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Feature

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Break-Up Fees in Bank Holding Company Bankruptcies

Differences or Mere Distinctions?

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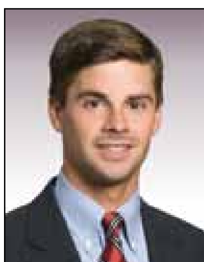

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The recent economic turmoil has contributed to capitalization problems for many bank holding companies and their banks. To address these problems, some bank holding companies have filed chapter 11 petitions and sought to sell the equity interests in their banks to purchasers willing to recapitalize the banks pursuant to § 363 of the Bankruptcy Code. In a number of these cases, disputes have arisen concerning the proposed break-up fees. Specifically, debtors and stalking-horse purchasers have argued that courts should consider the amounts that are necessary to recapitalize the subsidiary banks when determining whether a break-up fee is acceptable, while other parties have argued that only the consideration to the debtor's estate should be included in the analysis.

The outcome of these disputes can drastically affect the break-up fee amount. For example, if the purchase price to the bankruptcy estate is $10 million and the amount necessary to capitalize the bank is $90 million, a $2 million break-up fee would be 20 percent of the purchase price to the estate, but only 2 percent of the total amount of $100 million. This article discusses the break-up fee disputes in five recent contested cases: *Premier Bank Holding Co.*,[1] *Big Sandy Holding Co.*,[2] *First Place Financial Corp.*,[3] *Capital Bancorp.*[4] and *Rogers Bancshares Inc.*[5]

Break-Up Fees Generally

A break-up fee is a common deal protection that serves to compensate a stalking-horse bidder if the stalking horse is not the ultimate purchaser. A break-up fee typically is payable if the deal is terminated through no fault of the stalking horse, including if the seller elects to sell to a different buyer.

The acceptable amount of a break-up fee can be controversial and has been widely litigated in connection with § 363 sales because, among other things, if a break-up fee is excessive, it could have a chilling effect on bidding. Courts have refused requests for break-up fees when they are too large in comparison to the proposed purchase price.[6]

Bank Holding Company Break-Up Fees

Before discussing the contested cases, the authors first want to mention *In re AmericanWest Bancorp.*, because it is frequently cited in support of break-up fees in bank holding company cases.[7] In *AmericanWest*, the debtor sought approval of a $1 million break-up fee, which totaled approximately 15.38 percent of the proposed $6.5 million purchase price, but only approximately .05 percent if the calculation included the $200 million bank-recapitalization amount.[8] Objections to the proposed break-up fee by the U.S. Trustee and an investor in collateral debt obligations that held trust-preferred securities were resolved prior to the hearing.[9] The court approved the uncontested break-up fee without specifically addressing the reasonableness of the fee.[10]

1 Case No. 12-40550 (Bankr. N.D. Fla.).
2 Case No. 12-30138 (Bankr. D. Colo.).
3 Case No. 12-12961 (Bankr. D. Del.).
4 Case No. 12-58409 (Bankr. E.D. Mich.).
5 Case No. 13-13838 (Bankr. E.D. Ark.).
6 *See, e.g., In re Tama Beef Packing Inc.*, 321 B.R. 496, 498 (B.A.P. 8th Cir. 2005) (noting that fees in the range of 1 to 4 percent of purchase price are generally upheld as reasonable); *In re Bidermann Industries U.S.A. Inc.*, 203 B.R. 547, 553 (Bankr. S.D.N.Y. 1997) (refusing to approve break-up fees in range of 4.4 to 6 percent of purchase price).
7 *In re Rogers Bancshares Inc.*, Case No. 13-13838 (Bankr. E.D. Ark. July 5, 2013) [Doc. No. 4 at ¶ 29]; *In re First Place Fin. Corp.*, Case No. 12-12961 (Bankr. D. Del. Oct. 29, 2012) [Doc. No. 9 at ¶ 74]; *In re Big Sandy Holding Co.*, Case No. 12-30138 (Bankr. D. Colo. Sept. 28, 2012) [Doc. No. 5 at ¶¶ 83-84].
8 *See* Case No. 10-06097 (Bankr. E.D. Wash. Oct. 28, 2010) [Doc. No. 2 at ¶¶ 6, 74 and 117].
9 *See id.* at Doc. Nos. 42 and 44.
10 *See id.* at Transcript of Record at 65 (Doc. 88).

In re Premier Bank Holding Co.

In *Premier*, the debtor requested the approval of a $250,000 break-up fee, which was more than 17.6 percent of the proposed $1.415 million purchase price, but only 4 percent if the calculation included the $30 million that the debtor asserted was required to recapitalize the bank.[11] The debtor argued that the transaction was unique, involving both the sale of the bank stock and recapitalization of the bank, and that without the recapitalization, the bank would fail.[12]

Indenture trustees and holders of the debtor's trust-preferred securities objected to the break-up fee and contended that the appropriate calculation compares the amount of the break-up fee with the consideration to be provided to the debtor's estate.[13] They also argued that the debtor failed to cite any authority for the proposition that consideration paid to an entity other than the debtor should be considered when approving a break-up fee.[14]

Before the court ruled on the dispute, the stalking horse agreed to lower the amount of the break-up fee to $150,000, or approximately 10.6 percent of the purchase price.[15] The court concluded that the appropriateness of the break-up fee should be based only on the purchase price of $1.415 million.[16] Nevertheless, the court approved the reduced fee, but did not discuss why the amount was acceptable.[17]

In re Big Sandy Holding Co.

