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Cramdown confusion: The not-so-plain requirement of 11 U.S.C.A. § 1129(a)(10)

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MAY 26, 2020

The COVID-19 pandemic and related economic fallout have led to an increase in large Chapter 11 filings that involve multiple debtors and sprawling capital structures.[1] These filings harken back to restructurings past, as they may not be prepackaged or prearranged.[2]

The varying interests of creditors across multiple affiliated debtor entities, paired with the lack of a pre-negotiated resolution, will invariably increase the likelihood of disputes over plan confirmation.

Such disputes may leave plan proponents with little choice but to seek to a "cramdown" of their plans over the objection of dissenting creditors.

The Bankruptcy Code permits nonconsensual plans to be confirmed if "at least one class of claims that is impaired under the plan has accepted the plan."[3] Despite this seemingly clear statutory direction, confusion remains as to whether this means one class *per debtor*[4] or one class *per plan*.

This distinction can have major implications in multi-debtor cases with expansive corporate structures. With a number of mega-cases likely to be filed in the days ahead, confirmation orders could soon hinge on the bankruptcy court's interpretation of Section 1129(a)(10).

This commentary provides an introduction to the applicable legal principles and conflicting case law on the issue.

OVERVIEW OF A CRAMDOWN CHAPTER 11 PLAN

In any Chapter 11 proceeding, Section 1129 of the Bankruptcy Code provides two paths for plan confirmation. One is to seek confirmation by showing, among other things, that each class of claims or interests has either accepted the plan or is not impaired under it.[5]

Alternatively, where one or more impaired classes[6] oppose the plan, the plan proponent may still confirm the nonconsensual plan by satisfying Section 1129(b). This is referred to as a cramdown plan because it is figuratively "crammed down" on nonconsenting classes.

To confirm a cramdown plan, the plan proponent must demonstrate that it satisfies conditions precedent delineated under Section 1129(a).[7] One such condition is set forth in Section 1129(a)(10) — that "at least one class of claims that is impaired under the plan has accepted the plan."[8]

11 U.S.C.A. § 1129(A)(10)

Congress drafted Section 1129(a)(10) to ensure "some indicia of support [for a plan of reorganization] by affected creditors and prevent confirmation when such support is lacking."[9] "Since Chapter 11 is designed to promote consensual reorganization plans, [a] proposal that has no support from impaired creditors cannot serve its purpose."[10] Accordingly, Section 1129(a)(10) operates as a gatekeeper of sorts.

> Where the Chapter 11 proceedings involve multiple debtors in a contested confirmation process, courts have disagreed on whether Section 1129(a)(10) requires that a cramdown plan be accepted by one impaired class per debtor or per plan.

Cramdown is a powerful remedy available to plan proponents under which dissenting classes are compelled to rely on difficult judicial valuations, judgments and determinations. The policy underlying Section 1129(a)(10) is that before embarking upon the tortuous path of cramdown and compelling the target of cramdown to shoulder the risks of error necessarily associated with a forced confirmation, there must be some other properly classified group that is also hurt and nonetheless favors the plan.[11]

At first glance, the text of Section 1129(a)(10) appears simple. Indeed, its application is straightforward enough where there is only one debtor, or where the court has ordered substantive consolidation.[12]

However, where the Chapter 11 proceedings involve multiple debtors in a contested confirmation process, courts have disagreed on whether Section 1129(a)(10) requires that a cramdown plan be accepted by one impaired class per debtor or per plan.

THE 'PER DEBTOR' APPROACH

In *In re Tribune Co.*,[13] which involved competing plans for over 100 jointly administered debtors,[14] U.S. Bankruptcy Judge Kevin J. Carey of the District of Delaware held that Section 1129(a)(10) is unambiguous and must be satisfied on a per debtor basis.

Specifically, the *Tribune* court noted that Section 1129(a)(10)'s use of the term "plan" as opposed to "plans" was irrelevant because, under the bankruptcy rules of construction, "the singular includes the plural."[15]

The Bankruptcy Court also reasoned that Section 1129(a)(10) must be read in conjunction with other subsections — which have long been held to require satisfaction by *every* debtor.

