THE EVOLUTION OF CREDIT BIDDING:
ITS RECENT JOURNEY AND LOGICAL NEXT STEP

by

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LL.M., The University of British Columbia, 2007
J.D., The University of British Columbia, 2011

A THESIS SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR
THE DEGREE OF

MASTER OF LAWS

in

The Faculty of Graduate Studies

(Law)

THE UNIVERSITY OF BRITISH COLUMBIA
(Vancouver)

July 2013

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ABSTRACT

Credit bidding is a US construct that enables secured creditors to use their secured claims, instead of having to raise additional capital, to bid on their collateral at an asset sale. The US legislature amended the bankruptcy statutes to include credit bidding specifically to prevent the undervaluation of collateral. Recent US case law has re-evaluated when secured creditors are entitled to credit bid and when debtors might be able to deny this right through the use of a loophole subsection. This subsection allows a debtor to deny secured creditors the right to credit bid if the debtor can satisfy their claims by providing an “indubitable equivalent.” While the US Supreme Court ultimately determined that the indubitable equivalent subsection cannot be used to deny secured creditors the right to credit bid at an asset sale, the case law adeptly highlights the merits of credit bidding while demonstrating the dangers of specific legislation.

Although Canada does not have legislation regarding credit bidding, it has nonetheless been incorporated into Canadian insolvency proceedings through cross-border cases. This thesis discusses both the benefits and issues involved with credit bidding in a US and Canadian context, reviewing relevant case law and legislation in both jurisdictions. It also discusses the current status of credit bidding in Canada, which, without specific legislation to state otherwise, current case law has found to be permissible but not a right. Consequently, this thesis proposes that credit bidding should be added to Canadian insolvency legislation.
PREFACE

This thesis is an independent work designed and researched by the author.
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ACKNOWLEDGMENTS

I would like to express my utmost gratitude to my supervisor, Professor Bruce MacDougall for his continuous support and feedback. This project would have been immensely more difficult had it not been for his invaluable insight and positive reassurances. I am particularly grateful to Dr. Janis Sarra, for her wisdom and guidance. Her comments and assistance provided a deeper understanding of the subject matter.

I would also like to thank my family for their endless patience and support. Their encouragement has proved to be a light in the dark, especially during late nights of editing and re-editing.
DEDICATION

To my parents, who never stopped believing in me even when I did.
CHAPTER 1: INTRODUCTION

According to Darwin's *Origin of Species*, it is not the most intellectual of the species that survives, it is not the strongest that survives; but the species that survives is the one that is able best to adapt and adjust to the changing environment in which it finds itself.\(^1\)

The ability to adapt and evolve with the times is an integral requirement for every government. The present era is filled with international trade, an ever-expanding network of international businesses, and the growing realization that countries are all inter-dependent. Foreign direct investment stocks in Canada alone have increased from CND$340 billion in 2001 to over $599 billion in 2011.\(^2\) As more companies are operating across international borders, it is to be expected that there would also be an increase in the number of cross-border insolvency proceedings.\(^3\)

In response to these cross-border insolvencies, Canada has had to evolve to keep pace. Evolution, as commonly defined, requires a development or adoption of new traits so as to differentiate from an earlier form.\(^4\) The common law lends itself to being adaptable, as judges often have flexibility in their interpretation of laws.\(^5\) This flexibility enables the courts to adopt new principles and thereby progresses evolution of the common law.

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Throughout the course of history, evolution has resulted in the rise and fall of countless species. Analogous to Earth’s differentiating ecosystem, Canada’s own legal system has also seen the creation of new life, in the form of laws, as well as the subsequent extinction of legal codes that have outlived their usefulness. One of Canada’s more recent evolutionary leaps is the adoption of credit bidding in the Companies’ Creditors Arrangement Act (CCAA)\(^6\) proceedings through cross-border insolvency cases with the US. What is credit bidding? Credit bidding is best understood through a hypothetical US situation. For example, a secured creditor loans a restaurant owner $5,000 and takes security interest in a refrigerator. Subsequently, the restaurant owner files for protection under Chapter 11 of the US Bankruptcy Code\(^7\) and wants to sell the refrigerator free and clear of any attached liens. During the asset sale at an open auction, the secured creditor could credit bid up to $5,000 on the refrigerator without needing to produce actual cash. If the secured creditor happens to be outbid during the course of the auction by another purchaser, the secured creditor would still be entitled to receive his full $5,000.\(^8\)

The US courts have had the opportunity to amass case law regarding credit bidding, particularly regarding when creditors have the right to credit bid and when debtors have the ability to deny that right. However, the US case law is neither straightforward nor does it agree. In fact, this disparity in case law is largely due to

\(^6\) Companies’ Creditors Arrangement Act, RSC 1985, c. C-36, as amended \([\text{CCAA}]\).

\(^7\) 11 USC (2012).

another provision situated within the US Bankruptcy Code, which has recently served as a loophole for debtors in order to deny their creditors the right to credit bid providing that the secured creditors’ claims can be satisfied through an “indubitable equivalent.” The term “indubitable equivalent” was coined by Judge Learned Hand and is generally held by caselaw to mean that which is equivalent to the value of the collateral. The problem is not in the definition, but in identifying that which can be said to constitute the “indubitable equivalent.” A string of recent US cases have interpreted this provision so as to grant debtors the ability to deny secured creditors their right to credit bid; however, these decisions were met with a great deal of controversy and ultimately required the US Supreme Court to weigh in on the matter.

Credit bidding gained momentum in Canada when it was recently approved in White Birch Paper Holding Company, a case involving a cross-border insolvency proceeding. The recent inclusion of credit bidding in Canadian insolvency proceedings means that there is very little guidance or rules as to its application in a Canadian context. The few Canadian cases that exist often pertain to cross-border proceedings involving the US. The void of Canadian case law on the matter has not prevented the Canadian courts from approaching credit bidding with an open mind.

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10 In re Murel Holding Corp., 75 F 2d 941 at 942 (2d Cir 1935).
11 In re Philadelphia Newspapers, LLC, 599 F 3d 298 at 310 (3d Cir 2010).
12 See In re Philadelphia Newspapers, LLC, ibid; In re Pacific Lumber Co., 584 F 3d 229 (5th Cir 2009); River Road Hotel Partners, LLC v Amalgamated Bank, 651 F 3d 642 (7th Cir 2011) [River Road].
and while Canada’s aptitude and openness to accepting foreign doctrines is commendable, there may also be pitfalls from integrating credit bidding into domestic proceedings. First of all, credit bidding is still very much a controversial topic in the US, the country of its legislative and judicial conception. The uncertain nature of credit bidding in the US increases time and monetary expenditures as debtors and creditors dispute its application. These issues might seep into the Canadian arena just as easily as credit bidding was accepted into Canadian insolvency proceedings.

As with all life forms, the potential for mutation and the subsequent evolution of a new creature, such as credit bidding, is always a risk. Therefore, an argument can be made for the incorporation of credit bidding into legislation to cement it into place in the bankruptcy world. On the flip side, the beauty of the current Canadian regime, and the reason why credit bidding was able to be included in Canadian bankruptcy proceedings to begin with, is largely due to the flexible nature of the *CCAA*. Hence, adding more legislation could stifle further evolution. My thesis’ goal is to illuminate the gaps in the current Canadian bankruptcy and insolvency legislation, identify potential problems arising from adopting credit bidding without the checks and balances enjoyed by the US from years of case law and legislation, and discuss possible solutions to address the problem.
CHAPTER 2: CREDIT BIDDING OUTSIDE OF BANKRUPTCY

2.1 Introduction

The fundamental entitlement of secured creditors – in or out of bankruptcy – is to be paid in full, up to the value of their collateral, in priority to unsecured creditors.14

The above quote sums up concisely one key objective of commercial and insolvency legislation – satisfying secured creditors. The US and Canadian bankruptcy legislation provide guidance once a debtor becomes insolvent, but prior to a debtor’s descent into financial distress, the debtor-creditor relationship is governed by commercial legislation. According to the British Columbia Personal Property Security Act,15 a debtor is generally defined as one “who owes payment or performance of an obligation secured.”16 These obligations secured are often in the form of monetary loans, which secured creditors have extended with the expectation that the debtor will repay the loan. As a precaution, the secured creditors take a security interest in the debtor’s collateral in the event that the debtor should fail to meet the terms of the security agreement and default. Commercial legislation, such as the PPSA17 and the Uniform Commercial Code,18 sets out the specifics governing the relationship between a debtor and creditor, remedies, and a hierarchy of priorities when several creditors are involved. While the intricate details pertaining to commercial law are beyond the scope of this

15 Personal Property Security Act, RSBC 1996, c 359 [PPSA] (this legislation deals with secured transactions).
16 PPSA, ibid s 1(1).
17 For the purposes of this thesis, any references to the PPSA will be made with respect to the British Columbia PPSA.
thesis, the remedies available to secured creditors are much the same regardless of whether the debtor simply defaults on a secured creditor’s security agreement or he or she becomes insolvent. Hence, credit bidding has an application beyond the insolvency realm. A brief overview of the PPSA and the Uniform Commercial Code will highlight the important similarities of these two pieces of legislation and provide some insight as to how credit bidding can translate into not only a Canadian insolvency context but also into commercial law as well.

2.2 Personal Property Security Act

Secured transactions, collateral and the relationships between the debtor and creditor are all governed by versions of the PPSA\(^\text{19}\) in Canada and by Articles 8 and 9 of the Uniform Commercial Code in the United States. Large portions of the PPSA are taken directly from Articles 8 and 9 of the Uniform Commercial Code. Ontario was the first province to adopt Articles 8 and 9, with most other provinces subsequently using the Ontario version as a basis on which to model their own commercial legislation.\(^\text{20}\) It naturally flows from this derivation that these pieces of legislation are similar in nature.


Upon default by the debtor, the *PPSA* sets out statutory remedies that secured creditors may use in addition to any common law remedies already available.\(^{21}\) These remedies include remedies set out in the security agreement and remedies provided by the *PPSA* itself.\(^{22}\) The relevant remedy, for the purposes of this thesis, is the disposition of the collateral by the secured creditors, set out in section 59.\(^{23}\) The disposition of the collateral may be accomplished either through a public or private sale.\(^{24}\) A key element of this section is the ability of the secured creditors to purchase the collateral at a public sale, provided that the purchase price is a reasonable fair market value of the collateral.\(^{25}\) While the wording of the provision speaks to the legislature’s concern with the secured creditors undervaluing the collateral at a public auction to the obvious detriment of the debtor and any other subordinate parties, the *PPSA* seems to ignore the issue of outside third parties undervaluing the collateral at auction. An argument could be made that if the secured creditors suspected an undervaluation, they could simply submit a bid that reflected a more appropriate valuation of the collateral. Of course, this argument is based on the assumption that the secured creditors have the ability to expend more resources, and money, on the collateral, which may not be the case. Recognizing that the purchase money will be returned to the secured creditors to satisfy the obligation owed, the secured creditors must still face the dilemma of raising more capital to purchase the encumbered assets. Alternatively, if the secured creditors

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\(^{21}\) *PPSA, supra* note 15, s 68(1) (common law continues to apply so long as they are not inconsistent with the provisions of the Act).

\(^{22}\) *PPSA, supra* note 15, s 56(2).

\(^{23}\) *PPSA, supra* note 15, s 59.

\(^{24}\) *PPSA, supra* note 15, s 59(3).

\(^{25}\) *PPSA, supra* note 15, s 59(13).
wanted the collateral but had no means to purchase at auction, they could foreclose and take possession of the assets. The problem with this remedy is that it precludes the lenders from seeking any deficit that the collateral fails to cover. Foreclosing is deemed to have satisfied in full the obligation secured. A more logical solution to avoid this circular dilemma would be to allow credit bidding. Not surprisingly, credit bidding has been employed in receivership cases in Canada.

2.3 Uniform Commercial Code

The Uniform Commercial Code also enables secured creditors to dispose of collateral via private or public sale. The traditional procedural method for secured creditors to collect on their security, outside of bankruptcy, is to foreclose on the collateral through judicial procedure. The secured parties may then purchase the collateral subsequently either through a public disposition or privately if the collateral is the kind that has standardized prices or sold on recognized markets.

One noticeable difference between the Uniform Commercial Code and the PPSA is the remedy of foreclosure. As noted prior, the PPSA views a foreclosure on collateral as fulfillment of the obligation secured. Under the Uniform Commercial Code, “acceptance of collateral,” as it is called, fulfills the obligation secured only to

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26 PPSA, supra note 15, s 61(1).
27 PPSA, supra note 15, s 61(3).
29 UCC § 9-610(c) (2004).
31 Ibid § 9-610(c).
the extent agreed upon by both the debtor and secured creditors.\textsuperscript{32} In other words, secured creditors can still claim for any deficiency.\textsuperscript{33} Furthermore, and most importantly, lenders are entitled to credit bid.\textsuperscript{34}

Although there is no mention of credit bidding in the Uniform Commercial Code,\textsuperscript{35} various state courts and statutes have recognized the secured creditors’ right to credit bid.\textsuperscript{36} For example, in \textit{In re The Colad Group, Inc.} the secured creditor sought to have additional loan fees that were advanced to an insolvent debtor to be incorporated into the secured position of the original loan.\textsuperscript{37} The Bankruptcy Court reviewed the addition of the loan fees both from a bankruptcy perspective and a Uniform Commercial Code perspective, making note of the secured creditor’s ability to credit bid outside of bankruptcy in accordance with the “commercially reasonable” standard in Article 9.\textsuperscript{38} In \textit{Sky Technologies LCC v. SAP AG}, the secured creditor foreclosed on its security interests and then purchased the assets at a public auction using a credit bid whereby the secured creditor was the sole bidder.\textsuperscript{39}

Similarly, the court in \textit{Cornelison v. Kornbluth} found that in a non-judicial sale, a

\begin{itemize}
\item \textsuperscript{32} \textit{Ibid} § 9-620.
\item \textsuperscript{33} \textit{Ibid} § 9-620(g) (except in cases involving a consumer transaction).
\item \textsuperscript{34} \textit{In re The Colad Group, Inc.}, 324 BR 208 at 222 (Bankr WD NY 2005).
\item \textsuperscript{36} 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” (2011) 85 Am Bank LJ 127 (“[c]ase law and statutes in 42 states and the District of Columbia either expressly or implicitly authorize or recognize the right to credit bid” at 139, n 68).
\item \textsuperscript{37} \textit{In re The Colad Group, Inc.}, supra note 34.
\item \textsuperscript{38} \textit{Supra} note 29, § 9-610.
\item \textsuperscript{39} \textit{Sky Technologies LCC v SAP AG}, 576 F 3d 1374 (Fed Cir 2009).
\end{itemize}
creditor is entitled to credit bid “up to the amount of his indebtedness, since it would be useless to require him to tender cash which would only be immediately returned to him.”\textsuperscript{40} While the Uniform Commercial Code is silent with respect to credit bidding, state case law and statutes have generally come to the same conclusion – a secured creditor has a right to credit bid.

\textbf{2.4 Summary}

The secured creditors’ right to credit bid both in and out of a bankruptcy context appears to be well-established in the US. The rights and remedies afforded to secured creditors under commercial law do not cease to exist once the debtor becomes insolvent. Instead, upon entering financial distress, insolvency legislation acts in tandem with commercial legislation to control the relationship between creditors and debtors. Although not explicitly addressed in the Uniform Commercial Code, US courts have viewed credit bidding as a secured creditor’s right. It would be counterintuitive to allow credit bidding in an insolvency context but not extend the remedy to secured creditors generally, especially when the rights of secured creditors are meant to be served by both pieces of legislation. The fact that the \textit{PPSA} stems from the Uniform Commercial Code would imply that credit bidding, while not inconsistent with the objectives of the Uniform Commercial Code, would also not be inconsistent with the goals of the \textit{PPSA}. Credit bidding furthers the objectives of the \textit{PPSA} by providing yet another method to recoup the obligation secured. Therefore, while this thesis focuses on the impact on secured creditors in insolvency

\textsuperscript{40} Cornelison v Kornbluth, 15 Cal 3d 590 at 607 (Sup Ct 1975).
proceedings, the conclusions drawn from this thesis could also have implications on the rights of secured creditors outside of a bankruptcy context in Canada.
CHAPTER 3: US LEGISLATION – CREDIT BIDDING IS GIVEN LEGISLATIVE LIFE

3.1 Introduction

Prior to the current US bankruptcy scheme, debtors had considerable control over the execution of sales of collateral. The debtor could “pick the time when it want[ed] to either redeem or sell the collateral, and [could] redeem or sell without competition from the secured creditor, at a price set by the court or at auction.”41

Secured creditors were limited in their rights to the collateral, with courts stating that the most secured creditors could expect was protection “to the extent of the value of the property. There is no constitutional claim of the creditor to more than that.”42 However, the modest rights afforded to secured creditors would soon prove to be the impetus to encasing credit bidding in legislation. Bankruptcy laws were due for an overhaul and the In re Pine Gate case only added more fuel to the fire.43

3.2 In re Pine Gate

In re Pine Gate dealt with a Chapter XII property arrangement under the then in-effect Bankruptcy Code.44 According to the proposed arrangement plan, the debtors moved to have the mortgagee creditors’ collateral appraised and then to pay out the mortgagee creditors the appraised value in cash. However, the mortgagee creditors rejected this plan and instead demanded to be paid out the full amount of their claim or have the collateral handed over. The creditors acknowledged the fact that the value of their security was less than the debtor owed. As such, the court stated that

41 Tabb, supra note 14 at 117.
42 Wright v Union Central Life Insurance Co., 311 US 273 at 278 (1940) [footnotes omitted].
43 In re Pine Gate Associates, Ltd., 1976 US Dis LEXIS 17366 (Bankr ND Ga) [In re Pine Gate].
44 11 USC (Supp 1935).
they could not expect to be paid in full the amount owed since the collateral itself would not cover the whole of the debt and to pay the full amount would be, in essence, finding that the collateral is worth more than it actually is.\(^{45}\) Instead, the “adequate protection” guaranteed to the creditors in accordance with the act would have to be limited to the value of the collateral ascertained via appraisal.\(^{46}\) Furthermore, the court in \textit{In re Pine Gate} went on to add that “any reasonable method of ascertaining such an appraisal is constitutionally permissible, so long as the creditor is accorded procedural due process and receives the value of the debt.”\(^{47}\)

The response to this decision was general outrage from secured creditors as any potential lender could be forced to take a diminished cash pay out at time when the market might be depressed or if the appraised value was determined by a judge sympathetic towards the debtor.\(^{48}\)

3.3 A New Life Form Created – Credit Bidding Added to Legislation

Following \textit{In re Pine Gate}, Congress reconsidered its stance on secured creditors’ rights, and, as it happened to be in the midst of a general review of bankruptcy legislation, credit bidding was simply added to the list of proposed amendments.\(^{49}\) Credit bidding made its first appearance in 1977 as a provision in the draft bill to

\(^{45}\) \textit{In re Pine Gate, supra} note 43 at 27.
\(^{46}\) \textit{In re Pine Gate, supra} note 43 at 29.
\(^{47}\) \textit{In re Pine Gate, supra} note 43 at 53 [footnotes omitted].
\(^{48}\) Tabb, \textit{supra} note 14 at 118.
\(^{49}\) Tabb, \textit{supra} note 14 at 118-119.
amend the US bankruptcy legislation before being tweaked and restructured into the current scheme. Upon being signed into law in the Bankruptcy Reform Act of 1978, it appeared as if creditors had a guaranteed right to credit bidding. This right was secured in two different provisions: 1.) under an asset sale pursuant to § 363(k) and 2.) in a Chapter 11 reorganization plan under § 1129(b)(2)(A)(ii). Secured creditors now could rely on these legislated safeguards to prevent the undervaluation of their collateral.

