

COD & CREDIT BIDS IN BANKRUPTCY

INTRODUCTION

With U.S. corporate bankruptcies poised to hit a decade-long high as a result of the economic impact of COVID-19, we have prepared these materials that detail the key bankruptcy tax issues and guidance offered by Linda Swartz, the chair of Cadwalader's Tax Group, in old and new speeches and panels. We hope you find this presentation to be both useful and informative.

For additional information, contact [Linda Swartz](mailto:linda.swartz@cwt.com) (linda.swartz@cwt.com).

Upcoming speaking engagements:

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| October 14, 2020 | <ul style="list-style-type: none">• Linda Swartz will be presenting "Tax Strategies for Financially Troubled Businesses and Other Loss Companies" at PLI's Tax Strategies for Corporate Acquisitions, Dispositions, Spin-Offs, Joint Ventures, Financings, Reorganizations & Restructurings 2020 |
| November 5, 2020 | <ul style="list-style-type: none">• Linda Swartz will be presenting "A Cause for Distress? The Ways the Federal Income Tax Pushes Taxpayers into Bankruptcy" at The University of Chicago Tax Conference |
| January 25, 2021 | <ul style="list-style-type: none">• Linda Swartz will be presenting "Distressed Corporations: Creditor and Shareholder Issues" at the 2021 University of Southern California Federal Tax Institute |
| February 8, 2021 | <ul style="list-style-type: none">• Linda Swartz will be presenting "Workouts and Debt Restructurings" at PLI's 23rd Annual Real Estate Tax Forum |
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LINDA Z. SWARTZ



Linda Z. Swartz
Chair, Tax
New York
(212) 504 6062
linda.swartz@cwt.com

Linda Swartz, the longtime chair of Cadwalader's Tax Group and member of the Firm's Management Committee, focuses her practice on structuring complex restructurings, bankruptcies, mergers and acquisitions, spin-offs, joint ventures, and foreign tax planning strategies. She also regularly advises clients on fund structures, financings and derivative transactions.

Linda is consistently recognized as one of the leading tax lawyers in the country. She was recently named one of 14 "Influential Women In Tax Law" by *Law360*, noted for her role as "a key architect on billion-dollar transactions involving major multinational companies" with clients describing her tax structuring expertise as "so strong that we don't even go to the IRS to get a blessing from them. We go to Linda to get a blessing from her." She has been described by *Chambers USA* as "acclaimed for her vast reservoir of practical knowledge of the U.S. tax code" and "an expert on the law of today but cognizant of where the law might go in the future, allowing clients to make decisions which last for the next ten years." Clients quoted by *The Best Lawyers in America* have described Linda as "the foremost U.S. tax advisor on structured acquisition and divestiture deals" and "a professional force of nature" with "extraordinary technical ability, coupled with fiercest and most trenchant deal negotiation skills of any transactional tax lawyer." She was also recognized as "2017 Foreign Tax Planning Lawyer of the Year" by *Finance Monthly*, and *Dow Jones*, reporting on Procter & Gamble's Reverse Morris Trust transaction with Coty, noted that "it isn't often you see a tax adviser credited on a deal, but that's exactly what happened for Cadwalader, Wickersham & Taft in P&G's complicated \$12.5 billion unloading of its beauty business to Coty."

Linda is widely regarded as a thought leader in the industry and is a prolific speaker and writer on a wide range of transactional tax issues, with articles that include "Partnership Bankruptcy Tax issues," "Debt Exchanges," "Bankruptcy Tax Issues," and "Bankruptcy Tax 101." She also authors the chapters on Debt Exchanges in *Collier on Bankruptcy Taxation* (Matthew Bender) and Securities Lending Transactions in *Taxation of Financial Institutions* (Clark Boardman Callaghan). In addition to writing, she speaks on a broad range of topics, including each year on workout and bankruptcy tax issues at the corporate and real estate tax PLI conferences.

Linda is a member of the Executive Committee of the New York State Bar Association Tax Section and has chaired its Tax-Free Reorganizations; Corporations; Bankruptcy; Consolidated Returns; Real Property; and Tax Accounting and Basis Committees.

Linda received her J.D. from University of Pennsylvania Law School, and her B.A. from Bucknell University, where she graduated *magna cum laude* and was elected to Phi Beta Kappa.

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Asset sales pursuant to Bankruptcy Code (BC) section 363 are increasingly popular (Chrysler; GM).

Much faster than asset sales pursuant to plan of reorganization or liquidation and generally allow buyer to take assets “free and clear” of debtor liabilities.

Where property being sold is subject to prepetition liens, BC section 363(k) gives a secured creditor the right to “credit bid” all or part of its secured claim in the auction.

- Credit bids permit secured creditor to protect against low bids.
- Under bankruptcy law, the face amount of a debt claim bid for collateral is treated as the economic value of claim, even when collateral is worth less than amount of debt claim. See BC section 506(a); *SunMicron* case.

COD & CREDIT BIDS IN BANKRUPTCY (cont'd)

Debtor's acceptance of a credit bid should trigger COD income to the extent the issue price of the debt used to credit bid exceeds the FMV of assets acquired, even though credit bidder received "credit" for face amount of debt being bid in the 363 auction.

- Bankruptcy Code rule giving credit bidder face value "credit" does not change tax result because debtor has realized a benefit insofar as it is released from payment.
- *But consider* Reg. § 1.166-6(b)(2): As to the creditor, the amount of the debt "bid in" is treated as the fair market value **absent** clear and convincing evidence to the contrary, for purposes of (i) recognizing gain or loss with respect to the debt, and (ii) determining the tax basis of the acquired assets.
 - Would a lower valuation in bankruptcy be clear and convincing evidence?
- COD income realized in a section 363 credit bid sale should be eligible for the section 108(a) bankruptcy exclusion because the discharge of debt is granted by the court. See section 108(d)(2).
 - Order confirming results of auction should include language referencing section 108(d)(2).