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New York City Bankruptcy Conference

# Recent Confirmation Issues


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CONCURRENT SESSION

2023

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# Allocation of Increase in Collateral Value During a Bankruptcy Case

Kathryn A. Coleman, Esq.

# Lien Stripping in Bankruptcy

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## *Dewsnup v. Timm*, 502 U.S. 410 (1992) (Blackmun, J.)

- The Supreme Court in *Dewsnup* granted certiorari to resolve the issue of whether a debtor could strip down a secured party's security interest at an appraised amount in bankruptcy, which would result in a windfall to the debtor for any appreciation in value of the collateral. In *Dewsnup*, Justice Blackmun held that Section 506(d) simply does not apply to undersecured claims. Instead, Section 506(d) means that if the secured party's claim is not allowed under Section 502 of the Bankruptcy Code, then any lien securing that claim is also void.
- Most commentators and bankruptcy scholars disagreed with this view and believed that section 506(d) did indeed apply to undersecured creditors. The meaning of *Dewsnup* seems to be that any appreciation in value of the collateral belongs to the secured creditor, or at least until the collateral is sold or a plan is confirmed.
    - This would imply that *Dewsnup* also holds that bifurcations of undersecured claims are never final.



## *Bank of America v. Caulkett*, 575 U.S. 790 (2015)

- Following the holding in *Dewsnup,* the Supreme Court did not permit the stripping off of a junior lien in a chapter 7 case when the value of the property was less than the senior mortgage because the junior lienholder’s claim was both secured by a lien and allowed under Section 502.
    - The Supreme Court reasoned that if, under *Dewsnup*, Section 506(d) protects a partially unsecured lien of an allowed claim, then it follows that Section 506(d) also protects a wholly unsecured lien of an allowed claim.

## Lien Stripping in Chapter 11

- The great majority of post-*Dewsnup* decisions on the issue of lien stripping have limited the *Dewsnup* holding to the chapter 7 context and have allowed the practice in cases under chapter 11. *See* 4 Collier on Bankruptcy ¶ 506.06; *Palomar v. First Am. Bank (In re Palomar),* 722 F.3d 992, 995 (7th Cir. 2013)*; In re Heritage Highgate, Inc.,* 679 F.3d 132 (3d Cir. 2012)*; Wade v. Bradford,* 39 F.3d 1126 (10th Cir. 1994)*; Dever v. IRS (In re Dever),* 164 B.R. 132, 141 (Bankr. C.D. Cal. 1994)*; In re 680 Fifth Ave. Assocs.*, 156 B.R. 726 (Bankr. S.D.N.Y.), aff'd, 169 B.R. 22 (S.D.N.Y. 1993), *aff'd*, 29 F.3d 95, 31 C.B.C.2d 1085 (2d Cir. 1994). (Note that section 1123(b)(5), amended by the Bankruptcy Reform Act of 1994, changes the result in cases allowing lien stripping where the claim is secured solely by a mortgage on the debtor's primary residence).
- Various other sections of the Bankruptcy Code allow for such relief other than Section 506(d). *See, e.g.*, *Wade*, 39 F.3d at 1128-30 (holding that the bankruptcy court is authorized to modify a creditor's state law property rights through a chapter 11 reorganization plan); *In re heritage Highgate, Inc.*, 679 F.3d at 143-45 (permitting the stripping of investors' liens on chapter 11 debtors' real estate subdivision).



# Allowance of Post-Petition Interest

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## Bankruptcy Code Section 506(b)

- Section 506(b), allows a senior secured creditor to increase its claim after the petition date by adding interest and fees that are covered by the value of the collateral.
- In general, however, the increase of the amount of a senior secured claim will not negatively impact the amount of the junior secured claim because "the junior creditor may be entitled to adequate protection of its interest in the collateral" under 11 U.S.C. § 361(1). 4 Collier on Bankruptcy 506.04[5] (16th ed.); *see also In re Rupprect*, 161 B.R. 48, 49 (Bankr.D.Neb.1993) (holding that junior creditor entitled to adequate protection from interest accruing on senior claim).
- Conversely, principal payments to the senior creditor by the debtor after the petition date do not increase the value of the junior creditor's claim. *See Pitre v. First Federal Sav. & Loan Ass'n of Chicago (In re Pitre)*, 11 B.R. 777, 781 (Bankr. N.D. Ill. 1981).
- The value of the senior claim is therefore usually fixed as of the petition date for purposes of determining the secured status of the junior claim.



# Blanket Liens and The "Melting Ice Cube" Theory

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## Melissa B. Jacoby & Edward J. Janger, *Tracing Equity: Realizing and Allocating Value in Chapter 11*, 96 TEX. L. REV. 673 (2017-2018)

- The generally accepted view among scholars, lawyers, and judges is that Article 9 of the Uniform Commercial Code implements a single waterfall, which allows a secured lender to have a blanket lien over all the assets of a company enabling it to capture a distressed company's going-concern value. This has allowed senior secured lenders outsized control over the company when it falls into financial distress.
- However, this view is incorrect and neither Article 9 nor the Bankruptcy Code implements the single waterfall.
  - There is actually a distinction between claims with priority based on a property interest in the company's assets and claims to the residual value of the company.
  - While the company continues to operate, there should be two waterfalls: 1) a waterfall for encumbered assets; and 2) a waterfall for unencumbered assets and the going-concern of the company.
  - The value of a secured creditor's collateral may increase, but that creditor's entitlement to any value is limited to "identifiable proceeds" of assets encumbered as of the petition date
    - This implies that any increases in the going-concern value of the company, as well as other bankruptcy-created value, should be allocated to the bankruptcy estate for the benefit of all stakeholders.



## Melissa B. Jacoby & Edward J. Janger, *Ice Cube Bonds: Allocating the Price of Process in Chapter 11 Bankruptcy*, 123 YALE L. J. 862-1117 (2014)

- The "melting ice cube" theory has been routinely used to pressure courts into allowing quick all-asset Section 363 sales that might otherwise be considered sub rosa plans. This allows the purchaser (or secured creditor) to obtain assets at a depressed price robbing the estate and its stakeholders of any appreciation in the value of the collateral during bankruptcy.
  - In *Chrysler*, the Second Circuit found that there were exigent circumstances justifying the procedural shortcuts taken to accomplish a quick all-asset Section 363 sale, including the "melting ice cube" theory since the company was losing millions every day. *In re Chrysler LLC*, 576 F.3d 108, 114 (2d Cir. 2009), *vacated sub nom*. *Indiana State Police Pension Tr. v. Chrysler LLC*, 558 U.S. 1087 (2009).
    - While the Supreme Court vacated the Second Circuit decision in *Chrysler*, the application of the "melting ice cube" argument has been successfully used in many Section 363 sales involving large public companies. *See* Lynn M. LoPucki & Joseph W. Doherty, *Bankruptcy Fire Sales*, 106 MICH. L. REV. 1, 30-31 (2007)

## Melissa B. Jacoby & Edward J. Janger, *Ice Cube Bonds: Allocating the Price of Process in Chapter 11 Bankruptcy*, 123 YALE L. J. 862-947 (2014) (Cont'd.)

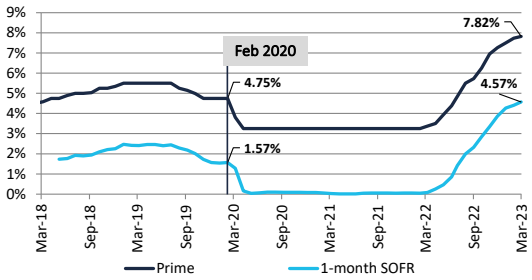
- Senior secured creditors typically will assert a first-priority lien on all of the company's assets, or a blanket lien, and will further assert that the company is worth less than the amount of its claim in order to strong-arm a Section 363 sale.
  - However, so-called blanket liens are somewhat questionable due to frequent creditor errors, gaps in the scope of statutory schemes, and value that cannot be subject to liens or is not traceable to the secured creditor's collateral.
- The state law liquidation value of collateral should be used to establish the distributional baseline for the purposes of fairness.
  - The remainder of the value of the debtor, consisting of the value allocated to unencumbered assets, post-petition effort of at-will employees and other unalienable value, and any appreciation that is not tied to encumbered assets, should go to the estate for the benefit of stakeholders. Declaring some portion of bankruptcy-created value as unencumbered does not necessarily determine who will receive it in the end. The drafters of the Bankruptcy Code contemplated that any chapter 11-created surplus of value would be the subject of negotiation and compromise through the chapter 11 plan process.

