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THE ART OF THE AUCTION: PRACTICAL INSIGHTS FROM SECTION 363 SALE PROCESSES

Navigating a bankruptcy-sale process requires the implementation of various procedures and following numerous requirements to ensure that the integrity of the sale process is preserved and a commercial reasonableness standard is satisfied. This article reviews the necessary steps in enabling a debtor in a chapter 11 bankruptcy to successfully implement a section 363 bankruptcy sale and cautions readers as to what may ensue if the appropriate steps are not followed.

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In bankruptcy, a powerful tool in the form of “Section 363 sales” exists, which provides a buyer with numerous protections as part of its acquisition of assets. Section 363 of the Bankruptcy Code authorizes a debtor (or trustee) to sell all or a portion of its assets “free and clear” of any liens, claims, interests and encumbrances outside of the ordinary court of business. These transactions are court-supervised and require notice and a hearing.

Auction sales conducted under Section 363 of the Bankruptcy Code also establish the ability to uncover the true worth of assets. When the value of a distressed business, real estate, or intellectual property is uncertain, auctions allow the market to speak for itself. They

replace closed-door negotiations and arbitrary valuations with open competition and structured price discovery.

More than a procedural formality, the auction process undergirding Section 363 sales is a critical mechanism for promoting transparency, fairness, and competition in distressed asset sales. By subjecting the asset-disposition process to competitive market dynamics, auctions mitigate information asymmetry and protect against insider favoritism. In doing so, auctions facilitate real-time price discovery, foster creditor confidence in distressed asset dispositions, and help achieve one of bankruptcy’s fundamental goals: maximizing value for the estate and its creditors.

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Auctions are highly advantageous due to their inherent flexibility. They allow for customization of the format — whether sealed bid, open cry, online formats, or stalking horse arrangements — to align with the specific characteristics of the asset and the dynamics of the market. Auctions also generate urgency and momentum, which are crucial in distressed situations. Most importantly, when thoughtfully designed, auctions ensure fairness by providing all participants with an equal opportunity to engage under the same conditions.

While auctions are powerful tools, their effectiveness hinges on thoughtful design, beginning with the terms of sale. If the terms are overly burdensome — such as requiring unreasonably high deposits, mandating immediate closings without contingencies, or imposing excessive legal obstacles — participation is stifled. This suppression of competition discourages risk-tolerant bidders and creates entry barriers that distort outcomes. Fewer bidders result in reduced price discovery and often lead to lower recoveries. Conversely, a process that is too lax — characterized by unclear bidding procedures, undefined overbid increments, or inconsistent qualification rules — can create information asymmetry and erode trust, further diminishing participation. Therefore, while auctions can be incredibly effective when done right, their power depends entirely on how well they are designed and executed.

One fundamental question here is: why do people participate in bankruptcy auctions? Bidders participate in bankruptcy auctions not just for the opportunity, but because they trust the process. Buyers are drawn to these auctions by the prospect to acquire assets at a discount, expand their businesses, or gain strategic advantages. They also participate because the rules are transparent. They understand that submitting the highest bid secures a win. Auctions offer clarity, finality, and the chance to compete on an equitable playing field. As professionals, it is their responsibility to ensure that the auction structure supports those principles — so that each sale delivers real value, robust competition, and judicial confidence. Below explores each stage of the Section 363 auction process and provides key insights from experienced practitioners for a comprehensive guide to the auction process in bankruptcy, from pre-bid preparation through court approval, and certain issues

and challenges that can arise throughout the auction process.

THE MARKETING PROCESS

The pre-bid phase is often the most crucial part of a bankruptcy-sale process. At this stage, the debtor and its advisors must develop a marketing plan. A successful marketing process is fundamental to achieving a competitive and value-maximizing bankruptcy sale. The first pivotal step involves identifying potential buyers — be they strategic acquirers, financial investors, or global bidders — who demonstrate both interest and capability to engage in the transaction. The engagement of seasoned investment bankers or M&A advisors is crucial, as they will orchestrate the marketing campaign, regulate the dissemination of information, and ensure the process maintains the necessary pace and professionalism.

Careful consideration must be given to the structure and scope of buyer outreach. While broad solicitation may be optimal for uncovering latent demand and enhancing price discovery, certain situations — such as those involving confidentiality, asset sensitivity, or creditor oversight — necessitate a more tailored, strategic approach, targeting a narrower, pre-vetted group of potential buyers.

During the marketing process, confidentiality agreements (“NDAs”) are crucial in safeguarding the debtor’s information. Beyond standard terms, NDAs should explicitly prohibit the misuse of proprietary data and frequently include restrictions on bidder communications with the debtor’s lenders, especially when a lender might later credit bid or serve as a stalking horse. These provisions are essential for maintaining process neutrality and mitigating the risk of backdoor negotiations or inequitable access to information.

