Understanding the 363 Bankruptcy Sale: High-Value Opportunities for Strategic Investors

Scott H. Hogan
Foster Swift Finance & Bankruptcy Law News
October 21, 2024

AUTHORS/ CONTRIBUTORS
Scott A. Chernich
Scott H. Hogan

PRACTICE AREAS
Bankruptcy & Restructuring
Business Law
Finance, Real Estate & Bankruptcy Law

In the high-stakes world of corporate finance, a 363 bankruptcy sale can be a game changer. This powerful legal mechanism has enabled renowned companies including **General Motors**, **Hertz** and **Neiman Marcus** to navigate existential financial threats and emerge from the reorganization process as much leaner, stronger businesses:

- **GM** leveraged a 363 sale to offload its entire European operation and other under-performing parts of the company. This allowed the auto giant to focus on the North American market and return to profitability.
- **Hertz** utilized a 363 sale to streamline its business model, selling off non-core assets and emerging with a more competitive market strategy.
- **Neiman Marcus**, the luxury department store, went through a 363 sale, shedding significant debt and focusing on revitalizing the classic brand.

These high-visibility success stories highlight the company-saving, transformative potential of 363 sales, which can offer a lifeline to the most distressed companies and provide high-value, low-cost opportunities for savvy investors.

Alternatively, it doesn’t always work out. **Borders Bookstores**, **RadioShack** and **Toys “R” Us** also conducted 363 sales -- with vastly different outcomes. All three of these fabled retailers are essentially out-of-business today.

How Does a 363 Bankruptcy Sale Work?

The process begins when a debtor files for bankruptcy under Chapter 11. The debtor then sells off assets, reorganizes its finances and endeavors to continue operations. While 363 sales are more commonly part of Chapter 11 proceedings, 363 sales can be utilized in a Chapter 7 liquidation.

- **Asset Identification** – The debtor company identifies the assets to be sold at the 363 sale. Qualified appraisers or experts value those assets.
- **Court Approval** – The debtor files a legal motion with the bankruptcy court seeking its approval to sell the identified assets in a 363 sale. The motion also seeks court approval to select a "stalking horse" bidder, whose bid will serve as a baseline asking price for the debtor's assets.
- **The "Stalking Horse" Bidder** – Debtors participating in a 363 sale will often select a "stalking horse" (literally: a horse that leads wild horses into a trap) bidder, which will enter an opening, baseline bid on the assets being sold. There are significant potential upsides for a stalking horse bidder, including first mover advantage, potential discounts, negotiation leverage with the debtor and the guarantee of a fair and transparent process overseen by the bankruptcy court.
- **Marketing and Sale of Assets** – The debtor markets and auctions the identified assets in a process which includes notifying potential bidders of the sale, providing detailed information about the assets for sale, hosting pre-auction inspections/tours and conducting the auction. Potential bidders invited to participate in the sale include companies, investors, financial institutions or other asset acquirers.
- **Closing the Deal** – The highest bidder(s) are awarded the assets, which are free and clear of liens and encumbrances. However, the bankruptcy court reserves the right to approve or deny the sale or portions or it.

Advantages of Participating in a 363 Bankruptcy Sale

- **Attractive Pricing/High Value** – The primary benefit of taking part in a 363 sale is the opportunity it provides for participants to acquire large lots of corporate assets at prices well below current market values. Debtors in bankruptcy sales are motivated to sell quickly, which can be a powerful advantage for qualified asset buyers.
- **Speed and Efficiency** – The 363 bankruptcy sale, designed to be an expedited process, can offer a unique opportunity for companies to strategically acquire assets and integrate them with their operations in a fraction of the time (60-90 days on average) needed for traditional asset acquisition and integration.
- **Free and Clear Title** – The assets acquired at a 363 sale are transferred to the buyer free and clear of any title liens or encumbrances, offering another layer of risk reduction.
- **Court Oversight** – The rigid oversight of the bankruptcy court guarantees that a 363 sale will be organized, transparent and fair for all. Because the court oversees the process and reserves the right to review the transaction, buyers can be relatively assured that the sale will be conducted in a manner that adheres to legal standards.

Potential Problems for 363 Sale Participants

- **Due Diligence Challenges** – While the speed of a 363 sale is one of its advantages, it can also be a drawback. The relatively short span of time required for a 363 sale can greatly limit the amount of time for potential buyers to conduct due diligence, increasing the risk of unforeseen, future liabilities. Caveat emptor.

- **Competing Bids, Changing Market Conditions, Regulatory Hurdles, Etc.** – Most 363 sales proceed smoothly with predictable outcomes, but that's not always the case. Changing market conditions, higher numbers of motivated bidders, fluctuating asset valuations, secured creditor objections, legal and copyright disputes, unexpected regulatory hurdles and other factors (even breaking news) can sometimes make for a 363 sale that is quite dynamic, spirited and unpredictable.
- **Financing Difficulties** – The securing of financing for assets to be purchased in a 363 sale can be problematic. Given the distressed situation of the assets, unknown potential liabilities related to assets for sale and the short timeline of the process, some lenders may take a cautious approach and impose more stringent terms.
- **Court Approvals Required** – Despite the expedited process of 363 bankruptcy sale, it is still a federal court proceeding and the requirements for review, approvals and delays due to legal challenges or objections from creditors could slow the closing process.

Conclusion: A 363 Bankruptcy Sale Can be Significant Growth Opportunity, but Proceed with Caution

A 363 bankruptcy sale can present a significant opportunity for select businesses -- including mid-sized operations – to acquire valuable assets at below-market prices. In addition, it's guaranteed to be a fair and transparent proceeding overseen by the court with all purchased assets free and clear of encumbrances and liens.

As noted, the 363 sale can present its own set of risks and challenges, including the need for swift due diligence and the possibility that bidding for the assets will become competitive and aggressive.

But with a studied and organized approach, which includes consulting with specialized legal and financial advisors, businesses can successfully navigate the complexities of a 363 sale and complete a transformative, cost-efficient acquisition in a short period of time.

Foster Swift's attorneys have a long and distinguished history of representing creditors, debtors, trustees and other interested parties in U.S. Bankruptcy Court. The firm's bankruptcy and restructuring counsel have experience with Chapter 11, Chapter 7 and Chapter 13 proceedings. If you're interested in acquiring or selling assets through a 363 bankruptcy sale or have other questi0ns related to bankruptcy, please contact Scott Chernich, Scott Hogan or another member of our FREB team.