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114 *Id.*

115 *Id.*

116 *Id.*

117 *Id.* at 304.

118 *Id.* at 305.

119 *Id.*

120 *Id.*

121 *Id.*

122 *Id.* at 307–08. The Supreme Court in *RadLAX Gateway Hotel* described how this canon would apply to § 1129(b):

> [T]he [general/specific] canon has full application . . . to statutes such as the one here, in which a general authorization and a more limited, specific authorization exist side-by-side. . . . Here, clause (ii) is a detailed provision that spells out the requirements for selling collateral free of liens, while clause (iii) is a broadly worded provision that says nothing about such a sale. The general/specific canon explains that the general language of clause (iii), although broad enough to include it, will not be held to apply to a matter specifically dealt with in clause (ii).

RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065, 2071–72 (2012) (internal quotation marks omitted), *aff'g* River Rd. Hotel Partners v. Amalgamated Bank, 651 F.3d 642 (7th Cir. 2011).

123 *In re Phila. Newspapers*, 599 F.3d at 312–13.

124 *See infra* Part III.A.

C. In re Philadelphia Newspapers *Dissent by Judge Ambro*

The majority opinion in *In re Philadelphia Newspapers, LLC* sparked a thorough dissent by Judge Ambro, who argued that § 1129(b) is an ambiguous statute necessitating an analysis of legislative history, statutory context, and additional canons of statutory construction to choose between two plausible interpretations.[125] Judge Ambro first rejected the majority's conclusion that § 102(5) of the Bankruptcy Code defining "or" as "not exclusive" means that the three subprovisions within § 1129 must be nonexclusive.[126] He cited to additional provisions of the Code—including §§ 365(g)(2)(B)(i)–(ii), 506(d)(1)–(2), and 1112(b)(1)—where "or" is interpreted to provide exclusive limitations.[127] From this, Judge Ambro concluded that the operative word in § 1129 is "provides," not "includes," as the majority suggested.[128]

With emphasis on "provides" and a reading of "or" as exclusive, Judge Ambro reasoned that "Congress did not list the three alternatives as routes to cramdown confirmation that were universally applicable to any plan, but instead as distinct routes that apply specific requirements depending on how a given plan proposes to treat the claims of secured creditors."[129] Under this plausible reading of the statute, if a plan provides for a creditor to retain liens on transferred property, it must follow clause (i). Similarly, if the plan sells the property free and clear of liens, it must follow clause (ii). And finally, only if the plan provides for something else not governed by

[125] 599 F.3d at 319 (Ambro, J., dissenting).

[126] *Id.* at 324.

[127] *Id. See also* Williams v. Tower Loan of Miss., Inc. (*In re* Williams), 168 F.3d 845, 847–48 (5th Cir. 1999) (holding that § 1325(a)(5)(B) and (C) required an exclusive "or" construction to avoid creating an option that Congress did not intend to create); 2 COLLIER, *supra* note 12, ¶ 102.06, at 102–16 & n.1 (noting that reading "or" nonexclusively is only appropriate "if context and practicality allow" and calling attention to § 1112(b) as an instance where "[i]t would be impossible for the court to do both" of the statute's alternatives).

[128] *In re Phila. Newspapers*, 599 F.3d at 324–25 (Ambro, J., dissenting). The text of § 1129(b)(2)(A) reads:

> With respect to a class of secured claims, the plan provides—
>
> (i)(I) that the holders of such claims retain the liens securing such claims, whether the property subject to such liens is retained by the debtor or transferred to another entity, to the extent of the allowed amount of such claims; and
>
> (II) that each holder of a claim of such class receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property;
>
> (ii) for the sale, subject to section 363(k) of this title, of any property that is subject to the liens securing such claims, free and clear of such liens, with such liens to attach to the proceeds of such sale, and the treatment of such liens on proceeds under clause (i) or (iii) of this subparagraph; or
>
> (iii) for the realization by such holders of the indubitable equivalent of such claims.

11 U.S.C. § 1129(b)(2)(A) (2006).

[129] *In re Phila. Newspapers*, 599 F.3d at 325 (Ambro, J., dissenting) (footnote omitted).

either clause (i) or (ii) may it follow the indubitable equivalent standard of clause (iii).[130] Judge Ambro concluded that since the debtors' plan proposes to sell the collateral free and clear of liens, it must follow clause (ii) and presumptively permit the creditors to credit bid up to the full value of their claim at auction.[131] He then analyzed the credit bidding right of § 1129 in conjunction with §§ 1111(b)[132] and 363(k)[133] to conclude that these sections are "part of a comprehensive arrangement enacted by Congress to avoid the pitfalls of undervaluation, regardless of the mechanism chosen."[134] Judge Ambro closed by analyzing the practical impact of failing to allow secured parties to credit bid when they rely upon it. He opined that it would likely raise the cost of capital as creditors must account for the likelihood of undervaluation.[135]

D. River Road Hotel Partners

The most recent circuit to weigh in on the credit bidding debate was the Seventh Circuit in *River Road Hotel Partners v. Amalgamated Bank*.[136] The debtors in this case were in the business of constructing airport hotels and had voluntarily filed for Chapter 11 protection after construction costs greatly exceeded their expectations.[137] The debtors filed a reorganization plan that proposed to sell substantially all of their assets without permitting the creditors to credit bid and without having the bankruptcy court judicially value the assets in advance of the sale.[138] The lead creditor objected to this plan, forcing the debtors to request confirmation under prong (iii) of § 1129(b)(2)(A).[139] The bankruptcy court refused to confirm the plan without granting the creditors the right to credit bid, citing Judge Ambro's dissent in *In re Philadelphia Newspapers*, and the debtors appealed the case directly to the Seventh Circuit.[140]

The Seventh Circuit, affirming the bankruptcy court, reasoned that "there are two plausible interpretations of the" plain language of § 1129(b)(2)(A) and the ambiguity required an analysis of canons of

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130 *Id.* at 326–27.

131 *Id.* at 330–33.

132 11 U.S.C. § 1111(b) allows an undersecured, nonrecourse creditor to elect secured recourse treatment unless its collateral is sold through § 363(k) or pursuant to a plan. *See supra* Part I.B.

133 11 U.S.C. § 363(k) grants a presumptive right to credit bid when assets are sold outside of the ordinary course of business.

134 *In re Phila. Newspapers*, 599 F.3d at 334 (Ambro, J., dissenting).

135 *Id.* at 337.

136 651 F.3d 642 (7th Cir. 2011), *aff'd sub nom.* RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065 (2012).

137 *Id.* at 643–44.

138 *Id.* at 645.

