

## **Motions for Authority to Sell Property Free and Clear of Liens and Encumbrances**

**Introduction.** Chapter 7 and Chapter 11 trustees, debtors in possession in Chapter 11 and Chapter 13 debtors (see 11 U.S.C. § 1303) often seek to sell property of the estate other than in the ordinary course of the debtor's business. Such transactions are governed by section 363(b)(1) of the Bankruptcy Code, which states simply that "[t]he trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate." Notice that this section does not refer to court authorization. The phrase "after notice and hearing" is defined in section 102(1):

(1) "after notice and a hearing", or a similar phrase -

(A) means after such notice as is appropriate in the particular circumstances, and such opportunity for a hearing as is appropriate in the particular circumstances; but

(B) authorizes an act without an actual hearing if such notice is given properly and if -

(i) such a hearing is not requested timely by a party in interest; or

(ii) there is insufficient time for a hearing to be commenced before such act must be done, and the court authorizes such act.

An actual hearing is not required - only the opportunity for one if time permits. For such an arrangement to work, the key component is adequate notice. Some courts have opined that in the absence of an objection, a trustee need not obtain an order to sell estate assets outside the ordinary course of business. *In re Bakalis*, 220 B.R.525, 531 (Bankr. E.D. N.Y. 1998) ("In fact, in most situations, sales that are properly noticed and set for hearing do not even require formal judicial approval. See *In re Telesphere Communications, Inc.*, 179 B.R. 544, 552 fn. 8 (Bankr. N.D. Ill.1994)"). Technically this appears true, at least if the property to be sold is

unencumbered, but the safer approach is to move for authority to conduct such a sale, which is what most lawyers do.

If the sale is to be free and clear of liens and encumbrances, the movant also must satisfy at least one subpart of section 363(f) with respect to each entity claiming a lien or encumbrance on the property to be sold. Section 363(f) provides:

(f) The trustee may sell property under subsection (b) or (c) of this section free and clear of any interest in such property of an entity other than the estate, only if -

- (1) applicable nonbankruptcy law permits sale of such property free and clear of such interest;
- (2) such entity consents;
- (3) such interest is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property;
- (4) such interest is in bona fide dispute; or
- (5) such entity could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest.

**Objections and Movant's Burden.** There are a handful of common objections to sales of assets. These include the lack of a business justification, an absence of good faith of the parties to the sale, unreasonable terms of the sale, the bypassing of the plan process in a Chapter 11 case, lack of adequate notice and an opportunity to review the proposed transaction, an inadequate sale price or failure to expose the assets to a relevant market with sufficient advertising and violations of rights of lienholders. When challenged, the movant has the burden of showing that a sound business basis for selling exists, that the sale is proposed in a good faith and that terms are fair and reasonable. *See 3-363 Collier on Bankruptcy - 15th Edition Revised P 363.01, et. seq.* If the property is to be sold free and clear of liens and encumbrances, the movant has the burden of showing that at least one subpart of section 363(f) is satisfied with respect to each holder of a lien or encumbrance. A movant cannot represent to the Court that no

impediment exists under section 363(f) if the movant has not conducted a search of public records to determine what liens or encumbrances have been recorded and obtained evidence of the amount of those liens or encumbrances.

**What the Motion Should Say.** With this background, the proper drafting of a motion to sell comes into sharp focus. A properly drafted motion will contain allegations of fact showing that there is business justification for the sale (at least in Chapter 11 cases) and that the terms of the sale, including price, and the method for conducting the sale, including advertising, are reasonable. With respect to negotiated sales, as opposed to auctions, the motion will show that the proposed transaction was negotiated at arms' length and in good faith.

The motion and the notice to be sent to creditors should contain the following specific factual allegations; The motion must contain those marked with an asterisk to satisfy every element of a section 363(f)(3) claim.

1. A description of the property to be sold.
2. The method used or to be used to market the property.
3. The name of the proposed buyer, if known, and an allegation that the sale transaction was or will be at arms' length.
4. The sale price or minimum bid price, if one has been set, the other material terms of the sale and an allegation that such price is or will be a fair value for the property.
5. An itemization of anticipated expenses and a statement concerning the maximum amount of expenses to be incurred in selling the property.
- \*6. The identity of each entity that has or may claim a lien against, or other interest in, the property, the nature of the lien or interest, the amount of debt owed to each such entity, and a

statement that after an appropriate search of public records, the movant is not aware of any other claimed interest or lien in the property.

\*7. The sum of the liens against the property.

\*8. An allegation that the sale price will exceed the sum of all costs of sale, all liens against the property and the debtor's exemption, except as such parties have consented to different treatment, the details of which are provided.

A motion to sell property free and clear of liens or other interests should be styled as a contested matter and should name as a respondent, each entity claiming a lien against, or other interest in, the property. **For each respondent, the motion must allege facts that satisfy at least one part of section 363(f).**

The fundamental point that the motion should make is that in closing the proposed sale, the trustee or debtor-in-possession will satisfy the fiduciary duty owed to the debtor, creditors and, if applicable, equity holders to maximize value by obtaining the best price on the best terms possible.

**Notice of the Motion.** Bankruptcy Rule 2002(a)(2) requires at least twenty days' notice by mail of "a proposed use, sale, or lease of property of the estate other than in the ordinary course of business, unless the court for cause shown shortens the time or directs another method of giving notice." Recall that section 363(b)(1) states that the trustee may sell property of the estate outside the ordinary course of business "after notice and a hearing." In order for this provision to have any sensible meaning, the notice must contain all the material facts concerning the proposed sale that a party interest would need to know in order to evaluate whether or not the

proposed sale makes business sense, is proposed in good faith and will bring the highest price under the best terms possible.

It is, therefore, not enough to say the house will be sold for \$125,000 and there will be approximately \$25,000 left over after paying liens and expenses. Rather, the movant must tell the parties in interest in the notice how the price was arrived at or will be arrived at, what efforts were or will be made in marketing the property, what the payment terms are and who will receive what from the proceeds of sale and why.

The notice should tell the recipients the deadline for objecting to the motion, where to file an objection, on whom it should be served, and the date, time and place of the hearing on the motion if one has been scheduled. The movant must also file a certificate of service showing proper service on each respondent and on the debtor, debtor's counsel if any, creditors and other parties in interest pursuant to Bankruptcy Rule 2002(a)(2).

**Service of the Motion.** Bankruptcy Rules 6004(c), 9014 and 7004 apply to motions to sell estate property free and clear of liens. Rule 6004(c) provides:

(c) Sale Free and Clear of Liens and Other Interests

A motion for authority to sell property free and clear of liens or other interests shall be made in accordance with Rule 9014 and shall be served on the parties who have liens or other interests in the property to be sold. The notice required by subdivision (a) of this rule shall include the date of the hearing on the motion and the time within which objections may be filed and served on the debtor in possession or trustee.

Bankruptcy Rule 9014, entitled "Contested Matters," states that a motion initiating a contested matter must be served in the manner provided for service of a summons and complaint by Bankruptcy Rule 7004.

I have posted a paper on service on my page on the Court's website. The points made there will not be repeated here, except to say that if a lienholder is not properly served, does not

waive proper service and is not paid in full, the lien will remain attached to the property being sold regardless of what the order authorizing the sale says. This has the potential of creating liability for professionals not paying attention to detail.

J.E.M.