The American Scene: Dealing with Dissenting Creditors in a Business Reorganization

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ALL YOU EVER WANTED TO KNOW ABOUT CRAM DOWN UNDER THE NEW BANKRUPTCY CODE

Kenneth N. Klee, Esq.*(1)
Stutman, Treister & Glatt
Suite 900, 3600 Wilshire Blvd.
Los Angeles, California
U.S.A. 90010-2739

I. INTRODUCTION

1. A new law (2) will govern reorganizations (3) cases commenced on or after October 1, 1979. (4) The substantive law is codified by Pub. L. No. 95-598 in title 11 of the United States Code entitled "Bankruptcy." Under the Code a debtor may choose among various kinds of relief available. In general the choice will be between liquidation (i.e., straight bankruptcy) under chapter 7 and reorganization under chapter 11. In liquidation, property of the debtor is gathered into an estate, liquidated, and the proceeds are distributed to creditors. In reorganization, generally the debtor rearranges its debt structure under a plan and continues in business. (5) In the vast majority of cases, the debtor will reach an agreement with creditors and a plan will be confirmed.

2. In a few cases, agreement with each class will not be reached and the plan may only be confirmed over the dissent of a class of claims or ownership interests—the "cram down" power. In those cases special rules apply to protect dissenting classes of secured claims, unsecured claims, and ownership interests. While these rules will be important in the context of confirmation of a plan when a class consents, one of the hypotheses of the Code is that the rules will also affect the negotiating posture of the debtor and creditors with respect to formulation of a plan. Hence, an ancillary effect of the cram down rules will be to produce a plan which all classes will accept voluntarily.

3. Thus, for judges, debtors, and creditors who will be affected by the new Code it is vital to know the conditions under which a plan of reorganization (6) may be confirmed (7) over the dissent (8) of classes of creditors, (9) to extract that knowledge involves a tortuous journey through the statute and legislative history that is fraught with complex concepts, terms of art, and nuances.

4. Before proceeding to consideration of the cram down power, first it is useful to examine the confirmation standards that generally apply in reorganization cases. In the vast majority of cases, all classes of claims and interests will accept the plan (10) and the plan need only meet the general standards of confirmation. (11) The Code requires both the plan (12) and the proponent of the plan (13) to comply with the applicable provisions of chapter 11. In
addition, the plan must be proposed in good faith and not by any means forbidden by law. Certain payments to be made under the plan or in connection with it must be disclosed to the court and approved as reasonable. The proponent of the plan must disclose the identity of individuals who are proposed to be officers or directors under the plans and the court must find the officers and directors to be consistent with the needs of creditors and equity security holders and the public interest. The proponent must also disclose the identity and compensation of any insider who will be employed by the reorganized debtor. Moreover, if the plan provides for a rate change, the change must have been approved by any regulatory commission with jurisdiction over the rates or conditioned on such approval.

5. There are four additional requirements which are more complex. First, the plan must meet a statutory best interests of creditors test. This test protects dissenting members of a class (as distinguished from the cram down power which protects dissenting classes) by requiring each member to receive under the plan at least as much as would be received on liquidation. Second, each priority claim must receive special treatment unless the claim holder agrees otherwise. Administrative expenses and certain post petition expenses in involuntary cases must be paid in cash on the effective date of the plan. Wage claims, fringe benefits, and certain claims of consumer creditors must be paid in cash on the effective date of the plan unless the class of claims accepts deferred cash payments that have a present value equal to the amount of the claims. Each priority tax claim must receive deferred payments over a period not exceeding six years from the assessment of the tax; also, the payments must have a present value equal to the amount of the tax claim. Third, at least one class of claims must accept the plan, without including acceptances by insiders holding claims of the class. This requirement is satisfied when there exists a class of claims that is not impaired, excluding any class of insider claims, since holders of unimpaired claims are deemed to have accepted the plan. Finally, the plan must be feasible, the Code defines this to mean that the plan is not likely to be followed by liquidation or reorganization of the debtor unless the plan is a liquidating plan.

6. In the vast majority of cases, if all of the above requirements are met, the plan will be confirmed. But if all of the requirements for confirmation of a plan of reorganization have been met, except that one or more classes of claims or interests have not accepted the plan, then confirmation can occur only by invoking the cram down power. In those circumstances the Code permits the proponent of the plan to request the court to confirm the plan not with standing the failure of one or more "impaired" classes to accept the plan. If certain protective conditions are met with respect to classes that are impaired and have not accepted the plan, then the court is required to confirm the plan. Before these conditions are discussed the concept of "impaired classes" must be understood.

II. IMPAIRED CLASSES

7. The concept of when a class is "impaired" or when a class is "unimpaired" is vital. It is necessary to know whether a class that has not voted for acceptance of a plan is
impaired or unimpaired under the plan. A class that is not impaired is deemed to have accepted the plan.47(49) On the other hand a class that has not voted for acceptance and is impaired is, what is called for convenience, a "dissenting" class. If a class dissents, special protective conditions must apply in order for a plan to be confirmed.

8. The Code specifies that a class of claims or interests is impaired under a plan unless at least one of three separate standards is met with respect to each claim or interest in the class.48(50) First the plan may leave unaltered the legal, equitable, and contractual rights to which the holder of the claim or interest is entitled. 49(51) If this is done the class is not impaired and consent of the class is not necessary to confirm the plan. Second, the plan may permit the proponent of a plan to negate an acceleration clause as a matter of law without the approval of any other party. The statute accomplishes this by providing, in essence, that the plan may cure defaults 50(52) and reinstate a claim or interest without otherwise altering the holder's legal, equitable, or contractual rights.51(53) In particular the maturity of the claim or interest must be reinstituted as it existed before the default. 52(54) The plan must compensate the holder of the claim or interest for any damages "incurred as a result of any reasonable reliance" by the holder on an acceleration clause. 53(55) Third, the plan may provide for the holder of a claim to receive cash on the effective date of the plan equal to the allowed 54(56) amount 55(57) of the claim.56(58) Alternatively, if applicable,57(59) the plan may provide for the holder of an ownership interest to receive cash on the effective date of the plan in the amount of any fixed liquidation preferences 58(60) or redemption price, 59(61) whichever is greater.60(62) The effect of this standard is to permit confirmation of a plan without the active consent of a class of claims or interests if the class is paid cash in an amount that is normally 61(63) the full amount of the debt owed.

III. CONFIRMATION OVER THE OBJECTION OF AN IMPAIRED CLASS OF UNSECURED CREDITORS OR OWNERSHIP INTERESTS

9. With a preliminary understanding of the concept of "impairment" and the general requirements of confirmation, the conditions under which a plan may be confirmed over the dissent 62(64) of a class of unsecured claims or ownership interests are more easily comprehended.

10. Even though a class dissents, the plan may be confirmed if the interests of the dissenting class are protected. If the proponent of a plan so requests,63(65) then the court is required to confirm 64(66) the plan, notwithstanding the dissent of a class of claims or interests, "if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan." 66(67) The conditions pertaining to unfair discrimination and fair and equitable treatment apply only with respect to dissenting 66(68) classes rather than to all classes or the plan as a whole 67(69).

11. Nothing in the Code aids the determination of whether a plan "does not discriminate unfairly" with respect to a dissenting class. The legislative history states that the requirement "is included for clarity" and applies in the context of subordinated debentures. 68(70) The requirement is intended to be complementary to the fair and equitable test and to compensate
for the complexity inherent in the relative priority 69(71) of classes caused by partial
subordination.70(72) In a nutshell if the plan protects the legal rights of a dissenting class in a
manner consistent with the treatment of other classes whose legal rights are intertwined with
those of the dissenting class, then the plan does not discriminate unfairly with respect to the
dissenting class.