139 *Id.*

140 *Id.* at 645, 647.

construction and statutory context to choose the more plausible option.[141] It found Judge Ambro's statutory analysis in *In re Philadelphia Newspapers* compelling, and also pointed out an inconsistency that would arise between methods of valuation supported by the Code if the debtors' argument were followed.[142] The court noted that the Code "recognizes two basic mechanisms for solving these types of valuation problems: judicial valuation of an asset's value, 11 U.S.C. § 506(a)(1), and free market valuation of an asset's value as established in an open auction, 11 U.S.C. §§ 363(k), 1129(b)(2)(A)."[143] The court reasoned that because both §§ 363(k) and 1129(b)(2)(A)(ii) contain a presumptive right to credit bid when collateral value is determined at an open auction, any sale of collateral in which the value is to be determined at auction should presumptively include a right to credit bid.[144] To hold that creditors *have* the right to credit bid during an auction sale of assets under § 363(k) but *do not have* the right to credit bid during an auction sale under § 1129(b)(2)(A) would create inconsistency within the Bankruptcy Code.[145]

Based on this analysis, the Seventh Circuit became the first circuit to hold that a § 1129 plan that proposes to sell "encumbered assets free and clear of liens at an auction [must] satisfy the requirements set forth in Subsection (ii) of the statute."[146] This holding conflicts with the Third Circuit in *In re Philadelphia Newspapers*; however, it is potentially reconcilable with the Fifth Circuit in *In re The Pacific Lumber Co*. As the Seventh Circuit noted, there are *two* ways to determine collateral value during a bankruptcy proceeding: (1) judicial valuation or (2) valuation by auction.[147] In *In re The Pacific Lumber Co.*, the collateral's value was determined judicially, and thus the judge verified indubitable equivalence in advance of plan confirmation.[148]

E. RadLAX Gateway Hotel, LLC v. Amalgamated Bank

The Supreme Court in *RadLAX Gateway Hotel* resolved the circuit split and affirmed the Seventh Circuit in a brief opinion by Justice Scalia.[149] Without justification, the Court deemed the text of § 1129(b)(2)(A)

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[141] *Id.* at 643, 649–51.
[142] *Id.* at 649–50.
[143] *Id.* at 650.
[144] *Id.*
[145] *Id.*
[146] *Id.* at 653.
[147] *Id.* at 650.
[148] *See supra* text accompanying notes 96–97.
[149] RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065, 2068, 2073 (2012), *aff'g* River Rd. Hotel Partners v. Amalgamated Bank, 651 F.3d 642 (7th Cir. 2011).

unambiguous[150] and yet called the debtor's interpretation—permitting a plan to satisfy any subsection per the use of the disjunctive "or"—"hyperliteral and contrary to common sense."[151] In the Supreme Court's "unambiguous" reading, what the plan proposes to do governs the provision under which it must be confirmed.[152] The Court asserted that "[a]s a matter of law, no bid procedures like the ones proposed here [an auction sale free and clear of liens without credit bidding] *could* satisfy the requirements of § 1129(b)(2)(A)."[153] The Court concluded this by resorting to a common canon of statutory construction: "the specific governs the general."[154] Curiously, however, the Court did not analyze additional textual indications,[155] and deemed analyzing the general statutory purpose or pre-Code practices as appropriate only if the text were ambiguous.[156]

The Supreme Court did not explain why it employed a canon of statutory construction if the text is unambiguous, nor did it explain why the interpretation might be swayed by textual indications[157] but not by analyzing the general statutory purpose or pre-Code practices.[158] The Court concluded by asserting that the merits of credit bidding, argued extensively by the parties and on both sides of the circuit split, "are for the consideration of Congress, not the courts."[159] Unfortunately, in doing so the Court unnecessarily limited the cramdown options available to the bankruptcy courts, essentially doing away with an alternative method of plan valuation and fostering aggressive lending strategies harmful to the rehabilitation of businesses. The impact of the *RadLAX* decision on businesses will be explored more fully in the remainder of this Note.

III. RESTRICTING CREDIT BIDDING IS AN EFFECTIVE TOOL TO COMBAT AGGRESSIVE LENDER STRATEGIES

Contrary to the Supreme Court's holding to require credit bidding, granting debtors and courts the *choice* to prohibit credit bidding would permit needed flexibility in a Chapter 11 proceeding. Even if judicial valuation *can* satisfy the indubitable equivalent standard, *should* courts

150 *Id.* at 2073.

151 *Id.* at 2070.

152 *Id.* at 2073.

153 *Id.*

154 *Id.* at 2071 (quoting Morales v. Trans World Airlines, Inc., 504 U.S. 374, 384 (1992)).

155 *Id.* at 2072. The Supreme Court did not define the phrase "textual indications," but the opinion suggests that the Court used this phrase to refer to an analysis of statutory context in order to shine light on statutory meaning.

156 *Id.* at 2073.

157 *See id.* at 2072.

158 *See id.* at 2073.

159 *Id.*

restrict credit bidding? The Supreme Court declined to discuss this policy, noting, "the pros and cons of credit-bidding are for the consideration of Congress, not the courts."[160] In so doing, the Supreme Court missed an opportunity to curtail an abusive bankruptcy practice that is currently stifling the rehabilitation of businesses.[161]

To illustrate how credit bidding chills auctions and how opportunistic investors influence the bankruptcy process, we will revisit our earlier example of a $100 million loan secured by a $50 million apartment complex.[162] Debtor hosts an auction sale of the apartment complex in order to pay back Creditor; however, Creditor has already sold its debt on the secondary market to Hedge Fund for $30 million. Hedge Fund desires to own and manage the apartment complex, believing that it will ultimately generate a profit from the enterprise. Debtor tries to recruit Bidder to enter the auction to bid for the apartment complex; however, Bidder knows from the early stages of his due diligence that Hedge Fund has a credit bid of $100 million and believes Hedge Fund desires to own the assets. Bidder is unwilling to spend additional money to investigate the potential apartment complex enterprise because Bidder assumes that he will be outbid by Hedge Fund's credit bid. As a result, Bidder and many other potential bidders never enter the auction, making Hedge Fund likely to win with a credit bid. Since Hedge Fund's bid establishes the "value" of the most senior lender's claim (the loan it purchased for $30 million), all of the junior lenders and creditors will yield nothing from the sale.

In recent bankruptcy auctions, lenders are using credit bidding as an *offensive* tool for strategic investors who wish to own the bankrupt entity with the goal of making a profit in the long term.[163] These investors buy discounted debt on the secondary market—they purchase debt from the original credit holders for less than the face value of the repayment obligation—and credit bid up to the full value of the debt to purchase the assets of the company. Investors using such tactics take advantage of the current depression in asset value and bet on the upside potential of an entity.[164] Giving debtors the choice to pursue judicial valuation can help to remedy this problem.