For instance, the Bankruptcy Court noted how Sections (a)(1) and (a)(3) cannot be satisfied unless all debtors comply with the Bankruptcy Code or act in good faith; the "best interest of the creditors" test of Section (a)(7) expressly relates to the "prescribed treatment for every impaired class of creditors for each debtor which is part of a joint plan"; and Section (a)(8) — the provision relating to confirmation by consent or nonimpairment under a plan as a whole — plainly applies to each class of claims.[16]

Although the Bankruptcy Court acknowledged that a per plan approach would be convenient in "complex, multiple-debtor Chapter 11 proceedings," it noted that "convenience alone is not sufficient reason to disturb the rights of impaired classes of creditors of a debtor not meeting confirmation standards."[17]

In reaching its conclusion, the Bankruptcy Court emphasized that, absent substantive consolidation, "entity separateness is fundamental."[18]

The *Tribune* ruling contrasted prior decisions, including those from the Bankruptcy Court for the Southern District of New York, that appeared to be establishing a trend of per plan interpretations in jurisdictions around the nation.[19]

In the *Tribune* court's view, previous courts had not considered "the [Section] 1129(a)(10) issue central to [their] decision in the matter before [them]."[20] Soon after the *Tribune* decision, the per debtor approach was cited with approval by another bankruptcy judge in the District of Delaware.[21]

THE 'PER PLAN' APPROACH

In 2018 the 9th U.S. Circuit Court of Appeals became the first appellate court to weigh in on the issue in the case of *In re Transwest Resort Properties*.[22] The *Transwest* court disagreed with the *Tribune* court's holding and instead said the plain meaning of Section 1129(a)(10) is that a joint plan need only be approved by one class of impaired creditors per plan.

Transwest involved jointly administered bankruptcy cases involving Transwest Resort Properties Inc., a debtor holding company that owned two "mezzanine" debtors, which themselves owned two operating debtors.[23] A lender held a $298 million prepetition claim against the operating debtors and later acquired a $39 million claim against the mezzanine debtors.

Although several classes of impaired creditors approved the debtors' subsequently filed joint plan of reorganization, the lender, which held the sole debt against the mezzanine debtors, sought to preempt plan approval by rejecting the plan of those debtors, leaving no impaired accepting classes.[24] The Bankruptcy Court found that this did not prevent confirmation under the auspices of the per plan approach.

The lender appealed this and a subsequent district court decision. Ultimately, the 9th Circuit also sided with the debtors. It explained that Section 1129(a)(10) "makes no distinction concerning or reference to the creditors of different debtors under 'the plan,' nor does it distinguish between single-debtor and multidebtor plans."[25]

> The 9th U.S. Circuit Court of Appeals found that the fact that other subsections of Section 1129(a) expressly stated that they applied on a per debtor basis weighed in favor of the per plan approach.

Moreover, the court reasoned that Section 102(7) — the section that provides that the singular includes the plural in references under the Bankruptcy Code — effectively amends Section 1129(a)(10) to read "at least one class of claims that is impaired under the plans has accepted the plans," which is consistent with a per plan interpretation.[26]

Furthermore, the 9th Circuit found that the fact that other subsections of Section 1129(a) expressly stated that they applied on a per debtor basis actually weighed in favor of the per plan approach — because Congress could have included that same language in Section 1129(a)(10) but chose not to.[27]

Although one of the appellate judges, U.S. Circuit Judge Michelle T. Friedland, agreed with the circuit's ultimate holding, she wrote a concurring opinion that highlighted a central issue that she thought was overlooked:

The problem in my view is not the interpretation of the statute, but rather that the plan effectively merged the debtors without an assessment of whether [substantive] consolidation was appropriate. Such an assessment would have required the Bankruptcy Court to evaluate whether it was fair to proceed on a consolidated basis.[28]

However, Judge Friedland explained that this did not sway her decision-making because the lender should have objected to

the plan on such a basis, as opposed to the requirements for confirming the plan.[29]

CONCLUSION

There are valid arguments on both sides of the Section 1129(a)(10) analysis, and it is difficult to predict which way any given court will rule on the issue outside of the 9th Circuit.

Bankruptcy courts in some of the most-frequented jurisdictions, the Southern District of New York and the District of Delaware, have so far come down on different sides (although the New York decisions pre-date *Tribune*). Additionally, to date, there are no published opinions citing to the 9th Circuit's decision.

In some of the massive cases that have been filed since the COVID-19 pandemic began, and likely in those to come, debtors face an uphill battle in securing the requisite support to confirm a Chapter 11 plan.

The sheer number of ably represented creditor constituencies vying for limited assets all but guarantees a difficult road. This backdrop provides fertile ground for the "per debtor/per plan" debate to continue. Accordingly, understanding the legal arguments in the debate is critical.

Notes

[1] *See, e.g., In re Intelsat SA*, No. 20-32299 (KLP) (Bankr. E.D. Va. May 13, 2020); *In re Frontier Comm'cns Corp.*, No. 20-22476 (RDD) (Bankr. S.D.N.Y Apr. 14, 2020).

