



AMERICAN
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INSTITUTE

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Chapter 11 Basics for Creditors' Attorneys

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CHAPTER 11 BASICS FOR CREDITORS' ATTORNEYS

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Eligibility differences between Chapter 13 and Chapter 11

Who may be a debtor in Chapter 13?

Only an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than \$250,000 and noncontingent, liquidated, secured debts of less than \$750,000, or an individual with regular income and such individual's spouse, except a stockbroker or a commodity broker, that owe, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts that aggregate less than \$250,000 and noncontingent, liquidated, secured debts of less than \$750,000 may be a debtor under chapter 13 of this title. 11 U.S.C. §109(e)

Who may be a debtor in Chapter 11?

Only a railroad, a person that may be a debtor under chapter 7 of this title (except a stockbroker or a commodity broker), and an uninsured State member bank, or a corporation organized under section 25A of the Federal Reserve Act, which operates, or operates as, a multilateral clearing organization pursuant to section 409 of the Federal Deposit Insurance Corporation Improvement Act of 1991 may be a debtor under chapter 11 of this title. 11 U.S.C. §109(d).

Individual vs. Non-Individual

- An individual may file Chapter 11 however, it is more expensive than Chapter 13.
 - o \$1,717.00 filing fee
 - o \$250 (or more) quarterly fee to U. S. Trustee
 - o Attorney's fees more because of Chapter 11 procedural requirements.
 - o An individual in Chapter 11 will usually be the person who does not qualify for a reorganization under Chapter 13 due to the debt limits for eligibility in that Chapter.
 - o Individual may not be a stockbroker or commodities broker (only Chapter 7)
 - o Discharge exceptions in section 523 apply
- Non-Individual
 - o Corporations and other business entities
 - o Official forms for Non-Individuals filing for bankruptcy

Small Business Classification 11 USC §101(51D)

- The term “small business debtor”—
 - (A) subject to subparagraph (B), means a person engaged in commercial or business activities (including any affiliate of such person that is also a debtor under this title and excluding a person whose primary activity is the business of owning or operating real property or activities incidental thereto) that has aggregate noncontingent liquidated secured and unsecured debts as of the date of the filing of the petition or the date of the order for relief in an amount not more than \$2,000,000 (excluding debts owed to 1 or more affiliates or

insiders) for a case in which the United States trustee has not appointed under section 1102(a)(1) a committee of unsecured creditors or where the court has determined that the committee of unsecured creditors is not sufficiently active and representative to provide effective oversight of the debtor; and

(B) does not include any member of a group of affiliated debtors that has aggregate noncontingent liquidated secured and unsecured debts in an amount greater than \$2,566,050 (excluding debt owed to 1 or more affiliates or insiders).

- 11 U.S.C. §1116, 11 U.S.C §1121(e) and Federal Rule of Bankruptcy

Procedure 1020

- o Only the debtor may file a plan for the first 180 days after the order for relief.
- o Plan and disclosure statement must be filed within 300 days or the order for relief.
- o Time periods may be extended if the debtor, by a preponderance of the evidence, can demonstrate it is likely a plan will be confirmed within a reasonable period of time and the order extending is signed before expiration of the existing deadline.

Voluntary vs. Involuntary

- 11 U.S.C. §301(a) - A voluntary case under a chapter of this title is commenced by the filing with the bankruptcy court of a petition under such chapter by an entity that may be a debtor under such chapter.
- 11 U.S.C §303(a) - An involuntary case may be commenced only under chapter 7 or 11 of this title, and only against a person, except a farmer, family farmer, or a corporation that is not a moneyed, business, or commercial corporation, that may be a debtor under the chapter under which such case is commenced.
- (b) An involuntary case against a person is commenced by the filing with the bankruptcy court of a petition under chapter 7 or 11 of this title—