Furthermore, timing is of paramount importance. The process must balance the urgency required in liquidity-constrained or “melting ice cube” situations with the necessity for bidders to perform thorough due diligence. Typically, a timeline of 30 to 45 days from process launch to bid deadline is standard in expedited cases. This duration should be sufficient to attract interest and

foster competitive bids, yet concise enough to prevent asset deterioration and mitigate financing risks.

Additionally, a secure and user-friendly virtual data room (“VDR”) is essential to a successful sale process. The data room should be well-organized, intuitive, and closely monitored. Providing accurate and timely information within a controlled environment not only expedites due diligence but also enhances bidder confidence and minimizes the risk of post-auction disputes.

Ultimately, the restructuring team must assess whether the contemplated sale timeline and marketing efforts satisfy the court’s standard of commercial reasonableness. This standard, though flexible, requires a showing that the sale process is structured to maximize value and ensure fairness to all stakeholders. A successful pre-auction marketing process requires strategic planning, robust advisor support, stringent confidentiality protocols, calibrated timing, and a carefully crafted diligence infrastructure. To build the evidentiary foundation necessary to defend the process, debtors must retain experienced investment bankers and financial advisors who can execute rapid but meaningful outreach. Documenting the scope and substance of these efforts — from the number of parties contacted to the nature of diligence requests — lays the groundwork for court approval.

BID PROCEDURES

Bid procedures serve as the structural blueprint of a bankruptcy auction. They define the rules of engagement and assure all stakeholders that the process is fair, orderly, and aimed at maximizing value. Asset sales can take the form of going-concern sales or piecemeal asset dispositions. Going-concern sales often prioritize buyer qualifications and transition planning, while piecemeal sales may involve lotting assets to maximize total value. Bid procedures should anticipate the possibility of selling assets in lots and provide flexibility to pair up or combine bidders when it would enhance the sale result.

Far from being mere boilerplate, these procedures are crucial to maintaining the integrity of the auction and ultimately influence whether the court will approve the sale. Key elements of effective bid procedures include clear bid submission deadlines, minimum overbid increments, required deposits, bidder qualification criteria, procedures for the assumption of liabilities, auction rules, and provisions for credit bidding. Importantly, these procedures must grant the debtor or its advisors the flexibility to adjust them as needed to

enhance competition or adapt to market changes. Courts typically defer to the debtor’s business judgment in these areas, provided the framework is reasonable and well-justified.

Qualifying bidders is a crucial component of the auction process, ensuring that only serious and financially capable participants are involved. Deposits, typically between 5% and 10% of the bid value, serve as a vital gatekeeping tool. These deposits demonstrate the bidder’s commitment and financial capability, effectively filtering out those who may not be genuinely interested or able to complete the transaction. Beyond deposits, the timely execution of confidentiality agreements and the submission of a proposed asset purchase agreement are standard prerequisites. Qualified bids must include a mark-up of the asset purchase agreement, adhering to the form provided by the debtor or the stalking horse bidder. This requirement ensures that all bids are genuinely actionable. Such measures preserve the integrity of the process and guarantee that all parties operate under uniform terms and conditions.

Additionally, for foreign bidders or newly established entities, additional due diligence may be required to verify their access to capital and the enforceability of their contractual obligations. This scrutiny is essential to mitigate risks associated with unfamiliar or untested entities. To address any perceived credibility gaps, parental guarantees or binding letters of credit are commonly employed, providing assurance of the bidder’s financial backing and commitment.

The bid procedures must also account for the nuances of strategic buyers versus financial buyers. Strategic buyers may present synergistic value but often require more time for due diligence and internal approvals. In contrast, financial buyers typically tend to act faster but may be more price sensitive. Where unsophisticated or first-time participants are involved, the process should include support mechanisms to ensure compliance and foster participation.

Credit bidding adds another layer of complexity and also must be handled with care. Under Section 363(k) of the Bankruptcy Code, secured lenders can credit bid up to the amount of their secured claims.¹ Lenders intending to credit bid are often mandated to declare their intent and specify the amount prior to the bid deadline. Although secured creditors typically possess the right to credit bid, they should still adhere to the

¹ 11 U.S.C. § 363(k).

same procedural framework as other participants to ensure a level playing field.