Section 363(k) of the US Bankruptcy Code now reads:

(k) At a sale under subsection (b) of this section of property that is subject to a lien that secures an allowed claim, unless the court for cause orders otherwise the holder of such claim may bid at such sale, and, if the holder of such claim purchases such property, such holder may offset such claim against the purchase price of such property.

Hence, if a debtor decides that its best bet is to sell the collateral during the course of bankruptcy, § 363(k) ensures that secured creditors may bid on the collateral at auction using the debt in lieu of cash. The courts have found that secured creditors are entitled to bid up to the “full face value of their secured claims under § 363(k).” Should the secured creditors suspect that the collateral is being undervalued at an auction, the creditors are entitled to submit a credit bid where, presumably, they would bid up to the estimated value of the collateral. Any remaining surplus claim

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50 US, Bill S 2266, 95th Cong, 1977 §363(e).
52 11 USC § 363(k) (2012).
53 Cohen v KB Mezzanine Fund II, LP (In re SubMicron Systems Corporation), 432 F 3d 448 at 459 (3d Cir 2006) [SubMicron].
that is not offset by the winning bid becomes an unsecured deficiency claim. If the creditors are outbid, then their lien attaches to the proceeds of the sale. Should they bid more than the collateral is worth, the secured creditors risk losing out on an unsecured deficiency claim.

However, if the debtor instead decides to pursue a plan of reorganization, secured creditors might still find themselves entitled to credit bid. Under § 1129(a), the Bankruptcy Code states that “[t]he court shall confirm a plan only if all of the following requirements are met...,” one of which necessitates that each class of claims or interests approve the proposed plan or are otherwise not impaired. Despite this provision, a debtor might still be able to “cram down” the plan over the protesting class by fulfilling requirements under § 1129(b). Included in the list of requirements is the provision that the plan must be “fair and equitable.” What constitutes “fair and equitable” is outlined in § 1129(b)(2)(A), which reads:

(2) For the purpose of this subsection, the condition that a plan be *fair and equitable* with respect to a class includes the following requirements:

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54 11 USC § 506(a)(1) (2012) ("[a]n allowed claim of a creditor secured by a lien on property in which the estate has an interest, or that is subject to setoff under section 553 of this title, *is a secured claim to the extent of the value of such creditor's interest* in the estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be, *and is an unsecured claim* to the extent that the value of such creditor's interest or the amount so subject to setoff is less than the amount of such allowed claim. 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" [emphasis added]).


57 *Kham & Nate’s Shoes No. 2, Inc. v First Bank*, 908 F 2d 1351 at 1359 (7th Cir 1990) (referred to as “cramdown plans” because they are “crammed down the throats of objecting creditors”).

(A) 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
defered 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.\textsuperscript{59}

The above provision outlines three alternative methods, considered to be fair and
equitable, which a debtor may use should it choose to proceed with an asset sale
notwithstanding the secured creditors' disapproval.\textsuperscript{60} The first of these alternatives
requires that if property secured by liens is transferred or sold, that all liens
attached to that property remain attached.\textsuperscript{61} The second alternative, as outlined in §
1129(b)(2)(A)(ii), states that an asset may be sold free and clear of any attached
liens, and should be in accordance to a sale under § 363(k).\textsuperscript{62} Finally, an asset sale
may also be approved where the secured creditors receive an "indubitable
equivalent" of their claim.\textsuperscript{63} It is the second and third alternatives that have proved
to be controversial in recent years. While a sale that purports to sell assets free and

\textsuperscript{59} 11 USC at § 1129(b)(2)(A) (2012) [emphasis added].
\textsuperscript{60}  Ibid.
\textsuperscript{63} 11 USC at § 1129(b)(2)(A)(iii) (2012).
clear of liens would appear to fall under § 1129(b)(2)(A)(ii), two cases that have garnered widespread attention have seen debtors persuading the courts that such a sale could also be classified as falling under § 1129(b)(2)(A)(iii). This new interpretation of the “indubitable equivalent” has drawn much debate across the legal arena since it essentially bypasses the hard won secured creditors’ right to credit bid.
CHAPTER 4: THE US CREDIT BIDDING CRISIS – EVOLVING LAWS?

4.1 Introduction

Having been embedded in American legislation since 1978, credit bidding has had ample time to be explored and discussed by US case law. However, a recent line of cases has called into question the previously unchallenged right entitling creditors to credit bid on their secured collateral at an asset sale. Kicking off this new interpretation of § 1129(b)(2)(A), the Fifth Circuit court In re Pacific Lumber Co. changed the rules of the game, and as such, set a new precedent that upset the previously settled right to credit bid.64 Instead of being required to permit the secured creditors the right to credit bid during an asset sale of the secured collateral, the court sided with the debtors’ argument that allowed them to use a loophole provision in § 1129(b)(2)(A)(iii), whereby the secured creditors need only be provided with their indubitable equivalent rather than the right to credit bid.

Within the span of just a few months, the Third Circuit was presented with a similar case.65 The Third Circuit, too, was persuaded by the debtors’ argument and held that a plan could be “crammed down” involving an asset sale without allowing the secured creditors the right to credit bid. This decision affirmed the Fifth Circuit’s ruling. What once could have been argued as a mere blemish and misinterpretation of the statute had now launched into a completely reworked interpretation of the statute and, consequently, when debtors could deny secured creditors their right to credit bid. These decisions, however, were not met with much favour from legal

64 In re Pacific Lumber Co., supra note 12.
65 In re Philadelphia Newspapers, LLC, supra note 11.
experts nor academics alike. Instead, there was an outpouring of literature with critics arguing that both the Fifth and Third Circuit courts had gotten it wrong. It seemed as if the entire bankruptcy arena was left with an unsettled feeling.

Two years later, the Seventh Circuit court was presented with the same dilemma. In an interesting turn of events, the court found that the debtors could not rely on § 1129(b)(2)(A)(iii) to deny secured creditors the right to credit bid during an asset sale, upholding the Bankruptcy Court’s ruling in In re River Road Hotel Partners, LLC and rejecting the Fifth and Third Circuit’s rulings as persuasive. The debtors appealed to the US Supreme Court.

Before delving into the details of the US Supreme Court’s decision, which ultimately ended the matter, the cases leading up to this pivotal decision are first reviewed below. The purpose of highlighting these relevant cases, aside from providing a better understanding of the US judiciary’s interpretation of credit bidding, is to illuminate the hazards and merits of incorporating credit bidding into legislation. If Canada were to implement its own version of credit bidding in a legislative format, proper consideration should be given to jurisdictions that have already had a long established framework. The US, which has this framework in place, and which is also responsible for the recent inclusion of credit bidding in Canadian insolvency

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67 River Road, supra note 12.
68 In re River Road Hotel Partners, LLC, 2010 Bankr LEXIS 5933 (Bankr ND Ill 2010) [In re River Road Hotel Partners, LLC].
69 RadLAX Gateway Hotel, LLC v Amalgamated Bank, 132 US 2065 (2012) [RadLAX Gateway].
proceedings, provides an exemplary opportunity to review such issues that arise from detailed legislation.

4.2 In re Pacific Lumber Co. – Mutation Occurs

As previously mentioned, In re Pacific Lumber Co. marked the critical turning point in the United States’ judiciary interpretation of credit bidding and spurred the discourse now seen in the scholarly realm. It signaled the new age of credit bidding, or perhaps a more apt description would be to say that it commenced the downfall of credit bidding. The US legislature had implanted this carefully constructed provision into the US Bankruptcy Code, intending to prevent the undervaluation of collateral as seen in the In re Pine Gate case. Yet, In re Pacific Lumber Co. appeared to undermine the legislature’s intention to afford secured creditors this additional protection. Whereas, historically, secured creditors were entitled to credit bid in asset sales that purported to sell the creditors’ collateral free and clear of liens, debtors could now deny secured creditors the right to credit bid by arguing that cram down plans involving the sale of creditors’ secured collateral could be approved under § 1129(b)(2)(A)(iii)\textsuperscript{70} and not the traditional § 1129(b)(2)(A)(ii).

The facts of the case are as follows. Pacific Lumber Company and Scotia Pacific LLC, abbreviated by the courts to “Palco” and “Scopac,” respectively, were affiliated entities involved in the redwood timber industry.\textsuperscript{71} Palco owned and operated a

\textsuperscript{70} 11 USC §1129(b)(2)(A)(iii) (2012) (“cramdown” plan may be approved under this subsection providing that the secured creditor receives an “indubitable equivalent” of their secured collateral).

\textsuperscript{71} In re Pacific Lumber Co., supra note 12 at 236.
power plant, sawmill, the town of Scotia, California and Scopac, a Delaware special purpose entity.\footnote{\textit{In re Pacific Lumber Co.}, supra note 12 at 236.} In 1998, Palco had transferred 200,000 acres of redwood timberlands to Scopac to facilitate the sale of $867.2 million in notes secured by the timberlands and other assets owned by Scopac.\footnote{\textit{In re Pacific Lumber Co.}, \textit{ibid} at 236.} On January 18, 2007, in the Southern District of Texas, Palco, Scopac and four additional affiliated debtors filed separate petitions under Chapter 11 of the \textit{Bankruptcy Code}.\footnote{\textit{In re Pacific Lumber Co.}, \textit{ibid} at 236.} The six petitions were procedurally consolidated by the Bankruptcy Court.\footnote{\textit{In re Pacific Lumber Co.}, \textit{ibid} at 236.} At the date of filing, Palco’s assets had an estimated value of $110 million, against which Marathon Structured Finance (“Marathon”) held a secured claim of $160 million.\footnote{\textit{In re Pacific Lumber Co.}, \textit{ibid} at 236.} Scopac owed its Noteholders $740 million in principal and interest on the timberland notes, in addition to the $36.2 million owed to Bank of America on a secured line of credit.\footnote{\textit{In re Pacific Lumber Co.}, \textit{ibid} at 236.} The Noteholders were represented by the Bank of New York during the bankruptcy cases pursuant to an indenture agreement (“Indenture Trustee”).\footnote{\textit{In re Pacific Lumber Co.}, \textit{ibid} at 237.}

Various plans of reorganization were filed, with the court ultimately finding the joint Mendocino Redwood Company (“MRC”) and Marathon plan to be confirmable, the former entity a competitor of Palco.\footnote{\textit{In re Pacific Lumber Co.}, \textit{ibid} at 236-237.} Under the MRC/Marathon plan, the six affiliated entities would be dissolved, intercompany debts cancelled and two new

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  \item \footnote{\textit{In re Pacific Lumber Co.}, \textit{ibid} at 236-237.}
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  \item \footnote{\textit{In re Pacific Lumber Co.}, \textit{ibid} at 237.}
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companies would be created from the ashes. Substantially all of Palco’s assets would be transferred to Townco, whereas the timberlands and sawmill would be transferred to Newco. The plan contributed $580 million towards the claims against Scopac. In addition, Marathon would convert its $160 million in secured claims against Palco to equity, which would enable Marathon to claim ownership over Townco, a 15% share in Newco and a new note in the amount of the sawmill’s working capital.

The proposed plan created 12 classes of interests. While two impaired classes voted in favour of the plan, thus making the plan confirmable, MRC and Marathon still had to “cram down” the plan on dissenting classes, mainly the Noteholders, in accordance with § 1129(b).

Of primary importance for the confirmation of the plan was the valuation of the timberlands securing the Noteholders’ claim. After extensive testimony, the court valued the timberlands at $510 million, stating that the valuation was the “indubitable equivalent” of the Noteholders’ secured claim on the timberlands. Subtracting an additional $3.6 million on non-timberlands collateral, the court’s valuation of the timberlands resulted in a portion of the Noteholders’ claim being

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80 In re Pacific Lumber Co., ibid at 237.
81 In re Pacific Lumber Co., ibid at 237.
82 In re Pacific Lumber Co., ibid at 237.
83 In re Pacific Lumber Co., ibid at 237.
84 In re Pacific Lumber Co., ibid at 238.
85 In re Pacific Lumber Co., ibid at 238.
86 In re Pacific Lumber Co., ibid at 238.
deemed as unsecured. The Bankruptcy Court then confirmed the plan with minor alterations. The Indenture Trustee and a few individual Noteholders moved for a direct appeal to the Fifth Circuit, which was granted.

Amongst the several issues on appeal, the Indenture Trustee asserted that the plan “violate[d] the absolute priority rule by paying junior Palco and Scopac creditors with the Noteholders’ collateral” and that the plan was not “‘fair and equitable’ because the plan sold the Timberlands collateral without providing the Noteholders the right to credit bid.”

The Fifth Circuit recognized that the absolute priority rule enforces a strict hierarchy of creditor classes’ rights, defined by Collier on Bankruptcy as to mean that “a plan of reorganization may not allocate any property whatsoever to a junior class on account of their interests or claims in a debtor unless such senior classes receive property equal in value to the full amount of their allowed claims...” Of parallel importance is § 1129(b) of the Bankruptcy Code, which states that the plan must be “fair and equitable” with respect to impaired classes. Thus, from these provisions it logically follows that a plan could not be fair and equitable if it violates the absolute priority rule.

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87 In re Pacific Lumber Co., ibid at 239.
88 In re Pacific Lumber Co., ibid at 239.
89 In re Pacific Lumber Co., ibid at 239.
The Fifth Circuit then turned to the Indenture Trustee’s “fair and equitable” argument. The Indenture Trustee argued that the Noteholders were denied their right to credit bid pursuant to § 1129(b)(2)(A)(ii), which entitles secured creditors the right to credit bid if their secured property is to be sold free and clear of liens.\(^91\) The Bankruptcy Court had designated the timberlands transaction as a “transfer” rather than a “sale,” which enabled the Marathon/MRC plan to side-step the Noteholders’ right to credit bid.\(^92\) The Fifth Circuit sided with the appellants (Indenture Trustee and the individual Noteholders) and found that the Bankruptcy Court erred in this decision ruling that the exchange of cash and debt by MRC/Marathon in return for title in the debtors’ assets was indeed a sale.\(^93\) The Fifth Circuit then went on to find that although the transaction is considered a sale, it does not necessarily mean that § 1129(b)(2)(A)(ii) applies.\(^94\)

The Fifth Circuit reviewed the statutory language of § 1129(b)(2)(A):

(A) 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

\(^91\) *In re Pacific Lumber Co.*, ibid at 245.
\(^92\) *In re Pacific Lumber Co.*, ibid at 245.
\(^93\) *In re Pacific Lumber Co.*, ibid at 245.
\(^94\) *In re Pacific Lumber Co.*, ibid at 245.
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.\(^{95}\)

The court viewed the use of the word “or” in subsection (ii) as meaning that the
three subsections are alternatives.\(^{96}\) Jones, C.J., delivering reasons for the court,
stated that the use of the word “includes” in § 1129(b)(2)\(^ {97}\) precludes the
subsections from being exhaustive.\(^ {98}\) She rejected the appellants’ argument that a
broad interpretation of subsection (iii) renders subsection (ii) as superfluous,
indicating that there may be circumstances in which an asset sale may entitle
secured creditors the opportunity to credit bid but not always.\(^ {99}\) Given the non-
exhaustive nature of the subsections, the court stated that treating these
subsections as “compartmentalized alternatives” would be inconsistent and
concluded that the MRC/Marathon plan’s cash payment to the lenders could be
categorized as meeting the “indubitable equivalent” requirement in subsection
(iii).\(^ {100}\)

\(^{95}\) 11 USC §1129(b)(2)(A) (2012) [emphasis added].
\(^{96}\) In re Pacific Lumber Co., supra note 12 at 245.
\(^{97}\) 11 USC §1129(b)(2) (2012) (where the statute states that the “condition that a plan be fair and
equitable includes the following requirements...” [emphasis added]).
\(^{98}\) 11 USC §102(3) (2012) (defines the term “includes” to not be limiting in nature).
\(^{99}\) In re Pacific Lumber Co., supra note 12 at 245.
\(^{100}\) In re Pacific Lumber Co., ibid at 245-246.
Given that the Fifth Circuit had found that an asset sale, which denied secured creditors the right to credit, could be approved under subsection (iii), the next issue to consider was whether the proposed payment under then plan was sufficient to constitute the “indubitable equivalent” required by subsection (iii). The Bankruptcy Court had originally heard expert testimony as to the appropriate valuation of the assets, and eventually determined the assets to be worth $510 million. This appraisal was substantially less than the value of the debt owed. The lenders argued that by refusing the right to credit bid, they did not in fact receive their indubitable equivalent by forfeiting potential increases in the collateral’s valuation.

The Fifth Circuit wrestled with the interpretation of indubitable equivalent, stating that “[w]hat measures constitute the indubitable equivalent of the value of the [lenders’] collateral are rarely explained in caselaw, because most contested reorganization plans follow familiar paths outlined in Clauses (i) and (ii).” This statement should have given the Fifth Circuit pause to reconsider if allowing the plan to proceed under subsection (iii) was indeed the right decision. After considering the literature regarding the interpretation of “indubitable equivalent,” Jones, C.J. found that regardless of its ambiguity, the indubitable equivalent subsection, and subsection (i) and (ii), all serve to protect the

101 In re Pacific Lumber Co., ibid at 238.
102 In re Pacific Lumber Co., ibid at 247.
103 In re Pacific Lumber Co., ibid at 246.
104 See Kenneth N. Klee, “All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code” (1979) 53 Am Bankr LJ 133 (“[t]he legislative history states that abandonment of the collateral to the class would satisfy [the indubitable equivalent], as would a replacement lien on similar collateral” at 156).
“repayment of principal and the time value of money.”\textsuperscript{105} By offering a reasonable cash payment to the Noteholders, Jones, C.J. ruled that the “indubitable equivalent” requirement of the plan was fulfilled.