- (1) by three or more entities, each of which is either a holder of a claim against such person that is not contingent as to liability or the subject of a bona fide dispute as to liability or amount, or an indenture trustee representing such a holder, if such noncontingent, undisputed claims aggregate at least \$10,000 more than the value of any lien on property of the debtor securing such claims held by the holders of such claims;
- (2) if there are fewer than 12 such holders, excluding any employee or insider of such person and any transferee of a transfer that is voidable under section 544, 545, 547, 548, 549, or 724(a) of this title, by one or more of such holders that hold in the aggregate at least \$10,000 of such claims;
- (3) if such person is a partnership—
 - (A) by fewer than all of the general partners in such partnership; or
 - (B) if relief has been ordered under this title with respect to all of the general partners in such partnership, by a general partner in such partnership, the trustee of such a general partner, or a holder of a claim against such partnership; or
- (4) by a foreign representative of the estate in a foreign proceeding concerning such person.
- (c) After the filing of a petition under this section but before the case is dismissed or relief is ordered, a creditor holding an unsecured claim that is not contingent, other than a creditor filing under subsection (b) of this section, may join in the petition with the same effect as if such joining creditor were a petitioning creditor under subsection (b) of this section.

Forms

- Petition for Non-Individual/Attachment to Petition
- 20 Largest Unsecured Claims
- Chapter 11 Statement of Current Income
- Schedules and SOFA – Non-individual

1st Day Motions – Can be requesting case dispositive relief or provide certain

creditors with priority treatment they may not be entitled to otherwise

- Application to employ counsel and other professionals. 11 U.S.C. §327 and Federal Rule of Bankruptcy Procedure 2014

- Motion to use cash collateral. 11 U.S.C. §363(a)
- Motion to continue to pay employees. 11 U.S.C. §105(a) – “necessary and appropriate”
- Motion to pay critical vendor/supplier claims. Paying pre-petition claim in exchange for post-petition trade credit. “Critical Vendor Doctrine”. 11 U.S.C. §105(a) – “necessary and appropriate. 11 U.S.C. §363(b) – payment of pre-petition debts to keep supply of critical goods is a use of property of the bankruptcy estate that is outside the ordinary course of business. *In re Kmart Corp.*, 359 F.3d 866 (7th Cir. 2004)
- Motion to assume executor contracts/unexpired leases. 11 U.S.C. §365 and Federal Rule of Bankruptcy Procedure 6006.
- Motion to approve post-petition financing. 11 U.S.C. §364 and bankruptcy rule 4001(c).

Proof of Claim – Filing, Considerations and Withdrawal - Federal Rules of Bankruptcy Procedure 3003 and 3006

- 3003(b)(1) *Schedule of Liabilities*. The schedule of liabilities filed pursuant to §521(l) of the Code shall constitute prima facie evidence of the validity and amount of the claims of creditors, unless they are scheduled as disputed, contingent, or unliquidated. It shall not be necessary for a creditor or equity security holder to file a proof of claim or interest

- No proof of claim needed in Chapter 11 case if the creditor agrees with the amount the debtor has listed on its schedules and the debt is not listed as disputes, contingent or unliquidated.
- File a claim if:
 - Claim not scheduled by the debtor
 - More is owed than scheduled
 - Claim is not classified on the proper schedule
- 3003(c)(3) *Time for Filing*. The court shall fix and for cause shown may extend the time within which proofs of claim or interest may be filed.
- What entity owes the debt?
 - Review documents relating to debt to determine debtor in Chapter 11 is the party responsible for the obligation.
 - Jointly administered cases
 - Multiple debtors
 - Guarantors
- Consent to Jurisdiction
 - Filing a proof of claim constitutes a party's consent to the jurisdiction of the bankruptcy court to determine matters relating to the claim.
- 3006
 - A creditor may withdraw a claim as of right by filing a notice of withdrawal, except as provided in this rule. If after a creditor has

filed a proof of claim an objection is filed thereto or a complaint is filed against that creditor in an adversary proceeding, or the creditor has accepted or rejected the plan or otherwise has participated significantly in the case, the creditor may not withdraw the claim except on order of the court after a hearing on notice to the trustee or debtor in possession