160 *Id.*

161 *See supra* note 85 and accompanying text. For a comprehensive discussion of the arguments *for* credit bidding, see Buccola & Keller, *supra* note 1, at 117–22.

162 *See supra* Part I.C.

163 *See* Amy L. Kyle, *Recent Trends in Asset Sales Under the Bankruptcy Code*, *in* TRENDS IN COMMERCIAL BANKRUPTCY FILINGS 55, 58 (2010), *available at* 2010 WL 3650163, at *2.

164 *See id.*

A. The In re Philadelphia Newspapers *Auction*

Despite debtors' continued insistence,[165] courts have been somewhat unresponsive to the argument that credit bidding chills auctions. Judge Ambro famously wrote in *In re Philadelphia Newspapers*: "Although some may argue that credit bidding chills cash bidding, that argument underwhelms; credit bidding chills cash bidding no more than a deep-pocketed cash bidder would chill less-well-capitalized cash bidders."[166] While Judge Ambro may have been underwhelmed by the argument, the financial results of the *In re Philadelphia Newspapers* asset sale presented a unique case study of how credit bidding can, and did, chill an auction proceeding.

The original *In re Philadelphia Newspapers* plan proposed to restrict credit bidding and conduct an all-cash auction. The bankruptcy court denied this plan.[167] Based on the bankruptcy court's ruling, the initial prospective bidders assumed credit bidding would be permitted at auction. There were seven total parties interested in bidding during this time.[168]

After the district court reversed the bankruptcy court and confirmed the all-cash auction plan, the number of interested parties jumped to fourteen,[169] and then rose again to twenty-nine in the weeks before the Third Circuit rendered its opinion affirming the district court.[170] No longer faced with the threat of a $300 million credit bid, the market responded to an all-cash auction by showing a four-fold increase in the number of bidders.[171] The original *In re Philadelphia Newspapers* lenders won the auction with a cash bid of $139 million.[172] This equated to "thirty-three cents on the dollar," a remarkable sum considering the senior debt was trading in the secondary market for "twenty cents on the dollar" for much of the duration of the bankruptcy case.[173]

Restricting credit bidding in the *In re Philadelphia Newspapers* asset sale fostered a more active and more competitive auction environment, supporting the argument that a $300 million credit bid had dissuaded bidders. The all-cash auction caused more bidders to enter with more aggressive bids.[174] The final auction price was higher than anticipated

165 *See* Marshall, *supra* note 85; Winikka & Simpson, *supra* note 85.

166 *In re* Phila. Newspapers, LLC, 599 F.3d 298, 321 (3d Cir. 2010) (Ambro, J., dissenting).

167 *Id.* at 301–02 (majority opinion).

168 Lawrence G. McMichael et al., *Quick Sales and Credit Bids* (ABI 6th Annual Mid-Atlantic Bankruptcy Workshop, Aug. 5–7, 2010), WL 080510 ABI-CLE 285.

169 *Id.*

170 *Id.*

171 *See id.*

172 *Id.*

173 *Id.*

174 *Id.*

during the pendency of the bankruptcy case.[175] Had a third party won the auction, the cash value received by the creditors would have likely supported a finding of indubitable equivalence.[176]

B. Restricting Speculative Credit Bidding Promotes Effective Debtor Rehabilitation

The recent economic downturn has fostered a Chapter 11 environment that is witnessing an increase in aggressive credit bidding strategies.[177] The secondary market for secured debt is trading at highly discounted values,[178] and the purchasers of this debt believe they can influence the bankruptcy process to derive a profit from these claims.[179] Additionally, the unavailability of capital is pushing many potential Chapter 11 reorganizations to resolve themselves with fast asset sales under § 363 followed by a liquidation plan.[180]

As traditional lenders declined to provide financing to distressed entities, nontraditional lenders—primarily specialized hedge funds—supplied credit, purchasing discounted debt from larger lenders and providing debtor financing through the Chapter 11 reorganization.[181] These nontraditional lenders are speculating on the future appreciation of the debt, either through a fast asset sale, or through the ownership, management, and subsequent sale of the reorganized entity.[182] The ability to credit bid up to the full face value of a claim virtually assures the nontraditional lender will emerge as the owner of the reorganized entity.[183] If the investor does not

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175 *Id.*

176 *See id.*

177 *See* Jonathan S. Covin & Brant C. Martin, *Kicking the Can Down the Road: Understanding the Current State of Commercial Bankruptcy Trends and Strategies*, *in* NAVIGATING RECENT BANKRUPTCY LAW TRENDS 75, 78–80 (2010), *available at* 2010 WL 4735522, at *4.

178 David Line Batty, *Necessity Is the Mother of Innovation During the Credit Crisis*, 14 N.C. BANKING INST. 1, 14 (2010).

179 Richard D. Thomas, Comment, *Tipping the Scales in Chapter 11: How Distressed Debt Investors Decrease Debtor Leverage and the Efficacy of Business Reorganization*, 27 EMORY BANKR. DEV. J. 213, 217–18 (2010) (discussing how distressed debt investors purchase debt positions in bankruptcy expecting to make a profit through the reorganization).

180 *See* Covin & Martin, *supra* note 177, at 76–77.

181 *See* David Peress & Thomas C. Prinzhorn, *Nontraditional Lenders and the Impact of Loan-to-Own Strategies on the Restructuring Process*, AM. BANKR. INST. J., Apr. 2006, at 48.

182 *See id.*

183 *See* Covin & Martin, *supra* note 177. Assets sold pursuant to a § 363 sale, or in accordance with a plan, are permitted under certain circumstances to be sold "free and clear" of liens, granting the investors clear title to the assets. *See* 11 U.S.C. § 363(f) (2006); *id.* § 1129(b)(2)(A)(ii). Additionally, when bankruptcy courts approve orders to sell all of the debtor's assets they "frequently include provisions that protect the purchaser from any subsequent fraudulent transfer claims based on the theory that the purchaser bought the assets from the debtor for less than 'reasonably equivalent value.'" Covin & Martin, *supra* note 177, at 78.

win the auction with a face-value bid, his lien will attach to the proceeds of the auction,[184] granting him the value of the security's rapid appreciation.