In circumstances where a sale involves selling an asset free and clear of attachments, credit bidding generally provides the secured creditors with recourse when they feel that the asset is being undervalued. In this case, the Noteholders argued that the plan failed to meet the “indubitable equivalent” requirement because the judicial valuation determined through expert testimony was significantly lacking and that “market valuation” would better determine the real value of the assets.\textsuperscript{106} The court disagreed, finding that while some circumstances may call for a sale via public auction,\textsuperscript{107} the Bankruptcy Court had heard sufficient expert testimonies to be able to make a judicial valuation. The Fifth Circuit found that the proposed plan’s cash payment would satisfy the lenders’ allowed secured claim, discrediting the lenders’ argument on the basis that the Bankruptcy Code is meant to protect the allowed secured claim and not the “upside potential” of possible increases in asset valuation.\textsuperscript{108}

The court seems to have missed the mark in its interpretation of subsection (ii) and (iii). Congress outlined three circumstances in which a plan may be “cram downed”

\textsuperscript{105} \textit{In re Pacific Lumber Co.}, supra note 12 at 246.
\textsuperscript{106} \textit{In re Pacific Lumber Co.}, ibid at 247.
\textsuperscript{108} \textit{In re Pacific Lumber Co.}, supra note 12 at 247.
dissenting creditors. While the *Bankruptcy Code* specifies that the use of “include” is not limiting in nature in regards to the overall interpretation of § 1129(b)(2), the court erred in its approach to understanding the meaning of “limiting,” instead confusing limiting to “overlapping.” A delineated list identifying key characteristics of proposed plans does not preclude other plans from being approved that do not meet the criteria in subsections (i)-(iii). However, a plan that does meet the criteria found within one of the outlined subsections, such as an asset sale free and clear of liens in subsection (ii), should then be subject to the delineated criteria. It defeats the purpose of listing any criteria at all if the plan can then be subsequently approved under subsection (iii). Thus, upon deciding whether a plan meets the “fair and equitable” standard, the court should first identify if the proposed plan falls into one of the three outlined subsections and proceed from there. In this particular case, the proposed plan clearly met the criteria listed in subsection (ii), which purported to sell the secured assets free and clear of liens. The circumstances in which secured creditors are entitled to credit bid are clearly outlined in § 363(k), where an asset is sold free and clear of liens. The court acknowledged that the plan did constitute a sale and yet bypassed § 363(k) by finding that the plan could be approved under § 1129(b)(2)(A)(iii). If Congress would go so far as to define conditions, or alternatives, under which credit bidding should be allowed, it would seem contradictory that they would then include another provision that would constitute a loophole unless the court erred in interpreting the provision to broadly. In rejecting the lenders’ argument that approving the plan renders subsection (ii) superfluous, the court glossed over the argument without providing any solid
evidence to support its conclusion. The purpose behind this case discussion is not merely to highlight the court’s erroneous interpretation of the statute, but rather, to point out that no legislation is free from the potential to be misinterpreted, a discussion that will be returned to in Chapter 7.

4.3 In re Philadelphia Newspapers, LLC – A New Species of Credit Bidding?

4.3.1 Background

Six months after the Fifth Circuit’s decision In re Pacific Lumber Co., the Third Circuit court soon faced the same dilemma in having to decide whether a debtor could sell assets free and clear of liens without allowing the secured creditor the ability to credit bid. As in the prior Fifth Circuit case, the debtor was attempting to proceed with the proposed plan under § 1129(b)(2)(A)(iii), which calls for the plan to provide the “indubitable equivalent” to the creditor.

The debtors, comprised of a group of entities including the parent company PMH Holdings, owned and operated the newspapers Philadelphia Inquirer and Philadelphia Daily News, in addition to an online publication. The debtors purchased these assets for $515 million in July 2006, of which $295 million came in the form of a loan from a lender syndicate (“lenders”). Approximately 2 years later, the debtors filed petitions under Chapter 11 of the Bankruptcy Code and later filed a joint plan of reorganization that included assets being sold free and clear of any liens. At the
time the Third Circuit heard the case, the value of the lenders’ loan had increased to $318 million.\textsuperscript{109}

Under the proposed plan, the assets were to be sold at a public auction with the help of a “stalking horse bidder,” Philly Papers, LLC. The majority interest of Philly Papers, LLC, was held by two entities, which also held 50% of the equity in PMH Holdings. If the stalking horse bid was successful, the sale would generate $37 million for the lenders in cash and the lenders would additionally receive the debtors’ headquarters valued at $29.5 million.\textsuperscript{110}

On August 28, 2009, the debtors brought a motion for approval of the bidding process, which was to preclude the lenders from credit bidding. The Bankruptcy Court denied the motion finding that the plan was structured as a sale under §1129(b)(2)(A)(ii), and thereby required that the lenders have the right to credit bid.\textsuperscript{111} The District Court overturned the ruling stating that the interpretation of §1129(b)(2)(A)(iii) was broad enough to encompass a plan that denied credit bidding provided that the plan offered the secured creditors an “indubitable equivalent.”\textsuperscript{112} The case was subsequently appealed to the Third Circuit court.

The lenders presented three arguments to support their right to credit bid, first arguing that the proper statutory interpretation precluded the debtor from denying

\textsuperscript{109} In re Philadelphia Newspapers, LLC, supra note 11 at 301.
\textsuperscript{110} In re Philadelphia Newspapers, LLC, supra note 11 at 302.
\textsuperscript{111} In re Philadelphia Newspapers, LLC, 2009 Bankr LEXIS 3167 (Bankr ED Pa 2009) [Philadelphia].
\textsuperscript{112} In re Philadelphia Newspapers, LLC, 418 BR 548 (ED Pa 2009).
the creditors the right to credit bid. The second argument turned on the interpretation of “indubitable equivalent,” which the lenders contended as being ambiguous. Finally, the lenders argued that denying the lenders the right to credit bid was inconsistent with other provisions in the Bankruptcy Code.113

4.3.2 The Majority Opinion

Fisher, C.J., writing for the majority of the Third Circuit, reviewed the statutory language of the three alternatives as set out in § 1129(b)(2)(A). Setting out the basics of statutory interpretation, Fisher, C.J. began by stating that the first course of action in interpreting any provision is to look at the statutory language.114 If the language should prove to be unambiguous, the statutory analysis ends there.115 Fisher, C.J. noted that the use of the word “or” means that the three alternatives are to be construed as operating independently of each other. A debtor is merely obligated to satisfy one of the alternatives and is not compelled to satisfy all three nor are the alternatives mutually exclusive.116 The lenders conceded that the use of “or” meant that the statute provided alternatives. However, they went on to argue that the specific wording of subsection (ii) should prevail over the more general terminology of subsection (iii). Essentially, this would mean that the “proposed

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113 In re Philadelphia Newspapers, LLC, supra note 11 at 304.
115 In re Philadelphia Newspapers, LLC, supra note 11 at 304.
116 See In re Pacific Lumber Co., supra note 12 at 245; Wade v Bradford, 39 F 3d 1126 at 1130 (10th Cir 1994).
treatment of collateral determines which of the § 1129(b)(2)(A) alternatives is applicable.”

The majority rejected this argument, stating that case law had interpreted the “specific governs the general” rule to apply only where it was clear that the specific provision was intended to limit the general provision. The majority, relying on the ruling in Varity Corp. v. Howe, stated that they could find no such intention in this circumstance, since Congress had intentionally included “indubitable equivalent” in order to approve alternative plans of asset sales. Fisher, C.J. also considered the Fifth Circuit court’s reasons in In re Pacific Lumber Co. before stating that the listed subsections under § 1129(b)(2)(A) were examples provided by Congress as to what could be considered “fair and equitable” in accordance with § 1129(b)(1).

The lenders’ second argument hinged on the interpretation of “indubitable equivalent.” They argued that the phrase was ambiguously broad. The court acknowledged that case law has seldom expressed the meaning behind indubitable equivalent, pointing to the Fifth Circuit’s discussion in In re Pacific Lumber Co. where it stated that it is “rarely explained in caselaw, because most contested

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117 In re Philadelphia Newspapers, LLC, supra note 11 at 306.
118 See In re Combustion Engineering, Inc., 391 F 3d 190 (3d Cir 2004) (traditional canon of statutory interpretation where “specific statutory provisions prevail over more general provisions” at 237, n 49); Varity Corp. v. Howe, 561 US 489 (1996) (“a warning against applying a general provision when doing so would undermine limitations created by a more specific provision” at 511).
119 In re Philadelphia Newspapers, LLC, supra note 11 at 308.
120 Supra note 58.
reorganization plans follow familiar paths outlined in Clauses (i) and (ii).” As similarly noted in regards to the Fifth Circuit’s decision, this statement should have given the majority pause to reconsider if approving this sale under subsection (iii) what the right decision. Despite this disadvantage, the court defined the phrase through *Webster’s Third New International Dictionary* where “indubitable” is defined as “not open to question or doubt,” and “equivalent” means “equal in force or amount” or “equal in value.” The *Bankruptcy Code* defines “secured claim” as “the extent of the value of such creditor’s interest in the estate’s interest in such property.” Hence, the court interpreted “indubitable equivalent” of secured claims to mean “the unquestionable value of a lender’s secured interest in the collateral.”

The majority acknowledged that while “indubitable equivalent” is broadly defined, it is not ambiguous, pointing to the Fifth Circuit’s postulation that subsection (iii) is governed by the same “fair and equitable” principles that govern subsections (i) and (ii). The court then cited cases where the debtor had supplied creditors with an indubitable equivalent. However, both these cited cases involved some form of collateral substitution, which precluded the plans from falling strictly under § 1129(b)(2)(A)(ii).

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121 *In re Pacific Lumber Co.*, supra note 12 at 246.


123 *Supra* note 54.

124 *In re Philadelphia Newspapers, LLC*, supra note 11 at 310.

125 *In re Pacific Lumber Co.*, supra note 12 at 246.

126 See *In re Sun Country*, 764 F 2d 406 (5th Cir 1985) (affirmed the Bankruptcy Court’s approval of the release of the lender’s lien on 200 acres in return for 21 notes secured by 21 lots of land, whereby the notes were found to fulfill the creditor’s “indubitable equivalent” of the lien); *In re Criimi Mae, Inc.*, 251 BR 796 at 807-808 (Bankr D Md 2000) (the court approved a plan, which involved an asset sale under subsection (iii) in addition to the substitution of collateral).
Having found that subsection (iii) was unambiguous and that the subsections merely provide non-exhaustive alternatives under which a debtor can cramdown a plan of reorganization, it flowed from this interpretation that the only way the lenders could insist on their right to credit bid was if it was expressly stated in the statute. Subsection (iii) contains no such language. The lenders counter-argued that in order to satisfy subsection (iii), the lenders must have the right to credit bid to establish the value of the collateral. Again, the court rejected the argument. The majority recognized the challenges associated with an under-secured creditor and the importance of credit bidding, but relied on In re Pacific Lumber Co. in finding that the secured creditors could potentially receive their indubitable equivalent despite being denied the right to credit bid.

The lenders’ final argument rested on congressional intent, citing a statement made by Representative Edwards:

Sale of property under section 363 or under a plan is excluded from treatment under section 1111(b) because of the secured party’s right to credit bid in the full amount of its allowed claim at any sale of collateral under section 363(k) of the House Amendment.127

The purpose of § 1111(b) is to provide recourse to under-secured creditors. Where the court-determined value of the collateral is less than the secured debt, the secured creditors have the option of making a § 1111(b) election whereby the deficiency claim is treated as secured. However, if the secured collateral is sold

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under a plan or § 363, then the secured creditors are prevented from electing § 1111(b).

The lenders argued that Congress clearly intended for secured creditors to have the right to credit bid should they be unable to make a § 1111(b) election. The court pointed out that the wording of § 363(k) includes “unless the court for cause orders otherwise.” 128 Accordingly, even if a sale were to proceed under § 363(k), the court could still deny secured creditors the right to credit bid. In addition to this for-cause exception, the court also noted that a sale of assets under § 1129(b)(2)(A)(i) does not entitle the lenders to credit bid either. Given these exceptions, the court disagreed with the lenders’ argument that denying the right to credit bid goes against congressional intent.

**4.3.3 Dissent**

Ambro, C.J. wrote a strong dissenting opinion that is touted by academics as the correct interpretation of § 1129(b)(2)(A). 129 According to Ambro, C.J. the majority should have reviewed § 1129(b)(2)(A) in the context of the entire Bankruptcy Code, keeping in mind legislative intent, which would have pointed “to the conclusion that the Code requires cramdown plan sales free of liens to fall under the specific requirements of § 1129(b)(2)(A)(ii) and not to the general requirements of subsection (iii).” 130

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128 Supra note 52.
129 See Brookner, supra note 36; Barney, supra note 8.
130 In re Philadelphia Newspapers, LLC, supra note 11 at 319.
Ambro, C.J. began his dissent with a general explanation of credit bidding, the rationale behind it being that a secured lender would not outbid a bidder unless the lender thought that it could make a greater profit on the collateral than would be received as a result of the bidder’s offer. Credit bidding protects the secured creditors’ collateral from being undervalued.

The following discussion then turned around the ambiguous nature of the subsections in question. He pointed to the recent different interpretations held by both the District Court and the Bankruptcy Court to reach the conclusion that the subsection was unclear and, as such, the court should have move beyond the first step of statutory interpretation. Ambro, C.J. stated that canons of statutory interpretation dictate that the “statutory scheme [should be read in a manner] that gives effect to every provision Congress enacted and avoids general provisions swallowing specific provisions, especially when to do so makes the specific superfluous.” The provisions also must be read in light of the statute as a whole. Finally, when ambiguity or uncertainty still remains, turning to the legislative history of a provision might provide the clarity needed.

131 SubMicron, supra note 53 at 460.
133 In re Philadelphia Newspapers, LLC, supra note 11 at 328.
134 In re Philadelphia Newspapers, LLC, supra note 11 at 334-335.
Ambro, C.J. then performed his own statutory analysis. Using the reasoning in the Fifth Circuit’s decision, In re Pacific Lumber Co., the majority in that case emphasized that the subsections were non-exhaustive alternatives based on the use of the word “or” and “includes” in § 1129(b)(2).\textsuperscript{135} However, Circuit Judge Ambro found that the longer-lived interpretation turned on the use of “provides.”\textsuperscript{136} He reasoned that “includes” applies to § 1129(b)(2) in general and not specifically to § 1129(b)(2)(A). However, upon delving deeper into § 1129(b)(2)(A), the operative word is “provides,” “whereby Congress prescribes specific treatments for specific scenarios of secured-claim treatment.”\textsuperscript{137} Given this understanding of the statute, Circuit Judge Ambro found that Congress intended there to be three distinct alternatives that may be used to cramdown plans. These distinct alternatives require the debtor to meet certain requirements depending on the chosen alternative, rather than leaving it open to the debtors to choose which alternative they wish to employ. Accordingly, any plan that proposes to sell secured creditors’ collateral free and clear of liens would entitle the secured creditors the right to credit bid.

Circuit Judge Ambro went on to state that the majority’s interpretation violated not only traditional canons of statutory interpretation, but also defeated the purpose of including credit bidding in § 1129(b)(2)(A)(ii) which was to protect the value of secured collateral. The “specific over general” canon embodies the principle that the “[g]eneral language of a statutory provision, although broad enough to include it,

\textsuperscript{135} Supra note 97.
\textsuperscript{136} Supra note 59.
\textsuperscript{137} In re Philadelphia Newspapers, LLC, supra note 11 at 325.
will not be held to apply to a matter specifically dealt with in another part of the same enactment.” Subsection (i) and (ii) are both specific provisions detailing the criteria that must be met to ensure that a plan is “fair and equitable.” Subsection (iii), however, is a much more generalized catch-all provision that should be used when plans do not meet criteria in subsections (i) or (ii), and not, as the majority found, just another alternative at the debtor’s disposal. Subsection (iii)’s application should be limited to those plans that do not fall under subsection (i) or (ii). Hence, Circuit Judge Ambro went on to find that confirming the plan under subsection (iii) and bypassing the secured creditors’ right to credit bid is contradictory to congressional intent.

He then went on to state that the majority’s interpretation violates not only the “specific over general” rule, but also renders subsection (ii) superfluous, violating the anti-superfluousness canon. The majority opinion found that plans might be confirmed under subsection (iii) even when subsection (ii) would apply. The majority reasoned that subsections (i) and (ii) were merely examples of what could constitute a “fair and equitable” plan. However, as Circuit Judge Ambro noted, this directly violates the anti-superfluousness rule. Moreover, he went on to add that if plans of sale can be approved under subsection (iii), then it was unnecessary for Congress to add a right to credit bid in subsection (ii).

\footnote{138} D. Ginsberg & Sons v Popkin, 285 US 204 at 208 (1932).
\footnote{139} TRW, Inc. v Adelaide Andrews, supra note 132 (no provision “shall be superfluous, void, or insignificant” at 31); See also Market Co. v Hoffman, 101 US 112 at 115-116 (1879).
Finally, Judge Ambro predicted that the majority’s decision would also create some discomfort in the loaning community, as a traditional right that lenders had previously relied on, was now being eroded creating unpredictability. He argued that credit bidding had been inserted as a right in the Code to protect lenders’ interests, not the debtors. He argued that this decision was contrary to Congressional intent, as future bankruptcy proceedings would likely be directed under the more flexible subsection (iii) where debtors could continue to cramdown plans that sell the lenders’ collateral free and clear of liens while simultaneously denying the lenders the right to credit bid.

4.4 Reaction to the Third and Fifth Circuit Decisions

Following the Third and Fifth Circuits’ rulings, academics and practitioners alike responded with an outpouring of commentaries and articles claiming that the courts were mistaken in their interpretation of § 1129(b)(2)(A)(ii) and § 1129(b)(2)(A)(iii), while simultaneously hailing Circuit Judge Ambro’s dissent as the proper interpretation. However, it appeared as if there was a new trend in statutory interpretation of these subsections, as this was the second major case that had upset prior case law history.

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140 See Resnick, supra note 55; Barney, supra note 8; Brookner, supra note 36; Vincent S. J. Buccola & Ashley C. Keller, “Credit Bidding and the Design of Bankruptcy Auctions” (2010) 18 Geo Mason L Rev 99.
The major concerns of most critics rested on the issues of undervaluation and lender certainty.\textsuperscript{141} Credit bidding enables lenders to step in and bid up to the face value of the debt owed on the secured collateral.\textsuperscript{142} Hence, if a bidder submits a low bid compared to the market value of the collateral, the secured creditors can submit a higher bid and, if successful, claim the collateral. Aside from potential valuation issues, credit bidding also avoids the secured creditors from having to raise additional capital, which could prove problematic for secured creditors that are short on capital or where lender syndicates are involved. As pointed out by Judge Ambro in his dissent, the decisions in \textit{In re Philadelphia Newspapers, LLC} and \textit{In re Pacific Lumber Co.} also impact secured creditors’ certainty with respect to credit bidding. Creditor uncertainty could lead to an increase in transaction costs as secured creditors might now face potential litigation as secured parties debate whether or not their “indubitable equivalent” is being met.\textsuperscript{143} This uncertainty might also result in a decrease in available credit. Whereas creditors once relied on credit bidding to ensure full repayment of the debt, lenders may decrease the amount of credit extended to debtors to account for the potential loss of credit bidding.\textsuperscript{144}

\textsuperscript{141} See Resnick, \textit{supra} note 55.