## REINSTATEMENT / CRAM DOWN

### REINSTATEMENT

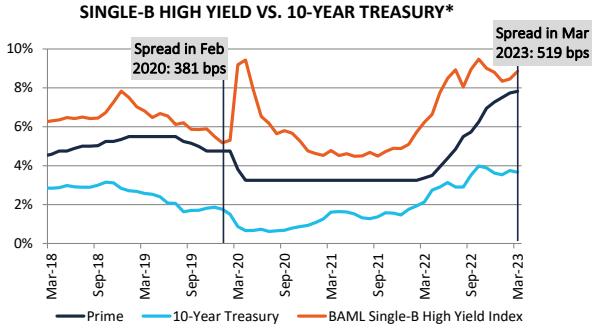
- In the current interest-rate environment, reinstatement can be value accretive to a debtor
  - As the charts show, debt issued in 2021 and prior may have coupon rate(s) lower than the cost of exit financing
  - Fixed rate notes may be less expensive than floaters since spreads have widened since 2019
    - Result = an estate "asset"
- Issues / Challenges:
  - Debt capacity at exit; plan feasibility
  - Ability to refinance at maturity
  - Legal determination that all rights under the indenture remain in place
  - Any or all of these issues may lead to a confirmation fight

**INTEREST RATES***




Source: Federal Reserve, Bloomberg Finance L.P.
*Monthly Average Rates

**SINGLE-B HIGH YIELD VS. 10-YEAR TREASURY***




Source: Federal Reserve Bank of St. Louis
*Monthly Average Rates

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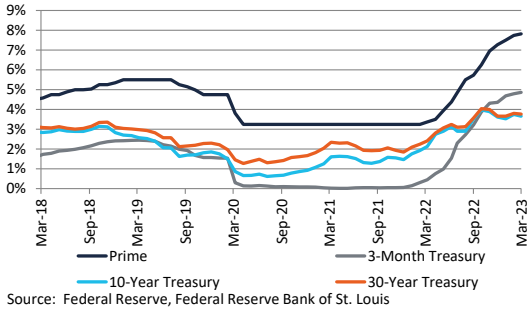
## REINSTATEMENT / CRAM DOWN

### CRAM DOWN

- Conversely, cram down very likely is not an attractive option today:
  - In addition, cram down has its own challenges at confirmation: efficient market theory (e.g. Momentive), certain districts interpret the "footnote" in SCOTUS Till decision as a way to argue for market rate(s) at exit
  - Till "formula" per SCOTUS majority decision - - at base (prime) rate plus 1%-3% likely is no better than (i) reinstatement, or (ii) exit financing at current rate(s)

**TREASURY YIELDS***




Source: Federal Reserve, Federal Reserve Bank of St. Louis
*Monthly Average Rates

**OVERALL DYNAMIC OR OPTIONS**
(Assuming legal hurdles are overcome)

| Current Rates | Contracted Rates | Possibly |
|---|---|---|
| High | Low | Reinstate |
| Low | High | Cram Down |

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BARNES & THORNBURG LLP

# MEMORANDUM

TO: ABI New York Panel on Confirmation Issues

FROM: Gregory G. Plotko

DATE: May 24, 2023

SUBJECT: Pre-Confirmation Support Agreements – New Issues and New Decisions

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PRE-CONFIRMATION SUPPORT AGREEMENTS – NEW ISSUES & DECISIONS

## I. INTRODUCTION

A. Pre-Confirmation Support Agreements maintain their popularity due to their ability to minimize disputes and costs, speed up restructurings and provide clarity and certainty in a chapter 11 proceeding.

B. Recently, objectors to pre-confirmation support agreement have raised the following issues:

1. Whether it is permissible to exclude claim holders (of the same class) from the opportunity of providing exit financing as part of a plan support agreement ("PSA"); and

2. whether *post-petition*, pre-disclosure statement, plan support agreements are permissible especially when tied to the allowance of a claim.

## II. EXCLUSIVE FINANCING OPPORTUNITIES & PLAN SUPPORT AGREEMENTS

A. Exclusive "new money" or backstop arrangements, when tied to a PSA has been the subject of objections and concern by creditors, courts and commentators alike.

B. In situations where an PSA provides for payment of backstop fees to creditors who provide both (1) a backstop commitment/exit financing and (2) an agreement to vote their existing claim in favor of a chapter 11 plan, it may be difficult to determine what portion of the backstop fees are attributable to the value of the backstop commitment itself versus the commitment to support the debtor's treatment of the existing claim under the plan.

C. This combination may implicate Section 1123(a)(4)'s prohibition on different treatment of claims in the same class.

1. Debtors will argue that they are offering the subset of creditors additional equity (or debt), not in consideration for the discharge of those creditors' claims, but rather in exchange for those creditors' agreement to help fund the debtors' reorganization by investing in the reorganized debtor.

2. Does the lack of opportunity in the class reach the level of discrimination under Section 1123(a)(4) or violate the market test requirements set forth in *Bank of America Nat. Trust and Savings Assoc. v. 203 N. LaSalle St. P'ship*, 526 U.S. 434 (1999)?

a) Why not market test?

b) Why not separately classify the exit financing group?

c) Why not make the offer to all creditors of the same class?

D. Bankruptcy Judges have recently commented:

1. In *Pacific Drilling*, Judge Wiles explained that those exclusive opportunities gave rise to "an equal treatment problem that's deadly to your plan, and I mean deadly." The Court then went on to state that: "[t]he theory of the Bankruptcy Code is that when the big creditors sit in a room and negotiate a deal, the little creditors who are in the same boat get the same deal. The Bankruptcy Code does not permit the unequal treatment of creditors in the same class; it also does not permit the payment of extra compensation to large creditors in exchange for their commitment to vote for a plan." Judge Wiles further stated that "the problem with special allocations in rights offerings, or with private placements that are limited to the bigger creditors who sat at the negotiating table, or big backstop fees that are paid to the bigger creditors who sat at the negotiating table but that are not even open to other creditors (and in particular to other creditors in the same class), is that it is far too easy for the people who sit at the negotiating table to use those tools primarily to take for themselves a bigger recovery than smaller creditors in the same classes will get." *In re Pacific Drilling*, Case No. 17-13193 (MEW) (Bankr. S.D.N.Y.), Sept. 18, 2018 Hrg. Tr. (Dkt. 622)

2. In *TPC Group*, Judge Goldblatt stated:

> And at some level it does seem as if, for example, the Supreme Court's decision in *203 North LaSalle* is highly relevant to that question and that, when you're asked is the reason a party, a creditor or interest holder receiving certain treatment on account of their claim or interest, on the one hand, or on account of a plan transaction on the other, that the way that's answered is by market testing. And I've got some concerns that these transactions here aren't market tested, which, if right, would counsel in favor of the view that it's actually consideration being given on account of the claims, which would give rise to claims of discriminatory treatment. *In re TPC Group Inc.*, Case No. 22-10493 (CTG), Transcript of Hearing, at 189 (Bankr. Del. July 29, 2022).

(1) The issue was ultimately resolved consensually by allowing the objecting creditor and others to participate.

3. In *LATAM Airlines*, Judge Garrity approved an exclusive financing arrangement under which the exclusive commitment creditor group, which controlled the class vote, received superior treatment under their exclusive new money investment compared with recoveries of excluded creditors in the same

class, including substantial backstop fees on their own commitments. Certain aggrieved parties appealed to the District Court which upheld Judge Garrity's analysis and dismissed concerns of discriminatory treatment based on a similar analysis conducted by the 8th Circuit in *Peabody Coal*. *See Ad Hoc Grp. of Unsecured Claimants v. Latam Airlines Grp. S.A. (In re Latam Airlines Grp., S.A.)*, 643 B.R. 756 (S.D.N.Y. 2022) *citing In re Peabody Energy Corp.*, 933 F.3d at 918 at 926 & n.4 (a "right to buy ... preferred stock at a discount" did not violate § 1123(a)(4)).

## III. RECENT POST-PETITION SOLICITATION CHALLENGES

### A. Background

1. Section 1125(b) of the Bankruptcy Code prohibits votes on a proposed plan from being solicited from a claim holder unless the plan (or a summary of it) is transmitted to the holder, either before or at the time of such solicitation, together with "a written disclosure statement approved, after notice and a hearing, by the court as containing adequate information." This proviso applies to post-petition and prepetition solicitations.

2. Section 1126(e) of the Bankruptcy Code authorizes the bankruptcy court to disallow the votes of any entity who accepted or rejected a plan other than "in good faith" or "was not solicited…in accordance with the provisions of this title."