The presence of these nontraditional lenders complicates a Chapter 11 asset sale by shifting the incentives of the bidders at auction. When traditional lenders approach a bankruptcy auction, their goal is to recoup as much of their loan as possible.[185] Nontraditional lenders, on the other hand, have the express goal of owning the assets after the reorganization, and will credit bid the full face value of their claim—a value in excess of the market value of the assets for an undersecured claim—in order to secure their ownership interest.[186] While a nontraditional lender may have to pay additional cash to the estate to satisfy a superior lien, administrative expenses, or both, the result of this reorganization typically leaves the subordinated and "unsecured creditors with little or no recovery."[187]

Nontraditional lenders employing these aggressive credit bidding techniques are betting on collateral appreciation—the upside potential. As noted in *In re The Pacific Lumber Co.*, "[t]he Bankruptcy Code . . . does not protect a secured creditor's upside potential; it protects the 'allowed secured claim.' If a creditor were over-secured, it could not demand to keep its collateral rather than be paid in full simply to protect the 'upside potential.'"[188] A judicial valuation of the debtor's collateral would fix the asset price at the current market value—the "allowed amount" of secured claims.[189] This valuation would provide the creditor with the indubitable equivalent of its claim, and a sale price in excess of this value would benefit the rest of the estate.[190] This procedure would bring a sale of assets pursuant to a plan more in line with the Chapter 11 purpose of rehabilitation and reorganization.

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184 § 1129(b)(2)(A)(ii).

185 *See* Peress & Prinzhorn, *supra* note 181.

186 *See* Robert J. Keach et al., *Resolved: Loan-to-Own DIP Lenders Should Not Be Allowed to Credit Bid* (ABI 25th Annual Spring Meeting, Apr. 15–17, 2007), WL 041207 ABI-CLE 85; Kyle, *supra* note 163.

187 *See* Keach, *supra* note 186.

188 Bank of N.Y. Trust Co. v. Official Unsecured Creditors' Comm. (*In re* The Pac. Lumber Co.), 584 F.3d 229, 247 (5th Cir. 2009).

189 § 1129(b)(2)(A)(i). *See also supra* Part I.B (discussing the process of valuation).

190 *See* § 1129(b)(2)(B) (dictating that the plan of reorganization must provide for the senior creditor to be paid in full to the allowed amount of its claim before a creditor with an interest junior to the dissenting senior creditor may receive anything under the plan). Fixing the allowed amount of a secured creditor's claim via a judicial valuation would satisfy the requirement that a secured creditor be paid in full, permitting recovery for junior creditors of the estate. *See In re The Pac. Lumber Co.*, 584 F.3d at 238, 244, 248 (permitting a judicial valuation to determine the indubitable equivalent of a creditor's claim).

IV. COURTS MAY USE THE INDUBITABLE EQUIVALENT STANDARD TO CRAM DOWN ASSET SALE PLANS THAT RESTRICT CREDIT BIDDING

The Supreme Court's interpretation of the cramdown provision of the Bankruptcy Code not only promotes improper policy, but also promotes inconsistency within the Code. Consistent interpretation between §§ 363 (granting creditors adequate protection against collateral devaluation) and 1129(b) (ensuring creditors are properly compensated when a plan is crammed down against their will) suggests that the Supreme Court should have interpreted the cramdown provision to grant more flexibility in plan design. A proper interpretation of § 1129(b) would permit plans to restrict credit bidding in bankruptcy auctions so long as the creditors are paid the value of their claim as determined judicially.[191]

Judge Ambro's dissent in *In re Philadelphia Newspapers* and the Seventh Circuit in *River Road* stress that the interpretation of an ambiguous statute would be incomplete without referring to the provision's legislative history;[192] however, the Supreme Court did not conduct this analysis.[193] The Senate Report addressing § 1129 confirms that the standard of indubitable equivalence is intended to follow the approach provided by Judge Hand's opinion in *In re Murel Holding Corp.*[194] Judge Hand stressed the flexibility granted to judges in crafting a solution under the indubitable equivalence subprovision.[195] He noted that in the cramdown context, providing the secured creditor with the indubitable equivalent of his claim is not "a 'method' at all; it merely gives power generally to the judge . . . to 'provide . . . adequate protection,' when the other methods are not chosen."[196] The bankruptcy judge has the discretion to determine whether adequate protection is satisfied.[197]

The floor debates remind us that the § 1129(b) list of factors that could satisfy the fair and equitable requirement of cramming down are nonexclusive, stressing that "[a]lthough many of the factors interpreting

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[191] But see Jason S. Brookner, Pacific Lumber *and* Philadelphia Newspapers*: The Eradication of a Carefully Constructed Statutory Regime Through Misinterpretation of Section 1129(b)(2)(A) of the Bankruptcy Code*, 85 AM. BANKR. L.J. 127, 146–47 (2011) for an argument that paying a lender the judicial valuation of its collateral does not provide it with the indubitable equivalent of its claim.

[192] *See* River Rd. Hotel Partners v. Amalgamated Bank, 651 F.3d 642, 649–50, 652 n.8 (7th Cir. 2011), *aff'd sub nom.* RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065 (2012); *In re* Phila. Newspapers, LLC, 599 F.3d 298, 319 (3d Cir. 2010) (Ambro, J., dissenting).

[193] *RadLAX*, 132 S. Ct. at 2071–72 (applying only "the specific governs the general" and the antisuperfluity canons of statutory interpretation).

[194] S. REP. NO. 95-989, at 127 (1978).

[195] Metro. Life Ins. Co. v. Murel Holding Corp. (*In re* Murel Holding Corp.), 75 F.2d 941, 942 (2d Cir. 1935). *See also supra* notes 60–66 and accompanying text (discussing the two ways to calculate the value of collateral).

[196] *In re Murel Holding Corp.*, 75 F.2d at 942.

[197] *Id.*

'fair and equitable' are specified in paragraph (2), others . . . were omitted from the House amendment to avoid statutory complexity."[198] They also dictate that a plan may be crammed down if *any* of the three subprovisions are satisfied, including the more general provision of indubitable equivalence.[199]

Floor debates discussing § 1129 note that the sale provision of subsection (ii)—providing for a sale free and clear of liens subject to credit bidding—is "self explanatory."[200] In clarifying the indubitable equivalent standard of § 1129(b)(2)(A)(iii), the floor debates note that "[a]bandonment of the collateral to the creditor" and "a lien on similar collateral" could qualify as the indubitable equivalent of the creditor's claim.[201] The legislative history does not restrict subsection (iii) to nonsale situations, nor does it explicitly permit it.[202] In order to add additional clarity to the meaning of the statute, we must now look to the statutory context within the Bankruptcy Code.