\textsuperscript{142} See \textit{SubMicron, supra} note 53.

\textsuperscript{143} Resnick, \textit{supra} note 55 at 357-358; \textit{In re Philadelphia Newspapers, LLC, supra} note 11 at 337.

\textsuperscript{144} Resnick, \textit{supra} note 55 at 358-359; \textit{In re Philadelphia Newspapers, LLC, supra} note 11 at 337.
4.5 River Road Hotel Partners, LLC v. Amalgamated Bank\textsuperscript{145} 

The facts of this case involve two parties of debtors, which can be simplified into River Road debtors and RadLAX debtors. Both parties had purchased hotels through a loan agreement from Longview Ultra Construction Loan Investment, the lenders.\textsuperscript{146} Due to unanticipated costs, both debtor parties defaulted and filed voluntary petitions under Chapter 11 of the US Bankruptcy Code in the United States Bankruptcy Court for the Northern District of Illinois, Eastern Division.\textsuperscript{147} River Road debtors and RadLAX debtors submitted plans of reorganization for court approval. The plans included an asset sale through which the assets would be sold to the highest bidder at auction with the help of a stalking horse bidder.\textsuperscript{148} In addition to the plans of reorganization, the debtors also sought approval of the bidding process, which precluded the lenders from credit bidding.\textsuperscript{149} 

The lenders objected to the plans. Since § 1129(a) requires lender approval, the debtors attempted to have the plan crammed down under § 1129(b)(2)(A)(iii). The lenders’ argued that the plan could not be approved under this subsection because a sale of assets free and clear of liens falls not under the scope of (iii) but § 1129(b)(2)(A)(ii). The lenders went on to say that since the plan fails to meet the requirements of (ii) by denying the lenders the right to credit bid the plan should be

\begin{footnotes}
\item[145] Supra note 12.
\item[146] River Road, supra note 12 at 643-644.
\item[147] River Road, supra note 12 at 644.
\item[148] See In re New River Dry Dock, Inc., 497 Fed Appx 882 (11th Cir 2012) (“[a] ‘stalking horse’ bid is the first bid from a potential buyer on a bankrupt debtor’s assets...to set the floor for the later competing bids of other potential purchases, thereby preventing lowball offers” at 884, n 2).
\item[149] River Road, supra note 12 at 645.
\end{footnotes}
rejected. The Bankruptcy Court ultimately ruled in the lenders’ favour,\textsuperscript{150} leading the debtors to appeal the judgment to the Seventh Circuit court.

As seen in the prior cases, the debtors argued that the proposed plans of reorganization should be confirmed under § 1129(b)(2)(A)(iii). The Bankruptcy Court had disagreed with the debtors and referred to Judge Ambro’s dissent in \textit{In re Philadelphia Newspapers, LLC} as the correct statutory interpretation of § 1129(b)(2)(A). On appeal, the Seventh Circuit reviewed the statutory language of the disputed subsection in order to formulate its own interpretation as to how the subsection should be applied. The court noted that “the majority of cramdown plans have sought confirmation under subsection (ii) of 1129(b)(2)(A),”\textsuperscript{151} a fact that had also been noted in both \textit{In re Philadelphia Newspapers, LLC} and \textit{In re Pacific Lumber Co.}\textsuperscript{152}

Unsurprisingly, the debtors relied on \textit{In re Philadelphia Newspapers, LLC} and \textit{In re Pacific Lumber Co.} to support their argument that their reorganization plan could be confirmed under § 1129(b)(2)(A)(iii). Unlike its sister circuits, the Seventh Circuit rejected the debtors’ argument and, instead, found Judge Ambro’s analysis persuasive. The court focused its discussion on two issues: 1) the scope of § 1129(b)(2)(A)(iii) and 2) the definition of “indubitable equivalent.” In addressing the scope of § 1129(b)(2)(A)(iii), the court acknowledged that there were two

\textsuperscript{150} \textit{In re River Road Hotel Partners, LLC}, supra note 68.
\textsuperscript{151} River Road, supra note 12 at 647.
\textsuperscript{152} \textit{In re Philadelphia Newspapers, LLC}, supra note 11 at 310; \textit{In re Pacific Lumber Co.}, supra note 12 at 246.
possible interpretations. The first interpretation involved limiting the scope of subsection (iii) to those plans not covered by subsection (i) and (ii). The second possible interpretation would define subsection (iii) as having a more global application.

The Seventh Circuit found that the debtors' interpretation of § 1129(b)(2)(A)(iii), where the subsection would be applied globally, violated a basic tenet of statutory interpretation.\footnote{Duncan v Walker, 533 US 167 (2001) (“a statute ought...to be construed so that, if it can be prevented, no clause, sentence, or word shall be superfluous, void, or insignificant” at 174).} The debtors argued that interpretation of (iii) in a broad manner should apply to approve asset sales that fail to meet the requirements of the prior subsections. The court took issue with this argument as the prior subsections would no longer serve any purpose if sales that failed to meet subsections’ (i) and (ii) requirements could still be approved under (iii). The court found that this type of statutory interpretation would defeat the subsections’ purpose and render them superfluous, a trait this is “highly disfavored”\footnote{River Road, supra note 12 at 651.} and could not have possibly been in line with Congressional intent.\footnote{See In re Philadelphia Newspapers, LLC, supra note 11 (Ambro, J., dissenting) (“it would be anomalous for Congress to draft a specific provision, clause (ii), providing protections above and beyond those given to secured creditors under the prior Bankruptcy Act, only to allow clause (iii) to be used to circumvent those protections and return to the precise mechanism used prior to the Code” at 335).} Instead, the court found that “plans could only qualify as ‘fair and equitable’ under Subsection (iii) if they proposed disposing of assets in ways that are not described in Subsections (i) and (ii).”\footnote{River Road, supra note 12 at 652.}
In addition to the statutory interpretation of the applicability of subsection (iii), the Seventh Circuit also reflected on the meaning of “indubitable equivalent.” The court stated that “the ‘indubitable equivalent’ of a creditor’s secured claim depends on the amount of the creditor’s lien and the current value of the secured asset.”\textsuperscript{157} The court noted that special care must be taken in valuing an under-secured creditor’s claim since it can be difficult to establish the market value of the collateral. The \textit{Bankruptcy Code} establishes a judicial valuation\textsuperscript{158} and free market valuation\textsuperscript{159} mechanism. Sales under § 363(k) and § 1129(b)(2)(A) engage the free market valuation mechanism. However, multiple factors can affect the free market valuation of the secured creditors’ collateral.\textsuperscript{160} Therefore, the inclusion of the right to credit bid under these provisions protects secured creditors from undervaluation of their collateral. If the secured creditors underbid, then they still receive the dollar value recovered in the sale. However, if they feel that the collateral will not fetch the fair market price (ie. other opportunistic purchasers are underbidding) then the secured creditors can use their credit to bid on the asset and trump would-be purchasers. Since the proposed plan denied credit bidding, the secured creditors were at a risk of not receiving their indubitable equivalent due to undervaluation of their collateral.\textsuperscript{161}

\textsuperscript{157} River Road, supra note 12 at 650.
\textsuperscript{158} 11 USC § 506(a)(1) (2012).
\textsuperscript{159} 11 USC § 363(k) (2012); 11 USC at § 1129(b)(2)(A) (2012).
\textsuperscript{160} See River Road, supra note 12 at 651, n 6.
\textsuperscript{161} River Road, supra note 12 at 650-651.
Having found that the debtors’ proposed interpretation of subsection (iii) would violate statutory canons of interpretation and would deny the secured creditors the protections intended by the legislature, the court rejected the debtors’ argument. Instead, the Seventh Circuit upheld the Bankruptcy Court’s decision, requiring that a plan constituting an asset sale free of the secured creditors’ claim must entitle the lenders to credit bid.162

This case was a near reversal of the findings in both In re Pacific Lumber Co. and In re Philadelphia Newspapers, LLC. The Seventh Circuit, which gave a unanimous judgment, sided instead with Judge Ambro’s dissenting opinion in In re Philadelphia Newspapers, LLC. The field of bankruptcy had become a tennis match, with credit bidding as the ball being hit from side to side.

4.6 The United States Supreme Court Steps into the Match

Following the Seventh Circuit’s decision, the US Supreme Court granted certiorari.163 Arguably the most important case regarding credit bidding, the US Supreme Court offered the shortest analysis. The Supreme Court noted that:

[t]he ability to credit-bid helps to protect a creditor against the risk that its collateral will be sold at a depressed price. It enables the creditor to purchase the collateral for what it considers the fair market price (up to the amount of its security interest) without committing additional cash to protect the loan.164

162 River Road, supra note 12 at 651-653.
163 Legal Information Institute, online: <http://www.law.cornell.edu/wex/certiorari> (Parties seeking a review of their case petition the US Supreme Court to issue a writ of certiorari. If granted, the writ requires the lower court to deliver its record of the case to the US Supreme Court for review).
164 RadLAX Gateway, supra note 69 at 2070, n 2.
In dismissing the debtors’ position that the plan should be approved under § 1129(b)(2)(A)(iii), the court referred back to traditional canons of statutory interpretation whereby “specific governs the general.”  

While the court acknowledged that the rule usually pertained to addressing contradictions such as specific statutory prohibitions in light of general permissions, the rule could also apply to statutory conflicts that were superfluous in nature. In *D. Ginseng & Sons, Inc. v. Popkin*, the US Supreme Court found that the “[g]eneral language of a statutory provision, although broad enough to include it, will not be held to apply to a matter specifically dealt with in another part of the same enactment.”

It is an old and familiar rule that, where there is, in the same statute, a particular enactment, and also a general one, which, in its most comprehensive sense, would include what is embraced in the former, the particular enactment must be operative, and the general enactment must be taken to affect only such cases within its general language as are not within the provisions of the particular enactment. This rule applies whenever an act contains general provisions and also special ones upon a subject, which, standing alone, the general provisions would include.

Flowing from this analysis, the US Supreme Court found that since the plan attempted to sell the assets free and clear of liens, the plan fell under the more specific provisions of subsection (ii), and as such, the lenders were entitled to credit bid, affirming the judgment of the Court of Appeals.

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166 *RadLAX Gateway*, supra note 69 at 2071.
168 *United States v Chase*, 135 US 255 at 260 (1890) [internal quotations omitted].
The judgment from the Supreme Court marked the end of a three-year debate, with lenders finally winning in regards to secured creditors’ rights. However, the debate also managed to draw much larger issues into the forefront, specifically the merits of credit bidding. The Supreme Court briefly touched on the importance of credit biddings in the Federal Government, which enables the circumvention of requesting more funds from an appropriations authority, but ultimately brushed over the discussion of any other merits to credit bidding, instead pointing to Congress as the appropriate forum for these discussions and not the courts. While the Supreme Court carefully avoided weighing in on the debate, it did acknowledge that these issues were discussed by Judge Ambro in his dissent in *In re Philadelphia Newspapers, LLC*. Perhaps the Court felt that there was no need to delve into a theoretical discussion since it need merely rely on the detailed *Bankruptcy Code* in its interpretation of the law.
CHAPTER 5: CANADIAN INSOLVENCY LEGISLATION

In Canada, the primary statutes regulating bankruptcy and insolvency laws\(^{169}\) are the *Bankruptcy and Insolvency Act (BIA)*\(^{170}\) and the *CCAA*. The *BIA* is a detailed code whereas the *CCAA* is adaptable in nature, thereby enabling the court more flexibility in its application to insolvency cases.\(^{171}\) However, both acts provide “a complimentary and inter-related scheme for dealing with the property of insolvent companies.”\(^{172}\) The *CCAA*’s elasticity has enabled Canadian courts to not only adapt to foreign doctrines applied in cross-border proceedings, but it has also enabled the Canadian courts to adopt foreign practices and incorporate these practices into Canadian insolvency proceedings. The adoption of credit bidding into Canada is one such example. And while the Canadian bankruptcy legislation makes no mention of credit bidding, this void, however, has not hampered the courts from using their broad statutory authority to import credit bidding into insolvency proceedings.\(^{173}\)

Although the *BIA* and the *CCAA* make no specific mention of credit bidding, provisions analogous to the US provisions, which enable a debtor to sell assets during the course of a restructuring or bankruptcy, can be found in both. It should be noted that the *PPSA* and Canadian insolvency legislation operate in tandem once

\(^{169}\) The *Winding-up and Restructuring Act*, RSC 1985, c W-11, as amended and *Farm Debt Mediation Act*, SC 1997, c 21, as amended are not addressed in this thesis.

\(^{170}\) *Bankruptcy and Insolvency Act*, RSC 1985, c. B-3, as amended [*BIA*].


\(^{172}\) Ibid at 10.

\(^{173}\) See *CCAA*, supra note 6, s 11; *Century Services Inc. v Canada (Attorney General)*, 2010 SCC 60 at paras 63-68, [2010] 3 SCR 379 [*Century Services*].
the debtor enters into financial distress.\textsuperscript{174} Hence, it would not be difficult to import credit bidding from insolvency legislation into commercial legislation, and vice versa.

On September 18, 2009, section 36 of the \textit{CCAA} and section 65.13 of the \textit{BIA} came into force. In putting forward its recommendation to enact these provisions, the Senate’s Standing Committee on Banking, Trade and Commerce listed certain pre-requisites to sustain a useful insolvency system. Fairness and predictability were at the forefront of this list.\textsuperscript{175} Of particular note, the Committee emphasized that “fairness and predictability provided by [insolvency] laws increase the amount of credit that is available and help to ensure that it is available at reasonable cost.”\textsuperscript{176}

Section 65.13 of the \textit{BIA} states:

\begin{enumerate*}
\item An insolvent person in respect of whom a notice of intention is filed under section 50.4 or a proposal is filed under subsection 62(1) may not sell or otherwise dispose of assets outside the ordinary course of business unless authorized to do so by a court. Despite any requirement for shareholder approval, including one under federal or provincial law, the court may authorize the sale or disposition even if shareholder approval was not obtained.\textsuperscript{177}
\item In deciding whether to grant the authorization, the court is to consider, among other things, \textit{(a) whether the process leading to the proposed sale or disposition was reasonable in the circumstances};
\end{enumerate*}


\textsuperscript{175} Senate, Standing Committee on Banking, Trade and Commerce, \textit{Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies’ Creditors Arrangement Act} (November 2003) at 5 (Chair Richard H. Kroft) [Standing Committee].

\textsuperscript{176} Standing Committee, \textit{ibid} at 10.

\textsuperscript{177} \textit{BIA}, supra note 170, s 65.13(1).
(b) whether the trustee approved the process leading to the proposed sale or disposition;
(c) whether the trustee filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy;
(d) the extent to which the creditors were consulted;
(e) the effects of the proposed sale or disposition on the creditors and other interested parties; and
(f) whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.\(^{178}\)

(7) The court may authorize a sale or disposition free and clear of any security, charge or other restriction and, if it does, it shall also order that other assets of the insolvent person or the proceeds of the sale or disposition be subject to a security, charge or other restriction in favour of the creditor whose security, charge or other restriction is to be affected by the order.\(^{179}\)

Subsection 65.13(1) allows the court to authorize a sale of the debtor’s assets. Subsection (4) requires the court to take into consideration whether the sale is reasonable in the given circumstances, any effects the sale will have on creditors and whether the consideration received is reasonable. Subsection (7) then enables the court to authorize the sale free and clear of any security interest. Subsection (7) is analogous to § 363(k) of the US Bankruptcy Code, whereby the court may authorize an asset sale free and clear of liens. However, instead of specifically mentioning that creditors may then credit bid on the asset, the BIA states that effects on creditors should be kept in mind and the consideration must be fair and reasonable, even when there is a dissenting creditor.

Similarly, section 36 of the CCAA reads:

\(^{178}\) BIA, supra note 170, s 65.13(4) [emphasis added].
\(^{179}\) BIA, supra note 170, s 65.13(7) [emphasis added].
(1) A debtor company in respect of which an order has been made under this Act may not sell or otherwise dispose of assets outside the ordinary course of business unless authorized to do so by a court. Despite any requirement for shareholder approval, including one under federal or provincial law, the court may authorize the sale or disposition even if shareholder approval was not obtained.  

(3) In deciding whether to grant the authorization, the court is to consider, among other things,

(a) whether the process leading to the proposed sale or disposition was reasonable in the circumstances;
(b) whether the monitor approved the process leading to the proposed sale or disposition;
(c) whether the monitor filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy;
(d) the extent to which the creditors were consulted;
(e) the effects of the proposed sale or disposition on the creditors and other interested parties; and
(f) whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.

(6) The court may authorize a sale or disposition free and clear of any security, charge or other restriction and, if it does, it shall also order that other assets of the company or the proceeds of the sale or disposition be subject to a security, charge or other restriction in favour of the creditor whose security, charge or other restriction is to be affected by the order.

Prior to this 2009 amendment, the court had statutory authority and discretion as to whether or not to approve asset sales. Yet, both the Joint Task Force on Business Insolvency Law Reform and the Standing Committee regarded the non-
exhaustive list of factors in section 36 as providing “substantive direction” to the court in regards to asset sale approvals.

However, one author argues that the courts have “largely ignored s. 36 as a substantive test for whether to approve asset sales,” instead relying on common law criteria.\(^\text{185}\) For example, in *Re Brainhunter Inc.*, Justice Morawetz stated that a distinction should be made between the approval of a sale process and approval of an actual sale.\(^\text{186}\) In approving a sale process, Justice Morawetz found that it is the *Nortel* criteria\(^\text{187}\) that are engaged, whereas section 36 is engaged when approving an actual sale.\(^\text{188}\)

The *Nortel* criteria set out the following when determining whether to approve a sale process in the absence of a plan:

- (a) is a sale transaction warranted at this time?
- (b) will the sale benefit the whole “economic community”?
- (c) do any of the debtors’ creditors have a *bona fide* reason to object to a sale of the business?
- (d) is there a better viable alternative?\(^\text{189}\)

These criteria have since become the cornerstone in deciding whether to approve asset sales, especially in Ontario cases.\(^\text{190}\)


\(^{186}\) *Brainhunter Inc.*, Re, [2009] OJ No 5578 at paras 16-17, 62 CBR (5th) 41.

\(^{187}\) *Nortel Networks Corp.*, Re, [2009] OJ No 3169, 55 CBR (5th) 229 [*Nortel*].

\(^{188}\) *Brainhunter Inc.*, Re, supra note 186 at paras 16-17.