3. Certain courts read Section 1125 narrowly to refer only to a "specific request for an official vote" on a plan as opposed to a written memorialization of a negotiation towards a settlement of legal issues that have prevented confirmation and are in furtherance of plan confirmation. *See Century Glove Inc. v. First Am. Bank of New York*, 860 F.2d 94 (3d Cir. 1989), *In re Heritage Org. LLC*, 376 B.R. 783 (Bankr. N.D. Tex. 2007); *In re Indianapolis Downs LLC*, 486 B.R. 286 (Bankr. D. Del. 2013).

4. Recent decisions have focus on different policy concerns including whether the plan support agreement negotiations are conducted by sophisticated parties and the content of a support agreement.

### B. In re Grupo Aeromexico, S.A.B. de C.V., No. 20-11563 (Bankr. S.D.N.Y 2021)

1. The Official Creditors' Committee objected to various motions seeking to settle creditor claims arguing that the settlements included plan-support provisions which constituted impermissible post-petition solicitation under Section 1125 of the Bankruptcy Code. The Committee argued that the plan support provisions were a "throw in" and not a settlement in further of plan confirmation that fell outside of similar cases such as *Century Glove*.

2. Judge Chapman disagreed and focused her analysis on the sophistication of all parties involved in these negotiations and found that the inclusion of plan support covenants were "economic decisions" made by the parties which added value to the debtors' estates. Transcript of Hearing, November 16, 2021.

a) The Court also made a similar ruling on the eve of confirmation when a party that bought a claim - that was subject to a plan support proviso - attempted to vote against the plan. Judge Chapman found that provision enforceable and refused to hold up confirmation over this issue.

**C. In re SAS AB, No. 22-10925 (MEW) (Bankr. S.D.N.Y 2022)**

1. The debtor sought approval to enter into an RSA with certain labor unions that included as a settlement term the allowance of certain union claims.

2. Judge Wiles *sua sponte* raised concerns about the debtor's use of the term RSA and took issue with the fact that the agreement did not describe any particular plan terms that are generally found in a more robust RSA and would allow a creditor to condition its vote on the plan containing the promised terms.

3. The Court found that the agreement was "just a flagrant violation of Section 1125(b)" and could not rely on the more narrow definition of "solicitation." *In re SAS AB*, No. 22-10925 (MEW) (Bankr. S.D.N.Y. Sept. 28, 2022), Transcript of Hearing at 9-22.

BARNES & THORNBURG LLP

# MEMORANDUM

TO: ABI New York Panel on Confirmation Issues

FROM: Gregory G. Plotko

DATE: May 2, 2023

SUBJECT: Equitable Mootness Update

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EQUITABLE MOOTNESS UPDATE

- **Background**: Equitable mootness is a court-created doctrine which cuts-off appellate review of bankruptcy court orders and results in a complete loss of appeal rights. Circuits have adopted different standards when considering whether to apply the doctrine - which are discussed below. A recent petition for certiori challenges the doctrine as a whole as well as the Second Circuit's current standards.
- **State of the Circuits**
  - **First Circuit:**
    - Recognizes equitable mootness and established a three-factor test. *See Cooperativa de Ahorro y Credito v. Fin. Oversight & Mgmt. Bd. (In re Fin. Oversight & Mgmt. Bd.)*, 989 F.3d 123, 129 (1st Cir. 2021).
    - "[T]he decision whether to reject an appeal of an order confirming a plan of reorganization because the plan has been implemented calls for us to consider at least three factors: (1) whether the appellant pursued with diligence all available remedies to obtain a stay of execution of the objectionable order; (2) whether the challenged plan proceeded to a point well beyond any practicable appellate annulment; and (3) whether providing relief would harm innocent third parties." *In re Fin. Oversight & Mgmt. Bd.*, 989 F.3d 123, 129 (1st Cir. 2021).
  - **Second Circuit:**
    - Recognizes equitable mootness and established a five-factor test for determining whether an appeal should be dismissed on mootness grounds. *See In re Chateaugay Corp.*, 10 F.3d 944, 952-53 (2d Cir. 1993)
    - The five *Chateaugay* factors are whether "(i) effective relief can be ordered; (ii) relief will not affect the debtor's re-emergence' (iii) relief will not unravel intricate transactions; (iv) affected third-parties are notified and able to participate in the appeal; and (v) [the] appellant diligently sought a stay of the reorganization plan." *In re MPM Silicones, LLC*, 874 F.3d 787, 804 (2d Cir. 2017) (citing *Chateaugay*, 10 F. 3d at 952-53).

- The Second Circuit has described the fifth *Chateaugay* factor as the "chief consideration" in the analysis. *In re Metromedia Fiber Network, Inc.*, 416 F.3d 136, 144 (2d Cir. 2005).

- Equitable mootness allows a court to dismiss a bankruptcy appeal "when, even though effective relief could conceivably be fashioned, implementation of that relief would be inequitable," *In re Metromedia Fiber Network, Inc.*, 416 F. 3d 476, 483 (2d Cir. 2012). The court held that this form of abstention is appropriate "when the debtor's reorganization plan has been substantially consummated," *In re BGI, Inc.*, 772 F.3d 102, 108 (2d Cir. 2014), and when the appellant did not diligently seek a stay of the confirmation order.
- Abuse of discretion review standard

- **Third Circuit:**
  - Takes a far more reserved and narrow approach but has applied the doctrine in certain circumstances. *See In re Tribune Media Co.*, 799 F.3d 272, 278 (3d Cir. 2015).
  - Elements: four factors, but condenses its analysis to "two analytical steps":
    - 1. Whether a confirmed Plan has been substantially consummated; and – if so-
    - 2. Whether granting the relief requested in the appeal will (a) fatally scramble the plan and/or (b) significantly harm third parties who have justifiably relied on the plan.

      *See In re Tribune Media Co.*, 799 F.ed 272 (3d Cir. 2015)
  - Abuse of discretion standard
  - "There is no jurisprudence in this Circuit that would allow a court to eschew exercise of its proper jurisdiction by refusing to entertain an appeal it has the power to hear on the basis of an ad hoc balancing of self-selected 'equitable considerations,' and we are not inclined to fashion such." *In re Zenith Electronics Corp.*, 329 F. 3d 338, 340 (3d Cir. 2003).
  - Circuit Judge Krause has criticized courts that applied the doctrine because in the opinion of Judge Krause, they have "allowed the doctrine itself to short-circuit the merits analysis" and it "precludes the development of bankruptcy law" relating the issues brought on appeal. *In re Nuverra Envtl. Solutions, Inc.*, No. 18-3084, 2021 U.S. App. LEXIS 244, at *11–14 (3d Cir. Jan. 6, 2021) (Krause, J., concurring in the judgment).
- **Fourth Circuit:**
  - Recognizes equitable mootness and applies a four-factor test to determine whether to dismiss an appeal as moot. *See In re Bate Land & Timber LLC*, 877 F.3d 188, 195 (4th Cir. 2017).

- Elements: four factors
    - (1) whether the appellant sought and obtained sought and obtained a stay; (2) whether the reorganization plan or other equitable relief order has been substantially consummated; (3) the extent to which the relief requested on appeal would affect the success of the reorganization plan or other equitable relief granted; and (4) the extent to which the relief requested on appeal would affect the interest of third parties. *In re Bate Land & Timber LLC*, 877 F.3d 188, 195 (4th Cir. 2017).

- **Fifth Circuit:**
    - Recognizes equitable mootness and applies a three-factor test to determine whether an appeal should be dismissed on mootness grounds. *Matter of Highland Capital Management, L.P.*, 48 F.4th 419 (5th Cir. 2022).
    - Elements: three factors
        - (i) whether a stay has been obtained, (ii) whether the plan has been 'substantially consummated,' and (iii) whether the relief requested would affect either the rights of parties not before the court or the success of the plan. *Matter of Highland Capital Management, L.P.*, 48 F.4th 419, 429 (5th Cir. 2022).
- **Sixth Circuit:**
    - Recognizes equitable mootness and applies a three-part test:
        - (1) whether a stay has been obtained; (2) whether the plan has been 'substantially consummated'; and (3) whether the relief requested would significantly and irrevocably disrupt the implementation of the plan or disproportionately harm the reliance interests of other parties not before the court. *In re City of Detroit, Michigan*, 838 F.3d 792, 798 (6th Cir. 2016).
    - Review is *de novo*
- **Seventh Circuit:**
    - Recognizes equitable mootness and has applied a two-factor test to determine whether to dismiss an appeal as moot:
        - "In evaluating the receiver's argument for equitable mootness, the two key factors are '(1) the legitimate expectations engendered by the plan; and (2) the difficulty of reversing the consummated transactions.' . . . This fact-intensive inquiry weighs 'the virtues of finality, the passage of time, whether the plan has been implemented and whether it has been substantially consummated, and whether there has been a comprehensive change in circumstances.'" *Duff v. Central Sleep Diagnostics, LLC*, 801 F.3d 833, 840 (7th Cir. 2015).
- **Eight Circuit:**

- Recognizes equitable mootness as a doctrine. *In re VeroBlue Farms USA, Inc.*, 6 F.4th 880, 883-84 (8th Cir. 2021).
- The "most important factors are whether the confirmed plan has been substantially consummated and, if so, what effects reversal of the plan would likely have on third parties," and courts must use "a sufficiently rigorous test to determine when a bankruptcy equities and pragmatics justify foregoing Article III judicial review of a bankruptcy court order confirming a Chapter 11 plan." *In re VeroBlue Farms USA, Inc.*, 6 F.4th 880, 883-84 (8th Cir. 2021).

