Trading up to a New Model: Rolling out Revisions to the ABA Model Asset Purchase Agreement for Bankruptcy Sales

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Biographies

**Ted Austin Dillman** is a member of Latham & Watkins’ Finance Department and the firm’s Restructuring, Insolvency & Workouts Practice. Mr. Dillman’s practice focuses on corporate restructuring, bankruptcy, distressed mergers and acquisitions, and workouts, as well as general finance and corporate matters. He represents debtors, strategic buyers, private equity funds, hedge funds, first and second lien holders, other creditors, and boards of directors. Mr. Dillman frequently authors finance-related articles for various publications and regularly presents on insolvency and finance related issues. He serves on the board of governors of the Financial Lawyers Conference and is a member of the American Bankruptcy Institute. Mr. Dillman is also a member of the ABA the task force charged with revising the ABA Model Asset Purchase Agreement to address issues that arise in the context of bankruptcy sales, and is a co-author of the debtor-in-possession financing chapter of *Reorganizing Failing Businesses*, which will be published by the ABA.

**Kyung S. Lee** is a partner at Diamond McCarthy, where he practices in the area of debt restructuring and corporate reorganizations. He has served as debtor's counsel for companies in the airline, real estate, oil and gas, communications, health care, distribution, manufacturing and convenience store industries. He has also represented lenders, creditors, creditors' committees and investors involved in workouts and Chapter 11 reorganizations as well as litigating on behalf of the various parties. He has extensive experience working closely with senior management and financial advisors on valuation of enterprises and assets and development of turnaround and restructuring business plans.

**Corali Lopez Castro** has been a partner at Kozya Tropin & Throckmorton since 1998. She was Managing Partner of the firm from 2011 through 2012. She concentrates her practice on bankruptcy and commercial litigation matters. Cori’s practice reflects her extensive experience and expertise with bankruptcy reorganizations and liquidations, receiverships, debt restructuring, and creditors’ rights. She has been involved with the liquidation of four significant bank holding companies in bankruptcy courts around the country and state court. Cori served on the panel of Trustees for the Southern District of Florida between 1998 and 2002, during which she was responsible for the liquidation of assets in bankruptcy cases filed in the United States Bankruptcy Court for the Southern District of Florida. In 2014, Cori was inducted as a Fellow into the 25th Class of the American College of Bankruptcy. The College recognizes individuals for their professional excellence and contributions to the field of restructuring and
Scott T. Whittaker is a member of Stone Pigman, where he has been practicing since 1984. He represents clients in a wide variety of transactions, including buying, selling and merging companies; private placements of securities; venture capital and private equity transactions; joint ventures; roll-ups, spin-offs and split-ups; and all phases of real estate acquisitions, development, and financing. Mr. Whittaker is an active member of the Committee on Mergers and Acquisitions of the American Bar Association, where he serves as Chair of the Judicial Interpretations Working Group of the Subcommittee on M&A Jurisprudence. The Best Lawyers in America named Mr. Whittaker “Lawyer of the Year” in New Orleans for Venture Capital Law in 2014 and Mergers & Acquisitions Law in 2013.

Shannon Lowry Nagle is the Assistant General Counsel of CIT Group, Inc. and leads the mergers and acquisitions efforts for the legal department. Prior to joining CIT, she was a partner in the restructuring groups at Fried, Frank, Harris & Jacobson LLP and O'Melveny & Myers LLP in their New York City offices. Ms. Nagle's practice has included representing bondholders, secured and unsecured creditors, debtor-in-possession lenders, ad hoc and official committees of creditors, and other parties in interest. Ms. Nagle also has represented debtors, including distressed portfolio companies, as well as private equity funds and others in connection with the acquisition of distressed companies and in the sale of assets of financially troubled entities. Ms. Nagle's experience covers a wide range of industries, including financial institutions, retail, healthcare, entertainment, construction, auto, airlines, textiles, and telecommunications. She has extensive in-court experience, having litigated before bankruptcy courts in numerous states. Ms. Nagle is Board Certified in Business Bankruptcy. Ms. Nagle graduated from the University of Florida and the University of Miami School of Law.
Several years ago, Patricia Redmond asked the Task Force Chairs to consider drafting a model Asset Purchase Agreement for bankruptcy sales. At the time, Mrs. Redmond served as the Chair of the Business Bankruptcy Committee of the American Bar Association’s Business Law Section. Her idea was to create a uniform model asset purchase agreement that practitioners could use for bankruptcy sales. The Task Force was born.

The Task Force commenced this project using the Negotiated Acquisitions Committee’s 2001 Model Asset Purchase Agreement as a guide. The Bankruptcy Model Asset Purchase Agreement differs in many respects from the 2001 non-bankruptcy version because an asset purchase in a bankruptcy context is quite different from an asset purchase outside of bankruptcy given legal issues and customs. The Bankruptcy Model Asset Purchase Agreement highlights the differences, includes commentary as a teaching mechanism, and provides ancillary documents and appendices.