12. The Code is fairly explicit in specifying whether a plan is fair and equitable with respect to a
dissenting class.71(73) The statute states that the requirement that a plan is fair and equitable
"includes" 72(74) several factors.73(75) If however the legislative history makes clear that
some factors which are "fundamental" to fair and equitable treatment of a dissenting class
were omitted from the statute to "avoid complexity".7(76) For example a requirement
contained in an earlier version 75(77) of the Code would have assured a dissenting class that
no senior class receives more than 100% of its claims, i.e., that it is not provided for more
than in full. 76(78) While the deletion of this standard may be beneficial to understanding the
statutory language, it is not clear that the result "avoids complexity."

13. The Code adopts three different tests to determine whether a plan is fair and equitable,
depending on whether the dissenting class is comprised of secured claims,77(79) unsecured
claims,78(80) or ownership interests.79(81) The tests regarding unsecured claims and
ownership interests essentially apply a relaxed 80(82) version of the traditional absolute
priority rule,81(83) under which a dissenting class must be provided for in full before any
junior class can receive or retain any property. However, the test for secured claims82(84) is
completely novel, affording protection for classes of secured claims that is not provided
under present law. 83(85)

14. Before discussing the test for secured claims it is beneficial to examine the tests for
dissenting classes of unsecured claims or interests. The plan may be confirmed
notwithstanding the dissent of a class of unsecured claims, only if one of two standards is
satisfied.84(86) First, the plan may provided for members of the class to receive or retain
property 85(87) that has a present value 86(88) equal 87(89) to the allowed amount 88(90) of
their unsecured claims. 89(91) Alternatively, the plan may provide any treatment for the class
as long as no junior 90(92) claim or interest will participate in the plan or will retain any
claim against or interest in the debtor. 91(93) This simple test protects members of a
dissenting class of unsecured creditors by entitling them to be provided for in full if any class
junior to them is to receive anything at all. It is permissible to propose a plan in which senior
classes give up value to junior claims or interests, but the plan will not be confirmed over the
dissent of a senior class or of any intermediate class that is not provided for in full. 92(94)
For example, a dissenting class of unsecured claims will be able to prevent confirmation of a
plan in which a class of senior claims proposes to give value to a class lower in priority to the
dissenting class - for example, a class of equity interests.

15. On the other hand, if a class of unsecured claims is the lowest in priority to receive or retain
property under the plan, such as unsecured creditors receiving stock when the interests of
former shareholders are eliminated, the alternative standard that no junior class receive or
retain property under the plan is satisfied, even if the class of unsecured claims dissents. The
plan will be confirmed as long as it is otherwise fair and equitable and does not discriminate
16. Likewise, a junior dissenting class is without power to prevent confirmation of a plan in which senior creditors give up value to an intermediate class. Thus, a class of shareholders whose equity interests are eliminated may not prevent senior creditors from giving up value to an intermediate class of junior unsecured creditors as long as no class is provided for more than in full. However, in order to determine whether junior creditors are provided for more than in full, it will be necessary to value the consideration received under the plan. If the consideration received is stock of the debtor, then the business will have to be valued. The threat of valuation gives negotiating leverage to the class of ownership interests. Since a valuation of the business must be made if the shareholders dissent, often seniors will give up value to shareholders to obtain their consent to the plan. If the shareholders consent, a costly valuation may be avoided.

17. The test to confirm a plan over the dissent of a class of ownership interests is similar to that for unsecured claims. The plan may be confirmed only if one of two standards is met. First, the plan may propose that each member of the class receive or retain on account of its interest property with a present value equal to the greatest of any liquidation preference, redemption price, or the value of the interest, based on a going concern valuation of the business. If a class of ownership interests is not entitled to a redemption price or liquidation preference, such as most common stock, then the plan must provide the class with property of a present value equal to the value of the ownership interests. If the reorganization values do not extend to a class of interests, such as common stock of an insolvent debtor, then the value of the interests is zero and the plan need not provide for the class. Secondly, the plan may provide any treatment for a class of interests as long as no junior interests receive any property under the plan or retain any interest in the debtor.

18. At first blush the second standard appears to permit every plan to eliminate ownership interests without risking denial of confirmation. However, eliminating ownership interests means the class of ownership interests is deemed to dissent, and the plan must be fair and equitable with respect to the dissenting class of stock in order to be confirmed. If the old stock has a positive reorganization value and the interests of former stockholders are to be eliminated under the plan, then by necessity some senior class is being provided for more than in full. In that event, the shareholders are not receiving fair and equitable treatment and the plan will not be confirmed.

COMMON FACTS FOR EXAMPLES

19. Perhaps the most useful method of understanding the operation of the fair and equitable rule in determining whether a plan of reorganization will be confirmed when a class of unsecured claims or interests dissects is to consider specific examples. Suppose an insolvent corporation has assets worth $2 million on a going concern basis and liabilities of $2.2 million. The liabilities side of its balance sheet could appear as follows:
Liabilities (in 000's)

Secured Debt $1,000
Unsecured Debt $1,200
Shareholders' Equity (200)

Example 1

The General Rule--A dissenting class of creditors must be entitled to receive the full amount of its claims if a junior class of creditors or owners receives reorganization values under the plan.

20. Suppose that the debtor proposes a plan that does not affect the secured debt and proposes to pay the unsecured creditor class $1 million cash in full satisfaction of its allowed claims of $1.2 million. Under the plan, stock in the corporation would be retained by the former shareholders whose legal rights are unaffected.

21. Will the plan be confirmed if the class of unsecured claims does not accept the plan by the requisite 2/3 in amount and majority in number? The plan will not be confirmed under the general confirmation standards because the class of unsecured claims is impaired and has not accepted the plan. The class is impaired because the plan is not paying the holders of unsecured claims the full amount of their claims ($1,200,000), even though the class is being paid the reorganization value of its claims ($1,000,000). Moreover, the plan likewise will not be confirmed over the objection of the unsecured class because the plan is not fair and equitable with respect to that dissenting class. The plan is not fair and equitable under 11 U.S.C. § 1129(b)(2)(B), because the class of unsecured claims is not receiving property equal to the full amount of its claims ($1,200,000) and a junior class (the former shareholders) is receiving or retaining property under the plan.

Example 2

A plan may compel a class of unsecured creditors to receive an extension of their claims and Yet allow a junior class to participate.

22. Assume the same facts as in Example 1, except that the class of unsecured claims of $1,200,000 is to be paid $1,500,000 without interest, in five equal annual installments of $300,000, commencing one year after the effective date of the plan. The plan will not be confirmed under the general confirmation standards because the class of unsecured claims has not accepted the plan and is impaired. The class is impaired under section 1124 because its members' legal rights are being altered and they are not being paid cash on the effective date of the plan equal to the allowed amount of their unsecured claims ($1,200,000).

23. Will the extension plan be confirmed not with standing the dissent of the class of unsecured claims? The plan will be confirmed, only if the plan is fair and equitable with respect to the
dissenting class of unsecured claims. In order for the plan to be fair and equitable with respect to that class, either members of the class must receive property equal to the allowed amount of their claims or no junior class may share in the plan. Since the former shareholders retain their equity interest in the corporation, the second criterion is not satisfied, and it would appear, at first blush, that the plan may not be confirmed. But if the deferred payments of $1,500,000 have a value as of the effective date of the plan equal to the allowed amount of the unsecured claims ($1,200,000), then the plan will satisfy the present value test of 11 U.S.C. § 1129(b)(2)(B)(i), will be fair and equitable with respect to the dissenting class of unsecured claims, and, therefore, will be confirmed. If the value of the deferred payments is less than $1,200,000, then the plan will not be fair and equitable and will fail of confirmation. The value of the deferred payments depends on the discount rate selected in computing present value, as more fully discussed in Example 6 below.