- **Ninth Circuit:**
  - Recognizes equitable mootness and has established a four-factor test for determining whether an appeal should be dismissed on mootness grounds (requires appellant to seek a stay with certain exceptions). *In re Transwest Resort Properties, Inc.*, 801 F.3d 1161, 1167-68 (9th Cir. 2015).
  - Factors: "We will look first at whether a stay was sought, for absent that a party has not fully pursued its rights. If a stay was sought and not gained, we will then look to whether substantial consummation of the plan has occurred. Next, we will look to the effect a remedy may have on third parties not before the court. Finally, we will look at whether the bankruptcy court can fashion effective and equitable relief without completely knocking the props out from under the plan and thereby creating an uncontrollable situation for the bankruptcy court." *In re Transwest Resort Properties, Inc.*, 801 F.3d 1161, 1167-68 (9th Cir. 2015).
  - Review is *de novo*
- **Tenth Circuit:**
  - Recognizes equitable mootness and utilizes six factors, including a quick look at the merits.
    - "Has the appellant sought and/or obtained a stay pending appeal? (2) Has the appealed plan been substantially consummated? (3) Will the rights of innocent third parties be adversely affected by reversal of the confirmed plan? (4) Will the public-policy need for reliance on the confirmed bankruptcy plan-and the need for creditors generally to be able to rely on bankruptcy court decisions-be undermined by reversal of the plan? 5) If appellant's challenge were upheld, what would be the likely impact upon a successful reorganization of the debtor? And (6) based upon a quick look at the merits of appellant's challenge to the plan, is [the argument] legally meritorious or equitably compelling?" *In re Stephens*, 704 F.3d 1279, 1282-83 (10th Cir. 2013).
  - Abuse of discretion standard
  - The courts should "focus less slightly on the issue of whether the parties sought a stay . . . [F]ailure to obtain a stay pending appeal cannot be

determinative on the issue of equitable mootness, because it is the absence of a stay that generally has caused the change of circumstances [, so t]his factor would thus be present in all appeals not stayed." *In re Paige*, 584 F.3d 1327, 1339 (10th Cir. 2009). (We will be more inclined to accommodate an appellant who has diligently but unsuccessfully pursued a stay, even if awarding him relief may adversely affect third parties.") *Id*. at 1341.

- **Eleventh Circuit:**
  - Recognizes equitable mootness as a doctrine.
  - "The court must determine whether the 'reorganization plan has been so substantially consummated that effective relief is no longer available.' . . . substantial consummation by itself does not resolve the issue. Even if substantial consummation has occurred, a court must still consider all the circumstances of the case to decide whether it can grant effective relief." *In re Club Associates*, 956 F.2d 1065, 1069 (11th Cir. 1992).
  - Review is *de novo*

- **PETITION OF WRIT OF CERTIORI: U.S. Bank N.A., v. Windstream Holdings, Inc. et al., No. 22-926**
  - **Background**: U.S. Bank, trustee for unsecured noteholders of Windstream, brought an action in the District Court alleging that a sale-leaseback transaction breached the noteholders' contract.
    - Windstream and its affiliates commenced a chapter 11 proceeding and then pursued and consummated a chapter 11 plan that cancelled more than $1 billion of unsecured notes without allowing any recovery.
    - US Bank timely appealed the confirmation order and sought to have its appeals expedited so that it could be decided before Windstream consummated its plan, which all parties understood would take several months because of the need for regulatory approval. When that request was denied, US Bank sought to have the confirmation order stayed both in the Bankruptcy Court and in the District Court. The Bankruptcy Court promptly denied the stay request. The District court failed to act before the chapter 11 plan was consummated. About a year later the District Court dismissed the appeal as equitably moot determining that US Bank did not diligently seek a stay. The Second Circuit subsequently affirmed and US Bank's request for en banc review was denied.

- **Questions Presented in the Petition for Writ of Certiori**:
  - Does the lack of statutory and constitutional basis for the equitable mootness doctrine, combined with its demonstrated potential for abuse, require it to be abolished?
  - Does the Second Circuit's rule that an appeal from a substantially consummated plan is automatically equitably moot if the appellant did not pursue a stay, regardless of a stay's availability or any other equitable factors, undermine any prudential purpose for the doctrine?

- Does the Second Circuit's rule that the appellant bears the burden of proof in showing lack of equitable mootness cause reviewing courts to speculate that effective relief is unavailable without evidence?

- **Points Made in Amicus Brief by a Group of Law Professors:**
  - **Whatever its doctrinal legitimacy, equitable mootness has expanded beyond its original purpose**
    - The Law Professors argue that equitable mootness traces its origins back to ***constitutional*** mootness but has now become untethered from its original constitutional roots.
      - Constitutional mootness is based on the requirement of a "case or controversy" in Article III and is "jurisdictional." *Reynolds v. Serisfirst Bank (In re Stanford)*, 17 F.4th 116, 122 (11th Cir. 2021).
        - The underlying rationale for constitutional mootness is based on a threshold determination that there is ***no possibility of*** "effective relief whatever." *Mills v. Green*, 159 U.S. 651, 653 (1895) (emphasis added).
      - As Justice Roberts wrote for a unanimous Court in *Chafin v. Chafin*, 568 U.S. 165, 172 (2013) "a case 'becomes moot' only when it is impossible for a court to grant any effectual relief whatever to the prevailing party. . . . As long as the parties have a concrete interest, however small, in the outcome of the litigation, the case is not moot" (citing Mills v. Green, 159 U.S. 651, 653).
      - ***Equitable*** mootness involves and unwillingness to alter an outcome. ***Constitutional*** mootness is characterized by an inability to alter an outcome.
    - Enlarging the reach of equitable mootness harms the bankruptcy system and represents an unwarranted migration of federal jurisdiction from Article III Courts to the bankruptcy courts.
    - The Second Circuit improperly expanded the notion of equitable mootness and imposed a presumption of mootness based on substantial consummation.
  - **The Court should grant certiorari in order to resolve the many significant conflicting decisions from almost every circuit court**
    - Even if the doctrine has some limited application, it has been applied unevenly and is currently lacking any semblance of uniformity and coherence.
  - **The unwarranted enlargement of the doctrine of equitable mootness has led to substantial abuses in the bankruptcy system, in particular, in larger Chapter 11 cases.**
    - The lack of appellate review is exacerbated by the significant increase in abusive techniques being employed in large Chapter 11 cases. "[C]lever

debtors and their lawyers . . . have developed procedural strategies that effectively disable the formal machinery of creditor protection . . . 'Two of the most important developments in recent bankruptcy practice [restructuring support agreements and deathtraps] are intended to distort, and clearly do distort, the voting process.'" Lynn LoPucki, *Chapter 11's Descent into Lawlessness*, 96 AM. BANK. L. JOURNAL, 247, 251 (June 2022)

- "[B]ankruptcy grifters have infiltrated the Chapter 11 process. Over the past few years, mass tort litigation arising out of the opioid crisis – including the bankruptcy of cases of opioid manufacturers Purdue Pharma and Mallinckrodt – has shifted from state and federal systems to bankruptcy courts." Lindsey D. Simon, *Bankruptcy Grifters*, 131 YALE L.J. 1154, 1157-58 (2022)

- **The recent Supreme Court decision, *MOAC Mall Holdings LLC v. Transform Holdco LLC*, 598 U.S. (2023)**, provides an insight as to how the Supreme Court may tackle equitable mootness.
  - The Supreme Court approached Transform's mootness argument by first declaring its prior disfavor for limiting appellate review on mootness grounds. The Supreme Court cited, *Chafin v. Chafin*, 568 U.S. 165 (2013), for the proposition that appellate review remains alive notwithstanding the fact that a successful reversal of a lower court order would not matter to effectuating the ultimate relief being sought. The court held that as long as the parties have a concrete interest, however small, in the outcome of litigation, the appeal could remain alive.
  - The Supreme Court also stated it would not become a court of "first view" regarding whether or not relief truly remained legally available to the appellant and was not convinced the parties no longer had a "concrete interest" in the outcome of the appeal. Accordingly, the court remanded the case to the Second Circuit for further proceedings consistent with their opinion.
  - Based on this reasoning, the Supreme Court may, one day, apply similar reasoning to the doctrine of equitable mootness, and greatly limit the applicability of this doctrine to those instances to where a lower court has properly determined that the parties no longer have a "concrete interest" in the outcome of an appeal as opposed to considering whether a plan has been substantially consummated and third party may be impacted by a reversal.