The members of the Bankruptcy Model Asset Purchase Agreement Task Force are:

Marc J. Carmel (Co-Chair) .................................................... Chicago, IL
Donald R. Kirk (Co-Chair) ..................................................... Tampa, FL
Adam C. Maerov (Co-Chair) .................................................... Calgary, Canada
G. Alexander Bongartz ........................................................ New York, NY
Ted Austin Dillman ............................................................. Los Angeles, CA
Robert Goodrich, Jr. .......................................................... Nashville, TN
Robert A. Klyman .............................................................. Los Angeles, CA
Kenneth D. Kraft .............................................................. Toronto, Ontario
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Jason M. Rudd ............................................................... Houston, TX
Todd M. Schwartz ............................................................ Palo Alto, CA
Martin A. Sosland ............................................................. Dallas, TX

The effort put forth by the Task Force members was substantial. The Co-Chairs and members spent countless hours in meetings at American Bar Association conferences and in engaging in the research necessary to draft the Bankruptcy Model Asset Purchase Agreement.
The Task Force also worked with numerous members of their own law firms and companies as additional resources to complete the project. We are thankful for everyone’s tireless and persistent effort.

Marc J. Carmel
Donald R. Kirk
Adam C. Maerov
Co-Chairs,
Model Asset Purchase Agreement Task Force
I. ASSET SALE PROVISIONS INSIDE AND OUTSIDE OF BANKRUPTCY

A. No-Shop Provisions

1. **Definition:** a covenant in a letter of intent or asset purchase agreement that is designed to prevent seller’s management from seeking out or cooperating with another bidder.

2. **Purpose:** to protect the buyer by giving it the exclusive right to the deal.
   a. A No-Shop provision restricts the seller from one or all of the following:
      i. Soliciting competing bids
      ii. Providing information to competing bidders
      iii. Encouraging or negotiating a competing transaction
      iv. Notifying buyer of any inquiry, request for information or competing bid it receives.

3. **Pre-Bankruptcy Sales**
   a. An Asset Purchase Agreement (APA) entered into, but not consummated, pre-petition is an executory contract.
   b. If the Debtor rejects the APA, the buyer cannot enforce a no-shop provision, and is limited to a rejection damages claim, which is a general unsecured claim.¹
   c. If buyer believes Debtor is only in bankruptcy to avoid its obligations, buyer may seek dismissal of the case under § 1112(b).

4. **Bankruptcy Sales:** Not generally used
   a. APAs entered into during bankruptcy are subject to court approval.
   b. Debtor is not bound by the terms of a no-shop provision until the APA is approved by the court.

5. **Enforceability:** A no-shop provision that is too restrictive is generally not enforceable because it prevents the selling company’s board of directors from satisfying its fiduciary duties to stockholders.²
   a. To make them enforceable, parties will agree to exceptions to no-shop provisions.
   b. The most common exceptions are “window shop” and “go shop” provisions.
      i. **Window Shop:** allows seller, subject to certain conditions, to respond to unsolicited, alternative transaction proposals by providing confidential information to, and entering into negotiations with, the third party bidder
      ii. **Go Shop:** more significantly carves back the no-shop provision to allow the seller to actively solicit competing bids and negotiate with third parties for a limited period of time after the signing of the transaction agreement (usually, 30 to 60 days)

¹ *In re Rega Properties, Ltd.*, 894 F.2d 1136, 1140 (9th Cir. 1990) (finding that specific performance was not available relief under section 365 because it would undercut the core purpose of rejection) quoting *Lubrizol Enter., Inc. v. Richmond Metal Finishers, Inc.* (In re Richmond Metal Finishers, Inc.), 756 F.2d 1043, 1048 (4th Cir. 1985).

iii. Another exception is the **fiduciary out**, which allows the seller to respond to alternative proposals if it is required to do so in order to discharge its fiduciary duties under applicable law.

iv. In bankruptcy, competitive auction process is commonly used to sell assets because the auction process decreases the risk of violating fiduciary duties.

**B. Buying and Selling Litigation Claims**

1. **Causes of action that accrue pre-petition are property of the estate,**\(^3\) which may be sold pursuant to 11 U.S.C. §363.\(^4\)

2. **Privilege:** the attorney-client privilege is generally lost when there is an intentional or inadvertent production of the communication to a third party.

   i. **Exception:** The Common Interest Doctrine

      a. When the parties to the communication share a common interest, the attorney-client privilege is not waived.

      b. This doctrine is relied upon by a potential purchaser when evaluating litigation claims held by a bankruptcy estate.

      c. For the doctrine to apply, the parties must have common interests that are legal, not just commercial, and most courts require that the interests be identical, not just similar.

      d. **Elements:**

         1) the communication was made by separate parties in the course of a matter of common interest,

         2) the communication was designed to further that effort, and

         3) the privilege has not otherwise been waived.\(^5\)

3. **Privilege, Common Interest, and Buying Litigation Claims**

   i. For disclosed information to remain privileged, a confidentiality agreement is required.\(^6\)

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\(^4\) In re Moore, 608 F.3d 253, 258 (5th Cir. 2010) (A trustee may sell litigation claims that belong to the estate, as it can other estate property, pursuant to § 363(b)); In re Rickel Home Centers, Inc., 209 F.3d 291, 297 (3d Cir. 2000); In re Parker, 499 F.3d 616, 628 (6th Cir. 2007); Simantob v. Claims Prosecutor, LLC (In re Lahijani), 325 B.R. 282, 287 (9th Cir. BAP 2005) (“Causes of action owned by the trustee are intangible items of property of the estate that may be sold.”).


