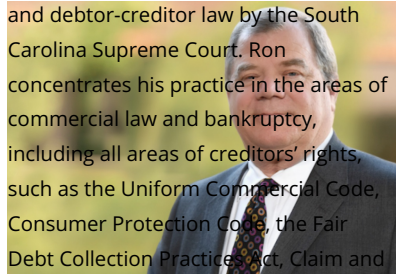


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### ABOUT THE AUTHOR



Ron Jones is a partner at Smith Debnam and a certified specialist in bankruptcy and debtor-creditor law by the South Carolina Supreme Court. Ron concentrates his practice in the areas of commercial law and bankruptcy, including all areas of creditors' rights, such as the Uniform Commercial Code, Consumer Protection Code, the Fair Debt Collection Practices Act, Claim and Delivery, Replevin, Foreclosure Law, Real Estate and Bankruptcy. Ron represents both secured and unsecured creditors, lenders, lessors, investors, asset purchasers, creditors' committees, and occasionally, debtors.

## Court Approves Sale of Assets to Third Party Despite Stalking Horse Bad Faith Allegations Against Purchaser

September 29, 2020 | by

United States Bankruptcy Judge John E. Waites approved a sale of substantially all the assets of a small business Chapter 11 Debtor over the protests of a "Stalking Horse" bidder who claimed the successful bidder was acting in bad faith. In a decision entered by the Court August 14, 2020, Judge Waites held that "[i]n determining a challenge to a purchaser's good faith status, the Fourth Circuit has indicated that '[t]ypically the misconduct that would destroy a purchaser's good faith status at a judicial sale involves fraud, collusion between the purchaser and other bidders or the trustee, or an attempt to take grossly unfair advantage of other bidders.'" (*Quoting, Willemain v. Kivitz*, 764 F.2d 1019, 1023 (4<sup>th</sup> Cir. 1985)). *In re: Watertech Holdings, LLC*, CIN 20-00662-jw (August 14, 2020). The opinion stands for the proposition that the Bankruptcy Code's good faith requirement should be focused less upon the motives of and relationship between the bidders, and more on the fairness and openness of the sale itself and the benefit to the estate and its creditors.

Watertech Holdings, LLC ("Watertech") filed Chapter 11 in the District of South Carolina on February 6, 2020, and operated and managed its business and assets as a debtor in possession pursuant to 11 U.S.C. §§1107(a) and 1108. Watertech was formed to develop products and disinfecting technologies. Prior to the petition, several groups negotiated with Watertech to purchase the property, with the expectation of a §363 sale process. On the petition date, Watertech filed a Motion to sell substantially all its assets and sought approval for the sale bidding procedures. The Stalking Horse Bidder initially sought to purchase the assets for \$125,000.00 in cash, plus waiver of a number of claims and the payment of a royalty based upon post-sale profits. Objections eventually resulted in an amended Stalking Horse Bid in the form of an Asset Purchase Agreement ("APA"), which included a payment of \$250,000.00 in cash and a closing within twenty (20) days of a final Order approving the sale. The Bid Procedures Order required: (1) a modest marketing period for the assets to other potential purchasers; (2) a deadline for submission of any qualified competing bid; (3) an purchase agreement substantially in the form of the Stalking Horse APA; (4) a deposit in the amount of \$125,000.00; and, (5) "topping bids" of at least \$25,000.00 more than the Stalking Horse Bid.

Though the Bidding Procedures Order provided a deadline for the submission of competing bids, the Court retained the ultimate authority to determine what constituted a qualified competing bid. The sale was delayed and the deadline for bids was extended in compliance with the Court's COVID Restrictions. After the deadline for competing bids had passed and less than a week before the hearing on the §363 Sale Motion, PureCycle, LLC submitted an untimely competing bid. The bid met all requirements set forth in the Bidding Procedures Order except for timeliness. PureCycle's principal had been involved with businesses affiliated with the Stalking Horse and its principal. Though the principals were involved in business disputes through other entities, neither PureCycle nor its principal was affiliated with the Stalking Horse. At the hearing, the Stalking Horse objected to the late bid filed by PureCycle and also asserted that PureCycle was not acting in good faith.

First, the Court found that it had absolute discretion to determine whether a party was a qualified bidder. The Court then determined that the PureCycle bid was superior to the Stalking Horse bid and met every other requirement under the Bidding Procedures Order. The Court further noted that the Debtor, exercising sound business judgment, had urged the Court to find that the PureCycle bid was a qualified bid allowing for the auction process envisioned by the Bid Procedures Order with all the parties able to proceed. The auction, held in open Court, ended with a sale to PureCycle for \$525,000.00 in cash with a closing to take place within ten (10) days.

As to the issue of good faith, the Court noted that there was an "apparently contentious relationship between principals and members of [the Stalking Horse] and PureCycle" arising from their joint participation other business relationships and that these "antagonistic relationships should not be a distraction from the ultimate goal of the case - to sell the Debtor's assets in a fair manner for the best price for the benefit of creditors." The Court found that the good faith determination is based on findings that the terms and conditions of the sale are fair and reasonable and/or appropriate, that they were reached through arms-length negotiations and bargaining between the Debtor and potential bidders, and that the process was open and fair to all participants.

Finally, the Court stated "it is not the Court's role to examine the motives for, or even the wisdom in, the bids offered for assets to be sold at a bankruptcy sale. Considering all of the circumstances of this case, "the Court found "that PureCycle is a good faith purchaser entitled to the protections afforded to sale transactions under §363(m)" and the objection of the Stalking Horse based upon "the alleged lack of good faith [was] overruled."

Postscript: The Stalking Horse later filed a Motion to Stay the Sale and a Motion to Reconsider both of which were overruled by the Court after an additional hearing.

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