Example 3

If former stockholders' interests are eliminated, a valuation is required to make sure that classes of claims are not being provided for more than in full.

24. One of the reforms of the new Code is to permit creditors to file and confirm plans over the objection of owners in some circumstances. Suppose the unsecured creditors propose a plan that does not affect the $1,000,000 secured debt but eliminates the ownership interests of former shareholders by giving the stock of the corporation to the class of unsecured claims in full payment of the $1,200,000 unsecured debt. Also suppose that the class of unsecured claims accepts the plan by the requisite majorities in number and amount, but that the class of ownership interests does not. The class of equity interests is impaired and is deemed to have rejected the plan under 11 U.S.C. § 1126(g).

25. Will the plan to be confirmed notwithstanding the dissent of the class of ownership interests? The plan will be confirmed only if it is fair and equitable with respect to the ownership interests under 11 U.S.C. § 1129(b)(1) & § 1129(b)(2)(C). The plan is fair and equitable, because it is consistent with 11 U.S.C. § 1129(b)(2)(C), in that the former shareholders receive the value of their stock interests. Since the corporation is insolvent on a going concern basis, the value of the former equity interest is zero.

26. It is worth mentioning that the plan would likewise be confirmed even if the class of unsecured claims failed to accept the plan by the requisite majorities but, as proponent of the plan, nevertheless requested confirmation. This might occur when the plan is accepted by 60 percent in both number and amount of unsecured claims so that the requisite approval of 2 3 in amount is not obtained. The plan is fair and equitable as to the class of unsecured claims because no junior class, i.e., equity, is receiving any property under the plan and no senior class is being paid more than in full; since the secured debt is unaffected, it is unimpaired and is deemed to have accepted the plan.

Example 4

If former shareholders' interests are eliminated and a class of creditors is provided for more than
27. Consider the example of a solvent corporation with assets valued on a going-concern basis at $2 million and unsecured liabilities of $1,200,000, and no other liabilities. Suppose the debtor has cash-flow problems and files a reorganization plan to restructure the indebtedness of the corporation by issuing 100,000 new shares of stock to the unsecured debt in satisfaction of $200,000 debt with the residual $1,000,000 unsecured debt remaining as an obligation of the debtor. The former shareholders retain their old 100,000 shares of stock. The class of unsecured claims accepts the plan by the requisite majorities, but the class of former equity interests dissent.

28. The plan will not be confirmed under the general confirmation standards because the class of ownership interests has not accepted the plan and is impaired. The class is impaired because the issuance of equity securities under the plan has altered the interest of the former shareholders and modified their legal rights.

29. If the debtor requests the court to confirm the plan notwithstanding the dissent of the class of equity interests, the plan will be confirmed only if it is fair and equitable with respect to those interests. Again, at first blush the plan appears to be fair and equitable with respect to the ownership interests under 11 U.S.C. § 1129 (b) (2) (C) (ii) since no junior interest receives or retains any property under the plan. But the plan is not fair and equitable with respect to the equity class because the class of unsecured claims is being provided for more than in full. The shareholders' equity attributable to the new stock—$2 of the equity of the reorganized business—is worth $500,000 and, when the value of the stock is added to the unaffected debt of $1,000,000, the unsecured class receives more than 100% of its $1,200,000 claims. Value of equity in the reorganized debtor is computed by noting that the total equity interest in the reorganized entity is worth $1,000,000 (due to assets worth $2 million and liabilities of $1 million) and the unsecured debt is receiving 100,000 of a total 200,000 shares. Since the value of the reorganization stock will exceed $200,000, the plan will not be confirmed.

30. If the same number of shares were issued in satisfaction of $800,000 unsecured debt, with the residual unsecured debt of $400,000 remaining a liability of the reorganized debtor, then the plan would be fair and equitable. Assets of the reorganized business valued on a going-concern basis would remain at $2 million, and the resulting liabilities of the reorganized corporation would be as follows:

<table>
<thead>
<tr>
<th>Liabilities of Reorganized Debtor</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unsecured debt</td>
</tr>
<tr>
<td>Shareholder equity</td>
</tr>
<tr>
<td>after reorganization (200,000 total shares)</td>
</tr>
</tbody>
</table>

31. The 100,000 shares of stock worth $800,000 given to the class of unsecured claims would equal the debt satisfied ($800,000), with the result that the unsecured claims would not be paid more than in full. Since no class junior to the former equity interests receives or retains
any property under the plan, the relaxed fair-and-equitable requirement of 11 U.S.C. § 1129(b)(2)(C)(ii) is met. Moreover, the present value requirement of 11 U.S.C. § 1129(b)(2)(C)(i) is incidentally complied with, since the former shareholders have retained the reorganization value of their ownership interest.

IV. MODIFICATION OF THE RIGHTS OF A CLASS OF SECURED CLAIMS WITHOUT ITS CONSENT (CRAM DOWN)

32. Before embarking on a discussion of modification of the rights of a class of secured claims without its consent, it is necessary to examine the concept of the "allowed amount" of a secured claim in a reorganization case. As a matter of nomenclature, the Code refers to a "class" of claims, but in most instances, each secured claim will be a class by itself. Preliminary analysis is confined to "recourse" secured claims, i.e., to the extent the collateral is insufficient to pay the debt, the debtor is liable for the deficiency. Special rules applicable to non recourse secured claims are discussed in V infra.

33. The "allowed amount" of a claim or interest is not a static concept. In a reorganization case schedules of claims are filed by the debtor 103(105) or by the trustee 104(106). A proof of claim or interest is deemed filed for any claim or interest that is scheduled, unless it is scheduled as disputed, contingent, or unliquidated. 105(107) A claim or interest that is filed 106(108) or deemed filed is deemed allowed unless a party in interest 107(109) objects. 108(110) If an objection is made, then the claim is determined as of the date of the filing of the petitions 109(111) and allowed in the amount determined except to the extent that a specified ground 110(112) exists to disallow the claim. 111(113)

34. Allowed claims that are secured are subject to special treatment under the Code. If an allowed claim is oversecured, its treatment is simple—there is an allowed secured claim for the full amount of the debt. Since there is no deficiency in the collateral to secure the debt, no portion of the allowed claim is an allowed unsecured claim. If the claim is undersecured, a different result occurs. To the extent that an allowed claim is secured by a lien 112(114) or subject to setoff,113(115) it will be divided into an allowed secured claim and an allowed unsecured claim.114(116) The claim is an allowed secured claim to the extent of the value 115(117) of the collateral 116(118) and is an unsecured claim to any extent that the value of the collateral is less than the amount of the allowed claim.117(119) For example, an allowed claim of $1,000 secured by collateral worth $400 would give rise to an allowed secured claim of $400 and an allowed unsecured claim of $600.

35. Both the Code 118(120) and the legislative history 119(121) indicate that the determination of how much of the allowed claim is secured and how much is unsecured may occur at several different times during the case, depending on the purpose of the valuation and the method used for valuing the collateral.120(122) An initial valuation for one purpose, e.g., relief from the automatic stay, is not res judicata with respect to a valuation for a different purpose, e.g., confirmation.

36. The dynamic concept of separating allowed claims into allowed secured claims and allowed
unsecured claims is complicated to a greater extent in a reorganization case. If a class of allowed claims does nothing, section 506(a) will apply as in a liquidation case. But the class may elect application of special treatment under section 1111(b)(2). 121(123) Section 1111(b)(2) provides that each claim of an electing 122(124) class is a secured claim to the extent the claim is allowed; the secured claim is not limited to the value of the collateral as if no election is made. 123(125) This means that a creditor 124(126) who has an allowed claim secured by collateral less than the allowed amount of the claim may elect to treat the entire allowed claim as an allowed secured claim. The result of the election is to waive any unsecured claim for a deficiency. For example, suppose a $1,000 creditor is secured by collateral worth $400. If the secured creditor elects application of section 1111(b)(2), the creditor will hold an allowed secured claim of $1,000 and no unsecured claim for a deficiency.