A. The Similarity Between §§ 361 and 1129(b) Strongly Suggests that They Should Be Interpreted Consistently

Before the Supreme Court's decision in *RadLAX*, the circuit split hinged on the ambiguity (or lack thereof) of § 1129(b). Because the Third and Fifth Circuits determined that the statute is clear on its face, they held that the disjunctive "or" meant a plan may satisfy the indubitable equivalent prong regardless of how the plan is structured.[203] The Seventh Circuit determined that the statute is ambiguous, and used legislative history, statutory context, and policy concerns to hold that a plan may satisfy the indubitable equivalent prong *only if* the plan is not structured in one of the other two ways provided by the statute.[204]

The Supreme Court, on the other hand, found "no textual ambiguity" within the statute.[205] However, rather than looking only to the text of the "unambiguous" statute in order to discern its meaning, the Court reiterated that analyzing statutory context or other "textual indications" can add clarity to the meaning of a statute and overcome the canon of construction presuming the "specific governs the general."[206] The Supreme Court

[198] 124 CONG. REC. 32,407 (1978).
[199] *Id.*
[200] *Id.*
[201] *Id.*
[202] *Id.*
[203] *See supra* notes 102–04, 118–21 and accompanying text.
[204] *See supra* notes 141–46 and accompanying text.
[205] RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065, 2073 (2012), *aff'g* River Rd. Hotel Partners v. Amalgamated Bank, 651 F.3d 642 (7th Cir. 2011).
[206] *Id.* at 2071–72.

asserted that no textual indications were present in the Bankruptcy Code to justify a departure from this canon of construction.[207]

Despite thorough contextual analyses, neither the Third, Fifth, or Seventh Circuits, nor the Supreme Court, analyzed § 1129(b) in conjunction with § 361, the section of the Bankruptcy Code that provides the means to grant a creditor adequate protection during the pendency of a bankruptcy proceeding.[208] Even if courts assume § 1129 is ambiguous, consistent interpretation of § 1129(b) with § 361 requires courts to conclude that a plan may satisfy the indubitable equivalent prong of § 1129(b) regardless of the plan's structure. Due to their substantial similarity, analyzing § 1129 in conjunction with § 361 can add clarity to the meaning of § 1129. When discussing the interpretation of the Bankruptcy Code, one judge noted: "Consistency in the meaning of language in a statute—and most certainly that of words of art—is not only a virtue, it is a hallmark of faithful statutory construction."[209]

Section 361 dictates alternate means of granting creditors adequate protection against devaluation of their collateral during a bankruptcy proceeding.[210] The format, purpose, language, and history of § 361 are remarkably similar to § 1129, and should give clarity to Congress's desired interpretation of § 1129(b)(2)(A)(i)–(iii). Furthermore, due to the similarities between these sections, interpreting them differently promotes undesirable inconsistency within the Bankruptcy Code.

Section 361 provides for three means by which a creditor can receive adequate protection. The section dictates:

> When adequate protection is required[,] . . . such adequate protection may be provided by—(1) requiring the trustee to make a cash payment or periodic cash payments to such entity, to the extent that [the Chapter 11 process] results in a decrease in the value of [the collateral]; (2) providing to such entity an additional or replacement lien to the extent that [the Chapter 11 process] results in a decrease in the value of [the collateral]; or (3) granting such other relief, . . . as will result in the realization by such entity of the indubitable equivalent of [the collateral].[211]

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[207] *Id.* at 2072.

[208] 11 U.S.C. § 361 (2006).

[209] United Sav. Ass'n of Tex. v. Timbers of Inwood Forest Assocs., Ltd. (*In re* Timbers of Inwood Forest Assocs., Ltd.), 808 F.2d 363, 378 (5th Cir. 1987) (Jones, J., dissenting) (discussing the importance of consistent interpretation between types of proposals that can satisfy the standard of indubitable equivalence under §§ 361 and 1129), *aff'd*, 484 U.S. 365 (1988). *Accord In re* Hoff, 54 B.R. 746, 753–54 (Bankr. D.N.D. 1985) (comparing the standard of indubitable equivalence given in § 1129 with the standard of indubitable equivalence in § 361 and concluding that the proposed method of reorganization did not satisfy the § 1129 indubitable equivalence standard because it did not satisfy the § 361 indubitable equivalence standard).

[210] § 361.

[211] *Id.*

These options are consistent with the cramdown options provided in § 1129(b)(2)(A). Both sections dictate that the subprovisions are nonexclusive.[212] Sections 361(1) and 1129(b)(2)(A)(i) both permit a debtor to protect a creditor's claim by making periodic cash payments to the creditor to compensate it for the full value of its claim.[213] Section 361(2) highlights the debtor's option of granting "an additional or replacement lien to the extent" the creditor's collateral has depreciated in value.[214] This § 361 provision is analogous to the means of cramming down a plan suggested by the legislative history of § 1129(b), proposing that "a lien on similar collateral" would satisfy indubitable equivalence.[215]

The legislative history surrounding § 361 notes that a court may provide adequate protection by "permitting a secured creditor to bid in his claim at the sale of the property and to offset the claim against the price bid in."[216] This method is nearly identical to § 1129(b)(2)(A)(ii), which provides for a sale of the debtors' assets with a presumptive right to credit bid.[217] Finally, both §§ 361 and 1129(b) include a catchall provision requiring the lenders to receive the "indubitable equivalent" of their interest in the entity's property.[218] This indubitable equivalent standard grants the bankruptcy court sufficient flexibility to confirm a reorganization plan or a method of providing adequate protection that precisely satisfies the circumstances of the case.

In order to promote uniform interpretation of similar provisions throughout the Bankruptcy Code, the Supreme Court should have interpreted § 1129's cramdown provision consistently with precedential interpretation of the means of granting adequate protection in § 361. A review of § 361 interpretations reveals two important conclusions that should also apply to courts' interpretation of § 1129: (1) the subprovisions are not exclusive and (2) what the debtor proposes to do does not govern the provision under which its plan must be confirmed.

Courts frequently approve means of granting adequate protection that are not listed within the text of § 361, which shows that the subprovisions

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212 *Id.* (noting that "such adequate protection *may be provided* by" several mechanisms (emphasis added)); *id.* § 1129(b)(2) ("[T]he condition that a plan be fair and equitable with respect to a class *includes* the following requirements . . . ." (emphasis added)).

213 *Id.* § 361(1) ("[R]equiring the trustee to make a cash payment or periodic cash payments to such entity, to the extent that [the Chapter 11 process] results in a decrease in the value of [the collateral] . . . ."); *id.* § 1129(b)(2)(A)(i)(II) (dictating "that each holder of a claim . . . receive . . . deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of [the collateral]").

214 *Id.* § 361(2).

215 124 CONG. REC. 32,407 (1978).

216 H.R. REP. NO. 95-595, at 340 (1977).

217 § 1129(b)(2)(A)(ii).