\(^{189}\) *Nortel*, supra note 187 at para 49.

\(^{190}\) See *Clothing for Modern Times Ltd.*, Re, 2011 ONSC 7522, 88 CBR (5th) 329; *Sino-Forest Corp.*, Re, 2012 ONSC 2063, 213 ACWS (3d) 831.
Yet, as Alfonso Nocilla noted, “it is difficult to imagine many cases where a court would hold that s. 36 has not been satisfied at the conclusion of a sale process approved under the Nortel criteria.”191 Accordingly, the courts would generally have to approve the subsequent sale of assets following the approval of the sale process. Hence, if section 36 is not referenced during the approval of the sale process and only at the actual sale, with primary regard being given to the Nortel criteria, then section 36 can hardly be giving the court the “substantive direction” that it was meant to achieve.192 A similar rendering of section 36 is given by the court in White Birch, whereby Justice Mongeon found that section 36 was not limitative nor did all the criteria need to be met in order for the court to approve a sale.193 Instead, he emphasized reviewing the transaction as a whole to verify that the sale is fair and reasonable in the given circumstances.194

The court in Aveos Fleet Performance Inc. was less dismissive in its view of the section 36 factors. It acknowledged that section 36(3) “lists some of the factors that the Court considers before authorizing a sale of assets.”195 The court then went on to state that these factors “largely overlap”196 with the criteria outlined in Royal

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191 Nocilla, supra note 185 at 241.
192 Nocilla, supra note 185 at 241.
193 White Birch, supra note 13 at para 48.
194 White Birch, supra note 13 at para 49.
196 Aveos Fleet Performance Inc., ibid at para 50.
Bank v. Soundair Corp.,\textsuperscript{197} which the court also ought to consider. In summary, while it appears as if the courts have used a combination of jurisprudence and statute in determining whether to approve an asset sale, it is debatable as to whether section 36 is providing the meaningful guidance intended by the legislature.

\textsuperscript{197} Royal Bank v Soundair Corp. (1991), 7 CBR (3d) 1, 4 OR (3d) 1 (Ont CA).
CHAPTER 6: CANADIAN CASE LAW

6.1 Introduction

The Canadian case law pertaining to credit bidding is particularly limited, with few cases discussing the advantages and disadvantages. The poor supply of case law on the matter can most likely be attributed to the fact that there are “few cases in Canada to date in which secured creditors have sought to use a credit bid to acquire the assets of a debtor in the context of a competitive and/or contested auction process.”

Hence, credit bidding has entered into Canada without much inquiry from the courts as to its validity. Credit bidding, in form but not in nomenclature, had been approved in an auction under the CCAA in Brainhunter. Re Canwest Publishing Inc. also discussed credit bidding, albeit under a different guise called “credit acquisition” and in the context of a stalking horse bid.

Yet, the first Canadian case to delve into several aspects of credit bidding was White Birch Paper Holding Company. Subsequent cases have done little to expand on the analysis presented in White Birch. Accordingly, a detailed review of White Birch is essential to understanding the concept of credit bidding as it stands in Canada.

199 Brainhunter, Inc., Re, 2010 ONSC 1035, 70 BLR (4th) 123 (court approved the use of secured notes held by the creditors to be used as “additional consideration in the auction if it were necessary to increase its bid” at para 7) [Brainhunter].
200 Canwest Publishing Inc. (Re), 2010 ONSC 222, [2010] OJ No 188 [Canwest Publishing Inc.].
201 White Birch, supra note 13.
202 See CCM Master, supra note 28 (court stated that the use of credit bid stalking horses “has been recognized by Canadian courts as a reasonable and useful element of a sales process” at para 7).
6.2 White Birch – Quebec Superior Court Decision

6.2.1 Background

On February 24, 2010, White Birch Paper Holding Company and its subsidiaries ("White Birch") filed for protection under the CCAA. White Birch is a Nova Scotia company with operations located primarily in Quebec. Its assets in Quebec included three pulp and paper mills. A fourth mill was located in the state of Virginia and operated by Bear Island Paper Company LLC ("Bear Island"), an affiliate of White Birch.

While White Birch had a market share of nearly 12% of the newsprint industry with annual net sales reaching $667 million, the recent economic downturn coupled with the ever-expanding usage of online media left White Birch unable to meet its financial obligations. White Birch's principal debt obligations consisted of a First Lien Term Loan with US$438 million in principal and interest owed, a Second Lien Term Loan with US$104 million in principal and interest owed, and a Revolving Asset-Based Facility with US$50 million in principal and interest outstanding. Additionally, White Birch was involved in several interest rate swaps that left them owing approximately US$58 million.

204 Ibid at paras 16-17.
205 Ibid at paras 44, 47.
206 Ibid at para 56-57.
With a liquidity crisis looming, White Birch sought an Initial Order under the *CCAA* on February 24, 2010. On the same day, Bear Island filed for protection under Chapter 11 of the US *Bankruptcy Code*.

On April 28, 2010, the US Bankruptcy Court for the Eastern District of Virginia approved the Sale and Investor Solicitation Process for White Birch's assets. The Quebec Superior Court issued a similar order the following day. On March 26, 2010, the US Bankruptcy Court issued an order recognizing the *CCAA* proceedings as the "foreign main proceeding." Hereafter, White Birch and Bear Island will be referred to as the "WB Group."

Several third parties expressed interest in the WB Group assets, which led to an Asset Sale Agreement between the WB Group and BD White Birch Investment LLC ("BD White Birch"). BD White Birch was to acquire the assets through a stalking horse bid process. Both the US Bankruptcy Court and the Quebec Superior Court issued orders approving the Asset Sale Agreement and the stalking horse bid process, with only a few modifications made by the Quebec Superior Court. On the final day of bidding, September 17, 2010, Sixth Avenue Investment Co. LLC ("SAI") submitted a bid.

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On September 21, 2010, the auction process began with the winning bid coming from BD White Birch at US$236,052,825.00. SAI’s bid offered US$500,000 less. However, the more important distinction between SAI’s bid and BD White Birch’s bid stems from the fact that BD White Birch’s winning bid contained a credit bid valued at US$78 million whereas SAI offered the additional US$78 million in cash.

Both BD White Birch and SAI were former lenders of the WB Group. BD White Birch was composed of various lenders from their First Lien Credit Agreement, whom were aggregately owed 65% of the First Lien debt. The First Lien debt was secured against the debtor’s fixed assets, and as “majority lenders” under the First Lien Credit Agreement, the BD White Birch group was entitled to make certain decisions including the right to use their security in the fixed assets in a credit bid.

SAI was also composed of lenders from the First Lien Credit Agreement, however they only held approximately 10% of the debt owed. As minority lenders, they were not entitled to use credit bidding as a component of their submitted bid.

The debtors then sought an order to approve the asset sale to BD White Birch, while SAI simultaneously requested that the application to approve the sale be dismissed and SAI be declared the winning bidder.
6.2.2 SAI’s Arguments Against BD White Birch’s Credit Bid

In SAI’s objections against the sale to BD White Birch, SAI argued that as agent for the First Lien lenders, BD White Birch lacked the proper authority to credit bid under the First Lien Credit Agreement since it had not obtained the minority lenders’ approval to credit bid.208 SAI went on to say that the credit bid, in addition to the US$4.5 million in cash BD White Birch attributed to the fixed assets, essentially allowed BD White Birch to take possession of the US mill for a value not exceeding the US$4.5 million offered.209 SAI claimed that “[b]y keeping the U.S. fixed assets for themselves at the expense of the other First Lien Lenders, [BD White Birch] clearly placed themselves in a conflict of interest and breached their fiduciary duties as agents...”210 SAI also objected to the importation of credit bidding, a US construct, into Canadian insolvency proceedings. They argued that § 363(k) was contained in the US Bankruptcy Code and therefore could not operate in Canada. As there is no equivalent of § 363(k) in the CCAA or in any Quebec statutes, the secured creditor, or in this case BD White Birch, could therefore only “sue on the covenant, sell the collateral or take all of the collateral in payment of all of the debt secured – none of which [was] happening here.”211

208 Latham, supra note 198 at 100.
209 White Birch, supra note 13 (Contestation of the Debtors’ Motion to Approve the Sale of Substantially All of the WB Group’s Assets and Cross-Demand by the Intervening Parties) (23 September 2010), Montreal 500-11-038474-108 (QC Sup Ct) at para 18, online: Ernst & Young Canada <http://documentcentre.eycan.com/eycm_library/128/English/Canadian%20Proceedings/Motion%20Materials/Motion%20to%20approve%20a%20sale%20of%20substantially%20all%20assets%20and%20related%20motions/Contestation%20Sixth%20AVE.PDF >.
210 Ibid at para 19.
211 Ibid at para 28.
6.2.3 BD White Birch Pushes Back

In response, BD White Birch submitted that the First Lien Credit Agreement\(^\text{212}\), the US First Lien Security Agreement\(^\text{213}\) and the Canadian Security Agreement\(^\text{214}\) entitled the “majority lenders,” as defined under Section 1.1 of the First Lien Credit Agreement\(^\text{215}\), to credit bid on behalf of all First Lien Lenders, including the minority lenders making up the SAI group.

In arguing that the right to credit bid was not inconsistent with the terms of the CCAA, BD White Birch referenced *Re Maax Corp.*\(^\text{216}\), *Brainhunter*\(^\text{217}\) and *Re Eddie

\(^{212}\) *White Birch*, *supra* note 13 (First Lien Credit Agreement cited in Intervention and Memorandum of Arguments of BD White Birch Investment LLC) (23 September 2010), Montreal 500-11-038474-108 (QC Sup Ct), online: Ernst & Young Canada <http://documentcentre.eycan.com/eycm_library/128/English/Canadian%20Proceedings/Motion%20Materials/Motion%20to%20approve%20%20of%20substantially%20all%20assets%20and%20related%20motions/Intervention%20BDWBI.pdf> (*Each Lender hereby irrevocably designates and appoints the Agents as the agents under this Agreement and the other Loan Documents, and each Lender irrevocably authorizes each Agent, in such capacity, to take such action on its behalf under the provisions of the Agreement and the other Loan Documents...*” at para 41) [emphasis in Intervention].

\(^{213}\) *White Birch*, *supra* note 13 (US First Lien Security Agreement cited in Intervention and Memorandum of Arguments of BD White Birch Investment LLC) (23 September 2010), Montreal 500-11-038474-108 (QC Sup Ct), online: Ernst & Young Canada <http://documentcentre.eycan.com/eycm_library/128/English/Canadian%20Proceedings/Motion%20Materials/Motion%20to%20approve%20%20of%20substantially%20all%20assets%20and%20related%20motions/Intervention%20BDWBI.pdf> [*[the Agents] shall be entitled, for the purposes of bidding and making settlement or payment of the purchase price for all or any portion of the [Collateral] sold at any such sale made in accordance with the UCC, to use and apply any of the Secured Obligations as a credit on account of the purchase price for any [Collateral] payment to the US Collateral Agent at such sale...*” at para 48) [emphasis in Intervention].

\(^{214}\) *White Birch*, *supra* note 13 (Canadian Security Agreement cited in Intervention and Memorandum of Arguments of BD White Birch Investment LLC) (23 September 2010), Montreal 500-11-038474-108 (QC Sup Ct), online: Ernst & Young Canada <http://documentcentre.eycan.com/eycm_library/128/English/Canadian%20Proceedings/Motion%20Materials/Motion%20to%20approve%20%20of%20substantially%20all%20assets%20and%20related%20motions/Intervention%20BDWBI.pdf>.

\(^{215}\) *Supra* note 212.

\(^{216}\) *Maax Corp., Re*, 2008 CarswellQue 15021 (Qc Sup Ct).

\(^{217}\) *Brainhunter*, *supra* note 199.
**Bauer of Canada, Inc.** In all three cases, the courts approved bidding procedures, which encompassed credit bidding. Furthermore, *Re Maax Corp.* was a Quebec Superior Court case, which demonstrated that credit bidding was in fact accepted not only by the federally operating CCAA, but also at the Quebec provincial level. Several provisions of the Quebec *Code of Civil Procedure* were also cited supporting this premise.

### 6.2.4 The Court’s Opinion

As noted by Joe Latham et al, the court in *White Birch* relied heavily on the various security documents provided by BD White Birch in supporting BD White Birch’s ability to credit bid rather than any specific legislation. Justice Mongeon referred to the Motion to Approve the Sale of the Assets which cites paragraph 24 of the Sale and Investor Solicitation Process, which states:

> The DIP Agent and First Lien Term Agent, on behalf of the lenders under the White Birch Dip Facility and the WB Group’s first lien term loan lenders, respectively, shall be permitted, in their sole discretion, to credit bid up to the full amount of any allowed secure claims under the White Birch DIP Facility and the first lien term loan agreement, respectively, to the extent permitted under section 363(k) of the Bankruptcy Code and other applicable law.

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218 Ed**1**die Bauer of Canada, Inc. (Re), [2009] OJ No 3784, 57 CBR (5th) 241 (Bidding Procedures).

219 *White Birch*, *supra* note 13 at n 7.

220 *Code of Civil Procedure*, arts 689, 730 CCP.

221 Latham, *supra* note 198 at 102.

222 *White Birch*, *supra* note 13 (Motion to Approve the Sale of Substantially All the WB Group’s Assets) (23 September 2010), Montreal 500-1 1-038474-108 (QC Sup Ct) at para 7, online: Ernst & Young Canada <http://documentcentre.eycan.com/eycm_library/128/English/Canadian%20Proceedings/Motion%20Materials/Motion%20to%20Approve%20a%20sale%20of%20substantially%20all%20assets%20and%20related%20motions/Motion%20to%20Approve%20the%20Sale%20of%20Substantially%20All%20of%20the%20WB%20Group’s%20Assets%20and%20List%20of%20Exhibits.pdf>.

223 *Supra* note 207 at para 24 [emphasis added].
A similarly worded phrase was also included in the debtors’ motion for approval of the bidding procedure. Justice Mongeon reasoned that “other applicable law” could “tolerate the inclusion of similar rules of procedure in the province of Quebec.”\textsuperscript{224} Expanding on this, Justice Mongeon stated that credit bidding was not foreign to Quebec, citing both the Quebec \textit{Code of Civil Procedure}\textsuperscript{225} and case law\textsuperscript{226} in support of this conclusion. This marks an important difference between the US and Canada, where credit bidding is a \textit{right}\textsuperscript{227} found in the US \textit{Bankruptcy Code} versus the \textit{ability} to credit bid in the Canadian context which was established through credit agreements and security documents.

Having noted that the use of credit bidding by BD White Birch was indeed permissible, Justice Mongeon then addressed the appropriate dollar value of a credit bid. He stated:

\begin{quote}
[I]t goes without saying that the amount of the credit bid should not exceed, but should be allowed to go as, high as the face value amount of the credit instrument upon which the credit bidder is allowed to rely. The credit bid should not be limited to the fair market value of the corresponding encumbered assets. It would then be just impossible to function otherwise because it would require an evaluation of such encumbered assets, a difficult, complex and costly exercise.\textsuperscript{228}
\end{quote}

Putting to rest the valuation argument, Justice Mongeon stated that if the “bitter bidder” had taken issue with the bidding process, the issue should have been

\begin{footnotes}
\item[224] \textit{White Birch}, supra note 13 at para 31.
\item[225] \textit{Supra} note 220, arts 689, 730.
\item[226] See \textit{Cie Montreal Trust c Jori Investments Inc.}, JE 80-220, 1980 CarswellQue 85 (Qc Sup Ct); \textit{EugèneMarcouxInc. c Côté}, [1990] R]Q 1221 (Qc CA).
\item[227] \textit{Supra} note 52 (except for where the court “for cause orders otherwise”).
\item[228] \textit{White Birch}, supra note 13 at para 34.
\end{footnotes}
addressed at an earlier time when the debtor had brought forth the motion to approve the auction process. Justice Mongeon went on to say that the process could not be simply invalidated on the basis of credit bidding once the bidding process had been approved, bids had been placed and a winner had been decided. To do otherwise would be the equivalent of “a complete eradication of all proceedings and judgments rendered to this date with respect to the Sale of Assets authorized in this file since May/June 2010...” The mere fact that credit bidding had been an authorized option available to BD White Birch, as found in the prior motions and agreements, should have alerted SIA to the notion that BD White Birch may in fact avail itself of credit bidding and any such issue SIA then may have had with credit bidding should have been dealt with at an earlier stage in the form of a proposal to modify bidding procedures. However, no such step was taken and failure to recognize credit bidding as a tool that BD White Birch could use was not an excuse in and of itself to justify an unfair auction nor could it be used to deem SIA the winning bidder. Even when SIA had learned of BD White Birch’s credit bid, SIA continued to engage in the auction process. Justice Mongeon found that SIA’s continued involvement in the auction was evidence that SIA did not actually take issue with the credit bid component, but instead with the outcome as the losing bidder.

The final portion of Justice Mongeon’s reasons dealt with the newly added section 36 of the CCAA. Section 36 reads:

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229 White Birch, supra note 13 at para 39.
36. (1) A debtor company in respect of which an order has been made under this Act may not sell or otherwise dispose of assets outside the ordinary course of business unless authorized to do so by a court. Despite any requirement for shareholder approval, including one under federal or provincial law, the court may authorize the sale or disposition even if shareholder approval was not obtained.

(2) A company that applies to the court for an authorization is to give notice of the application to the secured creditors who are likely to be affected by the proposed sale or disposition.

(3) In deciding whether to grant the authorization, the court is to consider, among other things,

(a) whether the process leading to the proposed sale or disposition was reasonable in the circumstances;

(b) whether the monitor approved the process leading to the proposed sale or disposition;

(c) whether the monitor filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy;

(d) the extent to which the creditors were consulted;

(e) the effects of the proposed sale or disposition on the creditors and other interested parties; and

(f) whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.

(4) If the proposed sale or disposition is to a person who is related to the company, the court may, after considering the factors referred to in subsection (3), grant the authorization only if it is satisfied that

(a) good faith efforts were made to sell or otherwise dispose of the assets to persons who are not related to the company; and

(b) the consideration to be received is superior to the consideration that would be received under any other offer made in accordance with the process leading to the proposed sale or disposition.

(5) For the purpose of subsection (4), a person who is related to the company includes

(a) a director or officer of the company;

(b) a person who has or has had, directly or indirectly, control in fact of the company; and
(c) a person who is related to a person described in paragraph (a) or (b).

(6) The court may authorize a sale or disposition free and clear of any security, charge or other restriction and, if it does, it shall also order that other assets of the company or the proceeds of the sale or disposition be subject to a security, charge or other restriction in favour of the creditor whose security, charge or other restriction is to be affected by the order.

(7) The court may grant the authorization only if the court is satisfied that the company can and will make the payments that would have been required under paragraphs 6(4)(a) and (5)(a) if the court had sanctioned the compromise or arrangement.