37. Some classes of secured claims are ineligible 125(127) to elect application of section 1111(b)(2). If the lien securing the claims is worthless or of inconsequential value, then the class is ineligible to make the election. 126(128) An example of such a worthless lien would be a third lien on real estate when the real estate is valued at $1,000 and the first and second liens secure debts of $3,000. Likewise a class of claims is ineligible to make the election if the holders have recourse against the debtor and the collateral is sold. 127(129) The recourse creditor will be able to bid in its claim when the collateral is sold and may have an unsecured claim for any deficiency.

38. To recapitulate, in a reorganization case concerning an under secured creditor, an allowed secured claim will equal the value of the collateral, 128(130) unless the creditor elects application of section 1111(b)(2). 129(131) If section 1111(b)(2) is applicable, the allowed secured claim equals the total amount of the debt, 130(132) and there will be no allowed unsecured claim. 131(133) But if the section 1111(b)(2) election is not made, 132(134) there will be an allowed unsecured claim to the extent the collateral is less than the debt. 133(135)

39. The concept of an "allowed claim" is an integral part of the standard under which a plan may be confirmed. In particular, often it will be necessary to determine if a secured creditor is unimpaired by a plan. Under section 1124(3)(A), a class of claims is unimpaired if the plan makes cash payments equal to the "allowed amount" of the claims in the class. If a secured creditor elects application of section 1111(b)(2), then the allowed secured claim is equal to the full amount of the debt, and the secured creditor may be "cashed out" only if the debt is paid in full. On the other hand, if the secured creditor does not elect application of section 1111(b)(2), the secured claim is only equal to the value of the collateral and the secured creditor can be "cashed out" for the value of the collateral without regard to the total amount of the debt.

40. If a class of secured claims is impaired and does not accept the plan, the plan must be fair and equitable with respect to that class in order to be confirmed. In order for the plan to be fair and equitable with respect to a dissenting class of secured claims, the plan must, at a minimum, 134(136) satisfy one of three separate requirements. 135(137) First, the plan may provide for the holders of claims in the class to retain the lien 136(138) that secures their claims to the extent of the allowed amount 137(139) of their claims. 138(140) (If the class has not elected application of section 1111(b)(2), then the allowed amount is the amount of the
collateral; if an election is made then the allowed amount is the amount of the debt).
Additionally, the plan must provide for the class to receive deferred 139(141) cash payments
totaling at least the allowed amount of their claims (the "principal amount" test) and the
payments must have a present value;140(142) as of the effective date of the plan, generally
equal to the value 141(143) of the collateral (the "present value" test).142(144) Second, the
plan may propose to sell 143(145) collateral free and clear of the lien held by members of the
dissenting class as long as the class has a chance to bid in their claims and the lien attaches to
proceeds.144(146) The plan must also propose to treat the lien on proceeds under one of the
other 145(147) two prescribed methods.146(148) Third, the plan may propose that each
member of the dissenting class realize the "indubitable equivalent" of his allowed
secured claim.148(150) The legislative history states that abandonment of the collateral to the
class would satisfy this standard, as would a replacement lien on similar collateral.149(151)
But present cash payments to the class less150(152) than the amount of the allowed secured
claims would not satisfy the standard because the class will not benefit from a future increase
in the value of the collateral.151(153) Nor are unsecured notes or equity securities sufficient
to constitute the "indubitable equivalent" of secured claims.152(154)

41. The "cram-down" standards appear to be Simple, but the appearance is deceiving. The
following examples illustrate how the variation of minor aspects of a plan affects the analysis
of confirmation.

COMMON FACTS FOR EXAMPLES

42. Consider a solvent corporation with assets valued on a going-concern basis at $2 million,
including real estate worth $600,000. Assume a mortgage on the real estate of $1 million (all
currently due and owing) and unsecured trade debt of $100,000. Also assume that there are
100,000 shares of stock authorized and outstanding which have a value of $900,000, and that
the debtor proposes a plan that leaves trade debt and equity interests unaffected. Assume
further that the plan proposes to pay the secured creditor total of $600,000, without interest,
in four equal annual installments of $150,000 commencing one year after the effective date of
the plan. The mortgage will remain on the real estate to secure those payments.

Example 5

A secured creditor is entitled to deferred payments of a present value equal to his allowed
secured claim.

43. It is agreed that the $1 million debt is represented by two claims: a secured claim of $600,000
(the value of the real estate) and an unsecured claim in the amount of $400,000 (the amount
of the deficiency). Suppose the secured creditor does not elect application of section
1111(b)(2) and rejects the plan. Assume that all of the requirements of section 1129(a) are
met, other than paragraph (8). (Note that 11 U.S.C. § 1129(a)(10) is met due only to the fact
that the trade-debt class is deemed to have accepted the plan by reason of the fact that it is
unimpaired). The debtor requests the court to confirm the plan under section 1129(b).
44. Whether the plan will be confirmed depends on whether it is fair and equitable with respect to the secured creditor’s mortgage on the real estate. The secured creditor will receive four annual installments of $150,000 each. Since the total principal payments equals the allowed amount of the secured claim ($600,000), section 1129(b)(2)(A)(i)(II) is satisfied as to the principal-amount test. But since no interest is to be paid, the present value of the four payments will be less than $600,000 and the present value test is not met. The plan will not be confirmed because it is not fair and equitable under the first standard. The second standard does not apply because the collateral is not proposed to be sold. The third standard is inapplicable because failure of the plan to provide interest should also mean that the extended payments will not constitute the "indubitable equivalent" of the $600,000 claim. Since none of the required standards is met, the plan is not fair and equitable with respect to the class of secured claims and confirmation will fail.

Example 6

A secured creditor who elects to be treated as fully secured waives his deficiency claim.

45. Suppose that the class of secured claims elects application of 11 U.S.C. § 1111(b)(2), which means that the class of secured claims is $1,000,000 (the amount of the debt), rather than $600,000 (the value of the collateral). Assume that the plan proposes to pay the secured creditor a total of $1 million, without interest, in four equal annual installments of $250,000, commencing one year after the effective date of the plan, secured by the mortgage on real estate. Also assume that the secured creditor votes to reject the plan and the debtor requests confirmation under section 1129(b). Note that due to the election of application of section 1111(b)(2), there is no class of unsecured claims representing the deficiency.

46. Whether the plan will be confirmed depends on whether the plan is fair and equitable as to the secured creditor. Principal payments of $1 million equal the amount of the allowed secured claim, so section 1129(b)(2)(A)(II) is again complied with as to the principal-amount test. Whether the four installments have a present value greater than or equal to the value of the collateral ($600,000), so that the present-value test is met, depends on the discount rate.

47. The discount rate is equivalent to the rate of interest that would be paid on an obligation of the debtor. However, the discount rate is used to reduce money that will be paid in the future to a sum of money with a present value. If that sum earns interest at a rate equal to the discount rate, then the result in the future will equal the original amount of money before discounting.

48. In the example, if the court determines that the discount rate is 25% then the present value of the payments is only $590,500 and confirmation will fail. If a 20% factor is used, the value of the payments as of the effective date of the plan is $647,250 and the plan will be confirmed.
49. Note that with a 20% discount rate, if the class of equity ownership interests were to dissent, the plan would not be confirmed as the secured creditor would receive more than payment in full. For the balance of the examples a discount factor of 20% will be assumed, unless otherwise indicated.