**Make-Wholes & Solvent Debtors**

**MAKE-WHOLES**

Basic rationale: compensate lenders for loss of income stream and effective yield originally bargained for. Though make-wholes are generally enforceable under state law (e.g., NY), there is developing case law at the circuit [appellate] and bankruptcy court levels as to whether (or when) such provisions are enforceable in chapter 11.

Most recently, in the chapter 11 cases of *Ultra Petroleum Corp*.,[1] the Fifth Circuit issued a significant decision addressing the enforceability of make-wholes. In the first opinion of its kind by a circuit court, it found that the typical make-whole formulation of discounting back the future interest to determine the make-whole amount was the economic equivalent of "unmatured interest," which, absent certain rare circumstances, is disallowed by the Bankruptcy Code. This decision was followed by a decision in the Delaware Bankruptcy Court in the Hertz bankruptcy case, where the court found that it was a factual issue whether the interest component of a make-whole formula is unmatured interest; it then decided that it was unmatured interest and thus disallowed. These two recent cases put at risk the enforceability of standard make-whole language in two of the most common jurisdictions for large chapter 11 filings.

**Ultra Petroleum (2022 – Fifth Circuit)**

- Ultra Petroleum commenced chapter 11 cases in deep insolvency, but a significant upswing in natural gas prices made the debtors solvent during the pendency of the chapter 11 cases and enabled them to propose a plan of reorganization, pursuant to which all unsecured claims would be paid in full in cash, including interest (i.e., were unimpaired).
- Certain unsecured noteholders objected to the plan, arguing that they were, in fact, impaired, because the plan did not provide for payment of the make-whole amounts to which they were entitled under the indenture. The Southern District of Texas Bankruptcy Court initially agreed with the noteholders that they should be paid the make-whole amounts.[2]
- The bankruptcy decision was appealed, and the Fifth Circuit remanded the case to the bankruptcy court to determine whether the make-whole amounts constitute "unmatured interest" that should be disallowed under Section 502(b)(2) of the Bankruptcy Code (in that case, the noteholders claims would, in fact, be "unimpaired" by the plan as it would be the Bankruptcy Code, not the plan, that disallowed the make-whole).[3]
- On remand, the bankruptcy court held that the make-whole is not unmatured interest or its "economic equivalent" and is not disallowed by the Bankruptcy Code.[4]
- A second appeal to the Fifth Circuit followed.
- In October 2022,[5] the Fifth Circuit became the first circuit court to address this issue. The Fifth Circuit overturned the bankruptcy court's decision. It held first that Section 502(b)(2) disallows not only claims for unmatured interest, but also claims for the "economic equivalent" of unmatured interest. It then proceeded to find that the make-whole provision was "expressly

[1] *In re Ultra Petroleum Corp.*, 51 F. 4th 138 (5th Cir. 2022).
[2] *In re Ultra Petroleum Corp.*, 575 B.R. 361 (Bankr. S.D. Tex. 2017).
[3] The court initially rendered judgment in January 2019, *In re Ultra Petroleum*, 913 F.3d 533 (5th Cir. 2019), but upon a petition for rehearing, the original opinion was withdrawn and a new one substituted in November 2019, 943 F.3d 758 (5th Cir. 2019).
[4] *In re Ultra Petroleum Corp.*, 624 B.R. 178 (Bankr. S.D. Tex. 2020).
[5] *Supra* n.1.

designed to liquidate fixed-rate lenders' damages" by calculating "the present value of all their future interest payments," which constitutes "nothing more than a lender's unmatured interest, rendered in today's dollars."

- Accordingly, the Fifth Circuit reached the conclusion that the make-whole is the "economic equivalent" of unmatured interest and should be disallowed. In doing so, the court rejected the noteholders' argument that make-whole premiums are not "interest" as they do not compensate the noteholders for the actual use or forbearance of their money. The Fifth Circuit was similarly unconvinced by the noteholders' argument that the make-whole formula is a present value calculation that discounts future interests that the noteholders would have received and therefore constitutes liquidated damages rather than unmatured interest, or that, under NY law, a make-whole cannot be both liquidated damages and the economic equivalent of unmatured interest.
- However, the Fifth Circuit did find that, in that particular case, the solvent-debtor exception applies and, therefore, the debtors, having become solvent in the course of the bankruptcy cases, were required to pay the make-whole premium.

**Hertz (2021-22 – Delaware Bankruptcy Court)**

- After confirmation of Hertz's plan of reorganization, certain bondholders filed a complaint seeking payment of a "Redemption Price", and the debtors filed a motion to dismiss the complaint.
- In 2021, Judge Walrath of the District of Delaware Bankruptcy Court denied the debtors' motion to dismiss on the basis that a factual issue existed as to whether the "Redemption Price" was the equivalent of a make-whole premium disallowed as economic equivalent of "unmatured interest" under Section 502(b) of the Bankruptcy Code.[6]
- Subsequently, Judge Walrath granted the debtors' motion for summary judgment, having found that all components of the "Redemption Price" "are unmatured interest or its economic equivalent" that should be disallowed.[7]
- Judge Walrath recognized that "whether a make-whole premium is the economic equivalent of interest . . . depends on the facts of each case," and that "the economic substance of the transaction governs, not the formalistic labels or dictionary definitions of the terms used."
- Based on these principles, the court determined that the bondholders may have framed the "Redemption Price" as a liquidated damages provision, but if its calculation entirely consists of discounting future unpaid interest, it was the economic equivalent of unmatured interest "regardless of [its] name" and should be disallowed.

[6] *Wells Fargo Bank, N.A. v. Hertz Corp.*, No. 20-11218, 2021 WL 6068390 (Bankr. D. Del. Dec. 22, 2021).
[7] *In re The Hertz Corp.*, No. 21-50995 (MFW) (Bankr. D. Del. Nov. 21, 2022) [Docket No. 71].

**SOLVENT DEBTOR EXCEPTION**

The solvent debtor exception generally permits unsecured creditors of solvent debtors to collect post-petition interest on their claims despite the general prohibition of unmatured interest in Section 502(b)(2) of the Bankruptcy Code. The Fifth Circuit held that this exception allows make-whole claims that are otherwise disallowed as unmatured interest.

This issue may still be resolved differently in other circuits.

**Ultra Petroleum (2019-20 – Fifth Circuit/Southern District of Texas Bankruptcy Court)**

- After debtors became solvent during pendency of the chapter 11 cases (due to rising energy prices), the Fifth Circuit asked the Southern District of Texas Bankruptcy Court to determine whether the make-whole premium constituted "unmatured interest," which would be disallowed under Section 502(b)(2) of the Bankruptcy Code.
- The bankruptcy court noted that the existence/enactment of the Bankruptcy Code does not itself repeal the solvent debtor exception recognized under the predecessor statute, the Bankruptcy Act.
- The bankruptcy court determined that the solvent debtor exception did exist and did require the debtors to pay a make-whole premium (even if it constituted unmatured interest) before distributing any value to shareholders.

**Ultra Petroleum (2022 – Fifth Circuit)**

- The Fifth Circuit confirmed, agreeing that the solvent-debtor exception was not abrogated by the adoption of the Bankruptcy Code (noting that it is "alive and well").
- The court looked to SCOTUS guidance not to infer an abrogation of a well-established pre-Code bankruptcy practice that constituted an exception to the text of prior statutes as well. *See Cohen v. de la Cruz*, 523 U.S. 213, 221-22, 118 S. Ct. 1212, 140 L. Ed. 2d 341 (1998); *Midlantic Nat'l Bank v. N.J. Dep't of Envt'l Prot.*, 474 U.S. 494, 501, 106 S. Ct. 755, 88 L. Ed. 2d 859 (1986); *Kelly v. Robinson*, 479 U.S. 36, 46, 53, 107 S. Ct. 353, 93 L. Ed. 2d 216 (1986).
- The court also ruled that a make whole does not constitute a penalty under NY law (if it were a penalty, the solvent-debtor exception would not have applied).
- Given the debtors' solvency, the make-whole premium was due and owing and post-petition interest was calculated at the agreed-upon contractual rate (and not the federal judgment rate as proposed by the debtors).