Justice Mongeon noted that the list of reasons for the court to consider when authorizing the disposition of assets was neither exhaustive nor limitative. He instead found that the “Court has to look at the transaction as a whole and essentially decide whether or not the sale is appropriate, fair and reasonable.” In support of this statement, Justice Mongeon referred to both Madam Justice Pepall in *Canwest* and Justice Morawetz in *Nortel Networks*. Quoting from Madam Justice Pepall:

> The proposed disposition of assets meets the Section 36 CCAA criteria and those set forth in the *Royal Bank v. Soundair Corp.* decision. Indeed, to a large degree, the criteria overlap. The process was reasonable as the Monitor was content with it. Sufficient efforts were made to attract the best possible bid; the SISP was widely publicized; ample time was given to prepare offers; and there was integrity and no unfairness in the process...The effect of the proposed sale on other interested parties is positive. Amongst other things, it provides for a going concern outcome and significant recoveries for both the secured and unsecured creditors.

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230 CCAA, supra note 6 [emphasis from Justice Mongeon’s reasons in *White Birch*].

231 *White Birch*, supra note 13 at para 49.

232 *Canwest Publishing Inc. (Re)*, 2010 ONSC 2870, [2010] OJ No 2190 [*Canwest*].

233 *Nortel Networks Corp. (Re)*, [2009] OJ No 4487, 56 CBR (5th) 224 [*Nortel Networks*].

234 *Canwest*, supra note 232 at para 13 [footnote omitted].
In *Nortel Networks*, Justice Morawetz restated the *Royal Bank v. Soundair Corp.* criteria as follows:

The duties of the Court in reviewing a proposed sale of assets are as follows:

1) It should consider whether sufficient effort has been made to obtain the best price and that the debtor has not acted improperly;

2) It should consider the interests of all parties;

3) It should consider the efficacy and integrity of the process by which offers have been obtained;

4) and it should consider whether there has been unfairness in the working out of the process.\(^{235}\)

Concluding his reasons, Justice Mongeon then granted the Motion to Approve the Sale.

**6.3 White Birch – Quebec Court of Appeal Decision**

SAI subsequently sought leave to appeal Justice Robert Monegon's decision granting the Sale Order to BD White Birch.\(^{236}\) SAI argued that Justice Mongeon erred in treating the bids the same by looking only at the nominal value offered by each bidder. Instead, SAI claimed that the bids should have been reviewed in accordance to what they offered to each class of creditors, specifically unsecured creditors. Furthermore, the applicants contended that credit bidding had been used unjustly since the assets that BD White Birch’s claim was secured against were worthless.

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\(^{235}\) *Nortel Networks*, *supra* note 233 at para 35.

The applicants also asserted that Justice Mongeon erred in his application of subsection 36(3)(e) of the CCAA, overlooking BD White Birch’s positing of their own interests above all others, including other First Lien Lenders for which BD White Birch was a sub-agent.

In addressing the applicants’ first argument regarding the validity of the credit bid, Justice Dalphond, J.A. recited a near identical rationale as found in Justice Mongeon’s reasons. Justice Dalphond reasoned that the rules of the bidding process had been decided and approved long before SAI had taken issue with credit bidding. Moreover, to assert that the fixed assets were worthless contradicted SAI’s prior valuation of the assets whereby they had attributed US$35.3 million of the bid to them. BD White Birch attributed US$78 million to the fixed assets, which was the value of the credit bid, and an additional US$4.5 million in cash. Holding that there was no error by Justice Mongeon, and acknowledging that a new bidding process would unduly hinder the reorganization process, Justice Dalphond dismissed the motion for leave to appeal.

6.4 Credit Bidding After White Birch and Beyond the CCAA

Following the decision in White Birch, the courts have been more concerned with the fairness and transparency of the sales process involving stalking horse credit bids rather than delving into the validity of credit bidding based on its own merits.
The courts in *CCM Master*237 and *PCAS Patient Care*,238 which dealt with stalking horse credit bids, looked to the criteria laid out in *Royal Bank v. Soundair Corp.*,239 when considering whether to approve a sale of the debtors’ assets. This criteria, which was also followed by the court in *White Birch*, entails the court reviewing:

(i) the fairness, transparency and integrity of the proposed process;
(ii) the commercial efficacy of the proposed process in light of the specific circumstances facing the receiver; and,
(iii) whether the sales process will optimize the chances, in the particular circumstances, of securing the best possible price for the assets up for sale.240

Yet, these criteria apply to all proposed sales by a court-appointed receiver and not just to those sales involving credit bidding. When credit bidding is involved, the courts in *CCM Master* and *PCAS Patient Care* both quoted Pamela Huff’s summary of additional considerations to be regarded when approving a sale, as derived from *Canwest*:

To be effective for such stakeholders, the credit bid had to be put forward in a process that would allow a sufficient opportunity for interested parties to come forward with a superior offer, recognizing that a timetable for the sale of a business in distress is a fast track ride that requires interested parties to move quickly or miss the opportunity. The court has to balance the need to move quickly, to address the real or perceived deterioration of value of the business during a sale process or the limited availability of restructuring financing, with a realistic timetable that encourages and does not chill the auction process.241

237 *CCM Master*, supra note 28.
238 *PCAS Patient Care Automation Services Inc., Re, 2012 ONSC 2840, 94 CBR (5th) 69 [PCAS Patient Care]*.
239 *Royal Bank v Soundair Corp.*, supra note 197.
Despite touching on issues such as chilling, the courts failed to undertake any further analyses of credit bidding, instead relying on generalized criteria from *Royal Bank v. Soundair Corp.* and Canwest’s pre-packaged credit bidding factors to approve the use of stalking horse credit bids as it applied to their respective cases. Subsequent cases that have dealt with the traditional notion of credit bidding, without a stalking horse element, have merely cited *White Birch* in approving the use of credit bidding under the *CCAA*.\(^\text{242}\)

While credit bidding has been employed under *CCAA* proceedings as seen in *White Birch* and under the *BIA* in *Re Parlay Entertainment Inc.*,\(^\text{243}\) it has not been limited to a strict insolvency context in Canada. Both *CCM Master* and *Canrock* are cases involving receiverships. In *Canrock*, the secured creditor obtained a court order appointing a receiver. After reviewing several offers, the receiver sought a court order approving a sale of the debtor’s assets, with the purchase agreement containing a credit bid component. While the court initially took issue with a lack of valuation of certain assets,\(^\text{244}\) the subsequent appraisal of these assets was a factor in the court granting approval of the sale.\(^\text{245}\) Similar to the court in *CCM Master*, the court in *Canrock* approved a sales process using the *Royal Bank v. Soundair Corp.* criteria without further reviewing the aspects of credit bidding. Hence, *White Birch*’s examination of the validity of credit bidding continues to be the predominant exposition on this subject in Canada to date.

\(^{242}\) See *Aveos Fleet Performance Inc.*, supra note 195.

\(^{243}\) *Parlay Entertainment Inc., Re*, 2011 ONSC 3492, 81 CBR (5th) 58.


\(^{245}\) *Canrock*, supra note 28.
CHAPTER 7: TIME TO ADAPT?

7.1 Introduction

Humans, as a species, are in a constant state of change. We do not sit idly by watching the world turn, but instead invent, discover and modify the society we live in. Recognizing that we do not live in a static environment, Canada's legal system must be able to adapt or risk becoming obsolete. Amending and revising legislation is an essential requirement needed for the evolution of law. Chapter 3 of this thesis has already detailed the benefit credit bidding has to offer secured creditors in that it prevents undervaluation of the collateral. The question that remains is whether or not credit bidding has a place in Canadian legislation. To put it another way, should secured creditors be entitled to credit bid through detailed legislation or should it remain subject to judicial discretion?

Comprehensive legislation is, by definition, meant to provide a conclusive and sound application of the law. The definitive structure of highly detailed laws, such as the US Bankruptcy Code, provides creditors and debtors with some security as to how a bankruptcy proceeding would unfold in the event that a debtor becomes insolvent. In essence, it creates a sturdy “box.” At first glance, the US’ rigid, structured bankruptcy regime would appear to offer parties more certainty in approaching bankruptcy applications. However, this sound structure can be deceiving and is not without its own pitfalls.

246 Eisenberg, supra note 5 at 5.
The rigid structure and precise wording found in the US legislation requires the courts to apply the letter of the law as stated, no more no less. Within this structure, a witty party may find an alternative means of restructuring not previously considered. The creative thinking and clever legal maneuvering which results from “thinking outside the box” can leave courts trapped. The string of recent credit bidding decisions in the US is an example of how structured legislation intended for clarity unintentionally became the source of uncertainty.

The Canadian insolvency arena is faced with two juxtaposed pieces of legislation; the verbose BIA and the succinct but brief CCAA. Recent amendments have attempted to harmonize these two statutes, including the addition of similar provisions in respect to sale of assets.247 Both the BIA and CCAA have provisions in place that enable a debtor to attempt a reorganization, a key difference between the two acts being the degree of flexibility and judicial discretion.248 This thesis focuses on the more flexible reorganization regime under the CCAA and the bankruptcy provisions as provided in the BIA.

Under the CCAA, plans of reorganization are not required to fit into any predetermined box and tied with a bow. Instead, there is no proverbial box at all. The CCAA enables the courts to maintain an open mind, looking more towards the fairness and reasonableness of any proposed plan rather than whether it fits into a

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247 An Act to amend the Bankruptcy and Insolvency Act, the Companies’ Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, 2005, SC 2007, c 36, ss 27, 78 [An Act to amend].

248 Century Services, supra note 173 at para 14.
preset mold.\textsuperscript{249} One might describe it as being more fluid in nature, allowing the courts to adapt quickly with every new practice. While it may seem that such a fluid regime would lend itself to being unpredictable, the vague nature of the legislation permitting judges to exercise some degree of subjectivity, it is also more reliable. Broad tests and standards, such as the concept of “fair and reasonable,”\textsuperscript{250} ensure that parties cannot cleverly devise novel deals that fit within the letter of the law but clearly betray what is intended by Parliament. The \textit{CCAA} provides a certain amount of leeway in enabling a judge to interpret what is indeed “fair and reasonable,” which thereby creates the certainty that is desired. The courts’ ability to exercise this judicial discretion is based on both its statutory authority, as provided in the \textit{CCAA},\textsuperscript{251} and its inherent jurisdiction, as “derived from its nature as a court of law.”\textsuperscript{252} It is the exercising of judicial discretion that has enabled the \textit{CCAA} to evolve to meet modern business needs and to ultimately include credit bidding in \textit{CCAA} proceedings.\textsuperscript{253} This flexibility is intrinsic to the proper operation of the statute, for without it, the \textit{CCAA} would not be able to respond to reorganizations of increasing


\textsuperscript{250} \textit{Canadian Red Cross Society (Re),} [1998] OJ No 3306, 5 CBR (4th) 299 (whether the purchase price of assets was fair and reasonable under the \textit{CCAA} plan); \textit{AbitibiBowater inc. (Arrangement relatif à),} 2010 QCCS 4450, [2010] QJ No 9504 (court discusses importance of a \textit{CCAA} plan being fair and reasonable).

\textsuperscript{251} \textit{CCAA, supra} note 6, s. 11 (“[d]espite anything in the \textit{Bankruptcy and Insolvency Act} or the \textit{Winding-up and Restructuring Act}, if an application is made under this Act in respect of a debtor company, the court, on the application of any person interested in the matter, may, subject to the restrictions set out in this Act, on notice to any other person or without notice as it may see fit, make any order that it considers appropriate in the circumstances”).

\textsuperscript{252} Madam Justice Georgina R. Jackson & Dr. Janis Sarra, “Selecting the Judicial Tool to get the Job Done: An Examination of Statutory Interpretation, Discretionary Power and Inherent Jurisdiction in Insolvency Matters” in Janis P. Sarra, ed, \textit{Annual Review of Insolvency Law 2007} (Toronto: Thomson Carswell, 2008) 41 at 76.

\textsuperscript{253} \textit{Century Services, supra} note 173 at para 58; See also Jackson, \textit{supra} note 252 at 71-73.
complexity. The  *BIA*, comparatively, is less flexible. As a more codified statute, the courts may still exercise judicial discretion as derived from both statutory interpretation and inherent jurisdiction, but to a lesser extent.

Given the ability to use both statutory interpretation and inherent jurisdiction to exercise broad judicial discretion in filling-in any perceived gaps in legislation, one could argue that the Canadian insolvency regime is the ideal legal system, in that it permits courts to adapt quickly to meet societal needs. Yet, in its current state in Canada, credit bidding is hardly a *right* that has been guaranteed in common law. The courts in *Canwest* and *White Birch* have found credit bidding to be *valid* as an approved bidding procedure, but they did not go so far as to state that it was a right. The court in *White Birch* relied heavily on the fact that the bidding procedures had made mention of the lenders’ option to credit bid, in addition to the security agreements, as support in their decision to approve the lenders as the winning bidder. Hence, an argument could be made that the outcome in *White Birch* would have been notably different if credit bidding had not been included in the court-approved bidding procedures or the security documents.

Subsequent cases have merely noted that credit bidding has been “recognized by Canadian courts as a reasonable and useful element of a sales process.” As seen similarly in *White Birch*, these cases deal with credit bidding in circumstances that

254 *Century Services, supra* note 173 at paras 14, 21.
255 *BIA, supra* note 170, s 183(1).
256 *Jackson, supra* note 252 at 78-82.
257 *CCM Master, supra* note 28 at 7; See also *PCAS Patient Care, supra* note 238 at 17.
required court-ordered approval of the sale and bidding procedures prior to the submission of a credit bid. While *Brainhunter* did contemplate the use of a credit bid that was not pre-approved by the court, ultimately the credit bid was not employed as it was merely an additional resource to outbid other interested parties. Hence, most insolvency cases involving credit bidding have validated its use in the context of court-approved stalking horse credit bids. The courts have not yet weighed in on whether secured lenders are entitled to credit bid irrespective of the pre-approved sales process. That is to say, the question is open for debate as to whether a secured lender has the right to credit bid its debt at an asset sale where the court has not approved its use in the bidding procedures. Without specific legislation to state otherwise, secured creditors have no guarantee that it may use credit bidding without explicit approval by the court. *Brainhunter* seems to stand for the proposition that credit bidding is *allowable*. The emphasis the court in *White Birch* placed on both the security documents and the court-approved bidding procedures in supporting BD White Birch’s credit bid, and other case law having approved credit bidding via “stalking horse credit bids” prior to the actual sales process commencing,\(^{258}\) also point to the conclusion that credit bidding is *allowable*, but certainly not guaranteed. While the courts have used their broad statutory authority to import credit bidding into insolvency proceedings, credit bidding has no statutory basis in Canada and is, thus, subject to the judicial discretion of the courts. Be this as it may, it is legislation that has created defined hierarchies of

\(^{258}\) See *CCM Master*, *supra* note 28; *PCAS Patient Care*, *supra* note 238.
secured creditors and an equitable method of distributing a bankrupt’s estate.\textsuperscript{259}

Furthermore, it is legislation that sets out rights and remedies for secured creditors.\textsuperscript{260} Hence, arguably, it is legislation that should be amended when considering the addition of credit bidding as a secured creditor’s right.

\subsection*{7.2 Embedding Credit Bidding in Canadian Insolvency Legislation}

Credit bidding, as discussed in Chapter 3, was added to the US \textit{Bankruptcy Code} largely in response to the \textit{In re Pine Gate} case, whereby the debtor forced secured creditors to take a payout on the collateral based on an appraisal rather than allowing the creditors to take ownership of the collateral.\textsuperscript{261} The legislature subsequently amended the legislation to include credit bidding in regards to cramdown plans that contemplated the sale of the secured creditors’ collateral free and clear of liens\textsuperscript{262} and in the bankruptcy provision that involves a liquidation of the debtor’s estate.\textsuperscript{263} These provisions are aimed at avoiding the sale of the collateral at an undervalued rate due to a depressed market or other external factors to the detriment of the secured creditor. Although cramdown plans are foreign to Canadian insolvency proceedings, liquidation of the debtor’s estate can take place under both the \textit{CCAA}\textsuperscript{264} and \textit{BIA}.\textsuperscript{265} Accordingly, § 363(k), which pertains

\begin{itemize}
\item \textsuperscript{259} Frank Bennett, \textit{Bennett on Bankruptcy}, 10th ed (Toronto: CCH Canadian Limited, 2008) at 32.
\item \textsuperscript{260} \textit{PPSA}, supra note 15; \textit{BIA}, supra note 170; \textit{CCAA}, supra note 6.
\item \textsuperscript{261} \textit{In re Pine Gate}, supra note 43.
\item \textsuperscript{262} 11 USC at § 1129(b)(2)(A)(ii).
\item \textsuperscript{263} 11 USC § 363(k) (2012).
\item \textsuperscript{264} \textit{CCAA}, supra note 6, s 36.
\item \textsuperscript{265} \textit{BIA}, supra note 170, s 65.13.
\end{itemize}
to credit bidding under liquidation of a debtor’s estate, could be reviewed in light of 
the liquidation provisions in Canadian insolvency proceedings.

Despite the fact that credit bidding serves to further legislative goals in the US that 
are not necessarily applicable to Canadian legislative goals, adding credit bidding to 
the Canadian insolvency regime brings the bankruptcy schemes of both the US and 
Canada into closer harmony. By minimizing the differences between these two 
regimes, harmonization smooths a path for future cross-boarder insolvency 
proceedings. Moreover, it appears as if harmonization of the two regimes is already 
slowly taking place. For example, under a Chapter 11 plan of reorganization, the 
absolute priority rule\textsuperscript{266} dictates that “no holders of junior claims or interests can 
receive any value in the plan unless senior classes are being paid in full.”\textsuperscript{267} 
Although Canada is without an absolute priority rule, recent case law\textsuperscript{268} and 
commentary\textsuperscript{269} suggests that the Canadian insolvency scheme is aligning more 
closely with that of the US, including the subordination of equity claims.\textsuperscript{270} 
Furthermore, recent amendments\textsuperscript{271} to the \textit{BIA} and \textit{CCAA} have resulted in similar

\textsuperscript{266} 11 USC § 1129(b)(2)(2012).
\textsuperscript{267} Daniel Keating, "RadLAX Revisited: A Routine Case of Statutory Interpretation or a Sub Rose 
\textsuperscript{268} See \textit{Canadian Airlines Corp., Re,} 2000 ABQB 442, [2000] AWLD 654 (“[w]here a company is 
insolvent, only the creditors maintain a meaningful stake in its assets” at para 143); \textit{Laidlaw Inc., Re,} 
[2002] OJ No 947, 34 CBR (4th) 72 (“the shareholders are very significantly underwater...it is 
realistic to note that the creditors will take a very severe “haircut” so that they will not come close to 
being paid out in full...under all foreseeable circumstances, it appears that the shareholders have no 
economic interest to protect” at para 2).
\textsuperscript{269} Shauna Towriss, “Through the Lens of Insolvency: Shareholder Equity in CCAA Restructurings” in 
533, 536-539.
\textsuperscript{270} Towriss, \textit{ibid}.
\textsuperscript{271} \textit{An Act to amend, supra} note 247, ss 49, 71.
equity subordination clauses. While discussing the merits of the US absolute priority rule and cramdown provisions in a Canadian context are beyond the scope of this thesis, it bears mentioning that if Canada should choose to adopt these principles in the future in an effort to further harmonize the two insolvency regimes, the legislation of credit bidding in Canada is a logical initiative. Currently, however, with the exception of the subordinated equity claims, the fact remains that the absolute priority rule and cramdown provisions that exist in US legislation are, contrastingly, mostly absent in Canadian statutes, which presents challenges for cross-border insolvencies. Adding credit bidding to Canadian legislation is one step that can align both regimes while also indirectly furthering the absolute priority rule in Canada. Enabling secured creditors to bid on their collateral frustrates other would-be bidders, including equity holders, from purchasing the collateral at a deflated value, in essence, furthering the objective of the absolute priority rule.