Moreover, bid procedures also govern the role of consultation parties. Although the debtor retains ultimate discretion in selecting the highest and best bid, consultation parties — such as the debtor in possession (“DIP”) lender, creditors’ committee, and occasionally the U.S. Trustee — provide valuable input. If any consultation party plans to submit a bid, safeguards must be implemented to prevent unfair access to competitive information. Bid procedures must clearly specify when such parties must recuse themselves from consultation rights or information-sharing roles. These safeguards are essential to prevent conflicts of interest and uphold the legitimacy of the auction process. In *Family Christian*, certain creditors served as consultation parties and also were allowed to credit bid on the debtors’ assets.² The court opined that a credit bidder acting as a consultation party, while the debtor knew that such a bidder submitted a bid on assets, was akin to insider trading.³

THE STALKING HORSE BIDDER AND BACK-UP BIDDER

The strategic use of a stalking horse bidder can anchor the sale process. A well-negotiated stalking horse bid sets a floor price, delineates transaction terms, and may deter non-serious bidders. In evaluating whether to proceed with a stalking horse, practitioners must assess the nature of the assets and the level of market uncertainty. In some cases, a “naked” auction — *i.e.*, one conducted without a stalking horse — may be the best option, particularly when the valuation is well-supported, the asset is widely marketable, and market demand is robust. Conversely, when asset valuation is unclear or timing constraints weigh heavily, a stalking horse can stabilize the process and attract interest.

Additionally, it’s important to note that a stalking horse bid may suppress competitive interest if prospective bidders perceive the stalking horse as having an undue advantage or if the breakup fee and bid protections are overly generous. Courts typically approve breakup fees ranging from 2% to 4% of the purchase price and expense reimbursements of 0.5% to 1%, but these amounts must be tied to tangible benefits conferred by the stalking horse. If the bid is conditional

or unlikely to withstand court scrutiny, bid protections may be unwarranted altogether.

Courts increasingly expect that backup bidders be designated in bid procedures. Backup bidder provisions are critical to maintaining sale momentum if the winning bidder fails to close. All qualified bidders are typically required to serve as backup bidders unless expressly waived. Backup terms generally require the bidder to hold its offer open through the closing deadline, without modification or additional diligence. In *In re Williams Industrial Services Group Inc., et al.* (Case No. 23-10961), in the Bankruptcy Court for the District of Delaware, the stalking horse bidder refused to serve as a backup bidder. Consequently, the bankruptcy court was unwilling to approve the bid procedures or the stalking horse protections until a junior secured lender agreed to backstop the stalking horse protections. This underscores the importance of proactively addressing contingencies and establishing backup bidder arrangements in advance.

THE AUCTION AND WINNING BID

Once qualified bids are received and the bid deadline has passed, the auction itself becomes the centerpiece of the sale process. The auction process must be transparent, orderly, and fair, while allowing for flexibility to maximize value. Auctions can be conducted in person, via Zoom, or in a courtroom setting, each with its advantages. Courtroom auctions provide the highest level of transparency, particularly in contested or high-stakes situations. In-person auctions tend to offer greater visibility and control, and are better suited for high-value or complex transactions where real-time negotiation is essential. Zoom auctions have become increasingly prevalent. They provide logistical convenience, lower costs, and broader participation, and when managed effectively, can offer an equally efficient forum as traditional in-person auctions.

Regardless of format, auctions must be governed by clear, pre-distributed rules. Best practices for conducting an auction include preparing a clear script, establishing a time-limited bidding format, and ensuring that all material communications are recorded. An experienced facilitator — usually debtor’s counsel or financial advisor — should manage the auction, enforce the rules, and handle disputes. If conducted virtually, technology checks should be performed beforehand to avoid disruptions. Bidders must acknowledge the rules at the outset, including the waiver of any objections to the process.

Qualified bidders, their advisors, and designated consultation parties are typically permitted to attend the

² *In re Family Christian, LLC*, 533 B.R. 600 (Bankr. W.D. Mich. 2015).

³ *Id.*

auction. Observers are generally excluded to protect confidentiality and encourage open bidding. Consultation parties — such as the unsecured creditors’ committee, DIP lender, or pre-petition lender — may observe the auction and provide input, but their role should be clearly defined. Bidder requalification may be necessary during the auction if bids increase significantly or involve structural changes. Bidding rounds with defined increments promote order, although auctioneers may allow a bidder to skip a round once before disqualification.