In *Big Sandy*, the debtor sought the approval of a $1 million break-up fee, which was 18.18 percent of the proposed $5.5 million purchase price, but only approximately 1 percent if the calculation included the $90 million that the debtor asserted was required to recapitalize the bank.[18] The debtor argued that the recapitalization amount and purchase price should be included in the break-up fee analysis because these were the two components of the transaction.[19] The debtor also asserted that without the proposed break-up fee, the stalking horse was unwilling to proceed with the transaction.[20]

The court approved the $1 million break-up fee, but declined to consider the $90 million capital contribution in its analysis.[21] Instead, the court appeared to base its decision on two separate arguments. First, the court noted that the break-up fee factored in the funds that were necessary to reimburse the stalking horse for its due-diligence efforts pre-petition and that the evidence showed that such expenses exceeded $1 million.[22] Second, the court recognized that the stalking horse testified that if the fee was approved, it would go forward as the stalking horse and make available to other qualified bidders the due-diligence materials that it obtained pre-petition.[23] The court concluded that the actual value to other bidders and the estate justified the high break-up fee.[24]

In re First Place Financial Corp.

In *First Place Financial*, the debtor sought approval of a $5 million break-up fee, which was 11.11 percent of the proposed $45 million purchase price but less than 2 percent of the $310 million that the stalking-horse bidder planned to commit to the sale, including $250 million to recapitalize the bank and $15 million to assume certain of the debtor's liabilities.[25] The debtor argued that the recapitalization amount should be included in the break-up fee analysis in this unique transaction because any prospective bank purchaser must compensate the estate for the value of the bank stock, as well as commit up to $250 million to recapitalize the bank and satisfy regulatory requirements.[26] The official committee of the trust-preferred securities and U.S. Trustee objected to the break-up fee and argued that only the consideration to the estate should be considered in determining the appropriate break-up fee amount.[27]

The court declined to approve the requested break-up fee, noting that it was "troublingly large" and that for purposes of determining whether the break-up fee was reasonable, the relevant metric was whether the fee was within a reasonable proportion to the "sale consideration," which the court found to be the amount that would actually flow to creditors — $45 million in cash, plus the $15 million in assumed liabilities.[28] The court also noted that almost every § 363 sale has some post-closing committed capital component to it.[29] Subsequently, the stalking horse agreed to reduce the break-up fee to 5 percent of the total consideration recognized by the court.[30] The committee supported this reduced fee, and while the court approved it in light of the committee's support, the court noted that it was "still ... a high number."[31]

In re Capital Bancorp.

In *Capital Bancorp.*, the debtor asked the court to approve procedures for a § 363 sale of any or all of its eight subsidiary banks and proposed that any stalking-horse bidder(s) would be entitled to collect a break-up fee.[32] The debtor did not have a stalking horse when it filed the bid-procedures motion.[33] The debtor also did not specify in its bid-procedures motion what would constitute a reasonable break-up fee, nor did it cite any case law in support of the break-up fee.[34]

Further, unlike the other bank holding company cases discussed herein, the debtor sought approval of the bid procedures approximately nine months after the petition date. The debtor commenced its chapter 11 case in August 2012 with a prepackaged plan that contemplated attracting new capital from outside investors.[35] In December 2012, the lead investor decided not to proceed with its investment in the debtor.[36] The debtor filed the bid-procedures motion in connection with its liquidation plan, which was filed in May