Secondly, credit bidding eliminates the necessity of raising additional capital in order to bid on collateral. This is of primary importance for secured creditors facing difficulty in securing short term financing and in cases where the additional

272 See BIA, supra note 170, s 140.1 (“[a] creditor is not entitled to a dividend in respect of an equity claim until all claims that are not equity claims have been satisfied”); CCAA, supra note 6, s 22.1 (“[d]espite subsection 22(1), creditors having equity claims are to be in the same class of creditors in relation to those claims unless the court orders otherwise and may not, as members of that class, vote at any meeting unless the court orders otherwise”).


274 Resnick, supra note 55 at 355.
advances in capital would require lender syndicate approval.\footnote{Note} As noted by Alan Resnick, in today's modern financial world, it has become increasingly common for lenders to be consolidated in the form of a lender syndicate and to be represented by an agent.\footnote{Note} In cases involving a sale of the lender syndicate's collateral, it could prove difficult to obtain the necessary lender syndicate consent to contribute additional capital towards the purchase of the assets.\footnote{Note} Furthermore, without a system in place to compel the members of the syndicate to furnish the necessary funds to make the asset purchase, the option of participating in an auction might be out of the question.\footnote{Note} Accordingly, credit bidding provides an alternative recourse for secured creditors when lender syndicates are involved.

Finally, and arguably most importantly, credit bidding serves as an alternative means for secured creditor recovery and provides the secured creditors the ability to bid on the collateral for a value they deem to be fair.\footnote{Note} Given the aforementioned reasons, an argument can be made that credit bidding should be enshrined in legislation as a secured creditor's right.

\section*{7.3 Purposes of Canadian and US Bankruptcy Legislation}

Conceding that credit bidding has not been accepted into common law as a secured creditor's \textit{right}, legislation would be required to cement credit bidding as a

\footnote{Note}{See Brad B. Erens & David A. Hall, "Secured Lender Rights in 363 Sales and Relates Issues of Lender Consent" 18 Am Bankr Inst L Rev 535 at 563-564.}
\footnote{Note}{Resnick, \textit{supra} note 55 at 355.}
\footnote{Note}{\textit{Ibid.}}
\footnote{Note}{\textit{Ibid.}}
\footnote{Note}{11 USC § 363(k) (2012); See \textit{River Road, supra} note 12 at 650-651.}
guaranteed option for secured creditors rather than relying on properly drafted security agreements that include credit bidding. Having explained the rationale behind the US’ legislation of credit bidding, does the same rationale apply to Canada? That largely depends on the goals that each jurisdiction’s bankruptcy legislation is meant to achieve. It reasons by analogy that if the legislative goals of both the US and Canadian bankruptcy legislation are similar, then credit bidding would also be consistent within the context of Canadian legislation and should be thus be incorporated.

Bankruptcy legislation in the US serves two purposes: providing a fresh start to the honest and unfortunate debtor while settling the estate for the benefit of creditors.280 The court in In re Philadelphia Newspapers, LLC stated that “Chapter 11 of the Bankruptcy Code strikes a balance between two principal interests: facilitating the reorganization and rehabilitation of the debtor as an economically viable entity, and protecting creditors’ interests by maximizing the value of the bankruptcy estate.”281 In In re Atlanta Packaging Products, Inc., the court said, “[i]t is a well-established principle of bankruptcy law that the objective of bankruptcy sales...is to obtain the highest price or greatest overall benefit for the estate.”282 As seen in case after case, maximization of the estate’s value is of primary importance in bankruptcy

280 Barney, supra note 8 at 59.
281 In re Philadelphia Newspapers, LLC, supra note 11 at 303; See also In re Integrated Telecom Express, Inc., 384 F 3d 108 at 119 (3d Cir 2004).
Charles Tabb wrote that protecting creditors’ interests is complicated by the fact that there are usually several different parties involved at various levels in the bankruptcy hierarchy, each competing with the others in an effort to achieve the most beneficial return on their securities. The regular privilege typically enjoyed by secured creditors in regards as to determining when and how they might realize on collateral outside of a bankruptcy may be forgone during a bankruptcy. In these circumstances, the only guaranteed right that a secured creditor has is the “value” of the collateral. Credit bidding furthers the goal of “maximizing the value of the bankruptcy estate” as it serves to prevent undervaluation of the collateral.

Canadian bankruptcy legislation focuses on “permit[ting] the debtor to continue to carry on business and, where possible, avoid the social and economic costs of liquidating its assets.” However, if reorganization should fail, the insolvency legislation is also meant to protect the interests of a bankrupt’s creditors and to ensure the fair distribution and resolution of the bankrupt’s estate. Since the CCAA is silent in terms of a failure to reorganize, the BIA sets out the relevant scheme of priorities should a CCAA reorganization not succeed. Another objective of Canadian bankruptcy legislation is achieved through the consolidation of all

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283 See Unsecured Creditors’ Committee v Southmark Corp. (In re Robert L. Helms Const. & Dev. Co.), 139 F 3d 702 at 706 (9th Cir 1998); Old Carco Motors LLC v Suthers (In re Old Carco LLC), 470 BR 688 at 704 (SD NY 2012); Commodity Futures Trading Commission v Weintraub et al., 471 US 343 at 352 (1985).
284 Tabb, supra note 14 at 110.
285 Ibid at 110.
286 Ibid at 110.
287 Century Services, supra note 173 at para 15.
288 Arnco Business Services Ltd. (Re), [1983] OJ No 974 at para 4, 49 CBR (NS) 188 (ON H Ct J).
289 Century Services, supra note 173 at para 23.
potential actions and claims against the debtor into one collective proceeding.\textsuperscript{290} This “single proceeding model” prevents each creditor from striking out on its own in an attempt to beat out other creditors to the assets and, instead, facilitates negotiations amongst the creditors and debtor to reach a compromise.\textsuperscript{291}

The \textit{CCAA}’s primary goal is to enable the debtor company to negotiate with its creditors in an attempt to reorganize and stay in business.\textsuperscript{292} As described in \textit{Chef Ready Foods, Ltd. v Hongkong Bank of Canada}, “[t]he purpose of the \textit{C.C.A.A.} is to facilitate the making of a compromise or arrangement between an insolvent debtor company and its creditors to the end that the company is able to continue in business.”\textsuperscript{293} The Supreme Court of Canada emphasized in \textit{Re Indalex Ltd.} the remedial nature of the \textit{CCAA}, whereby the underlying objective “is not to disadvantage creditors but rather to try to provide a constructive solution for all stakeholders when a company has become insolvent.”\textsuperscript{294} Creditors are not the only major player in reorganizations. A key goal to any workout under the \textit{CCAA} is the continuation of the business as a going concern, hence, the \textit{CCAA} is also mindful of other parties including trade suppliers, employees and consumers while reorganization is underway.\textsuperscript{295} It also serves to keep the creditors at bay while the debtor works out a proposed plan. The fact that the \textit{CCAA} is more concerned with

\textsuperscript{290} Century Services, supra note 173 at para 22; AbitibiBowater Inc., Re, 2012 SCC 67 at para 21, 221 ACWS (3d) 264.

\textsuperscript{291} Century Services, supra note 173 at para 22.

\textsuperscript{292} Ivaco Inc. (Re), [2006] OJ No 4152 at para 3, 83 OR (3d) 108 (ONCA).

\textsuperscript{293} Chef Ready Foods, Ltd. v Hongkong Bank of Canada, [1990] BCJ No 2384, 51 BCLR (2d) 84 (BCCA).

\textsuperscript{294} Indalex, Ltd., Re, 2013 SCC 6 at para 205, 96 CBR (5th) 171.

\textsuperscript{295} Sarra, “Debtor in Possession”, supra note 249 at 340.
keeping the debtor company afloat rather than liquidation would appear to
downplay the usefulness of credit bidding in a CCAA reorganization. Yet, it should
be noted that in recent CCAA cases where credit bidding has been employed, the
subsequent workouts involved sales of the debtors’ companies as going-concerns
rather than liquidations.\textsuperscript{296}

However, not all proposals are successful and the CCAA does have a provision that
allows for liquidation of the company’s assets should a proposed plan fail. Courts
have recognized that the CCAA may be used for the sole intention of winding-up a
company and not just as an alternative solution when proposals fail.\textsuperscript{297} Justice
Campbell stated in \textit{Re TRG Service Inc.} that the CCAA can be used “to permit an
orderly liquidation that would permit a greater distribution to creditors than would
be possible under the BIA.”\textsuperscript{298} The court in \textit{Re Hollinger Inc.} acknowledged the
“application of judicial discretion and flexibility of the CCAA to achieve a variety of
purposes including... the ability to effect a sale of assets and winding up or
liquidation of a debtor company.”\textsuperscript{299} In fact, in \textit{Re Indalex Ltd.}, the debtor company
chose to pursue liquidation of its assets under the CCAA without any attempt of a
reorganization.\textsuperscript{300}

\textsuperscript{296} \textit{PCAS Patient Care, supra} note 238 at para 8; \textit{Canwest, supra} note 232 at para 13; \textit{White Birch
\textsuperscript{297} \textit{Lehndorff General Partner Ltd. (Re), [1993] OJ No 14, 17 CBR (3d) 24.}
\textsuperscript{298} \textit{TRG Service Inc. (Re), [2006] OJ No 4521 at para 68, 26 CBR (5th) 203.}
\textsuperscript{299} \textit{Hollinger Inc., Re, 2012 ONSC 5107 at para 42, 220 ACWS (3d) 261.}
\textsuperscript{300} \textit{Indalex Ltd., Re, 2011 ONCA 265 at para 180, 75 CBR (5th) 19.
Section 36 of the *CCAA* details that the court may approve a liquidation of the debtor’s assets and lists the factors that should be considered in doing so. Subsection 36(4) of the *CCAA* states that the consideration received for the asset must be a superior offer than would have been received under any plan of reorganization.\(^{301}\) Hence, the *CCAA* is also concerned with maximizing creditor recovery.\(^{302}\) Accordingly, it would not be a reach to state that enabling secured creditors to credit bid on assets at auction would further the goal of achieving maximum value for the collateral. Making credit bidding a right would add an additional safeguard in protecting against the sale of assets at an undervalued rate, which is in line with the objective of subsection 36(4).

Similar to the *CCAA*, the *BIA* provides the debtor with the means to reorganize albeit under a “rules-based mechanism that offers less flexibility.”\(^ {303}\) The *BIA* also contains express language for liquidation of the debtor’s assets. When reorganization fails, the court in *Abramyk v. Abramyk* stated:

> The underlying objective of the Act is to provide for an orderly and efficient means of realizing on the property of the bankrupt, determining legitimate debts and liabilities, applying the proceeds of disposition to those debts and then discharging the bankrupt from the balance of those debts so that he or she can start anew with a clean slate.\(^ {304}\)

\(^{301}\) *CCAA*, supra note 6, s 36(4).


\(^{303}\) *Century Services*, supra note 173 at para 15.

The court in *Saulnier v. Royal Bank of Canada* noted that the BIA’s overall goal is to balance the rights of creditors with the desire to give the bankrupt a fresh start.\(^\text{305}\) Janis Sarra states that “Canada’s insolvency and bankruptcy regime has traditionally been viewed as a secured creditor-friendly regime in that the legislative history has been one of protecting senior creditors’ claims, subject to some statutory preferences.”\(^\text{306}\) The reasoning behind this stance is Parliament’s desire to ensure debtors have access to credit and for debtors to be able to assess lending risks with some certainty.\(^\text{307}\) As also recently stated by Janis Sarra:

> Objectives of the insolvency system include maximization of the value of the debtor company’s assets and thus overall enterprise value; orderly and equitable treatment of creditors; protection of multiple stakeholder interests; recognition of creditor priorities; consideration of the public interest and public policy implications of particular decisions; balancing the benefits and costs of liquidation and reorganization; protection of the position of regulators under securities, environmental and other remedial legislation; and certainty, timeliness and cost-effectiveness of the process.\(^\text{308}\)

Again, credit bidding furthers these policy objectives by ensuring creditors can maximize on the value of their collateral in insolvency proceedings.

### 7.4 Arguments Against Credit Bidding

Credit bidding is not without its critics.\(^\text{309}\) Arguments against credit bidding include the potential “chilling effect” it might have on would-be bidders,\(^\text{310}\) deterring

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\(^{306}\) Sarra, “Debtor in Possession”, *supra* note 249 at 347.

\(^{307}\) Ibid at 347.


potentially interested parties from submitting a bid at auction.\textsuperscript{311} In situations involving lender syndicates where an agent is involved, dissenting minorities have disputed the agent’s authority to submit a credit bid using all of the outstanding debt.\textsuperscript{312} Valuation issues also arise in the context of credit bidding, where opponents have argued that the valuation of credit bids should be limited to the fair market value of the collateral and not the total debt obligation secured by the collateral.\textsuperscript{313} Yet another argument rests on the premise that the secured lenders who are credit bidding their claim are often in a position to influence the sales process. The issue then becomes on ensuring the fairness and integrity of the sales process. These issues are addressed in sequence.

\textbf{7.4.1 Chilling}

One argument against credit bidding rests on the notion that it could potentially chill cash bidders.\textsuperscript{314} The premise is that if a credit bidder holds a claim that outweighs the market value of the collateral, then that credit bidder would be able to outbid any cash bidder.\textsuperscript{315} Assuming then that the cash bidders are aware of the potential credit bidder and the value of the debt, the argument states that the cash

\begin{itemize}
  \item\textsuperscript{310} Kling, \textit{supra} note 309 at 280-282.
  \item\textsuperscript{312} See \textit{In re Metaldyne Corp.}, 409 BR 671 (Bankr SD NY 2009) [\textit{In re Metaldyne Corp.}].
  \item\textsuperscript{313} See \textit{SubMicron}, \textit{supra} note 53.
  \item\textsuperscript{314} Kling, \textit{supra} note 309 at 280-282.
  \item\textsuperscript{315} Kling, \textit{supra} note 309 at 280-202.
\end{itemize}
bidders would be deterred from submitting competing bids knowing that the credit bidder has the ability to outbid them.\textsuperscript{316}

The court in \textit{In re River Road Hotel Partners, LLC} viewed chilling as a viable argument that can be used to deny the lender the option to credit bid.\textsuperscript{317} In coming to this conclusion, the court referenced \textit{Collier on Bankruptcy}, which states that the court could deny credit bidding if it was viewed that allowing the bid would chill the process.\textsuperscript{318} However, the court went on to add that the debtor is required to provide evidence substantiating the potential chilling effect, which the debtor had failed to do in the case at bar.\textsuperscript{319}

The Bankruptcy Court in \textit{Philadelphia} also noted that credit bidding could potentially have a chilling effect. In that case, the debtors stated that the lenders’ claim to the secured assets far exceeded their actual market value, and would subsequently deter any potential bidders from expending time and energy to bid on those assets.\textsuperscript{320} Hence, the debtors reasoned that in order to maintain a fair auction, the lenders should be denied the right to credit bid. The lenders alternatively argued that denying them the right to credit bid would be “chilling” in its own way,

\begin{itemize}
\item \textsuperscript{316} \textit{In re Philadelphia Newspapers, LLC, supra} note 11 at 321.
\item \textsuperscript{317} \textit{In re River Road Hotel Partners, LLC, supra} note 68 at 5-6.
\item \textsuperscript{319} \textit{In re River Road Hotel Partners, LLC, supra} note 68 at 6.
\item \textsuperscript{320} \textit{Philadelphia, supra} note 111 at 10.
\end{itemize}
by preventing the lenders from bidding on the assets, and thereby creating a less competitive auction.\textsuperscript{321} The Bankruptcy Court sided with the lenders.

While the above case examined the notion that “chilling” could occur from allowing or denying a credit bid, there has been very little case law to date that has denied credit bidding solely on the basis of a potential chilling effect.\textsuperscript{322} Buccola & Keller go so far as to completely refute the “chilling” argument through an illustrative example:

For instance, if a would-be bidder knows that Warren Buffett plans to attend an auction, she is also surely aware that Buffett can top her reservation price for any or all of the assets on the block. Yet nobody proposes to ban wealthy cash bidders from participating in a bankruptcy auction.

That, of course, makes good economic sense. Would-be bidders understand that a deep-pocketed player’s ability to top their reservation price does not imply a willingness to do so. Warren Buffett did not become wealthy by overpaying for things, so it is possible, indeed, probable, that his reservation price for an asset at auction will be beneath that of another buyer. And buyers know this in advance. The same logic holds for secured creditors.\textsuperscript{323}

While critics have suggested that potential chilling is indeed a prominent issue that hampers perceived benefits from credit bidding,\textsuperscript{324} the case law seems to contend otherwise.\textsuperscript{325}

\textsuperscript{321} Philadelphia, supra note 111 at 28-29.
\textsuperscript{322} See In re Morgan House General Partnership, 1997 US Dist LEXIS 1306 (ED Pa 1997) (refused to prohibit credit bid based on potential to chill bidding process) [In re Morgan House].
\textsuperscript{323} Buccola, supra note 140 at 123 [emphasis added].
\textsuperscript{324} Kling, supra note 309 at 283.
\textsuperscript{325} See In re Morgan House, supra note 322; Philadelphia, supra note 111.
7.4.2 Majority Lenders vs. Minority Lenders

Where there is one senior secured creditor, the decision to credit bid is relatively straightforward. However, when the senior creditor involves a syndicate of lenders, the potential for discord amongst the various creditors increases. As seen in White Birch where the lenders fragmented into two parties involving majority and minority lenders, lender syndicates pose an additional obstacle for credit bidding. While having previously discussed the advantages of credit bidding in the context of a lender syndicate earlier in this Chapter, the inherent nature of lender syndicates as being composed of several creditors, escalates the opportunity for creditors to disagree amongst themselves in respect to submitting a credit bid at an asset sale. The US and Canada have addressed this dilemma by relying on provisions in the security agreements and loan documents to override the dissenting minority and approve sales that sell assets free and clear to majority lenders using credit bids.326

The US court in In re Metaldyne Corp. approved the right of the agent to credit bid as directed by the holders of the first lien debt over objections of the minority lenders, which held $3.5 million of the $425 million owed.327 The lenders’ rights were governed by both the security agreement and the credit agreement. These agreements “irrevocably appointed” the agent upon default, whereby the agent then credit bid the full value of the lenders’ claim.328 The minority lenders objected, first arguing that only they could credit bid their claim, and in the alternative, that the

326 See In re Metaldyne Corp., supra note 312; In re GWLS Holdings, Inc., 2009 Bankr LEXIS 378 (Bankr D Del); White Birch, supra note 13.
327 In re Metaldyne Corp., supra note 312.
328 In re Metaldyne Corp., supra note 312 at 676.
agent must first have obtained the minority lenders’ written consent.\textsuperscript{329} The court found that the loan documents had delegated authority to the agent, and as such, approved the sale.