**Example 7**

A secured creditor's collateral May be sold if the Proceeds are protected.

50. Assume that the plan proposes to sell the real estate for $600,000 free and clear of the secured party's lien under section 363(k) with the lien to attach to the proceeds of sale. The class of secured claims cannot elect application of 11 U.S.C. § 1111(b)(2), because the class is ineligible to do so once the plan proposes to sell 1(165)63(166) collateral.

51. Recall that in Example 5 confirmation failed when application of 11 U.S.C. 1111(b)(2) was not elected. Similarly, in this example the plan will not be confirmed if the secured creditor rejects the plan and the debtor requests confirmation under section 1129(b). Sale of the collateral does not change the result.

52. Under the Code the recourse creditor is entitled to a deficiency claim if the collateral is sold subject to section 363(k).164(167) Therefore, if the property is sold for $600,000, there is an allowed secured claim of $600,000 and an unsecured claim of $400,000. With the assumed discount rate of 20%, the present-value standard cannot be satisfied regardless of the apportionment of the $250,000 installments between the secured and unsecured class and the plan will not be confirmed. 165(168)

**V. NONRECRUENCE SECURED CLAIMS**

53. The Code provides special treatment for the holder of a secured claim not entitled to recourse against the debtor in the event the collateral is less than the debt. Recall that in a liquidation case under chapter 7, the holder of a non recourse claim has an allowed secured claim to the extent of the value of the collateral and no claim for any deficiency. 166(169) However, in a reorganization case under chapter 11, the claim is allowed under section 11111(b)167(170) as if the creditor has recourse, and the creditor is given an unsecured claim for the deficiency. The non recourse creditor loses the deficiency claim if the collateral is sold or the creditor elects to treat the entire allowed claim as secured under section 1111(b)(2).168(171)

54. The Code begins by stating that a claim secured by a lien on property of the estate generally is to be allowed 169(172) as if the holder of the claim had recourse against the debtor, even if the claim is non recourse (there is no legal recourse against the debtor for any deficiency by which the collateral is less than the debt).170(173) This means that as a general rule in a reorganization case both a recourse and a non recourse lender will have an allowed unsecured claim to the extent the value of the collateral is less than the allowed claim.171(174)
55. There are two exceptions to the general rule. First, recourse status for a non recourse lender is not available if the collateral securing the loan is sold. The reason for this exception is that the non recourse lender will have a chance at the sale to bid in the total amount of his claim against the purchase price. Second, there will be no deficiency claim if the class of which the Lender's secured claim is a part elects application of section 1111(b)(2) of the Code. However, in the event the class of which the non recourse lender is a member elects application of section 1111(b)(2), the non recourse lender probably has an allowed secured claim for the full amount of the debt owed.

56. Granting the nonrecourse lender an unsecured claim for a deficiency is a novel remedy. The approach differs from the provisions of the Bankruptcy Act which permitted the entire interest of the secured party to be bought out for the appraised value of the collateral. By offering the creditor the options described above, the Code tends to prevent a debtor from cashing out an undersecured non recourse secured creditor.

57. The standards for confirming a plan over the dig sent of a non recourse secured creditor contain the same language that applies to a recourse secured creditor. However, application of the language sometimes produces different results than for a recourse claim. The dynamics of the Code are best illustrated by examples.

COMMON FACTS FOR EXAMPLES

58. Consider a solvent corporation with assets valued on a going-concern basis at $2 million including, real estate worth $600,000. Assume a mortgage on the real estate of $1 million (all currently due and owing) and unsecured trade debt of $100,000. Also assume that there are 100,000 shares of stock authorized and outstanding which have a value of $900,000, and that the debtor proposes a plan that leaves trade debt and equity ownership interests unaffected.

Example 8

The non recourse creditor is entitled to the present value of both his secured and unsecured deficiency claims.

59. Assume further that the plan proposes to pay the secured creditor a total of $600,000, without interest, in four equal annual installments of $150,000 commencing one year after the effective date of the plan. The mortgage will remain on the real estate to secure those payments. It is agreed that the $1 million non recourse debt is represented by two claims: a secured claim of $600,000 (the value of the real estate) and an unsecured claim of $400,000 (the amount of the deficiency). The plan does not affect the deficiency claim. Suppose the secured creditor does not elect application of section 1111(b)(2) and rejects the plan. All of the requirements of section 1129(a) are met, other than paragraph (8). The debtor requests the court to confirm the plan under section 1129(b).
60. As in Example 5, supra, the plan will not be confirmed. Failure of the plan to provide an interest rate means that the present value of the four payments will be less than the amount of the secured claim even though the principal amount of the four payments equals the amount of the secured claim. 179(182)

Example 9

A non recourse creditor who elects to be treated as fully secured is entitled to payments of a present value equal to the value of the collateral.

61. Assume that the nonrecourse secured creditor elects application of section 1111(b)(2) and the plan proposes to leave the creditor’s lien undisturbed and to pay the secured creditor a total of $1 million, without interest, in four equal annual installments of $250,000 commencing one year after the effective date of the plan. As in Example 6, supra, the plan will be confirmed if the discount rate is 20 percent, so that the present value of the four $250,000 installments exceeds the value of the collateral ($600,000). 180(183) Continue to assume a discount rate of 20% for the balance of the examples.

Example 10

A nonrecourse creditor whose collateral is sold is protected as to the proceeds of sale.

62. Assume that the plan proposes to sell the real estate for $600,000 free and clear of the secured party's lien under section 363(k) with the lien to attach to the proceeds of sale. Also assume that the nonrecourse secured creditor does not elect application of section 1111(b)(2) and that the plan proposes to pay the secured creditor a total of $1 million, without interest, in four equal annual installments of $250,000 commencing one year after the effective date of the plan.

63. Recall that in Examples 5 and 7, supra, the plan was not confirmed when application of section 1111(b)(2) was not elected. However, in this example, if the debtor requests confirmation to be determined under section 1129(b), the plan will be confirmed.

64. Under the Code the non recourse creditor is not entitled to a deficiency claim if the collateral is sold subject to section 363(k). 181(184) Therefore, there is an allowed secured claim of $600,000 and no impaired class of unsecured claims. With the assumed discount rate of 20%, both the principal-amount and present-value standards 182(185) are satisfied and the plan will be confirmed. 183(186)

65. Note that unlike the recourse secured creditor in Example 7, supra, the non recourse secured creditor is eligible 184(187) to elect application of section 1111(b)(2) when the plan proposes to sell the collateral either subject to or free and clear of the secured party's lien under section 363(k). However, in this example, election of the application of section 1111(b)(2) will not
alter the result; presumably the collateral will be sold for $600,000 and the installment payments will be in a principal amount of $1 million with a present value of $647,500, so that the plan will be confirmed.185(188)

VI. PLANS ALTERING RIGHTS OF MULTIPLE CLASSES

66. Having analyzed the treatment of secured and unsecured claims and ownership interests in detail, it is now feasible to examine the application of the statute when more than one class of claims or interests is impaired under the plan.

COMMON FACTS FOR EXAMPLES

67. Consider an insolvent corporation with assets valued on a going-concern basis at $2 million, including real estate worth $600,000. Assume a nonrecourse mortgage on the real estate of $1 million (all currently due and owing) and unsecured trade debt of $1,200,000. Also assume that there are 100,000 shares of stock authorized and out-standing which are worthless (reflecting a negative shareholder equity of -$200,000). The debtor proposes a plan that will pay the nonrecourse secured creditor a total of $1 million, without interest, secured by a mortgage on the real estate, in four equal annual installments of $250,000 commencing one year after the effective date of the plan, with a present value of $600,000 as of the effective date of the plan.