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11 *See* Case No. 12-40550 (Bankr. N.D. Fla. Sept. 6, 2012) [Doc. No. 14]. Hunton & Williams represented one of the objecting parties in *Premier*.
12 *See id.* at Doc. No. 14, ¶ 29; *id.* at Transcript of Record at 147 (Doc. 136).
13 *See id.* at Doc. Nos. 52, ¶ 16, and 54, and ¶ 48.
14 *See id.* at Doc. Nos. 52, ¶ 14, and 54, and ¶ 45.
15 *See id.* at Transcript of Record at 174 (Doc. 136).
16 *See id.* at Transcript of Record at 182 (Doc. 136).
17 *See id.* at Transcript of Record at 183 (Doc. 136).
18 *See* Case No. 12-30138 (Bankr. D. Colo. Oct. 25, 2012) [Doc. No. 5, ¶¶ 2 and 49].
19 *See id.* at Doc. No. 5, ¶ 84.
20 *See id.* at Doc. No. 5, ¶ 85.
21 *See id.* at Transcript of Record at 13-14 (Doc. 63).
22 *See id.* at Transcript of Record at 14-15 (Doc. 63). Although it is outside the scope of this article, the courts in *Premier* and *Rogers Bancshares* were willing to approve expense reimbursements in addition to the break-up fees, including by permitting the stalking horse to seek an administrative claim for such expenses in *Rogers Bancshares*. *See infra* n.12; *supra* n.43.
23 *See id.* at Transcript of Record at 15 (Doc. 63).
24 *See id.* at Transcript of Record at 16 (Doc. 63).
25 *See* Case No. 12-12961, Transcript of Record at 9 and 21-23 (Bankr. D. Del. Oct. 29, 2012) (Doc. 125).
26 *See id.* at Doc. No. 9, ¶¶ 67-68.
27 *See id.* at Doc. Nos. 90 and 94.
28 *See id.* at Transcript of Record at 31 and 58 (Doc. 125).
29 *See id.* at Transcript of Record at 31 (Doc. 125).
30 *See id.* at Transcript of Record at 58 (Doc. 125).
31 *See id.* at Transcript of Record at 59 (Doc. 125).
32 *See* Case No. 12-58409 (Bankr. E.D. Mich. May 16, 2013) [Doc. No. 426].
33 *See id.*
34 *See id.*
35 *See id.* at Doc. No. 425, 18.
36 *See id.* at Doc. No. 425, 22.

2013, just days after the Federal Deposit Insurance Corp. (FDIC) and state regulators seized three of its subsidiary banks.[37]

The unsecured creditors' committee objected to the proposed break-up fee because the debtor did not place any limits on what constituted a reasonable fee and asserted that the size of the fee should be limited to 3 percent of the purchase price.[38] At the bid-procedures hearing, the debtor argued that a break-up fee based on the total transaction amount, including any capital contribution required to recapitalize the bank(s), was necessary to attract a stalking horse.[39] The court agreed with the debtor and entered an order that approved break-up fee(s) that could be as much as 3 percent of (1) the cash purchase price of the outstanding shares of the applicable bank(s), (2) cure costs for any assumed contracts *and* (3) the capital contribution necessary to recapitalize the applicable bank(s).[40]

In re Rogers Bancshares Inc.

The debtor in *Rogers Bancshares* sought approval of a $4 million break-up fee, which was 25 percent of the proposed $16 million purchase price but only approximately 4.4 percent when including the $74.2 million that the stalking horse identified as the recapitalization amount.[41] The debtor argued that the break-up fee analysis should have included the recapitalization amount, because without the capital contribution, the bank stock would be worth nothing or very little.[42] The debtor also contended that if the proposed break-up fee was not approved, the stalking horse would walk away from the transaction.[43] The unsecured creditors' committee and the U.S. Trustee objected to the amount of the break-up fee and argued that (1) only the amount to be paid to the debtor's estate should be considered, and (2) many bankruptcy sales require purchasers to commit capital to the purchased business, and so such amounts are routinely excluded from the break-up fee analysis.[44]

Prior to the bid-procedures hearing, the stalking horse agreed to reduce the break-up fee from $4 million to $3.25 million. The committee and U.S. Trustee continued to object to the reduced fee.[45] At the hearing, the court concluded that only the purchase price to the estate should be considered in determining the appropriate amount of the break-up fee.[46] The court approved a break-up fee of $640,000, which was 4 percent of the purchase price.[47]

Conclusion

Since September 2012, at least five bankruptcy courts have addressed contested break-up fees in bank holding company bankruptcies. Four of those courts have held that the bank-recapitalization amount should not be included in the break-up fee analysis.[48] However, given the perceived benefits of large break-up fees, stalking horses in bank holding company cases may continue to seek substantial break-up fees; consequently, the body of case law may continue to expand. abi

37 *See id.*
38 *See id.* at Doc. No. 471, § 4 (committee did not cite any case law in its objection to break-up fee).
39 *See id.* at Transcript of Record (Doc. 515).
40 *See id.* at Doc. No. 519, ¶ 8.
41 *See* Case No. 13-13838 (Bankr. E.D. Ark. July 5, 2013) [Doc. No. 4, ¶ 16 and 19(e)]; Transcript of Record at 6 (Doc. 94). Hunton & Williams represents the official committee of unsecured creditors in *Rogers Bancshares*.
42 *See id.* at Doc. No. 4, ¶ 29; Transcript of Record at 22 (Doc. 94).
43 *See id.* at Transcript of Record at 23 (Doc. 94).
44 *See id.* at Doc. Nos. 62 and 66; *id.* at Transcript of Record at 40 (Doc. 94).
45 *See id.* at Transcript of Record at 7-8 (Doc. 94).
46 *See id.* at Transcript of Record at 248 (Doc. 94).
47 *See id.*
48 *See also Mercantile Bancorp.*, Case No. 13-11634 (Bankr. D. Del. Aug. 8, 2013) [Doc. No. 109] (approving debtor bank holding company's uncontested break-up fee of 3 percent of purchase price, which consisted of $22,277,000 cash payment, less amounts that bank owed to FDIC under cross-guaranty liability for two of debtor's other subsidiary banks that had been placed in receivership).

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