Critical discussions regarding bid increases or sale terms must occur on the record and in front of all bidders. To prevent backdoor negotiations or collusion, sidebars between bidders and lenders should be limited and monitored. When appropriate, parties may be allowed to partner mid-auction if such a combination yields a superior offer. Any *ex parte* communication — especially involving insiders — can jeopardize the entire process. In *Family Christian*, the debtors’ CEO’s off-the-record conversation with an insider bidder during the auction led to the initial denial of a sale.⁴

Time limits for rounds and the use of sealed bids can help prevent stagnation and bring the auction to a close. Adjournments, whether overnight or brief recesses, may be useful for bidder recalibration and deal structuring. If the auction extends late into the evening, adjourning until the next morning may better serve the estate’s interests. Fresh deliberation often yields better outcomes than decisions made in the early hours after a marathon session.

The auction itself is the focal point of the process, and its administration must be beyond reproach. When a bidder asks how to avoid the auction altogether, the immediate response must be caution. The integrity of the process cannot be compromised to expedite a private deal. Exceptions exist — such as where a bidder offers a demonstrably superior price and terms — but these must be supported by robust disclosures and stakeholder consent. Ultimately, the auction is an iterative and dynamic process, but it must be firmly anchored in a structure that balances flexibility with discipline. When conducted properly, it reveals market-tested value and positions the sale for court approval.

REOPENING AUCTION

The bankruptcy courts generally refrain from reopening fairly conducted auctions and must balance

the debtor’s duty to maximize the value of the estate with the need to preserve finality and integrity of the auction process when a higher and better bid for the assets is offered after the auction has concluded. In *In re Instant Brands Acquisition Holdings Inc.*, Case No. 23-90716 (Bankr. S.D. Tex., 2023), the losing bidder sought to submit a higher bid after the auction was concluded. The court found the auction had closed and would remain closed unless the parties failed to consummate the sale, stating “a few more dollars is irrelevant . . . in terms of protecting the integrity of the process.”⁵ Some courts have adopted a sliding scale approach under which smaller increases in value can justify reopening an auction before sale confirmation, while larger increases are required after sale confirmation. According to this approach, a court’s broad discretion to review the reasonableness of the sale narrows significantly after the court confirms the sale because the parties’ expectations have become more solidified at that point, and the gravity of finality has increased.⁶

Courts consider various factors in determining whether to reopen an auction to permit a late overbid, including: (1) the adequacy of the price; (2) material deviations from court-approved bidding procedures; (3) equitable considerations, such as due process issues, fraud, substantial unfairness, or mistake; (4) the bidders’ reasonable expectations and local customs of the court; (5) benefit to unsecured creditors; (6) whether the new bidder acted in good faith; (7) whether a sale order had been entered; and (8) support from the debtor, creditors’ committee, and other parties in interest. In *re Sunland, Inc.*, 507 B.R. 753 (Bankr. D.N.M. 2014).

For example, a bid can be found grossly inadequate when there is a substantial disparity between the prevailing bid and the appraised value of the asset, or where there is a reasonable degree of probability that a substantially better price can be obtained by reopening an auction.⁷ Also, courts are more likely to reopen an

⁵ *Id.*

⁶ *In re Food Barn Stores, Inc.*, 107 F.3d 558 (8th Cir. 1997); *In re Fin. News Network Inc.*, 980 F.2d 165 (2nd Cir. 1992); *First Nat’l Bank of Jefferson Parish v. M/V Lightning Power*, 776 F.2d 1258 (5th Cir. 1985).

⁷ *First Nat’l Bank of Jefferson Parish v. M/V Lightning Power*, 776 F.2d at 1261; *In re W. Biomass Energy LLC*, 2013 WL 4017147 (Bankr. D. Wyo. August 6, 2013) (the gross inadequacy of the sale price, combined with providing only partial payment to one creditor and leaving others uncompensated, highlighted unfairness warranting consideration of higher post-auction bids, despite no irregularities in the sale process).

⁴ *In re Family Christian, LLC*, 533 B.R. 600.

auction if there have been material deviations from the court-approved bidding procedures or other flaws in the auction process. On the other hand, courts may decline to reopen auctions to consider enhanced offers where the parties followed the bidding procedures.⁸ Additionally, courts may reopen an auction before confirming a sale based on equitable considerations.⁹

While accepting late bids may mean more money for creditors, over time there is risk of undermining confidence in judicial sales and discouraging parties from making their highest bids in a timely manner during the auction. Late bidders may maximize their chances of a court reopening an auction in multiple ways. First, they can demonstrate that there were material deviations from the court-approved bidding procedures or identify other flaws in the auction process, such as fraud, substantial unfairness, or mistake. Second, they can obtain support from the debtor, creditors' committee, and other interested parties. Finally, they can submit an offer that is significantly better than the prevailing bid or provides value to unsecured creditors who would otherwise receive no distribution.