\(^6\) E.g., Devon It, Inc. v. IBM Corp., CIV.A. 10-2899, 2012 WL 4748160, at *1 (E.D. Pa. Sept. 27, 2012) (where the documents produced to the third-party funder were subject to a “Confidentiality, Common Interest and NonDisclosure Agreement” there was no waiver of the attorney-client privilege or the work product doctrine).
ii. Disclosure of protected communications in a manner that substantially increases the opportunity for potential adversaries to obtain the information could result in a waiver of the privilege.  
   a. Oral argument extending beyond vague statements could constitute this sort of disclosure.

iii. The Common Interest Doctrine is not an absolute protection against the waiver of privilege.
iv. Attorney-client privilege and its waiver are state-law issues.
v. Methods to reduce the risk of waiver:
   1) Execute a common interest agreement;
   2) Identify the common interest;
   3) Limit access to any privileged information;
   4) Transfer any privileged information through counsel;
   5) Limit the amount of privileged information shared; and
   6) Clearly mark all privileged documents.

vi. Debtor should also seek approval of a provision in the bidding procedures order that protects attorney-client privilege with respect to litigation claims on which the bidders are conducting diligence.

C. Post-Sale Claims
1. Generally
   i. Post-closing claims usually relate to a breach of a representation or warranty as to the condition of the property being sold.
   ii. APAs may also include post-closing adjustments whereby one party has a claim against the other as a result of post-closing performance or information.

2. Bankruptcy Sales
   i. As is, where is sale: Debtors usually provide little or no representations or warranties on the condition of the assets in bankruptcy sales.
      a. Why? The debtor-seller is administering its estate for a limited period of time with the objective of confirming a chapter 11 plan or otherwise fully administering its estate.
   ii. After debtor administers its estate it will have little or no assets to satisfy any post-closing claims.

3. Non-Bankruptcy Sales
   i. Equity owners may guaranty post-closing claims; however, in bankruptcy sales, the equity owners are generally out of the money and have no incentive to guarantying post-closing claims.

4. Considerations when Addressing Post-Closing Claims
   i. Limitations on survival of claims:
      a. Caps on amount of recovery; and
      b. Limitation on time period to assert claims.

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8 Id.
II. NEW MODEL APA PREVIEW: COMMENTARY ON SELECT SECTIONS

A. Assumption and Assignment of Contracts

1. Executory Contracts and Unexpired Leases
   a. Section 2.1(e) of the Model Agreement provides for the assignment of all of the seller’s contracts, and Section 2.10 of the Model Agreement addresses consents required related to assignments of contracts.
   b. Because these issues are usually handled differently in bankruptcy, Section 2.1 and 2.10 of the Commentary discuss how executory contracts and unexpired leases are treated in bankruptcy transactions.
   c. In section 2.10 of the Commentary, we provide a sample provision addressing assumption and assignment of executory contracts and unexpired leases in bankruptcy.

2. The Basics: Executory Contracts
   a. Definition: “Executory contract” is not defined in the Bankruptcy Code.
      i. Countryman test: an executory contract is a contract under which the obligation of both the debtor and the other party to the contract are so far unperformed that failure of either to complete performance would constitute a material breach excusing the performance of the other. 9
   b. Exceptions: Not every contract that appears executory in nature will fall under the ambit of Section 365 and the debtor will not have the same rights to assume or assign such agreements. Courts and Congress have excepted these agreements from the debtor’s right to free assignment of contracts.
      i. Collective bargaining agreements; 10
      ii. Retiree benefit plans; 11
      iii. Pension plans; 12
      iv. Personal service contracts, loans, and other financial commitments and contracts for which applicable non-bankruptcy law excuses performance by the counterpart; 13
      v. FCC licenses; 14

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9 Sharon Steel Corp. v. Nat’l Fuel Gas Distribution Corp., 872 F.2d 36 (3d Cir. 1989); In re Wegner, 839 F.2d 533 (9th Cir. 1988). This definition, referred to as the “Countryman test,” was first set forth by Prof. Vern Countryman in his definitive article, Executory Contracts in Bankruptcy (Part I), 57 Minn. L. Rev. 439 (1973), and became part of the Bankruptcy Code’s legislative history. H.R. REP. 95-595, 1978 U.S.C.C.A.N. 5963.
f. Intellectual property licenses may or may not be assignable, and assignability is determined on a fact-specific basis, and g. “Leases” in the oil and gas industry.

iii. Court approval: required to assume or reject an executory contract.

a. The debtor must also give notice to the other party to the contract and the U.S. Trustee.

iv. Timing: 120 days to assume or reject commercial real estate leases.

a. Only one 90-day extension allowed unless the landlord consents in writing to additional extensions.

3. Section 2.1(j): Avoidance Actions

i. Because avoidance actions are largely unique to bankruptcy and frequently subject to negotiation with the creditors’ committee and other parties, we included the following definition of avoidance actions, and discussed the considerations that impact the sales of avoidance actions.

“Avoidance Action”—any and all claims, rights, or causes of action of Seller arising under Bankruptcy Code sections 544 through 551, and actions under similar state and federal laws, including fraudulent transfer or fraudulent conveyance claims.