Example 11

Confirmation fails if dissenting unsecured creditors are not provided for in full and ownership interests share.

68. Assume that the partially secured creditor does not select application of section 1111(b)(2). Also assume that the plan proposes to leave the equity interests unaffected and to pay the class of unsecured claims, which includes the trade debt and the nonrecourse creditor's deficiency claim, fifty cents on the dollar in full satisfaction of its claims. Further assume that the trade debt votes to accept the plan but the partially secured creditor does not.

69. Since section 1111(b)(2) does not apply, the plan is fair and equitable with respect to the dissenting class of allowed secured claims. The lien remains on the collateral and both the principal-amount and present-value requirements are satisfied.186(189)

70. The class of unsecured claims is comprised of trade debt with claims of $1,200,000 and the partially secured creditor with a deficiency claim of $400,000. If more than one creditor holds the trade debt the plan will be confirmed 187(190) because the class has accepted the plan by the requisite two-thirds in amount and majority in number of claims voted. 188(191) In the unlikely event that there is only one holder of the trade debt, the class of unsecured claims will not have accepted the plan because only half the voting holders of claims (the
holder of the trade debt) voted to accept the plan. Since the class is impaired and has not accepted the plan, the plan will be confirmed only if the plan is fair and equitable with respect to the dissenting class of unsecured claims. The plan is not fair and equitable because the dissenting class is provided for less than in full 189(192) and junior claims and interests will retain their rights against the debtor.190(193) (For future examples assume that more than one creditor holds the trade debt).

Example 12

For a Plan to be confirmed when stockholders are eliminated, creditors must not be Provided for more than in full.

71. Assume the same facts as in Example 11, except that instead of paying unsecured claims fifty cents on the dollar, the plan proposes to eliminate the interests of former shareholders by giving all stock in the debtor to the $1.6 million class of unsecured claims (the $1.2 million trade debt and $400,000 deficiency claim) in full satisfaction of their claims, and that the class 191(194) of unsecured claims votes to accept the plan by the requisite majorities. 192(195)

72. Will the plan be confirmed? As in Example it, one plan is fair and equitable as to the secured claim, because the principal-amount and present-value tests are satisfied. The plan does not need to be fair and equitable with respect to the class of unsecured claims because it has accepted the plan. However, since the former shareholders' interests are eliminated, they are deemed not to accept the plan.193(196) In order for the plan to be confirmed it must be fair and equitable with respect to this class of dissenting equity.194(197) Apparently, the plan should be confirmed with respect to the equity class since the value of the former equity interests is zero based on a going-concern valuation of the business. 195(198) But note that if the stock in the reorganized debtor is worth more than the $1,600,000 of unsecured claims, the plan is not fair and equitable with respect to the former shareholders and the plan will not be confirmed.196(199)

73. In order to determine the value of the stock in the reorganized debtor, a reorganization balance sheet is used. Of the $2 million in assets valued on a going-concern basis, nothing is being distributed on confirmation. This leaves assets worth $2 million and liabilities of $600,000 representing the installment payments due to the secured creditor. Thus, the equity held by the unsecured creditors is worth $1,400,000 and the plan will be confirmed.

VII. PLANS AFFECTING SUBORDINATED DEBT.

74. Occasionally, a debtor will have two classes of debt resulting from a subordination agreement where some unsecured creditors contract to subordinate their claims to all other unsecured claims. This complicates application of the fair and equitable rule by creating a class of senior unsecured debt and a class of junior unsecured debt. If the junior debt agrees to subordinate its claims to certain unsecured claims only, then there are three kinds of unsecured creditors—a kind that is senior and a kind that is junior under the subordination
agreement and a third kind that is not a party to the subordination agreement. For example, junior debentures may be subordinated to senior debentures and there may also be trade debt which is unaffected by the subordination agreement. Although it is not clear, it may be possible for a debtor to place senior debt, junior debt, and trade debt in separate classes under a reorganization plan. If so, application of the fair and equitable rule is very complex.

COMMON FACTS FOR EXAMPLES

75. Consider an insolvent corporation with assets valued on a going-concern basis at $2 million, including real estate worth $600,000. Assume a nonrecourse mortgage on the real estate of $1 million (all currently due and owing) and unsecured trade debt of $200,000. Also assume, that senior debenture holders hold 800 debentures (face amount $1,000 each) that will mature in 5 years. Junior debenture holders hold 200 subordinated debentures (face amount $1,000 each) that will mature in 3 years. There are 100,000 shares of stock authorized and outstanding which are worthless (reflecting a negative shareholder equity of -$200,000). The debtor proposes a plan that will pay the non recourse secured creditor a total of $1 million, without interest, secured by a mortgage on the real estate, in four equal annual installments of $250,000, commencing one year after the effective date of the plan, with a present value of $600,000 as of the effective date of the plan.

Example 13

The plan must not discriminate unfairly between classes of unsecured debt.

76. Assume that the plan proposes to pay the class of unsecured claims, which includes senior debt and unsecured deficiency claim, ninety cents on the dollar and to leave the subordinated debt unaffected. Assume further that the debtor proposes a plan to eliminate the equity interests of the former shareholders and to give the trade debt 100% of the stock in the reorganized debtor, and that the class of trade debt votes to reject the plan, but all other classes of creditors vote to accept the plan.

77. Will the plan be confirmed? Since the trade debt is impaired and has not accepted the plan, in order for the plan to be confirmed it must be fair and equitable with respect to the trade debt. If the value of the stock in the reorganized debtor were to equal the allowed amount of the trade debt ($200,000), then the plan would be fair and equitable with respect to the trade debt; however, whatever the value of the stock, since no junior class receives any property, the plan is fair and equitable with respect to the trade debt. But in order to be confirmed, the plan must also not discriminate unfairly against the trade debt.

78. As a class, the trade debt is entitled to share on an equal basis with the senior debentures and subordinated debentures. Holders of the senior debentures are being paid ninety cents on the dollar and the holders of the subordinated debentures retain their claims against the reorganized debtor. Since the value of the stock ($120,000) in the reorganized debtor is less than ninety percent of the trade debt ($180,000), the trade debt is being unfairly discriminated against and the plan will not be confirmed. The value of the stock is computed by noting that
of the $2 million in assets $1,080,000 is being paid on confirmation to the $1.2 million class of unsecured claims. This leaves assets of $920,000 and liabilities of $800,000 (the $600,000 secured debt and the $200,000 subordinated debt) which means the stock is worth $120,000. It should be noted that the same result will occur even if the stock were worth $180,000, the plan would not be fair and equitable as to the trade debt. The plan is not fair and equitable as to that class because the claims of the subordinated debenture holders remain obligations of the reorganized debtor. The trade debt is entitled to have $40,000 (20% of $200,000) of its debt remain unaffected since 20% of the senior and junior debentures as a whole remain unaffected.

Example 14

A class of subordinated debt may be eliminated as long as senior debt, trade debt, and the deficiency claim of a non recourse lender are treated fairly.

79. As a final example, assume that the subordinate debentures and the interests of former stockholders are eliminated, and that the stock in the reorganized debtor is allocated 62.5% to the senior debentures, 12.5% to the trade debt, and 25% to the deficiency claim of the mortgagee. Also assume that the senior debentures, trade debt, and mortgagee deficiency claim are all in different classes and that the trade debt and mortgagee deficiency claim are to be paid fifty cents on the dollar, while the senior debentures are paid 62.5 cents on the dollar in cash on the effective date of the plan. The secured claim is to be paid in four annual installments of $250,000 commencing one year after the effective date of the plan, with a present value of $600,000 as of the effective date of the plan, and the payments are secured by a lien on the real estate. The class of the secured claim, the class of the unsecured $400,000 deficiency claim, and the class of trade debt all vote to reject the plan. The senior debentures vote to accept the plan. The debtor requests the court to confirm the plan under section 1129(b) notwithstanding the three dissenting classes.