\textit{In re GWLS Holdings, Inc.} also dealt with a similar lender syndicate issue.\textsuperscript{330} The first lien lenders’ agent submitted a credit bid on substantially all of the debtors’ assets. All but one of the first lien lenders consented to the credit bid, Grace Bay, which held $1 million of the $366 million in outstanding debt. Grace Bay pointed to the credit agreement stating that no amendment, supplement or modification of the agreement could be made without unanimous lender consent. The first lien agent relied on the credit agreement and the collateral agreement, which irrevocably appointed the first lien agent, as confirmation of it’s authority to credit bid the entire value of the debt owed. The court placed great importance on the fact that both the credit agreement and collateral agreement were drafted at the same time, and therefore, the collateral agreement could not be viewed as amending or changing in anyway the credit agreement. Both documents had to be read as complementing one another. The collateral agreement delegated the rights and remedies traditionally enjoyed by lenders to the first lien agent. The court concluded that the first lien agent was acting within its authority to credit bid the debt on behalf of all of the first lien lenders.

\textsuperscript{329} \textit{In re Metaldyne Corp.}, supra note 312 at 675.
\textsuperscript{330} \textit{In re GWLS Holdings, Inc.}, supra note 326.
The ability of majority lenders to credit bid has also been addressed in a Canadian context in *White Birch*. The case discussed the issue of whether or not the majority lenders, which were viewed as acting in an agent capacity for the minority lenders, were allowed to credit bid through the various lien and security agreements. The court found the various security documents highly persuasive in determining that the majority lenders were entitled to credit bid despite not having obtained the minority's consent.

While these cases have ruled in favour of credit bidding by the majority lenders, it does not diminish the fact that there is still an ongoing dilemma faced by lender syndicates when dissenting minority parties are involved. The security agreements have played key roles in both the US and Canadian courts' decisions to approve the use of a credit bid by the majority lenders. Yet, an argument could be made that although the security agreements expressly authorize agents to deal with the collateral, each lender is the owner of his or her own debt and any credit bid the agents purport to make is, in fact, the equivalent of forcing each lender to submit a cash bid.\(^{331}\)

### 7.4.3 Valuation of Credit Bids

Another popular issue with respect to credit bidding surrounds the question of the appropriate dollar value to be attributed to credit bids. Those against the use of credit bidding generally argue that the value of the credit bid should be limited to

\(^{331}\) Erens, *supra* note 275 at 565-566.
the economic value of the collateral.\textsuperscript{332} This “economic value” approach to credit bidding was the precise argument put forward in \textit{In re SubMicron Systems Corporation}, whereby several secured creditors came to an agreement with Sunrise Capital Partners to credit bid their secured claims towards the purchase of SubMicron’s assets in return for equity in Sunrise Capital Partners’ new entity created for the purpose of purchasing the assets.\textsuperscript{333} The sale was then approved by the District Court.\textsuperscript{334} On appeal to the Third circuit, the Plan Administrator, acting on behalf of the unsecured creditors, opposed the sale on several grounds including the improper use of a credit bid. The Plan Administrator submitted that in order for the secured creditors to be entitled to credit bid, the collateral that secures the claim must have an economic value in accordance with § 506(a). Since the collateral was found to be of nominal value, the Plan Administrator stated that the secured creditors should not be allowed to credit bid.

The court disagreed with the Plan Administrator’s argument, citing several cases to support the premise that “creditors can bid the full face value of their secured claim under § 363(k).”\textsuperscript{335} The court pointed to \textit{In re Suncruz Casinos, LLC}, where the court found that “the plain language of the statute makes clear that the secured creditor may credit bid its entire claim, including any undersecured deficiency portion

\begin{footnotesize}
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\item[\textsuperscript{332}] \textit{SubMicron, supra} note 53 at 459-460.
\item[\textsuperscript{333}] \textit{SubMicron, supra} note 53.
\item[\textsuperscript{334}] \textit{Cohen v KB Mezzanine Fund II, LP (In re Submicron Systems Corporation)}, 291 BR 314 (Bankr D Del 2003).
\item[\textsuperscript{335}] \textit{SubMicron, supra} note 53 at 460.
\end{itemize}
\end{footnotesize}
thereof.” In response, the Plan Administrator argued that the secured creditors were not just partially undersecured but were completely undersecured, distinguishing this case from the other cases the court previously cited. The court was not swayed by this argument either, pointing out that regardless of the extent to which the secured creditors are undersecured, they are still entitled to the proceeds from the sale of the assets. As such, credit bidding merely “preserve[d] their right to the proceeds.”

*White Birch* also dealt with the question of valuation, stating “it goes without saying that the amount of the credit bid should not exceed, but should be allowed to go as high as the face value amount of the credit instrument upon which the credit bidder is allowed to rely.” The court went on to note that the value of the credit bid should not be subject to the fair market value of the assets. It was the court’s opinion that this practice had been well-established in Canada.

Although parties have attempted to argue against the secured creditors' ability to credit bid the full face value of the claim, the courts in both the US and Canada have rejected these submissions with relative ease. While these previous unsuccessful attempts at arguing against the current method of valuation will not likely deter

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336 *In re Suncruz Casinos, LLC*, 298 BR 833 at 839 (Bankr SD Fla 2003). See *In re Midway Investments, Ltd.*, 187 BR 382 (Bankr SD Fla 1995) (“[s]ection 363(k) provides the right to credit bid the full amount of the claim” at 391); *In re Morgan House*, *supra* note 322; *In re Realty Investments, Ltd. V.*, 72 BR 143 (Bankr CD Cal 1987) (the ‘allowed claim’...must (for purposes of credit bidding), be its total claim without reference to the ‘value’ of the property’ at 146).

337 *SubMicron, supra* note 53 at 461.

338 *White Birch, supra* note 13 at para 34.

339 *White Birch, supra* note 13 at para 34.
potential parties from raising this issue in the future, current case law has shown the courts as being resolute on this subject.

7.4.4 Secured Creditors and the Integrity of the Sale Process

If secured lenders choose to credit bid their claim at a sale of the assets, a primary concern is the ability of the secured creditor “to truncate the sales process or otherwise manipulate the process in such a way that the credit bid is a foregone conclusion or value is not otherwise maximized for subordinate creditors.”\textsuperscript{340} The court in \textit{Canwest Publishing Inc.}, dealt precisely with this issue.\textsuperscript{341} Faced with accumulating liabilities, the debtor company came to an agreement with its senior secured lenders. According to the agreement, the secured lenders would offer a stalking horse credit bid in return for substantially all of the debtors’ assets. If a solicitation process failed to produce a better offer, then the debtor company would proceed with the secured lenders’ credit bid. A more favourable bid was submitted by an entity comprised of 9.25\% of senior subordinated noteholders representing certain unsecured creditors; however, this offer was contingent on the entity securing financing. The debtor company proceeded in a manner that resulted in a “dual track”, with the debtor company complying both with the secured creditors’ support agreement that provided the credit bid while simultaneously taking steps to finalize an asset sale to the senior subordinated noteholders. In the end, an asset sale was concluded with the senior subordinated noteholders, but the judgment rendered by Madam Justice Pepall reiterates the test as to when a sale will be

\textsuperscript{340} Huff, \textit{supra} note 241 at 11.

\textsuperscript{341} \textit{Canwest Publishing Inc.}, \textit{supra} note 200.
approved under section 36 of CCAA, highlighting the requirement that the sales process be reasonable and fair.\textsuperscript{342} Although the court in \textit{Canwest}, looked at several factors regarding what constitutes fair and reasonable, concern remains for undue influence to be exerted by secured creditors on the unfortunate debtors. As such, there is some speculation that the court appointed monitor should take a more active role in ensuring the integrity of the sales process.\textsuperscript{343}

### 7.5 Legislation as a Tool?

Given that credit bidding is not established as a common law right nor statutory right in Canada, the question then turns on which is the preferable medium in which to encase credit bidding as a right: common law or legislation? The differences between common law and statutory law are vast. One is largely based on a conceptual understanding while the other is based on textual interpretation.\textsuperscript{344} Neither system is perfect. Doctrines in common law take shape as cases mold and tailor principles to suit the problem at hand. While the underlying meaning of the doctrine may remain firm, the ability for each judge to re-state and refine the principle undoubtably makes common law more fluid in nature.

While the courts have statutory authority to fill in the gaps of legislation, this discretion is not as flexible as in common law due to limitations imposed by the statute itself. From the text, judges are required to interpret the legislation and then

\textsuperscript{342} \textit{Canwest}, supra note 232 at para 13.

\textsuperscript{343} Huff, \textit{supra} note 241 at 11.

apply the understood concept to the case. The interpretative element adds an additional step not seen in the application of common law doctrines. For instance, in deciding if a “case has been decided correctly the observer must consider not only whether the judge properly understood and applied the relevant concepts but also whether those concepts are justifiable interpretations of the statute.”

Misinterpretation of legislation is a familiar quandary faced by the courts. The previously discussed US cases of In re Philadelphia Newspapers, LLC and In re Pacific Lumber Co., which are regarded by scholars as a misinterpretation of the statute, clearly demonstrate the difficulties the courts are confronted with in interpreting legislation and the resulting complications from misinterpretation. The potential for misinterpretation adds another factor to be considered when proposing legislation.

However, where the common law is unclear or insufficient to provide guidance on certain issues, there is little alternative other than enacting legislation. Credit bidding could be said to have a “foot in the door” with respect to Canada’s current insolvency regime, but how does credit bidding go from being a merely allowable option, generally permitted via court approval, to becoming a wholly solidified right without explicit legislation? According to Eisenberg, there are “four foundational principles that govern the manner in which law is established and changed by the courts.” The first principle, objectivity, requires the courts to establish universal

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345 Ibid at 248-249.
346 Supra note 140.
347 Eisenberg, supra note 5 at 8.
rules that can be applied similarly to parties in the future and not just to those involved in the immediate dispute while the courts maintains an element of impartiality towards the parties. Furthermore, these universal rules developed by the courts must be “supported by the general standards of the society.” It is also of critical importance that the courts’ decisions and reasoning should be replicable so as to provide certainty and predictability in legal matters. Finally, and perhaps most importantly for the purpose of this thesis, is the requirement that the courts “are obliged to be responsive to what the [legal] profession has to say.”

The courts interact with the legal profession through cases argued before the court and through legal commentary provided in the way of law reviews, opinions from sister courts and conferences, to name a few.

The ability to use credit bidding at an asset sale under Canadian insolvency legislation has been affirmed by the courts, but whether a secured creditor can rely on credit bidding, as an implied right, is still uncertain. Furthermore, there is very little literature in Canada discussing the merits of making credit bidding a right. Hence, it would appear as if credit bidding has only taken marginal steps towards becoming a common law right in reference to Eisenberg’s four principles.

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348 Eisenberg, supra note 5 at 8-9.
349 Eisenberg, supra note 5 at 9.
350 Eisenberg, supra note 5 at 10-11.
351 Eisenberg, supra note 5 at 12.
352 Eisenberg, supra note 5 at 12-13.
353 See Janis Sarra, “Manoeuvring through the Insolvency Maze – Shifting Stakeholder Identities and Implications for CCAA Restructurings” (2011) 27:1 BFLR 155 at 174-175 (discussing whether credit bidding should be legislated).
Legislation, alternatively, is no "quick fix" either. Amending legislation is time consuming but the benefits of incorporating credit bidding into statute are readily identifiable, the predominant advantage being that it provides secured lenders with an additional means of protecting their collaterals’ value. Legislation can also provide the courts guidance when dealing with issues that arise from lender syndicates, credit bidding valuations and addressing the overall integrity of the sales process when credit bidding is used.

The right to credit bid should not be limited to those secured creditors savvy enough to include credit bidding in security and loan agreements, but should instead be extended to all secured creditors through explicit legislation. However, legislation, as detailed earlier in this thesis, has its drawbacks. It adds additional requirements that the court must take into account during an insolvency proceeding.

Another argument that can be made against legislation is its potential to be misconstrued. This is an inherent risk in any legislation and relying on such an argument would have a preposterous result. Arguably, the Canadian insolvency regime, which includes both tests to be applied from common law and statute, would prevent the same unfortunate mishap as seen in the US in In re Philadelphia Newspapers, LLC and In re Pacific Lumber Co. By using the criteria laid out in Nortel Networks and Royal Bank v. Soundair Corp., the courts would have discretion to approve plans and asset sales that meet the goals of the act. Enacting credit bidding
not only brings Canada more in line with US legislation, but it also provides some clarity for secured creditors and security in knowing that they have an additional option available to them in the case of a default. This extra right might also free up additional credit or encourage more lenders to more willingly extend credit. While the potential positive attributes that credit bidding might have on the financial economy in Canada would be mere speculation, the impact on secured creditors is real. As such, legislation of credit bidding should be the next step taken in Canada's ever-evolving insolvency regime.

7.6 Proposed Amendments to the BIA and the CCAA

To maintain harmony with the US legislation and to facilitate cross-border insolvency proceedings, any proposed amendments to the BIA and CCAA, in respect to credit bidding, should mirror the US § 363(k). The US Congress found it fit to insert an “unless the court for cause orders otherwise” clause as an escape hatch.354 While this does not preclude Canada from following a different path, the US case law is persuasive in determining that Canada should also have a backdoor option if it were to legislate credit bidding.

Arguments against credit bidding, including the potential chilling of the bidding process and the potential undermining of the integrity of the sales process, might suggest that more specific legislation delineating limitations to credit bidding is required. However, the Nortel criteria and Royal Bank v. Soundair Corp. largely

354 Supra note 52.
ensure that the sales process is fair and just in light of the given circumstances. Arguably, any specific legislation as to the operation of credit bidding could stifle the flexible nature of the CCAA or restrict its application in terms of the BIA. Both statutes have endowed the courts with judicial discretion and, when coupled with a review by the court appointed monitor, this discretion serves as a check-and-balance mechanism that need not be duplicated in explicit statutory language. Furthermore, the “unless the court for cause orders otherwise” clause permits the courts to continuing using their judicial discretion in determining whether credit bidding is fair in the given circumstances.

It could be viewed that enacting a provision that entitles the courts to continue using judicial discretion to determine whether credit bidding is allowable defeats the purpose of embedding credit bidding in legislation to begin with. However, this argument overlooks the fact that legislated credit bidding would now be an explicit right as provided for by legislation with the courts subsequently having to be furnished with evidence as to why this right should be denied rather than the current system, where parties argue as to why credit bidding should be allowed.

Accordingly, the proposed credit bidding section would read very similar to § 363(k):

At a sale under [section 36 of the CCAA or section 65.13 of the BIA] of property that is subject to a lien that secures an allowed claim, unless the court for cause orders otherwise the holder of such claim may bid at such sale, and, if the holder of such claim purchases such property, such holder may offset such claim against the purchase price of such property.
Under plans of reorganization, the US code lists three alternatives that must be adhered to in respect to cramdown plans. The CCAA has no cramdown contingency in the event that there is a dissenting class. Hence, the issues surrounding the “indubitable equivalent” under § 1129(b)(2)(A) is not necessarily relevant to proposed amendments. That being said, if the legislature pursues amending the statute to incorporate “cram down” plans in the future, the “indubitable equivalent” component is an unneeded complication which should be omitted. The insolvency legislation in both the US and Canada aims to protect secured creditors’ rights. However, Canada’s supplementation of insolvency legislation with common law tests alleviates the requirement of including a general “catchall” provision, the same provision that enables the US courts to approve alternative plans. Instead, the Canadian courts are already endowed with the flexibility needed to approve unique plans not previously considered by the legislature and subsequently included in US legislation.
CHAPTER 8: CONCLUSION

The ability of secured creditors to credit bid their claim against the collateral at an asset sale underscores an important concern addressed by the US legislature, the undervaluation of collateral. Following its incorporation into the US Bankruptcy Code, secured creditors had enjoyed the security of knowing that should a debtor default, the secured creditors had the right to credit bid their secured claim on the collateral should other bidders submit “lowball” offers or if the collateral suffered from market fluctuations. This right could be invoked in one of two ways, at an asset sale of the debtor’s estate or under a plan of reorganization whereby the debtor attempted a “cramdown” over the dissenting creditors.

Although credit bidding had maintained a relatively stable existence in US case law, In re Philadelphia Newspapers, LLC and In re Pacific Lumber Co. upset the predominant interpretation of the statute and essentially allowed the debtors to bypass the secured creditors’ right to credit bid through the use of the “catchall” indubitable equivalent subsection. The US Supreme Court righted the wrong in RedLAX returning credit bidding to its prior status as a secured creditor’s right.

While cramdown plans are not embodied in Canadian insolvency legislation, the above US case discussion has highlighted several interesting points regarding credit bidding, first and foremost being the merits and reasons behind encasing credit bidding in legislation. Of note, also, is the US courts’ approach to resolving issues such as valuation of credit bids, the potential of chilling and lender syndicate
consent. Additionally, while this thesis advocates for legislation of credit bidding, the recent US cases also illustrate the potential for misinterpretation of legislation.

While *White Birch* and *Canwest* have solidified the use credit bidding in Canadian insolvency proceedings, there are several issues that have yet to be addressed including implications that credit bidding might have on the integrity of an asset sale under the *CCAA*. Proper legislation of credit bidding in Canada, which can alleviate some of these issues in conjunction with the statutory tests already established by the courts in *Nortel* and *Royal Bank v. Soundair Corp.*, is the logical next step. Credit bidding has had a tumultuous journey in recent years, having been subject to misinterpretation in the US courts to being imported into Canada through cross-border insolvency proceedings. Arguably, its journey is far from over as the Canadian courts continue to grapple with its presence.
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