4. Section 2.2: Excluded Assets

i. Section 2.2 of the Commentary does not include proposed language revisions, but discusses the considerations that go into the decision to exclude assets in the bankruptcy context, and notes that buyers often preserve the right to move acquired assets to excluded assets for some period after the agreement is executed (e.g., the sale hearing or closing).

5. Section 2.3: Consideration

i. Types of Consideration

a. In Section 2.3 of the Commentary, we discuss the most common forms of consideration in bankruptcy transactions (cash, assumption of liabilities, and credit bids), and discuss the Model Agreement’s inclusion of a note payable over time as part of the purchase price, which is atypical in bankruptcy transactions.

1) Among other things, we included the following sample language that could be added if a credit bid were part of the process:


“...the release and waiver by Buyer of any obligations, claims, rights, actions, causes of action, suits, liabilities, damages, debts, costs, expenses and demands whatsoever, in law or in equity, arising under, or otherwise relating to, the [RELEVANT CREDIT AGREEMENT] against Seller and any guarantors (and their respective successors and assigns), in an aggregate amount equal to _____ dollars ($______). . .”

b. Deposits
   i. The Model Agreement did not include a deposit, whereas deposits are common in bankruptcy transactions, and are virtually always required for bidders other than the stalking horse. Accordingly, we included sample provisions addressing deposits, both for a stalking horse and non-stalking horse bidder, which are set forth below:

   ii. Sample stalking horse provision:

   “On the next Business Day following the date of this Agreement, Buyer shall execute and deliver to Seller an escrow agreement and shall deposit with the Escrow Agent ________ dollars ($[______]) (the “Deposit”). The Deposit shall not be subject to any lien, attachment, trustee process, or any other judicial process of any creditor of Seller or Buyer. Interest accrued on the Deposit shall become a part of the Deposit and shall be paid to the party entitled to the Deposit. The Deposit shall be credited to the Purchase Price if the Closing occurs, and otherwise distributed pursuant to the applicable escrow agreement.”

   iii. Sample competing bidder provision:

   “On the Business Day following Buyer’s receipt of notice from Seller that an Auction will occur in accordance with the Bidding Procedures, Buyer shall deposit ________ dollars ($[______]) (the “Deposit”), which shall be held in escrow pursuant to the Bidding Procedures Order. The Deposit shall not be subject to any lien, attachment, trustee process, or any other judicial process of any creditor of Seller or Buyer. Interest accrued on the Deposit shall become a part of the Deposit and shall be paid to the party entitled to the Deposit. The Deposit shall be credited to the Purchase Price if the Closing occurs, and otherwise distributed pursuant to the Bidding Procedures Order and terms of this Agreement.”

   iv. Section 2.3 of the Commentary also includes a sample provision addressing application and return of the deposit, as well as limitations on remedies.
6. **Section 2.4: Liabilities**
   i. The Model Agreement includes assumption of a number of liabilities to facilitate the continuous operation of the business.
   ii. But the buyer in a bankruptcy transactions often assumes only liabilities arising after Closing, so we included the following sample provision in the “Assumed Liabilities” section:

   “(#[#]) any Liability to the extent occurring and arising from and after the Effective Time as a result of Buyer’s ownership and operation of the Assets.”

   iii. We also noted the following provision in the Retained Liabilities (a/k/a excluded liabilities), that frequently appears in bankruptcy transactions:

   “(#[#]) any Liability relating to or arising, whether before, on, or after the Closing, out of, or in connection with, any of the Excluded Assets.”

   iv. This section of the Commentary also discusses the circumstances under which the buyer may choose to assume a broader set of liabilities and the value of assuming these liabilities when evaluating the buyer’s bid for the assets.

7. **Section 2.5: Allocation**
   i. The substantive issues involved in the tax allocation of the Purchase Price are much the same in bankruptcy and non-bankruptcy transactions.
   ii. But the debtor’s creditors and the Bankruptcy Court will typically not want purchase price allocation (usually controlled by the buyer) to determine creditors’ rights or recoveries through the bankruptcy process. Accordingly, we included the following addition to Section 2.5 of the Model Agreement:

   “(b) Notwithstanding the allocation of the Purchase Price in Section 2.5(a), nothing in the foregoing shall be determinative of values ascribed to the Assets or the allocation of the value of the Assets in any Chapter 11 plan of reorganization or liquidation that may be proposed. Seller reserves the right on its behalf and on behalf of Seller’s estate, to the extent not prohibited by applicable law and accounting rules, for purposes of any Chapter 11 plan of reorganization or liquidation, to ascribe values to the Assets and to allocate the value of the Assets to Seller in the event of, or in order to resolve, creditor disputes in the Bankruptcy Case.”

   iii. Section 2.5 of the Commentary also includes a sample provision concerning allocations between domestic and foreign sellers subject to insolvency proceedings in more than one jurisdiction.

8. **Section 2.8: Adjustment Amount and Payment**
   i. Section 2.8 of the Model Agreement contains a working capital adjustment.
   ii. We included the following sample provision to address the bankruptcy priority of the buyer’s right to recover any amounts determined to be owed to the buyer as a
result of the purchase price adjustment (and discuss a variety of other issues relating to purchase price adjustments):

“Any obligation of Seller hereunder shall constitute a super-priority administrative claim under Sections 503 and 507 of the Bankruptcy Code, and Buyer shall be deemed to have a first-priority lien on and security interest in all sale proceeds, senior to the claims of all secured and unsecured creditors, until such time as Seller has made all payments required hereunder.”