80. The now familiar analysis is straight forward. The plan is fair and equitable with respect to the dissenting class of the secured claim because the lien remains on the collateral and the principal-amount and present-value tests are complied with.201(204) The plan is fair and equitable with respect to the class of dissenting trade debt because no junior class receives or retains property under the plan.202(205) The plan does not discriminate unfairly against the trade debt because, of the $1.6 million in unsecured claims of which the $200,000 trade debt is a part, the trade debt receives 12.5% of the value of the property distributed, i.e., $100,000 and 12.5% of the stock.203(206) The plan is fair and equitable with respect to the dissenting class comprised of the $400,000 deficiency claim because no junior class receives or retains any property under the plan.204(207) The plan does not discriminate unfairly against such class because of the $1.6 million total unsecured debt, the class receives 25% of the value of property distributed under the plan, i.e., $200,000 and 25% of the stock.205(208)

81. Since both the class of subordinated debentures and the former shareholders are eliminated, they are deemed not to accept the plan 206(209) and confirmation requires that the plan be fair and equitable with respect to them. The plan is fair and equitable with respect to the class of subordinated debentures since no junior class receives or retains any property 207(210) and the same is true for the class of equity interests.208(211) However, the plan will not be
fair and equitable if any senior class is paid more than in full and that depends on the value of the stock in the reorganized debtor. It is obvious that if the stock is worth more than $800,000, the plan is not fair and equitable as to both the subordinated debentures and the former equity because both the trade debt and deficiency claim are being paid more than in full. But note that if the stock is worth exactly $800,000 then the senior debt is being paid $1 million on a debt of $800,000 and the plan is not fair and equitable. If, however, the stock is worth $480,000 or less, the fair and equitable test is met. Moreover, with a stock value of $480,000 or less, the plan does not discriminate unfairly because the senior debentures are entitled to be paid in full before the subordinated debentures may participate and neither the trade debt nor the deficiency claim are receiving more than their pro-rata share. Thus, assuming all of the other requirements for confirmation are met, 209(212) the plan must be confirmed when the stock in the reorganized debtor is not worth more than $480,000.

82. In order to determine the value of the stock in the reorganized debtor, a reorganization balance sheet is used. Of the $2 million in assets valued on a going-concern basis, $800,000 is being paid under the plan in cash on confirmation. Senior debt receives $500,000, trade debt receives $100,000, and the mortgagee receives $200,000 on account of the deficiency claim. The only remaining liability of the reorganized debtor is the $600,000 debt to the mortgagee secured by a lien on the real estate. This leaves a shareholders' equity of $600,000 for the new shareholders.

83. Accordingly the senior debenture holders receive stock (62.5%) worth $375,000 in addition to $500,000 in cash on confirmation for a total of $875,000 on a debt of $800,000. Thus the plan discriminates unfairly against the subordinated debentures and is not fair and equitable as to the former shareholders. In order to obtain confirmation, the debtor would need to modify the plan to allocate 50% of the stock ($300,000) to the senior debentures and 12.5% of the stock to the subordinated debentures. Such a plan would not unfairly discriminate against the trade debt, since the total consideration received by that class ($175,000) is proportionate with that received by the senior and subordinated debentures ($875,000). The modified plan would be confirmed because it is fair and equitable as to the former equity interests, since no senior class is being paid more than in full.

VIII. CONCLUSION

84. The foregoing discussion examines many of the complexities of the cram-down power under the new Code. Some possibilities, such as a sale of part of a secured party's collateral, were not examined, because the Code provides no clear answer and the variations are innumerable. Nevertheless, the complexity of cram down should encourage the debtor to bargain with creditors to gain acceptance of a plan in the vast majority of cases. In the event a court is required to apply the cram-down test, the above examples may be of assistance.
Endnotes

1 (Popup)

* The author, formerly associate counsel to the House Judiciary Committee and one of the principal draftsmen of the new Code, practices bankruptcy law in Los Angeles with Shutan & Trost Professional Corporation. The author encourages lay readers to peruse the text and ignore the footnotes.

2 (Popup)


3 (Popup)

2. Under the Code, the term "reorganization" encompasses every kind of case that may be filed under chapter X, XI, or XII of the Bankruptcy Act, as well as railroad reorganizations.

4 (Popup)


5 (Popup)


6 (Popup)

5. A plan of reorganization under chapter 11 of the Code may affect any combination of secured or unsecured claims or equity securities as well as other ownership interests. 11 § U.S.C. 1123(b)(1). This article does not treat with cram down under a chapter 13 plan adjusting debts of individuals with regular income.

7 (Popup)

§ 1129. Confirmation of Plan

(a) The court shall confirm a plan only if all of the following requirements are met:

(1) The plan complies with the applicable provisions of this chapter.
(2) The proponent of the plan complies with the applicable provisions of this chapter.

(3) The plan has been proposed in good faith and not by any means forbidden by law.

(4)(A) Any payment made or promised by the proponent, by the debtor, or by a Person issuing Be aunties or acquiring property under the plan, for services or for costs and expenses in, or in connection with, the case, or in connection with the plan and incident to the case, has been disclosed to the court; and

(B) (i) any such payment made before confirmation of the plan is reasonable; or

(ii) if such payment is to be fixed after confirmation of the plan, such payment is subject to the approval of the court as reasonable.

(5)(A) (i) The proponent of the plan has disclosed the identity and affiliations of any individual proposed to serve, after confirmation of the plan, as a director, officer, or voting trustee of the debtor, an affiliate of the debtor participating in a joint plan with the debtor, or a successor to the debtor under the plan; and

(ii) the appointment to, or continuance in, such office of such individual, is consistent with the interests of creditors and equity security holders and with public policy.

(B) The proponent of the plan has disclosed the identity of any insider that will be employed or retained by the reorganized debtor, and the nature of any compensation for such insider.

(6) Any regulatory commission with jurisdiction, after confirmation of the plan, over the rates of the debtor has approved any rate change provided for in the plan, or such rate change is expressly conditioned on such approval.

(7) With respect to each class-

(A) each holder of a claim or interest of such class -

(i) has accepted the plan; or

(ii) will receive or retain under the plan an account of such claim or interest property of a value, as of the effective date of the plan, that is not less than the amount that such holder would so receive or retain if the debtor were liquidated under chapter 7 of this title on such date; or

(B) if section 1111(b)(2) of this title applies to the claims of such class, each holder of a claim of such class will receive or retain under the plan on account of such claim property of a value, as of the effective date of the
plan, that is not less than the value of such creditor's interest in the estate's interest in the property that be cures such claims.

8 (Popup)
continued from 6

(8) with respect to each class-

(A) such class has accepted the plan; or

(B) such class is not impaired under the plan.

(9) Except to the extent that the holder of a particular claim has agreed to a different treatment of such claim, the plan provides that-

(A) with respect to a claim of a kind specified in section 507(a)(1) or 507(a)(2) of this title, on the effective date of the plan, the holder of such claim will receive on account of such claim cash equal to the allowed amount of such claim;

(B) with respect to a class of claims of a kind specified in section 507(a)(3), 507(a)(4), or 507(a)(5) of this title, each holder of a claim of such class will receive-

(i) if such class has accepted the plan, deferred cash payments of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or

(ii) if such class has not accepted the plan, cash on the effective date of the plan equal to the allowed amount of such claim; and

(C) with respect to a claim of a kind specified in section 507(a)(6) of this title, the holder of such claim will receive on account of such claim deferred cash payments, over a period not exceeding six years after date of assessment of such claim, of a value, as of the effective date of the plan, equal to the allowed amount of such claim.