**Hertz (2021 – Delaware Bankruptcy)**

- In Hertz, the District of Delaware Bankruptcy Court declined to reach a broader conclusion as to whether make-whole premiums constitute unmatured interest; instead, it only determined whether the premium was the economic equivalent of unmatured interest under the specific facts of the case.
- The bankruptcy court did acknowledge that the solvent debtor exception is relevant if the make-whole is determined to be unmatured interest.
- The bankruptcy court, however, found that the mere fact of the debtor's solvency does not eliminate the application of Section 502(b) nor does the solvent debtor exception require a solvent debtor to pay post-petition interest at the applicable contract rate and that federal judgment rate is sufficient.
- This matter was certified directly to the Third Circuit and the Third Circuit has accepted the appeal. Oral argument is scheduled for October 26, 2023.

**PG&E (2022 – Ninth Circuit)**

- In September 2022, the Ninth Circuit held that, in a solvent debtor case, unsecured creditors have an equitable right to post-petition interest at the applicable contractual rate – not the federal judgment rate.
  The solvent debtor exception is an equitable doctrine (not codified), it is based on the concept of absolute priority.
- PG&E's plan provided for payment in full of general unsecured claims, including post-petition interest at the federal judgment rate, and classified such claims as unimpaired.
- However, the Ninth Circuit held that the plan altered the unsecured creditors' equitable rights, rendering them impaired under Section 1124(1).

**LATAM Airlines (2022 – Second Circuit)**

- In December 2022, the Second Circuit suggested that the solvent debtor exception survived the enactment of the Bankruptcy Code and would require a solvent debtor to pay pendency interest on unsecured claims to render them unimpaired under its plan of reorganization.[8]
- That suggestion, though, was necessarily *dicta* because the debtor in that case was insolvent.
- The Second Circuit did not address the rate at which interest need be paid under the solvent debtor exception, but its holding cites favorably to language from *PG&E* (described herein) that references creditors' "equitable entitlement to contractual postpetition interest when a debtor is solvent".

[8] *TLA Claimholders Grp. v. LATAM Airlines Grp. S.A. (In re LATAM Airlines Grp. S.A.)*, 55 F.4th 377, 380 (2d Cir. 2022) ("Although 11 U.S.C.S. § 1124(1) does not expressly refer to solvency, it does protect a creditor's equitable rights. That includes whatever survives of the solvent-debtor exception.").

## Reinstatement

### Overview

The use of reinstatement of loans in chapter 11 plans is beneficial when the interest rate on the existing, defaulted loan is lower than the market rate of interest on a new loan. The plan proponent is entitled to deaccelerate a defaulted loan and reinstate the original maturity, by complying with the provisions of the Bankruptcy Code to render the lender class unimpaired. By doing so, the lender is conclusively presumed to accept the plan.

Compliance with the monetary requirements to render a loan unimpaired is not where most controversies occur. The curing of nonmonetary covenants, if required to be cured or even capable of being cured, is where the litigation ensues.

### Applicable Code Provisions - §§ 1124(2), 1126(f)

#### 1124. Impairment of claims or interests

Except as provided in section 1123(a)(4) of this title, a class of claims or interests is impaired under a plan unless, with respect to each claim or interest of such class, the plan –

* * * * * * * * * * *

(2) notwithstanding any contractual provision or applicable law that entitles the holder of such claim or interest to demand or receive accelerated payment of such claim or interest after the occurrence of a default –

(A) cures any default that occurred before or after the commencement of the case under this title, other than a default of a kind specified in section 365(b)(2) of this title or of a kind that section 365(b)(2) expressly does not require to be cured;

(B) reinstates the maturity of such claim or interest as such maturity existed before such default;

(C) compensates the holder of such claim or interest for any damages incurred as a result of any reasonable reliance by such holder on such contractual provision or applicable law;

(D) if such claim or such interest arises from any failure to perform a nonmonetary obligation, other than a default arising from failure to operate a nonresidential real property lease subject to section 365(b)(1)(A), compensates the holder of such claim or interest (other

than the debtor or an insider) for the actual pecuniary loss incurred by such holder as a result of such failure; and

(E) does not otherwise alter the legal, equitable, or contractual rights to which such claim or interest entitles the holder such claim or interest.

**1126. Acceptance of plan**

(f) Notwithstanding any other provision of this section, a class that is not impaired under a plan, and each holder of a claim or interest of such class, are conclusively presumed to have accepted the plan, and solicitation of acceptances with respect to such class from the holders of claims or interests of such class is not required.

**Cross-referenced provisions**

**365(b)(2)** does not require the curing of defaults that relate to *ipso facto* provisions, such as bankruptcy or insolvency, or penalty rates or other penalty provisions relating to nonmonetary defaults.

**365(b)(1)(A)** does not require the curing of defaults that are impossible to cure because they require performance at some time in the past

**Salient Prior Cases**

***JP Morgan Chase Bank, N.A. v. Charter Communications Operating, LLC (In re Charter Communications)***, 419 B.R. 221 (Bankr. S.D.N.Y. 2009), *appeal dismissed as equitably moot sub nom. R2 Investments, LDC v. Charter Communications, Inc. (In re Charter Communications, Inc.)*, 449 B.R. 14 (S.D.N.Y. 2011), *aff'd*, 691 F.3d 476 (2d Cir. 2012)

The lender opposed reinstatement on several grounds including a change in control covenant that it asserted was violated by the plan. The bankruptcy court rejected the lender's interpretation of the covenant at issue and the lender's other alleged covenant defaults and confirmed the plan. The appellate courts dismissed the appeals as equitably moot.

***In re Young Broadcasting Inc.***, 430 B.R. 99 (Bankr. S.D.N.Y. 2010)

The lenders opposed confirmation of the creditors' committee's plan, which included reinstatement, also asserting that a change in control covenant was violated. The bankruptcy court agreed with the lenders, denied confirmation of the committee's plan, and confirmed the debtor's plan instead.

***In re NNN 3500 Maple 26, LLC***, No. 13-30402-HDH-11, 2014 WL 1407370 (Bankr. N.D. Tex. Apr. 10, 2014)

The bankruptcy court denied confirmation of the debtor's plan because it fundamentally altered the nature of the borrower of the loan at issue, by creating a new entity including the debtor and other tenants in common that shared ownership of an office building in Dallas.

**Recent Case**

***In re 975 Walton Bronx LLC***, No, 21-40487-jmm, 2022 WL 5265041 (Bankr. E.D.N.Y. Oct. 6, 2022)

The lender opposed the debtor's reinstatement because the debtor violated the change in control covenant of the loan. The bankruptcy court agreed but gave the debtor the opportunity to demonstrate that equitable principles prevented the lender from accelerating the loan. After a trial, the court held that the debtor had not demonstrated that equitable principles prevented the lender's acceleration of the loan.

The court recognized that, under New York law, equity can intervene to prevent acceleration, such as when

- a technical default is not willful – to prevent a forfeiture; or
- the lender engages in conduct that is fraudulent, exploitive, overreaching, or unconscionable conduct

The court also held that in accordance with the decision in *In re 53 Stanhope LLC*, 625 B.R. 573 (Bankr. S.D.N.Y. 2021), *appeal dismissed as equitably moot*, Nos. 21-CV-5177, 21-CV-2807, 21-CV-5867 (CS), 2022 WL 3025930 (S.D.N.Y. Aug. 1, 2022), which did not involve reinstatement, a court would not enforce an acceleration clause based on a nonmonetary default, if

- the lender did not suffer actual damages as a result of the nonmonetary default;
- the nonmonetary default did not impair the lender's security; and
- the nonmonetary default did not make future monetary defaults more likely to occur

The court determined that the debtor had not proved any of the above exceptions.

## Cram Down

### Overview

The use of cram down becomes necessary if a deal with the secured creditor cannot be struck and reinstatement is unavailable or impractical. The search for an appropriate cram down interest rate in chapter 11 has changed considerably since the Bankruptcy Code went into effect. Although several different methodologies were used in the early days of the Code, currently the approaches have essentially come down to two:

- the *Till* methodology from a 2004 Supreme Court plurality decision in a chapter 13 case – prime rate plus 1% to 3%; or
- a preference for the rate determined by an efficient market for chapter 11 exit loans, if such an efficient market exists, with a fallback to the *Till* methodology, if such market does not exist.