9. Section 2.9: Adjustment Procedure
   i. Section 2.9(c) of the Model Agreement establishes the mechanics for determining the working capital adjustment, and provides that disputes will be resolved by independent accountants.
   ii. But because the Bankruptcy Court will generally adjudicate disputes related to the purchase price in a bankruptcy transaction, we included the following replacement provision in Section 2.9 of the Commentary:

“(d) If Seller duly gives Buyer such notice of objection, and if Seller and Buyer fail to resolve the issues outstanding with respect to the Closing Financial Statements and the calculation of the Closing Working Capital within thirty (30) days of Buyer’s receipt of Seller’s objection notice, Seller and Buyer shall submit the issues remaining in dispute to the Bankruptcy Court for adjudication. Seller and Buyer shall each bear its own fees and expenses relating to such adjudication.

10. Selling Contracts: Assumption/Assignment
   i. Power to Assume or Reject: Debtor can assume and assign the vast majority of its executory contracts and unexpired leases without the consent of the non-debtor counterparty, notwithstanding any provision in the agreement "that prohibits, restricts, or conditions the assignment of such contract or lease."20
      a. This power will usually significantly reduce the number of contracts - material or nonmaterial - requiring the consent of the non-debtor party.
      b. But, when the cure amount or adequate assurance of future performance is disputed by the non-debtor counterparty to the agreement, these issues can be carried over to a subsequent hearing, particularly when the sale process is very accelerated. In these situations, Buyer typically retains the right to either accept assignment of, or reject, these contracts or leases pending the Bankruptcy Court’s resolution of these disputes.
   ii. Assumption
      a. Requirements: An executory contract may be assumed if the Trustee:
         1) Cures (or provides adequate assurance of prompt cure) of default. Courts usually limit to no more than one year;

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2) Compensates (or provides adequate assurance of prompt compensation) for actual damages resulting from default; and
3) Provides adequate assurance of future performance.\textsuperscript{21}

b. Unenforceable contract provisions

1) Ipso facto clauses;\textsuperscript{22}
2) Penalty rate and penalty provisions arising from non-monetary defaults;\textsuperscript{23}
3) Debtor need not cure non-monetary defaults that are impossible to remedy at and after the time of assumption. Defaults resulting from a lease provision that prohibits a debtor from “going dark” may be “cured by performance at and after the time of assumption in accordance with such lease.” Debtor must provide an “economic cure” for monetary losses arising pursuant to a non-monetary default.\textsuperscript{24}

iii. Lease Assignment

a. Requirements: Trustee may assign a lease if:
   1) the lease is assumed; and
   2) the Trustee provides adequate assurance of assignee’s future performance, whether or not there has been a default in such contract or lease.\textsuperscript{25}

b. Restrictions on Assignment

1) Loan or financing commitments.
2) Terminated nonresidential real property lease.
3) Applicable law (other than lease or contract provision prohibiting assignment of rights or delegation of duties) excuses party from accepting performance or rendering performance to an entity other than the debtor or debtor-in-possession.

c. Assignment relieves the estate of liability for subsequent breach.\textsuperscript{26}

d. Special Rules and Provisions:

1) Shopping Center provisions;\textsuperscript{27} and
2) Rejection of Intellectual Property contracts.\textsuperscript{28}

\textsuperscript{21} 11 U.S.C. § 365(b)(1).
\textsuperscript{22} 11 U.S.C. § 365(e).
\textsuperscript{23} 11 U.S.C. § 365(b)(2)(D).
\textsuperscript{26} 11 U.S.C. § 365(k).
\textsuperscript{27} 11 U.S.C. § 365(b)(3).
\textsuperscript{28} 11 U.S.C. § 365(n)(1)–(4).
11. Section 2.10: Consents
   i. Section 2.10 of the Model Agreement addresses the situation where third party consents are not obtained prior to Closing, and provides for different approaches depending on whether the contracts are material or nonmaterial.

   ii. As a result of, among other things, Section 365 of the Bankruptcy Code, the assumption and assignment of executory contracts and unexpired leases in a bankruptcy transaction is generally handled differently than outside of bankruptcy, and poses its own set of issues unique to the bankruptcy process (e.g., cure of defaults and adequate assurance of future performance).

   iii. Accordingly, Section 2.10 of the Commentary discusses assumption and assignment of executory contracts and unexpired leases, and includes the following sample provision addressing these issues and the bankruptcy mechanics:

   **2.10 CONSENTS; ASSUMPTION AND ASSIGNMENT OF CONTRACTS**

   1) Assignments. Seller shall transfer and assign all Seller Contracts to Buyer, and Buyer shall assume all Seller Contracts from Seller, as of the Closing Date pursuant to, inter alia, Section 365 of the Bankruptcy Code and the Sale Order; provided, however, that Buyer may designate any Seller Contracts as an Excluded Asset in accordance with Section 2.2(f) and as set forth below (the “Excluded Contracts”). Seller Contracts not designated as Excluded Contracts are referred to herein as the “Assumed Contracts”.