[2] *See, e.g., In re Avianca Holdings SA*, No. 20-11133 (MG) (Bankr. S.D.N.Y. May 10, 2020).

[3] 11 U.S.C.A. § 1129(a)(10).

[4] Large Chapter 11 cases, often called "mega-cases," can involve dozens or even hundreds of debtors. *See, e.g., In re Tribune Co.*, 464 B.R. 126, 137 (Bankr. D. Del. 2011) ("Tribune Company directly or indirectly owns all (or substantially all) of the equity in 128 subsidiaries ... of which 110 are debtors."). Under the per debtor approach, this would require one impaired accepting class at each of the entities being restructured.

[5] *See* 11 U.S.C.A. § 1129(a)(8).

[6] A class is considered "impaired" if its legal, equitable or contractual rights are altered by the plan. *See* 11 U.S.C.A. § 1124.

[7] *See, e.g., In re Neff*, 60 B.R. 448, 451-52 (Bankr. N.D. Tex. 1985), *aff'd*, 785 F.2d 1033 (5th Cir. 1986); *In re Armstrong*, 294 B.R. 344, 355 (10th Cir. 2003).

[8] In addition to satisfying Section 1129(a)(10), a plan proponent seeking to confirm a cramdown plan must demonstrate that the plan does not discriminate unfairly and is fair and equitable. A full discussion of these requirements is beyond the scope of this commentary.

[9] *In re Combustion Eng'g Inc.*, 391 F.3d 190, 243-44 (3d Cir. 2004) (quoting *In re Windsor on the River Assocs.*, 7 F.3d 127, 131 (8th Cir. 1993)).

[10] *In re Windsor on the River Assocs.*, 7 F.3d at 131.

[11] *In re 266 Washington Assoc.*, 141 B.R. 275, 287 (Bankr. E.D.N.Y. 1992); *see In re Anderson Oaks (Phase I) Ltd. P'ship*, 77 B.R. 108, 112-13 (Bankr. W.D. Tex. 1987) ("There must be some one other than the debtor, other than the insiders, and other than the target of the cram down, who cares enough about the reorganization and whose rights must also be considered to invoke the equitable grounds that justify resort to cram down.").

[12] Substantive consolidation legally combines all of the assets and liabilities of all debtors, which, in turn, may affect the substantive rights of creditors. As such, to be invoked, it generally requires its proponent to demonstrate: "(i) prepetition they disregarded separateness so significantly their creditors relied on the breakdown of entity borders and treated them as one legal entity, or (ii) postpetition their assets and liabilities are so scrambled that separating them is prohibitive and hurts all creditors." *In re Owens Corning*, 419 F.3d 195, 211 (3d Cir. 2005).

[13] *See In re Tribune Co.*, 464 B.R. 126, 183 (Bankr. D. Del. 2011).

[14] Chapter 11 proceedings involving two or more related debtors may be jointly administered by a single bankruptcy court. Generally, joint administration allows parent companies, as well as their subsidiaries and affiliates, to operate in bankruptcy as one cohesive unit — this saves time and money that would otherwise be spent on duplicative proceedings.

[15] *See In re Tribune Co.*, 464 B.R. 126, 183 (Bankr. D. Del. 2011) at 182 (citing 11 U.S.C.A. § 102(7)).

[16] Id.

[17] Id.

[18] Id. at 182.

[19] *See, e.g., In re Station Casinos Inc.*, No. 09-52477 (Bankr. D. Nev. Aug. 27, 2010); *In re Charter Commc'n*, 419 B.R. 221 (Bankr. S.D.N.Y. 2009); *In re Enron*, No. 01-16034, 2004 WL 6075307 (Bankr. S.D.N.Y. July 15, 2004) (unpublished opinion); *In re SGPA Inc.*, No. 01-2609, 2001 WL 34750646 (Bankr. M.D. Pa. Sept. 28, 2001).

[20] *See Tribune*, 464 B.R. at 182.

[21] *See In re JER/Jameson Mezz Borrower* II LLC, 461 B.R. 293, 301-02 (Bankr. D. Del. 2011) (noting in dicta that debtors could not confirm a joint plan absent a consenting class for each individual debtor).

[22] *See In re Transwest Resort Props.*, 881 F.3d 724, 729 (9th Cir. 2018).

[23] Id. at 726.

[24] Id.

[25] Id. at 729.

[26] Id. at 729-30.

[27] Id. at 730.

[28] Id. at 732 (Friedland, J., concurring).

[29] Id. at 733.

This article appeared on the Westlaw Practitioner Insights Commentaries web page on May 26, 2020.

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