218 *See id.* § 361(3); *id.* § 1129(b)(2)(A)(iii).

are not exclusive. The most common nonstatutory means of adequate protection is the existence of an equity cushion. An equity cushion exists when a creditor is oversecured.[219] Since the purpose of providing adequate protection according to § 361 is to protect the creditor from a decline in the value of its collateral,[220] if the collateral has a present value sufficiently in excess of the creditor's claim, courts are willing to deem that creditor adequately protected.[221] Courts can also find adequate protection through a combination of restrictions on the debtor's use of cash collateral to operate the business, reporting requirements imposed upon the debtor,[222] and third-party guarantees.[223]

In addition, courts regularly confirm plans that propose to combine methods of providing adequate protection.[224] The acceptance of these plans shows that the debtor's proposed method of granting adequate protection (what the plan *provides*) does not govern the provision of the section under which it must be confirmed.[225] A proposal that uses a method listed in the statute combined with a method not listed in the statute does not make the proposal invalid; instead, courts analyze the proposal under the indubitable equivalent prong to determine whether it provides adequate protection.[226]

Courts approve plans calling for periodic cash payments (permitted by § 361(1)) in addition to replacement liens on property (provided for in § 361(2)).[227] Additionally, courts do not require the debtor to make periodic cash payments if an appointed trustee makes them instead.[228] Combining an equity cushion with periodic cash payments is another popular

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219 2 BANKRUPTCY DESK GUIDE § 21:39 (2007).

220 *See, e.g.*, *In re* Mosello, 195 B.R. 277, 288 (Bankr. S.D.N.Y. 1996) (quoting *In re* 495 Cent. Park Ave. Corp., 136 B.R. 626, 631 (Bankr. S.D.N.Y. 1992)); Barclays Bank of N.Y. v. Saypol (*In re* Saypol), 31 B.R. 796, 800 (Bankr. S.D.N.Y. 1983) ("[T]he legislative history confirms that adequate protection centers on protection of a secured creditor from suffering a decline in the value of the collateral during the bankruptcy proceeding.").

221 *See, e.g.*, Bray v. Shenandoah Fed. Sav. & Loan Ass'n (*In re* Snowshoe Co.), 789 F.2d 1085, 1088 (4th Cir. 1986); Pistole v. Mellor (*In re* Mellor), 734 F.2d 1396, 1401 (9th Cir. 1984); *In re* Norton, 347 B.R. 291, 298 (Bankr. E.D. Tenn. 2006); *In re* Avila, 311 B.R. 81, 83 (Bankr. N.D. Cal. 2004); *In re* T.H.B. Corp., 85 B.R. 192, 194 (Bankr. D. Mass. 1988).

222 *See, e.g.*, *In re* Inforex, Inc., 10 B.R. 497, 499–500 (Bankr. D. Mass. 1979).

223 *See, e.g.*, People's United Bank v. Lombardo's Ravioli Kitchen, Inc. (*In re* Lombardo's Ravioli Kitchen, Inc.), No. 08-20774, 2009 WL 585814, at *4–5 (Bankr. D. Conn. Feb. 20, 2009).

224 *See, e.g.*, Metro. Life Ins. Co. v. San Felipe @ Voss, Ltd. (*In re* San Felipe @ Voss, Ltd.), 115 B.R. 526, 527–28, 531 (S.D. Tex. 1990).

225 *See In re* Phila. Newspapers, LLC, 599 F.3d 298, 308–09 (3d Cir. 2010).

226 Corestates Bank v. United Chem. Techs., Inc., 202 B.R. 33, 53 (E.D. Pa. 1996).

227 *See, e.g.*, *In re* Selby Farms, Inc., 15 B.R. 372, 374 (Bankr. S.D. Miss. 1981).

228 *See, e.g.*, *In re* Beaver, 337 B.R. 281, 285 (Bankr. E.D.N.C. 2006) (noting that "[t]he legislative history [of 11 U.S.C. § 361(3)] merely paraphrases the statute and does not suggest that Congress intended to limit a debtor's adequate protection options").

alternative.[229] In analyzing plans proposing a mixture of methods, courts do not discuss whether the method proposed exactly conforms to the subprovisions of § 361 but, rather, focus on whether the debtor's proposal provides the creditor with the indubitable equivalent of its claim.

That treatment of § 361 runs contrary to how the Supreme Court and the Seventh Circuit in *River Road*, and Judge Ambro's dissent in *In re Philadelphia Newspapers*, read the word *provides* in § 1129(b). They dictate that a plan should be crammed down according to the subprovision that is most similar to the plan's proposed action.[230] Like § 1129(b), § 361 also uses the term "provides." When a court determines adequate protection to be necessary, § 361 reads, "such adequate protection *may be provided by*"[231] and then lists three options. This wording is essentially identical to § 1129(b), which reads, "the condition that a plan be fair and equitable with respect to a class includes the following requirements: (A) With respect to a class of secured claims, the plan *provides*," followed by the three cramdown subprovisions.[232] Surely with Code provisions this similar, a mere difference in the tense of the verb "to provide" does not create a different statutory meaning.

Until the decision of *River Road*, courts' treatment of § 1129 mirrored their treatment of § 361. Plans of reorganization that proposed a combination of statutorily provided means and novel means were confirmed under the indubitable equivalent standard of § 1129(b)(2)(A)(iii).[233] A common reorganization plan accepted under the indubitable equivalent standard of § 1129 proposes to completely abandon collateral to the creditor in satisfaction of its debt.[234] A subset of this method is the "dirt for debt" plan that proposes to surrender a portion of the

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229 *See, e.g.*, Prudential Ins. Co. of Am. v. Monnier (*In re* Monnier Bros.), 755 F.2d 1336, 1340 (8th Cir. 1985).

230 RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065, 2073 (2012), *aff'g* River Rd. Hotel Partners v. Amalgamated Bank, 651 F.3d 642 (7th Cir. 2011); *see also River Rd*., 651 F.3d at 652; *In re Phila. Newspapers*, 599 F.3d at 326–27 (Ambro, J., dissenting). *Accord* Brookner, *supra* note 191, at 136–37.

231 11 U.S.C. § 361 (2006) (emphasis added).

232 *Id.* § 1129(b)(2) (emphasis added).

233 *See, e.g.*, *In re* Atlanta S. Bus. Park, Ltd., 173 B.R. 444, 449 (Bankr. N.D. Ga. 1994) ("A plan that includes the partial return of collateral may be confirmable under certain circumstances. One circumstance occurs where, as here, the creditor is oversecured and the value of the surrendered collateral is equivalent to the amount of the creditor's claim."). *See also In re* May, 174 B.R. 832, 837 (Bankr. S.D. Ga. 1994) (concluding that a proposal to surrender only a portion of collateral to an oversecured creditor in full satisfaction of its claim can provide such a creditor with the indubitable equivalent of its claim).