   2) Determination of Cure Amounts. Schedule 2.10(a) hereto sets forth Seller’s good faith estimate of the Cure Amount (as defined below) for each Seller Contract. Prior to the Sale Hearing, Seller shall commence appropriate proceedings before the Bankruptcy Court and otherwise take all necessary actions in order to (a) determine any costs necessary to cure all defaults (as required by Section 365 of the Bankruptcy Code) under each Assumed Contract (the “Cure Amounts”), and (b) resolve any disputes as to Cure Amounts prior to or at the Sale Hearing. All Cure Amounts for the Assumed Contracts shall be the sole responsibility of [Buyer/Seller], irrespective of the aggregate amount of such Cure Amounts (whether reflected on Schedule 2.10(a) or otherwise) and shall be paid by [Buyer/Seller] on or as soon as practicable following the Closing Date.

   3) Exclusion of Contracts. At any time (and from time to time) prior to the Closing, Buyer may identify any Seller Contract as one that Buyer no longer desires to have assigned to Buyer.
4) Consents; Non-Assignable Contracts; Government Authorization. To the maximum extent permitted by the Bankruptcy Code or other applicable law, the Assumed Contracts and Government Authorization shall be assumed by Seller and assigned to Buyer as of the Closing Date. Notwithstanding anything to the contrary in this Agreement, to the extent that the assignment to Buyer of any Assumed Contract or Government Authorization is not permitted by law or is not permitted without the consent of another Person and, in the case of the Assumed Contracts and Government Authorization that are the subject of Section 365 of the Bankruptcy Code and the Sale Order, as applicable, such restriction cannot be effectively overridden or canceled by the Sale Order, or other related order of the Bankruptcy Court, then this Agreement will not be deemed to constitute an assignment or an undertaking or attempt to assign the same or any right or interest therein if such consent is not given and the Closing shall proceed with respect to the remaining Assumed Contracts and Government Authorization without any reduction in the Purchase Price; provided, however, that the foregoing shall not constitute a waiver, if any, of any closing condition of Buyer related to Material Consents or the assignment of Seller Contracts; provided, further, that Seller will use commercially reasonable efforts to obtain any such consents to assign such Assumed Contracts and Government Authorization to Buyer following the Closing; provided, further, that Seller shall not be required to incur any Liabilities or provide any financial accommodation in order to obtain any such consents.

5) Further Assurances. Seller and Buyer shall use commercially reasonable efforts to take, or cause to be taken, all appropriate action, do or cause to be done all things necessary, proper or advisable under applicable law, and execute and deliver such documents and other papers, as may be required to consummate the transactions contemplated by this Agreement at or after the Closing, including, subject to Section 2.10(d), assistance by Seller with the transfer of the Assumed Contracts and Government Authorization; provided, however, that nothing in this Section 2.10(e) shall prohibit Seller from ceasing operations or winding up its affairs following the Closing. Buyer shall use commercially reasonable efforts to cooperate with Seller and provide Seller with information reasonably sufficient to enable Seller to demonstrate adequate assurance of future performance (as required by Section 365 of the Bankruptcy Code) as to Buyer.
12. Sections 3.8 and 3.20: Representations and Warranties Dealing with Contracts

i. Section 3.8 of the Model Agreement: provides a Seller representation that Part 3.8 accurately describes all Real Property Leases. One of the benefits of conducting sales transactions in a bankruptcy case is the ability to assume and assign certain executory contracts and unexpired leases without the need to obtain consent from the contract or lease counterparty, even where consent is required under the contract or lease. Accordingly, Buyers should seek additional representations and warranties in the Agreement about the validity and enforceability of real property leasehold interests by modifying Section 3.6 of the Model Agreement through adding language similar to the following:

... Seller has a valid and enforceable leasehold interest under each of the Real Property Leases under which it is a lessee, subject to applicable bankruptcy, insolvency, reorganization, moratorium and similar laws affecting creditors’ rights and remedies generally and subject, as to enforceability, to general principles of equity (regardless of whether enforcement is sought in a proceeding at law or in equity). Each of the Real Property Leases is in full force and effect. There is no default under any Real Property Lease by Seller, by any other party thereto, and no event has occurred that with the lapse of time or the giving of notice or both would constitute a default thereunder. No party to any of the Real Property Leases has exercised any termination rights with respect thereto ...

ii. Section 3.20 of the Model Agreement: sets forth general Seller representations and warranties regarding Seller Contracts that are disclosed in Part 3.20(a).

a. Section 3.20(b) of the Model Agreement provides certain Shareholder representations in respect of Seller Contracts. Shareholders will not benefit from, and may in fact be excluded from, the Section 363 sale process. Therefore, it is unusual for a shareholder to be party to or make representations in respect of asset purchase agreements in Section 363 sales in bankruptcy. Section 3.20(b) of the Model Agreement should be deleted or modified accordingly.

b. Section 3.20(c)(ii) provides a Seller representation that each Contract identified or required to be identified in Part 3.20(a) and which is being assigned to or assumed by Buyer is assignable by Seller to Buyer without the consent of any other Person.

1) As described above, one of the benefits of conducting sales transactions in a bankruptcy case is the ability to assume and assign certain executory contracts and unexpired leases without the need to obtain consent from the contract or lease counterparty, even where consent is required under the contract or lease.