Chapter 11 General Procedure for Disclosure Statement and Plan

- Federal Rule of Bankruptcy Procedure 3016
 - o (a) Every proposed plan and any modification thereof shall be dated and, in a chapter 11 case, identified with the name of the entity or entities submitting or filing it.
 - o (b) ...a disclosure statement under §1125 of the Code or evidence showing compliance with §1126(b) shall be filed with the plan or within a time fixed by the court....
- Federal Rule of Bankruptcy Procedure 3017
 - o (a) Except as provided in Rule 3017.1, after a disclosure statement is filed in accordance with Rule 3016(b), the court shall hold a hearing on at least 28 days' notice to the debtor, creditors, equity security holders and other parties in interest as provided in Rule 2002 to consider the disclosure statement and any objections or modifications thereto.
 - o (c) On or before approval of the disclosure statement, the court shall fix a time within which the holders of claims and interests

may accept or reject the plan and may fix a date for the hearing on confirmation.

- (d) Upon approval of a disclosure statement...the debtor in possession, trustee, proponent of the plan, or clerk as the court orders shall mail to all creditors and equity security holders, and in a chapter 11 reorganization case shall transmit to the United States trustee.

Chapter 11 Specifics and Definitions

- No trustee as disbursing agent unless one is appointed by motion for cause or if it is in the best interest of the creditors. 11 U.S.C. §1104
- Debtor is “debtor-in-possession”
 - Fiduciary with rights and powers of Chapter 11 Trustee
 - Must account for property of the estate, examine and object to claims and file monthly operating reports
- Equity security holder
 - In a non-individual Chapter 11, this class is made up of shareholders/partners of the debtor.
- Plan not due with filing or immediately thereafter
 - Debtor has 120 day exclusivity period to file Plan
- Disclosure Statement generally required
 - This statement must provide adequate information concerning the affairs of the debtor to enable the holder of a claim to make an informed decision regarding acceptance or rejection of the Plan.

- Role of the Office of the United States Trustee (UST)
 - Conducts 341 Meeting of Creditors
 - Monitors progress and supervises administration
- Creditors' Committee
 - Appointed by the UST
 - Usually consists of the unsecured creditors holding the 7 largest claims
 - May consult with Debtor regarding case administration
 - May investigate Debtor's conduct
 - May participate in formulation of a Plan
- Plan Confirmation
 - Approval of Disclosure Statement. 11 U.S.C. §1125
 - Once approved, Disclosure Statement, Plan and Ballot are provided to each creditor in the case.
 - Confirmation hearing. 11 U.S.C. 1128(a). Requires 28 days' notice of the deadline for filing objections to confirmation and the date of the hearing.
 - Objection to Plan. Federal Rule of Bankruptcy Procedure 3020(b)
 - Requirements for confirmation. 11 U.S.C. §1129(a)(1)-(16)
 - Ballots and Class Acceptance
 - 11 U.S.C. §1126(c) - A class of claims has accepted a plan if such plan has been accepted by creditors, other than

any entity designated under subsection (e) of this section, that hold at least two-thirds in amount and more than one-half in number of the allowed claims of such class held by creditors, other than any entity designated under subsection (e) of this section, that have accepted or rejected such plan.

- Confirmation without required acceptances. 11 U.S.C. §1129(b).
 - The Plan must satisfy applicable provisions of 11 U.S.C. §1129(a) and
 - Must not unfairly discriminate and
 - Must be fair and equitable.
 - Absolute Priority Rule
 - No payment in excess of allowed claim

Effect of Confirmation – 11 U.S.C. §1141

(a) ...the provisions of a confirmed plan bind the debtor, any entity issuing securities under the plan, any entity acquiring property under the plan, and any creditor, equity security holder, or general partner in the debtor, whether or not the claim or interest of such creditor, equity security holder, or general partner is impaired under the plan and whether or not such creditor, equity security holder, or general partner has accepted the plan.

(b) Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor.

(c) Except as provided in subsections (d)(2) and (d)(3) of this section and except as otherwise provided in the plan or in the order confirming the plan, after confirmation of a plan, the property dealt with by the plan is free and clear of all claims and interests of creditors, equity security holders, and of general partners in the debtor.

(d)(1) ... confirmation of a plan—

(A) discharges the debtor from any debt that arose before the date of such confirmation, and any debt of a kind specified in section 502(g), 502(h), or 502(i) of this title, whether or not—

- (i) a proof of the claim based on such debt is filed or deemed filed under section 501 of this title;
- (ii) such claim is allowed under section 502 of this title; or
- (iii) of such claim has accepted the plan; and

(B) terminates all rights and interests of equity security holders and general partners provided for by the plan.