234 *See, e.g.*, Sandy Ridge Dev. Corp. v. La. Nat'l Bank (*In re* Sandy Ridge Dev. Corp.), 881 F.2d 1346, 1354 (5th Cir. 1989); *In re* Hardy Mach., No. 93-80633, 1994 WL 722084 (Bankr. N.D. Ala. Dec. 16, 1994).

debtor's assets to a secured creditor in satisfaction of the creditor's claim.[235] In another variation, the plan proposes to satisfy either all or a portion of the creditor's claim with a lien on substitute collateral.[236]

All of these plans require the court to judicially value both the initial collateral and the replacement collateral to ensure the creditor is receiving the indubitable equivalent of its claim. In certain circumstances, a court may subordinate a replacement lien if the value of the collateral securing the primary and secondary lien is sufficient to cover both claims.[237] Courts are just as receptive to plans proposing a number of options; as one court has noted: "[T]here is no prohibition on a debtor using several methods to provide a secured creditor with the indubitable equivalent of its claim. Courts have routinely allowed combinations of cash payments, payments over time, abandonment of collateral, and substitution of collateral."[238] The Supreme Court's decision changes this history, requiring a plan to conform to the subprovision to which it is most similar.[239] This reduces the flexibility relied upon by bankruptcy courts to confirm nontraditional plans that offer creditors the indubitable equivalent of their claims.

Section 1129(b) of the Bankruptcy Code should be interpreted consistently with § 361 to grant nonexclusive means of providing fair and equitable treatment to dissenting creditors. Historical treatment of both §§ 361 and 1129 shows routine use of nonstatutory means of providing adequate protection and fair and equitable treatment, echoing legislative history promoting the "not exclusive" nature of the sections.[240] Debtors routinely propose plans that utilize a mixture of statutory means—either with nonstatutory or other statutory means—showing that what the plan proposes to do does not govern the provision under which it must be confirmed.

Additionally, consistent interpretation of the statute demands more than granting like terms the same meaning in different parts of the statute—

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[235] *See, e.g.*, Arnold & Baker Farms v. United States (*In re* Arnold & Baker Farms), 85 F.3d 1415, 1423–24 (9th Cir. 1996) (noting that a partial distribution of collateral could satisfy the indubitable equivalent standard even though the particular plan before the court did not); *In re* Bannerman Holdings, LLC, No. 10-01053-SWH, 2010 WL 4260003, at *1, *6 (Bankr. E.D.N.C. Oct. 20, 2010); *In re* May, 174 B.R. at 840.

[236] *See, e.g.*, Brite v. Sun Country Dev., Inc. (*In re* Sun Country Dev., Inc.), 764 F.2d 406, 408–09 (5th Cir. 1985).

[237] *See, e.g.*, Woods v. Pine Mountain, Ltd. (*In re* Pine Mountain, Ltd.), 80 B.R. 171, 174–75 (B.A.P. 9th Cir. 1987).

[238] *In re* Bryant, 439 B.R. 724, 747 (Bankr. E.D. Ark. 2010); *see also id.* (assessing the debtor's plan to (1) make a partial lump-sum payment, (2) abandon certain collateral, and (3) provide cash payments over time to satisfy the remainder of the claim).

[239] RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065, 2073 (2012), *aff'g* River Rd. Hotel Partners v. Amalgamated Bank, 651 F.3d 642 (7th Cir. 2011).

[240] *See supra* notes 198–99 and accompanying text.

one must also interpret the substance of the provisions consistently. Section 361 ensures that creditors are treated fairly and their rights to the value of their collateral are respected. It provides specific examples of ways to ensure creditors are treated fairly, but also permits courts to use their own discretion to craft equitable remedies. The primary focus of § 1129(b) is to provide a means to confirm a plan of reorganization despite the objection of creditors; however, § 1129 ensures that we protect the interests of these creditors and only confirm plans that are fair. As the primary concern of § 361 is fairness to creditors, courts should look to § 361 to help illuminate the fairness of the plans under § 1129.

Consistent interpretation of §§ 361 and 1129(b) strongly supports the conclusion that a plan proposing to sell a creditor's collateral free and clear of liens without permitting credit bidding may be confirmed under the indubitable equivalent prong as long as the plan provides the creditors with the indubitable equivalent of their claims. While both *In re Philadelphia Newspapers* and *In re The Pacific Lumber Co.* reached this conclusion, only *In re The Pacific Lumber Co.* took the necessary step of evaluating the proposed plan to confirm that it satisfied the standard of indubitable equivalence.[241] The Supreme Court argues that "[a]s a matter of law, no bid procedures like the ones proposed [in the RadLAX plan] *could* satisfy the requirements of § 1129(b)(2)(A)."[242] By making this assertion, the Supreme Court unnecessarily restricts valuation during a sale to valuation by auction with credit bidding, when the Bankruptcy Code clearly also permits judicial valuation.[243] The bankruptcy court should retain the discretion to permit either valuation by auction or judicial valuation. With judicial valuation, not only *can* the bid procedures provide for the indubitable equivalent of a claim, they may offer a far better approximation of the current market value.

B. *A Judicially Valued Asset Sale Plan Satisfies Indubitable Equivalence*

The indubitable equivalent provision *can* apply to plans proposing to sell assets at auction without credit bidding; however, just because it is permitted to apply does not mean the proposed plan will satisfy the high standards of indubitable equivalence. Courts must be stringent in their analysis of the creditor's return under the proposed plan to ensure that it provides the indubitable equivalent of the creditor's claim. Rather than remanding for a factual determination, *RadLAX* concluded as a matter of

[241] Bank of N.Y. Trust Co. v. Official Unsecured Creditors' Comm. (*In re* The Pac. Lumber Co.), 584 F.3d 229, 246–47 (5th Cir. 2009).

[242] *RadLAX*, 132 S. Ct. at 2073.

[243] *See supra* notes 60–62.

law that the indubitable equivalent standard could not be met.[244] Had the Court continued to a factual analysis, it would have concluded that a plan providing for the sale of a debtor's assets without credit bidding does not fail to satisfy § 1129(b)(2)(A) as a matter of law, but rather can satisfy the indubitable equivalent standard if the court equitably determines the value of the secured creditor's claim.

As discussed earlier, the Bankruptcy Code recognizes two equally valid means of determining the value of a creditor's claim: via a judicial proceeding[245] or by selling the collateral at a public auction.[246] A judicial determination of value, codified in § 506(a),[247] provides the means for both the debtor and the creditor to present evidence of the collateral's appraised value.[248] Courts recognize that this is often an "inexact science";[249] however, it may be the best alternative given the purpose of the valuation and the goals of the particular bankruptcy reorganization. The Supreme Court in *Associates Commercial Corp. v. Rash* blessed the use of a judicial valuation for cramdown plans and determined that the replacement value standard is the appropriate valuation to use.[250]

In order for a court to determine if the objecting creditor is receiving the indubitable equivalent of its claim, the court must first value the collateral. If the proposed plan limits valuation by auction subject to credit bidding, the court must value the collateral by the only other option recognized by the Bankruptcy Code: judicially. Thus, a plan proposing to sell the debtor's assets free and clear of liens while restricting credit bidding without cause can only satisfy the standard of indubitable equivalence if the court first values the claim judicially. *RadLAX* fails to

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[244] In contrast, *In re The Pacific Lumber Co.* completed both parts of the analysis by first determining whether the indubitable equivalent prong was permitted to apply, and then determining whether the creditor received the indubitable equivalence of its claim. *See* 584 F.3d at 244–47.