The Second and Sixth Circuits have adopted the latter approach. Many bankruptcy courts outside the Second and Sixth Circuits use the former approach. In an environment of rising interest rates, either approach presents legal and financial problems.

### Applicable Code Provision - § 1129(b)(2)(A)(i)(II)

**1129 – Confirmation of plan**

(II) that each holder of a claim of such class receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property.

### Historical Overview

Neither the Code nor the legislative history provides guidance on how to determine the "value, as of the effective date of the plan" of the "deferred cash payments" that amount to at least the value of the "holder's interest in the estate's interest" in the relevant collateral. The courts initially developed several different methodologies:

- the contract rate, if recently entered into
  - *E.g., Prudential Ins. Co. v. Monnier (In re Monnier Bros.)*, 755 F.2d 1336, 1339 (8th Cir. 1995)
- a riskless rate, adjusted for the risks associated with the particular debtor
  - *E.g.*, *In re Computer Optics, Inc.*, 126 B.R. 664, 672 (Bankr. D.N.H. 1991)

- a market rate or coerced loan method
    - *E.g., Travelers Ins. Co. v. Bryson Props., XVIII (In re Bryson Props., XVIII)*, 961 F.2d 496, 500 (4th Cir. 1992)

- investment bands, dividing the coerced loan into senior and junior secured loans with different rates to form a blended rate
    - *E.g.*, *In re Cellular Info. Sys., Inc.*, 171 B.R. 926, 942-44 (Bankr. S.D.N.Y. 1994)

In 2004, the Supreme Court decided ***Till v. SCS Credit Corp.*, 541 U.S. 465 (2004)**, a chapter 13 cram down case involving a used truck. Notably, the chapter 13 cram down provision is substantially the same as the chapter 11 version. In a plurality opinion, the Supreme Court rejected the contract method, the market or coerced loan method as imposing excessive evidentiary costs, and improperly including an element of profit.

The *Till* Court opted for a straightforward formulaic approach:

- the prime rate, adjusted by 1% to 3%.

The Court noted in its footnote 14 that the chapter 11 cram down analysis may be different, because the court observed that "there is no free market of willing cramdown lenders" in chapter 13 cases. The Court further observed that "the same is *not* true in the Chapter 11 context, as numerous lenders advertise for financing for Chapter 11 debtors in possession . . . Thus, when picking a cramdown rate in a Chapter 11 case, it might make sense to ask what an efficient market would produce."

Despite this observation, bankruptcy courts have applied the *Till* formula to chapter 11 cram down interest rates. In the Fifth Circuit observed in 2013 that "the vast majority of bankruptcy courts have taken the *Till* plurality's invitation to apply the prime-plus formula under chapter 11." *Wells Fargo Bank v. Texas Grand Prairie Hotel Realty, L.C.C. (In re Texas Grand Prairie Hotel Realty, L.L.C.)*, 710 F.3d 324, 333 (5th Cir. 2013) (declining to set a standard methodology for chapter 11 cram down interest rates).

Nevertheless, in the aftermath of *Till* at least two courts of appeals determining chapter 11 cram down interest rates have generally taken the approach suggested by footnote 14:

- First, determine whether there is an efficient market for a chapter 11 exit loan, and if so, apply the rate set by such market; and

- If no such market exists, apply the *Till* formula,

The method has been adopted in:

*Bank of Montreal v. Official Comm. of Unsecured Creditors (In re American HomePatient, Inc.)*, 420 F.3d 559, 568 (6th Cir. 2005)

*Momentive Performance Materials Inc. v. BOKF, N.A. (In re MPM Silicones, L.L.C.)*, 874 F.3d 787, 800 (2d Cir. 2017)

- On remand to the bankruptcy court, a market rate of interest for exit financing was imposed.

**Recent Cases**

***In re CE Electrical Contractors, LLC***, No. 21-20211 (JJT), 2022 WL 1420094 (Bankr. D. Conn. May 4, 2022)

The court denied confirmation of the debtor's plan on several grounds, including unfair discrimination, and other proposed modifications to the loan, apart from the interest rate, that the court considered unfair and inequitable. Pertinent to the present discussion, the court, bound by the *MPM Silicones* methodology, stated that the parties had agreed that there was no efficient market for an exit loan for this particular debtor.

The court noted the debtor had provided a list of reasons why there was no efficient market, including:

- the debtor's assets are already fully encumbered
- the debtor's anticipated income is only about twice its debt loan
- the debtor's principal had issued millions of dollars in personal guarantees and was the target of lawsuits in several states
- the debtor's cash flow during the plan term was sufficient for operating needs but not for a new lender
- the debtor had defaulted on its pre-bankruptcy secured debt

As a result, the court resorted to the *Till* formula and applied a 2% increment over the prime rate to set the cram down interest rate.

***In re Twisted Oak Winery, LLC***, No. 21-90484-E-11, 2022 WL 5264708 (Bankr. E.D. Cal. Oct. 5, 2022)

The court applied the *Till* formula to determine the cram down interest in this subchapter V case in accordance with the parties' agreement. The debtor proposed a rate of 4.5%, when the prime rate was 3.5%. At the time of the confirmation, the prime rate had increased to 4.75%, and further increased to 4.85% shortly thereafter. In light of the low risk to the lender, the court imposed a 1% increment over the prime rate at the time of the confirmation hearing, resulting in a 5.75% cram down interest rate.

# Faculty

**Kathryn A. Coleman** is a partner in Hughes Hubbard & Reed LLP's New York office. She has handled a wide range of chapter 11 representations and other high-stakes insolvency-related matters in her more than 30 years in practice, including dealing with "bet-the-company" litigation claims, representing acquirers in chapter 11 sale transactions, representing DIP lenders, and handling cross-border insolvency matters, out-of-court restructurings and distressed investments. Ms. Coleman's clients include individuals and companies defending trade secret theft and RICO lawsuits, publicly traded and privately held companies restructuring their financial affairs, traditional and nontraditional secured lenders, unsecured creditors (both official committees and significant creditors for their own account), equityholders, potential acquirers, equity sponsors, and financial and strategic buyers. She also is experienced in advising management and boards of directors on corporate governance, fiduciary duty and D&O insurance matters. Ms. Coleman has advised clients on, and litigated at the trial and appellate levels, the significant legal issues inherent in modern restructuring and finance practice, including contested plan confirmations, prepackaged plans, credit bidding, exclusivity, debtor-in-possession financings, valuation, adequate protection of security interests, the ability to collaterally attack orders of the bankruptcy court and cash-collateral usage. She has experience litigating venue, remand, removal and stay issues, and has represented recovery trustees dealing with myriad post-confirmation issues and litigation. Ms. Coleman is a Fellow of the American College of Bankruptcy and served two terms on ABI's Board of Directors, and she co-chairs ABI's annual Complex Financial Restructuring Program. She was recently named a *Law360* Bankruptcy MVP and a Notable Woman in Law by *Crain's New York Business*. Ms. Coleman frequently speaks on bankruptcy law and distressed investing, participating in programs sponsored by the Practising Law Institute, ABI, the Turnaround Management Association, AIRA, The M&A Advisor, the New York City Bar Association and the American Bar Association. She also serves on the Steering Committee of the NYC Bankruptcy Assistance Project. Ms. Coleman graduated *magna cum laude* from Pomona College and received her J.D. from Boalt Hall School of Law (U.C. Berkeley), subsequently clerking for Hon. C. Martin Pence, U.S. District Judge for the District of Hawaii.