(2) A discharge under this chapter does not discharge a debtor *who is an individual* from any debt excepted from discharge under section 523 of this title.

- Unless otherwise stated in the confirmed plan, confirmation terminates the automatic stay.

Post-confirmation

- Implementation and Jurisdiction – 11 U.S.C. §1142
 - (a) Notwithstanding any otherwise applicable nonbankruptcy law, rule, or regulation relating to financial condition, the debtor and any entity organized or to be organized for the purpose of carrying out the plan shall carry out the plan and shall comply with any orders of the court.
 - (b) The court may direct the debtor and any other necessary party to execute or deliver or to join in the execution or delivery of any instrument required to effect a transfer of property dealt with by a confirmed plan, and to perform any other act, including the satisfaction of any lien, that is necessary for the consummation of the plan.
- Motion to Convert to Chapter 7
 - 11 U.S.C. §1112
 - (a) The debtor may convert a case under this chapter to a case under chapter 7 of this title unless –
 - (1) the debtor is not a debtor in possession.
 - (2) the case originally was commenced as an involuntary case under this chapter; or

(3) the case was converted to a case under this chapter other than on the debtor's request

(b) ...on request of a party in interest or the United States trustee or bankruptcy administrator, and after notice and a hearing, the court may convert a case under this chapter to a case under chapter 7 of this title or may dismiss a case under this chapter, whichever is in the best interest of creditors and the estate, for cause, including -

(1) continuing loss to or diminution of the estate and absence of a reasonable likelihood of rehabilitation;

(2) inability to effectuate a plan;

(3) unreasonable delay by the debtor that is prejudicial to creditors;

(4) failure to propose a plan under section 1121 of this title within any time fixed by the court;

(5) denial of confirmation of every proposed plan and denial of a request made for additional time for filing another plan or a modification of a plan;

(6) revocation of an order of confirmation under section 1144 of this title, and denial of confirmation of another plan or a modified plan under section 1129 of this title;

(7) inability to effectuate substantial consummation of a confirmed plan;

(8) material default by the debtor with respect to a confirmed plan;

(9) termination of a plan by reason of the occurrence of a condition specified in the plan; or

(10) nonpayment of any fees or charges required under chapter 123 of title 28.

- Federal Rule of Bankruptcy Procedure 1019

Chapter 11 Basics for Creditors' Attorneys

REVIEW CHECKLIST

What do creditors' attorneys need to consider upon receipt of notice of a Chapter 11?

- ☐ Ensure no stay violations
- ☐ Understand the case background and context
- ☐ Docket dates
- ☐ File an appearance
- ☐ Meet or revisit client to discuss options and strategy
- ☐ Contact debtor's counsel to obtain more information or to discuss particular issues

What are some strategies and considerations for secured creditors to lift the stay

- ☐ Did debtor advise, work with secured creditor before the case?
- ☐ What is your collateral/ collateral position?
- ☐ Is the collateral properly insured?
- ☐ Has debtor provided or offered adequate protection from diminution?
- ☐ Any issues with debtor's management, reporting, budget?
- ☐ What is the current value of the equipment/equity cushion?
- ☐ Is the equipment necessary for an effective reorganization?

How active should unsecured creditors be in a chapter 11 before a plan is filed?

- ☐ Are you a contract party/ special position?
- ☐ Are you still doing business with the debtor post-petition?

☐ Is there an unsecured creditors committee?

☐ How active is the case? Is there a sale or other motion filed that will determine the case issues prior to confirmation?

What strategies and considerations go into creditors evaluations of and voting on a plan?

☐ Classification

☐ Treatment/ Fair and Equitable/ Absolute Priority Rule

☐ Contracts

☐ Claim allowance and distributions

☐ Releases

Are proofs of claim handled differently?

☐ Is your client's claim scheduled as non-contingent, liquidated and undisputed in the correct amount?

☐ Proof of Claim filing deadlines are not always included on a Notice of Commencement