2) The representation and warranty in Section 3.20(c)(ii) of the Model Agreement should be modified to take advantage of the full protection of Section 365 of the Bankruptcy Code by adding language such as:

... under Section 365 of the Bankruptcy Code ...
c. Because contracts must be executory to be assumed and assigned, Buyer may seek additional Seller representations and warranties in the Agreement concerning the enforceability of, and lack of defaults and lack of termination events of, the Contracts Buyer seeks to assume by adding language similar to the following:

. . . Seller has a valid and enforceable interest under each of the Contracts set forth in Part 3.20(a), subject to applicable bankruptcy, insolvency, reorganization, moratorium, and similar laws affecting creditors’ rights and remedies generally and subject, as to enforceability, to general principles of equity (regardless of whether enforcement is sought in a proceeding at law or in equity). Each of the Contracts identified in Part 3.20(a) is in full force and effect. There is no default under any Contract set forth in Part 3.20(a) by Seller, by any other party thereto, and no event has occurred that with the lapse of time or the giving of notice or both would constitute a default thereunder. No party to any of the Contracts set forth in Part 3.20(a) has exercised any termination rights with respect thereto . . .

d. Section 3.20(d) of the Model Agreement provides general Seller representations and warranties that, among other things, Seller is and has been in compliance with all applicable terms and requirements of each Seller Contract which is being assumed by Buyer. Because Seller, as a debtor in bankruptcy, may not be able to make all of the representations and warranties in Section 3.20(d) of the Model Agreement, Seller should review this section carefully and modify (or delete provisions thereof) accordingly.

B. Removing Excluded Assets

1. When Seller is subject to an onerous lease, or when Buyer has its own premises, Buyer may decide not to assume Seller’s leases (likewise where Buyer acquires only Seller’s profitable locations and leaves behind unprofitable locations). Accordingly, depending on the specific circumstances of the sale, there may be purchased assets located on premises that Buyer will not acquire. If this is the case, Section 10.5 of the Model Agreement would need to be revised, for instance, by requiring Seller to relocate Assets in facilities that will not be acquired by Buyer to facilities that will be acquired.

2. Alternatively, because Seller may refuse to allow relocation of assets pre-closing due to concern about the ramifications of these steps if the sale does not close, Section 10.5 of the Model Agreement could be revised to require either Buyer or Seller to relocate Assets and excluded assets to the appropriate locations within a designated post-closing period (e.g., within 30 days following Closing). However, while the Bankruptcy Code allows unexpired leases to be assigned to Buyer, the Bankruptcy Court typically will not allow Buyer to use a facility leased by Seller for an extended period post-closing without assuming the lease. In addition, the post-petition rent under Seller’s leases will be an administrative claim in Seller’s Bankruptcy Case, so Seller will typically seek to reject
leases that are not assumed and assigned to Buyer promptly following (or effective as of) the Closing. Accordingly, while it is typical for a transition period to allow for Buyer to take possession of the acquired assets on Seller’s premises subject to leases that will not be assigned to Buyer, this transition period is usually brief. In addition, the party responsible for relocating the assets and bearing the cost of doing so (as well as lease costs during any post-closing period) would be a negotiated item. Buyer may prefer to bear these costs and responsibilities and reduce or otherwise adjust its Purchase Price for the following reasons: (a) most bankruptcy sales are “as is, where is;” (b) Buyer will typically have the right to determine whether to assume a lease; (c) Buyer is often wary of Seller’s ability to perform after the sale is consummated (when Seller will often have few continuing employees); and (d) Seller’s ability to pay damages for Seller’s failure to meet post-closing obligations may be limited. Accordingly, Section 10.5 of the Model Agreement may need to be substantially revised by replacing the language with alternative language as set forth below, placing responsibility on Buyer and providing for post-closing relocation:

10.5 REMOVING ASSETS

On or before the date that is thirty (30) days following the Closing Date (a) Buyer shall remove all Excluded Assets from all Facilities and other Real Property to be occupied by Buyer (in the case of leased Facilities and other leased Real Property, as to which such lease has been assumed and assigned to Buyer pursuant to Section 2.1), and (b) Buyer shall remove all Assets from all Facilities and other Real Property that is not to be occupied by Buyer (in the case of leased Facilities and other leased Real Property, as to which such lease has not been assumed and assigned to Buyer pursuant to Section 2.1). The cost of repairing any damage to the Excluded Assets or to the Facilities or other Real Property not to be occupied by Buyer and resulting from such removal shall be borne by Buyer. Should Buyer fail to remove the Assets as required by this Section, Seller shall have the right, but not the obligation, (a) to remove the Assets at Buyer’s sole cost and expense; (b) to store the Assets and to charge Buyer all out-of-pocket storage costs associated therewith; or (c) to exercise any other right or remedy conferred by this Agreement or otherwise available at law or in equity.

C. Section 14.1: Guaranty

1. Buyers often use a newly formed acquisition subsidiary in bankruptcy acquisitions, raising concerns as to the buyer-entity’s financial wherewithal.
2. To address these concerns, Section 14.1 of the Commentary sets forth a sponsor/parent guaranty, and various guaranty-related waivers parties may consider.

