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Trekking Cross-Border Bankruptcy Sales

The Eddie Bauer sale serves as an example of how a cross-border bankruptcy sale can be executed quickly

By Aubrey E. Kauffman, Stephen Erlichman and Stuart Brotman

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Eddie Bauer, the iconic outdoor goods retailer long popular in the U.S. and Canada, avoided a fatal fall down the mountain this year when it filed for bankruptcy and was subsequently purchased at a "363" auction by private-equity firm **Golden Gate Capital**.

The quick rescue of Eddie Bauer for a reported $286 million provides a blueprint for how an integrated cross-border business can execute a successful sale of assets when faced with financial distress.

A 363 transaction involves a sale of assets during a U.S. bankruptcy case. The name is derived from Section 363 of the Bankruptcy Code, which permits the disposition of assets in bankruptcy, out of the ordinary course of business, and on a free and clear basis.

At a time of increasing cross-border bankruptcies, the Eddie Bauer proceeding also serves as an example of how the different restructuring regimes in the U.S. and Canada can be reconciled for an efficient, fair and seamless sale process.

Eddie Bauer's troubles

Eddie Bauer, which began as a bait and tackle shop in Seattle and became famous for outfitting the first American to scale Mt. Everest, operated some 370 stores in both the U.S. and Canada.

The two businesses were highly integrated: the Canadian subsidiary could not operate without the infrastructure of the U.S. business, and the U.S. business benefited from the profitability of its Canadian arm.

In the summer of 2009, Eddie Bauer was in dire financial straits. and the solution was to file for bankruptcy protection and seek a sale of assets in both countries.

In the U.S., the vehicle selected for sale was a stalking-horse auction process under Section 363 of the Bankruptcy Code. The challenge was then to find a method in Canada to parallel the 363 process, allowing all assets to be sold together, free and clear from all claims.

The solution was to file the Canadian Eddie Bauer entities under the Canadian Companies' Creditors Arrangement Act (CCAA) and run a Canadian sale coordinated with the U.S. 363 process. It was felt that a Canadian ancillary proceeding would not be adequate to achieve the goals of the transaction.

By way of contrast with the rigid and detailed U.S. bankruptcy code, in a recent Canadian court decision involving the restructuring of Nortel, the CCAA was described as both "a flexible statute" and "skeletal in nature."

Not surprisingly, a restructuring under the CCAA leaves a great deal of discretion to the presiding judge to fashion an appropriate solution to a particular problem. This can be disconcerting to those more accustomed to the Bankruptcy Code and its more specific roadmap for particular issues.

Although there historically was no express provision in the CCAA permitting a sale of assets before a plan is put to creditors,

Canadian law allowed such sales in appropriate circumstances, as was the case during the recent Nortel proceeding. Amendments to the CCAA, which became effective on September 18, 2009, have codified this practice.

Similarly, although stalking-horse sales and auctions are not as common in Canada as in the U.S., they will be ordered in appropriate circumstances. As a result of this flexibility, a coordinated cross-border process was crafted for the sale of Eddie Bauer.

The road to a sale

Private-equity group **CCMP Capital** and Eddie Bauer Holdings signed a stalking-horse purchase agreement on June 16, and CCMP Capital agreed to buy the U.S. and Canadian Eddie Bauer business.

On June 17, U.S.-based Eddie Bauer Holdings filed under Chapter 11 and also filed motions for the standard first-day orders.

On the same day, the Canadian entities obtained an initial order under the CCAA. In addition to some standard provisions, the order gave permission to the Canadian business to borrow from its U.S. counterpart, through a grid note secured by a court-ordered lien on Canadian assets.

The note and charge were assigned by the U.S. entities to the U.S. debtor-in-possession lender as part of its loan security. In this way, the Canadian entities were able to indirectly access the U.S. DIP facility in a manner that restricted the lien on Canadian assets to the extent of new money borrowed.

This addressed some concerns voiced by Canadian courts that the value of Canadian subsidiaries not be tapped by U.S. parents to the detriment of unsecured creditors in Canada.

On June 29, a joint hearing took place between the Canadian and U.S. courts. Objections filed in the U.S. case were dealt with by the U.S. court - there were no objections raised before the Canadian court - and then both courts approved the process and agreement.

Thus, both the Canadian and U.S. assets were subject to the same agreement, process and timetable, and interested parties on both sides of the border had an opportunity to object.

On July 16, an auction was conducted at the offices of the U.S. debtors' attorneys in New York.

The bidding was robust and resulted in a competitor to the stalking horse -- Golden Gate Capital -- emerging as the successful bidder at a substantially higher price.

The Eddie Bauer sale serves as an excellent example of how a cross-border bankruptcy sale can be executed quickly, despite the many nuanced differences between the bankruptcy and insolvency regimes in the U.S. and Canada.

As we continue to see an increase in bankruptcy filings by brand-name companies with operations on both sides of the border, we should keep the Eddie Bauer example in mind.

Aubrey Kauffman and Stuart Brotman are partners in the insolvency practice of Fasken Martineau. Stephen Erlichman is a partner in the securities and mergers and acquisitions practice of Fasken Martineau. They are based in Toronto, and served as Canadian counsel to CCMP Capital, the stalking-horse bidder for Eddie Bauer.