**Jay M. Goffman** is client chairman of Teneo's Financial Advisory Business in New York. In this role, he leads client development and execution for Teneo's North American Financial Advisory business, while also working across the broader business globally. Prior to joining Teneo, Mr. Goffman was vice chair of Global Advisory at Rothschild & Co., a large international investment bank, where he advised clients across Rothschild's Restructuring, Debt Advisory and M&A practices. Before Rothschild, he spent 36 years as a lawyer focused on restructuring, debt advisory and distressed M&A. For the last 24 years of his legal career, he practiced at Skadden Arps, where he was the global head of its Corporate Restructuring Department. Over the course of his career, Mr. Goffman has consistently been recognized as one of the leading and most innovative restructuring advisors in the world. He was named a "Dealmaker of the Year" by *The American Lawyer* and one of the "Most Influential Lawyers of the Decade" by *The National Law Journal*. He has also received several Lifetime Achievement and Hall of Fame honors, in addition to numerous philanthropic awards. Mr. Goffman is best known for having devised and pioneered the "prepackaged" restructuring, which revolutionized the field of restructuring and has been successfully used over the past 35 years to reorganize hundreds of companies in a quick, efficient and cost-effective manner. As a result of his efforts, pre-

packs are now the predominant method used in major restructurings. Mr. Goffman has successfully reorganized businesses out of court and in court across multiple industries and geographies, including some of the largest, most high-profile and most complex cases in history. Many of his deals and accomplishments have been profiled in various publications, including *The Wall Street Journal*. Mr. Goffman has chaired restructuring panels and legislative review committees, in addition to chairing and speaking at numerous restructuring and distressed M&A conferences. He also has published extensively on restructuring, fiduciary duties and distressed M&A. Mr. Goffman received his B.S. in 1980 in chemical psychobiology from the State University of New York at Binghamton and his J.D. in 1983 with honors from the University of North Carolina at Chapel Hill, where he was a member of the *University of North Carolina Law Review*. In 2018, the University of North Carolina School of Law presented him with its Distinguished Alumni Award.

**Christopher J. Kearns, CPA, CFA, CTP, CIRA** is a managing director and co-head of Berkeley Research Group, LLC's Corporate Finance practice in New York. He specializes in financial restructuring advisory services, crisis management and expert testimony in the troubled-company and corporate finance environment. Mr. Kearns has represented parties in interest in numerous complex, multinational matters and has served as CEO, CRO, responsible officer, receiver and trustee. Mr. Kearns has rendered expert testimony in multiple jurisdictions on matters involving valuation, lost profits, solvency, credit analysis, liquidation and recovery analysis, and other issues in distressed situations. He also has advised major investment banks and potential purchasers on acquisition strategies and post-merger integration. Before joining Berkeley Research Group, Mr. Kearns co-founded Capstone Advisory Group, LLC. He also was a senior managing director at the Policano & Manzo legacy practice of FTI Consulting and was with the predecessor firm Kahn Consulting. Previously, Mr. Kearns spent three years with Bristol-Myers Squibb in assignments that included assistant corporate controller. He also spent 10 years in the mergers and acquisitions group and the audit practice of a major international public accounting firm. Mr. Kearns is a member of AICPA, the New York State Society of CPAs and the Association of Insolvency and Restructuring Advisors. He served as president of the New York chapter of the Turnaround Management Association. Mr. Kearns received his B.B.A. in accounting from Iona College.

**Alec P. Ostrow** is a partner in the New York law firm of Becker, Glynn, Muffly, Chassin & Hosinski LLP and has been specializing in bankruptcy, creditors' rights, corporate reorganizations, workouts, cross-border insolvency and commercial litigation for more than 40 years. He is a Fellow of the American College of Bankruptcy and since 2000 has been an adjunct professor at St. John's University School of Law in its LL.M. in bankruptcy program. Mr. Ostrow has been selected to *Super Lawyers* since 2006, and in 2020 he was honored with the Marquis Who's Who Albert Nelson Marquis Lifetime Achievement Award. He has lectured on numerous bankruptcy issues, including at conferences sponsored by ABI, the American Bar Association, the American Law Institute - American Bar Association, the American Institute of Certified Public Accountants, the Judicial Conference of the Second Circuit, the National Association of Bankruptcy Trustees, the Association of Insolvency and Restructuring Advisors and the New York State Society of Certified Public Accountants. He also has published many articles on diverse topics in bankruptcy law, including the *American Bankruptcy Law Journal*, the *ABI Law Review* and the *Norton Annual Survey of Bankruptcy Law*. Mr. Ostrow received his undergraduate degree *magna cum laude* from Dartmouth College in 1977 and his J.D. from New York University School of Law in 1980.

**Gregory G. Plotko** is a partner with Barnes & Thornburg LLP in New York and has more than 25 years of experience advising creditors, distressed investors and corporate debtors on virtually all types of insolvency, restructuring and bankruptcy litigation matters. He provides legal counsel to a diverse range of clients, including credit funds, financial institutions (distressed desks), secured and unsecured creditors, debtors and other parties involved in complex chapter 11 and chapter 15 bankruptcy cases. He also counsels clients on the rights and remedies of various debt-holders, handicapping legal outcomes and returns on investment (recovery ranges and timing), as well as analyzing capital structures, credit covenants and indenture provisions. He has deep experience in special-situations lending, alternative financing, litigation funding and claims trading. As an advocate for creditors, Mr. Plotko's experience includes negotiating and litigating chapter 11 plans, cash-collateral orders, debtor-in-possession and exit-financing documents and equity commitment agreements, as well as developing, negotiating and implementing rights offerings. His experience with debtors includes assisting companies in navigating the complex legal, financial and operational issues that arise in chapter 11, receiverships and out-of-court restructurings. He is well-versed in negotiating and obtaining forbearance agreements and support from trade vendors, negotiating and implementing sales of business segments and companies, and negotiating debtor-in-possession financing and confirming chapter 11 plans. Prior to joining the Barnes & Thornburg, Mr. Plotko was a partner with an AmLaw 100 firm in New York. He is a member of ABI and the Turnaround Management Association, and he received the Legal Aid Society's Outstanding Pro Bono Immigration Service Award from 2005-06. Mr. Plotko received his B.S. in 1995 from Cornell University and his J.D. in 1998 from Benjamin N. Cardozo School of Law.

**Hon. Brendan L. Shannon** is a U.S. Bankruptcy Judge for the U.S. Bankruptcy Court for the District of Delaware in Wilmington, appointed in 2006. He manages a full chapter 11 docket and also handles all chapter 13 consumer bankruptcy cases filed in Delaware. He served as Chief Judge from 2014-18. Prior to his appointment to the bench, Judge Shannon was a partner with Young Conaway Stargatt & Taylor, LLP in Wilmington, Del., where he primarily represented corporate debtors and official committees in chapter 11 cases. He is an adjunct professor in the Bankruptcy LL.M. Program at St. John's University School of Law in New York, and at Widener School of Law in Delaware. He also serves on the board of editors of *Collier on Bankruptcy* (16th ed.) and is a contributing author for *Collier Forms* and for several chapters covering the Federal Rules of Bankruptcy Procedure. In addition, he serves on the editorial board of the *American Bankruptcy Institute Law Review*. In 2011, Judge Shannon was appointed to serve as a member of the National Bankruptcy Conference. In 2020, he was inducted as a member of the American College of Bankruptcy. Judge Shannon is a member of the Delaware State Bar Association, the American Bar Association, ABI and the Rodney Inns of Court in Wilmington, Del. He is also a member of the board of directors of the Delaware Council on Economic Education. Judge Shannon received his undergraduate degree from Princeton University and his J.D. from the Marshall-Wythe School of Law at the College of William and Mary.

**Stephen D. Zide** is a Financial Restructuring partner with Dechert LLP in New York and represents a diverse range of clients in chapter 11 bankruptcy and out-of-court restructuring matters. He has led numerous high-profile restructurings across a number of industries, and his clients include both official and ad hoc creditor and equity committees, debtors, bondholders, investors and secured lenders. On the creditor side, Mr. Zide advises clients on distressed and bankrupt companies with complex corporate and capital structures. He provides analysis and advice regarding fraudulent conveyance, fiduciary duty, intercreditor and valuation disputes; developing, negotiating and confirming chapter

11 plans; negotiating and litigating cash-collateral orders, debtor-in-possession financing and equity commitment agreements; and developing and implementing rights offerings. Mr. Zide's practice representing creditors is complimented by his experience representing distressed companies, and assisting debtors in navigating the complex legal, financial and operational issues that arise in chapter 11. He is consistently recognized as a leading lawyer by *Chambers USA* for bankruptcy/restructuring. The M&A Advisor recognized him as "Legal Advisor of the Year" in 2020, and in 2019, he was named one of *Turnaround & Workouts*' "Outstanding Restructuring Lawyers." Mr. Zide has been regarded as a rising star for bankruptcy by some of the most prominent legal and industry publications, including *Turnaround & Workouts*, *Law360* and The M&A Advisor. He also was recognized as a *New York Super Lawyer* from 2019-21 and was a *Super Lawyers* "Rising Star" from 2014-17. Mr. Zide received his B.A. *magna cum laude* in political science in 1999 from Queens College, The City University of New York, and his J.D. *magna cum laude* in 2004 from Brooklyn Law School, whwere he served as notes and comments editor of the *Journal of Law and Policy*, received the CALI Excellence for the Future Awards in Securities Arbitration and New York Civil Practice and The American Bankruptcy Award Journal Student Prize, and was a Carswell Merit Scholar.