D. Section 15: Designation Rights

1. If, at the time of the sale, Seller has not yet rejected certain executory contracts, and it has not yet been determined whether Buyer will assume such contracts, then the parties may desire to give Buyer the option to elect to assume and assign such contracts (referred to as “Designation Rights”). As a result of the reduced time to assume or reject leases and pressure from lenders, Debtors quickly file sale motions. To maximize value obtained by
the estate in such sales and curb administrative rent expense, Debtors not only sell the right to conduct GOB sales (inventory and FF&E in stores) but often sell the right to assume to reject the store leases as well.29

2. Typically the sale of Designation Rights is included in the sale procedure motion.
   i. Landlords beware – the motion may attempt to fix cure amounts unless an objection is filed, provide for an extremely abbreviated notice period with respect to the proposed assignee (ultimate purchaser of the lease) and establishing cure amount, extend the Section 365(d)(4) period beyond 210 days, or permit the designation rights owner to assign the lease to another third party marketing agent for a fee.
      a. Landlords have objected in the Cache, Deb Stores and similar retail cases requesting adequate protection for administrative rent and cure amounts. Concerns over payment of all GOB sale proceeds to secured lender or subsequent bankruptcy filings of purchasers of leases prior to satisfying cure obligations.30
   ii. Liquidating Agent (often a newly formed joint venture between an inventory liquidator and real estate marketing firm) pays rent and related charges and performs all obligations under the lease pursuant to the terms of the agency agreement/sale agreement until the lease is assumed and assigned, or rejected.31

3. Recent retail cases expand Designation Rights to include the agent’s ability to profit from selling not only store leases, but also intellectual property, licenses, and a variety of assets.32

4. Consideration: In exchange for these valuable Designation Rights, Seller will want to receive consideration from Buyer. This consideration can be structured in several ways. One way is to require Buyer to assume responsibility for the obligations under the contracts subject to the Designation Rights (any such contract, a “Designation Rights Contracts”) through the effective date of assumption or rejection of the Designation Rights Contract. This structure balances the interests between Buyer and Seller by having Buyer pay for obligations associated with such Designation Rights Contract until Buyer either exercises its rights or the period of time to exercise the Designation Rights (referred to as the “Designation Rights Period”) has expired.

5. Accordingly, the parties may wish to modify the Model Agreement to include an additional section dealing with Designation Rights. An example of such a provision is as follows:

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29 The leading case to address selling the right to make the assumption/rejection decision is In re Ames Dept. Stores, Inc., 287 B.R. 112 (Bankr. S.D.N.Y. 2002).


32 See Id.
(a) Any Seller Contract not designated by Buyer as either an Assumed Contract or an Excluded Asset [__] days prior to the Closing Date shall constitute a Designation Rights Contract. Buyer shall have the right, by written notice to Seller within the Designation Rights Period, to specify any Designation Rights Contracts to be held by Seller and not rejected pursuant to Section 365 of the Bankruptcy Code for the duration of the Designation Rights Period; and, further, that with respect to any such Designation Rights Contract (i) Buyer shall reimburse Seller and thereby be solely responsible for all obligations associated with the continuation by Seller of such Designation Rights Contract, as set forth in a budget proposed by Seller and approved by Buyer no later than [__] days prior to the Closing Date (such budget, the “Designation Rights Budget”), for the period from the Closing through the earlier of (A) the end of the Designation Rights Period or (B) the date of Seller’s receipt of written notice from Buyer authorizing Seller to seek the rejection of such Designation Rights Contract, (ii) all cash collected by Seller in respect of, and other benefits deriving from, such Designation Rights Contract shall be promptly delivered to Buyer, and (iii) the foregoing shall not affect the validity of the transfer to Buyer of any other Asset that may be related to such Designation Rights Contract. In the event that the costs associated with any Designation Rights Contract exceed the Designation Rights Budget (a “Designation Cost Overage”), Buyer shall have the right to include such Designation Rights Contract if Buyer increases the Designation Rights Budget in an amount equal to or exceeding the Designation Cost Overage.

(b) As to each Designation Rights Contract, as soon as practical after receiving further written notice(s) (each, an “Assumption Notice”) from Buyer during the Designation Rights Period requesting assumption and assignment of any Designation Rights Contract, Seller shall, subject to Buyer’s demonstrating adequate assurance of future performance thereunder, use its best efforts to seek to assume and assign to Buyer pursuant to Section 365 of the Bankruptcy Code any Designation Rights Contract(s) set forth in an Assumption Notice, and any applicable Cure Amounts shall be satisfied in accordance with this Agreement.

(c) As to each Designation Rights Contract, as soon as practical after receiving further written notice(s) from Buyer during the Designation Rights Period requesting rejection of any Designation Rights Contract (each, a “Rejection Notice”), Seller shall use its best efforts to reject such contract pursuant to Section 365 of the Bankruptcy Code.

(d) Notwithstanding anything herein to the contrary, on the date any Designation Rights Contract is assumed and assigned to Buyer pursuant to an Order of the Bankruptcy Court, such Designation Rights Contract shall be deemed an Assumed Contract for all purposes hereunder and Buyer shall
have, from and after the date of the Order of the Bankruptcy Court, no liability to Seller for any obligations accruing or becoming due thereunder.