[245] 11 U.S.C. § 506(a)(1) (2006) ("Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.").

[246] *Id.* § 363(b), (k); *id.* § 1129(b)(2)(A)(ii); Takisaki v. Alpine Grp., Inc. (*In re* Alpine Grp., Inc.), 151 B.R. 931, 935 (B.A.P. 9th Cir. 1993) ("The offered price . . . is conclusive evidence of the property's value.").

[247] § 506(a); River Rd. Hotel Partners v. Amalgamated Bank, 651 F.3d 642, 650 (7th Cir. 2011), *aff'd sub nom. RadLAX*, 132 S. Ct. 2065. *See also supra* Part I.B (discussing the process of valuation).

[248] 3 COLLIER, *supra* note 12, ¶ 361.04, at 361-22 to -23.

[249] Gennrich v. Mont. Sport U.S.A., Ltd. (*In re* Int'l Ski Serv., Inc.), 119 B.R. 654, 657 (Bankr. W.D. Wis. 1990) (citing Gen. Indus., Inc. v. Shea (*In re* Gen. Indus., Inc.), 79 B.R. 124, 135 (Bankr. D. Mass. 1987)). *See also* Boyle v. Wells (*In re* Gustav Schaefer Co.), 103 F.2d 237, 242 (6th Cir. 1939) ("The valuation of property is an inexact science and whatever method is used will be only an approximation . . . .).

[250] 520 U.S. 953, 960 (1997) (describing the replacement value standard as "the price a willing buyer in the debtor's trade, business, or situation would pay to obtain like property from a willing seller").

discuss judicial valuation at all. *River Road* discusses judicial valuation as an alternative to valuation by auction, but does not discuss why it restricts judicial valuation when assets are to be sold.[251] *In re The Pacific Lumber Co.* correctly recognized these options, concluding that the judicial valuation was not erroneous and that the stringent indubitable equivalent standard was met.[252]

CONCLUSION

Congress, in response to the *RadLAX* decision, should amend the Bankruptcy Code to permit judicial valuation of claims to combat aggressive lending strategies and promote the rehabilitation of businesses. The debate surrounding § 1129(b) has occurred during a time of elevated Chapter 11 filings with significantly undersecured creditors.[253] Granting debtors the choice to restrict credit bidding will offer them essential flexibility to restructure their entities. Rather than host an asset sale in which potential bidders will likely be dissuaded by a nontraditional lender holding a credit bid far in excess of the current market value of the assets, debtors will be able to fix the collateral valuation judicially. Any bids received in excess of the judicial valuation will benefit the subordinated creditors and equity holders within the estate.[254] Additionally, as the *In re Philadelphia Newspapers* auction shows us, increased bidder attendance brought on by a restriction on credit bidding will foster a more competitive auction environment, likely resulting in a higher asset sale price.

The Supreme Court should have followed the approach taken by *In re The Pacific Lumber Co.* and permitted debtors to choose whether to prohibit credit bidding at an auction sale.[255] Due to their similarity in text and purpose, the Court should have analyzed § 1129(b) in conjunction with § 361 in a way that reflects uniform interpretation.[256] Because § 361 does not impose a *functional* plan classification (i.e., what the plan *provides* does not govern under which subprovision it must be confirmed), § 1129(b)

[251] *River Rd.*, 651 F.3d at 650.

[252] Bank of N.Y. Trust Co. v. Official Unsecured Creditors' Comm. (*In re* The Pac. Lumber Co.), 584 F.3d 229, 247–49 (5th Cir. 2009).

[253] *See* Covin & Martin, *supra* note 177, at 76.

[254] *See* 11 U.S.C. § 1129(b)(2)(B) (2006) (dictating that the plan of reorganization must provide for the senior creditor to be paid in full to the allowed amount of its claim before a creditor with an interest junior to the dissenting senior creditor may receive anything under the plan). Fixing the allowed amount of a secured creditor's claim via a judicial valuation would satisfy the requirement that a secured creditor be paid in full, permitting recovery for junior creditors of the estate. *See In re The Pac. Lumber Co.*, 584 F.3d at 238, 244, 248 (permitting a judicial valuation to determine the indubitable equivalent of a creditor's claim).

[255] *In re The Pac. Lumber Co.*, 584 F.3d at 247.

[256] *See* § 1129(b) (dictating the means to cram down a plan against a dissenting class of creditors); *id.* § 361 (dictating the means to provide adequate protection to creditors).

should also not impose such a functional classification. Instead, § 1129(b) should apply in a consistent manner with § 361, permitting a plan to be confirmed under the indubitable equivalent prong even if it has characteristics that are similar to other subprovisions.

Asset sale plans that restrict credit bidding can satisfy the indubitable equivalent standard if the creditors are paid the judicially determined value of their collateral. The Bankruptcy Code permits valuation to occur either judicially or via an auction sale, subject to the ability to credit bid.[257] If credit bidding is restricted at auction, judicial valuation provides an alternative that will assure that the creditors are receiving the indubitable equivalent of their claim.[258]

When addressing this circuit split, the Supreme Court should have ensured an internally consistent interpretation of the Bankruptcy Code, and also an interpretation that promotes the purpose of Chapter 11. The Bankruptcy Code does not protect a creditor's upside potential; however, nontraditional lenders are using credit bidding as a tool to accomplish just that.[259] The Supreme Court in *RadLAX* affirmed a practice that protects the investments of creditors at the expense of a reorganizing entity. In response to this, Congress should amend the Bankruptcy Code so that the cramdown provisions once again promote effective rehabilitation and reorganization of debtors.

[257] *Id.* § 363(b), (k); *id.* § 506(a)(1) ("Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest."); *id.* § 1129(b)(2)(A)(ii); Takisaki v. Alpine Grp., Inc. (*In re* Alpine Grp., Inc.), 151 B.R. 931, 935 (B.A.P. 9th Cir. 1993) ("The offered price . . . is conclusive evidence of the property's value.").

[258] Assocs. Commercial Corp. v. Rash, 520 U.S. 953, 960 (1997) (blessing the use of a judicial valuation for cramdown plans).

[259] *In re* Phila. Newspapers, LLC, 599 F.3d 298, 317 (3d Cir. 2010) (quoting *In re The Pac. Lumber Co.*, 584 F.3d at 247).