COURT APPROVAL AND SALE CLOSING

Following a successful auction, the sale must be brought before the bankruptcy court for approval. This step is critical, as the court's approval both finalizes the transaction and grants the purchaser protection under Section 363(m), which limits the risk of later reversal. The sale order itself is a cornerstone of buyer protection. It must clearly state that the assets are transferred "free and clear" under Section 363(f), and that the buyer qualifies as a good faith purchaser under Section 363(m) of the Bankruptcy Code.

A robust evidentiary record is key to obtaining court approval — particularly if objections have been raised. Debtor's counsel should be prepared to present witness testimony, usually from the investment banker or restructuring advisor, to verify the fairness of the process

including the marketing process, the number of bids received, the auction mechanics, and the rationale for bid selection, and support the finding that the winning bid represents the highest and best offer. If contested, the hearing may resemble a mini-trial, requiring live witness testimony and documentary evidence.

Courts recognize that the highest bid is not necessarily the best bid. Evaluating bids requires a comprehensive review of balancing cash consideration with non-monetary factors such as execution risk, employment continuity, vendor relationships, cure costs, and transaction timing. Liquidators, for example, may offer guaranteed percentages but little assurance of job preservation or business continuity. Conversely, a going-concern buyer may offer less cash but deliver broader stakeholder value. In *Family Christian*, the second-highest bidder submitted a higher bid than the winning bidder but was not selected as the winner.¹⁰ The court stated that a debtor, acting as a fiduciary in the auction process, should consider additional factors such as contingencies, conditions, timing, and other uncertainties that might make an offer less attractive.¹¹

Assumption and assignment of executory contracts or leases demand further diligence. The debtor must demonstrate that the winning bidder can provide adequate assurance of future performance — typically through financial statements, operational plans, or third-party guarantees. Practitioners should anticipate these requirements and incorporate adequate assurance submissions early in the process. To allow for post-closing flexibility, many debtors include a post-sale window (i.e., 30 days) for buyers to designate contracts for assumption and assignment.

Judges often inquire into process integrity, bidder access to diligence, marketing efforts, and the impact of bid protections or insider involvement. To facilitate approval, the sale order should recite critical findings of fact, including the good faith of the purchaser and the reasonableness of the auction process. Where insider bids or credit bids are involved, additional scrutiny is expected, and the debtor should be ready to demonstrate that the sale was negotiated and executed in good faith and without unfair advantage.

Once approved, the parties move to close the sale. Prompt execution is often required to preserve asset value and honor financing timelines. Conditions precedent and closing deliverables must be carefully

⁸ *In re Bigler, LP*, 443 B.R. 101 (Bankr. S.D. Tex. 2010).

⁹ *In re Sunland, Inc.*, 507 B.R. 753 (the court found that a post-auction bid offering payment to otherwise uncompensated unsecured creditors supported reopening the auction, as it served the estate's best interest); *In re Farmland, Indus., Inc.*, 284 B.R. 111, 119-20 (Bankr. W.D. Mo. 2002) (the court reopened an auction before approving the sale after determining that a third-party's due process rights were violated due to lack of notice, unfairly denying them their contractual right of first refusal to match the highest offer.).

¹⁰ *In re Family Christian, LLC*, 533 B.R. 600.

¹¹ *Id.* at 622.

tracked, particularly in complex transactions involving employee transitions, assumed contracts, or regulatory approvals. Transition services agreements and cure payments should be finalized and coordinated among the relevant parties. The debtor's professionals should remain closely involved post-approval to troubleshoot last-minute issues and facilitate smooth consummation.

Importantly, finalizing the sale does not end court involvement. If the purchaser fails to close, the debtor may seek forfeiture of the deposit and designate the backup bidder. In some cases, disputes may arise post-sale, requiring court interpretation or enforcement of the sale order's terms. Therefore, careful drafting and documentation throughout the process — including the sale motion, notice, order, and asset purchase agreement — are essential to ensure enforceability and mitigate future risk.

CONCLUSION

Navigating a bankruptcy auction demands a thoughtful blend of legal, financial, and strategic

acumen. From the initial stages of preparing a marketing process and establishing sound bid procedures, to the live auction and eventual court approval, each phase is critical to preserving value and fostering trust among stakeholders. The success of a Section 363 sale hinges not only on attracting qualified bidders, but also on ensuring that the process is perceived as fair, transparent, and designed to achieve the best possible outcome for the estate.

Best practices such as using experienced advisors, tailoring bid protections, managing insider conflicts, and maintaining clear communication lines with the court and key constituencies can significantly influence the trajectory and success of the auction. While no two sales are identical, the framework laid out in this guide offers a roadmap for practitioners to navigate the unique challenges and opportunities that arise in distressed asset sales. ■