(10) At least one class of claims has accepted the plan, determined without including any acceptance of the plan by any insider holding a claim of such class.

(11) Confirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan, unless such liquidation or reorganization is proposed in the plan.

9 (Popup)

7. A class of claims has accepted the plan if eligible creditors holding at least two-thirds in
amount and more than one-half in number of those claims of the class that are voted, vote to accept the plan. 11 U.S.C. § 1126(c). A class of interests has accepted the plan if eligible interest holders, holding at least two-thirds in amount of the allowed interests that are voted, vote to accept the plan. 11 U.S.C. § 1126(d). Moreover, a class of claims or interests that is not impaired under 11 U.S.C. § 1124 is deemed to have accepted the plan. 11 U.S.C. § 1126(f). For convenience, if a class of claims or interests has not accepted the plan for any reason, it may be said to have "dissented." If a plan provided for no property to be received or retained by a class of claims or interests, then the class is deemed not to have accepted the plan. 11 U.S.C. § 1126(g).

10 (Popup)
8. Although acceptances under 11 U.S.C. § 1126 are voted by creditors or holders of interests, the ultimate inquiry is whether a class of claims or interests has accepted the plan. See 11 U.S.C. § 1129(a)(8)(A).

11 (Popup)

12 (Popup)

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17 (Popup)

17. The term "insider" is defined in 11 U.S.C. § 101(25) in a very broad sense.


20. 11 U.S.C. § 1129(a)(7)(A)(ii). The statute permits a class to agree unanimously to accept less than liquidation value. In addition, a special provision applies to classes which have elected application of 11 U.S.C. § 1111(b)(2), note 167 infra. 11 U.S.C. § 1129(b)(7)(B). Since those creditors elect to treat an undersecured claim as fully secured and to waive their deficiency claims, they have agreed to receive less than they would receive in many liquidation cases.


24. The "effective date" of the plan is not a defined term but usually would be the first day after which the order of confirmation becomes final.

28 (Popup)

29 (Popup)

30 (Popup)

31 (Popup)

32 (Popup)
30. See note 140 infra.

33 (Popup)

34 (Popup)

35 (Popup)

36 (Popup)
34. See note 17 supra.

37 (Popup)
38 (Popup)

39 (Popup)

40 (Popup)
38. See note 6 supra.

41 (Popup)
39. A class of interests might comprise equity securities, partnership interests, or proprietorship interests.

42 (Popup)
40. Whether the "request" will be by complaint, motion, or application will be determined by the Rules of Bankruptcy Procedure. See H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 304 (1977) [hereinafter cited to as "House Report"].

43 (Popup)
41. A class that is not impaired within the meaning of 11 U.S.C. § 1124 is deemed to have accepted the plan under 11 U.S.C. § 1126(f). Thus any class that has not accepted the plan must be "impaired" by definition. To this extent the references to impairment in 11 U.S.C. § 1129(a)(8)(B) & 1129(b)(1) are superfluous.

44 (Popup)
42. 11 U.S.C. § 1129(b)(1).

45 (Popup)
43. Section 1129(b) of title 11 specifies the conditions. See notes 65, 84, 96 & 135 infra.

46 (Popup)
44. The Code states that the court "shall" confirm the plan if certain conditions are met. 11 U.S.C. § 1129(b)(1). See note 65 infra.

47 (Popup)
46. The Code does not use the word "vote," but that is the most convenient word to refer to acceptances which will be "filed" under the Rules of Bankruptcy Procedure.

See House Report, note 40 supra, at 304. cf. Pub. L. No. 95-598, 405(d) and Chapter XI Rule 11-37 (filing of acceptances required under current rules, which will continue in effect to the extent not inconsistent with the Code until repealed or superseded by new rules).

49 (Popup)
47. 11 U.S.C. § 1126(f).

50 (Popup)
48. 11 U.S.C. § 1124. An exception is provided to permit a given holder of a claim or interest to agree to a less favorable treatment of his claim or interest in accordance with 11 U.S.C. § 1123(a)(4).

51 (Popup)
49. 11 U.S.C. § 1124(1).

52 (Popup)
50. A default under a forfeiture clause, such as an ipso facto clause or bankruptcy clause specified in 11 U.S.C. § 365(b)(2), need not be cured. 11 U.S.C. § 1124(2)(A). House Report, note 40 supra, at 408. A postpetition default may also be cured. Id.

53 (Popup)
51. 11 U.S.C. § 1124(2).

54 (Popup)
52. 11 U.S.C. § 1124(2)(B). The reinstatement is effective "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." 11 U.S.C. § 1124(2).
55 (Popup)
53. 11 U.S.C. § 1124(2)(C). See note 52 supra for a description of an "acceleration clause". As the law concerning the treatment of acceleration clauses in reorganization cases becomes known, it is doubtful whether a creditor's reliance on acceleration clause would ever be reasonable if reorganization of the debtor were a foreseeable possibility. The legislative history indicates that damages are limited to those incurred by the holder and not by a third party. 124 Cong. Rec. H 11,103 (daily ed. Sept. 28, 1978) (remarks of Rep. Don Edwards) [hereinafter cited to as "House Record"]; 124 Cong. Rec. S 17,420 (daily ed. Oct. 6, 1978) (remarks of Sen. DeConcini) [hereinafter cited to as "Senate Record"].

56 (Popup)

57 (Popup)
55. The plan must pay the allowed amount of the claim rather than the reorganization value or market value. For example, the holder of a debenture with a face amount of $1,000 and a market value of $200 must be paid $1,000 in cash on the effective date of the plan in order to be unimpaired. This is true even if the class of debentures is "underwater", i.e., the debentures are worthless under the traditional fair and equitable rule because reorganization values do not reach that far down the line of priority.

58 (Popup)
56 11 U.S.C. § 1124(3)(A)

59 (Popup)
57. Many interests, e.g., common stock or interests in a partnership, will have neither a fixed liquidation nor a fixed redemption price in which case 11 U.S.C. § 1124(3)(B) is inapplicable.

60 (Popup)

61 (Popup)

62 (Popup)
60. 11 U.S.C. § 1124(3)(B).
63 (Popup)
61. The allowed claim or interest will be less than the debt owed if the claim or interest is disallowed in whole or in part, such as for unconscionability or usury, under 11 U.S.C. § 502(b). Additionally, if a class of claims is secured, the amount of the allowed secured claims will be less than the amount of the debt if the value of the collateral is less than the amount of the debt unless an election is made under 11 U.S.C. § 1111(b)(2). See note 167 infra.

64 (Popup)
62. A dissenting class has not voted to accept the plan and is impaired. See note 7 supra.

65 (Popup)
63. See note 40 supra.

66 (Popup)
64. The court is not permitted to rewrite the terms of the plan. If the plan discriminates unfairly or is not fair and equitable with respect to a dissenting class, then the plan will not be confirmed. The only recourse of the plan's proponent is to modify the plan under 11 U.S.C. § 1127(a). See House Report, note 40 supra, at 414.

67 (Popup)
65. 11 U.S.C § 1129(b)(1) provides as follows:

§ 1129. Confirmation of plan

* * *

(b)(1) Notwithstanding section 510(a) of this title, if all of the applicable requirements of subsection (a) of this section other than paragraph (8) are met with respect to a plan, the court, on request of the proponent of the plan, shall confirm the plan not with standing the requirements of such paragraph if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan.

This is known as "cram down" because the plan is forced on a dissenting class. House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 17,420.

68 (Popup)
65. 11 U.S.C § 1129(b)(1) provides as follows:

§ 1129. Confirmation of plan
(b)(1) Notwithstanding section 510(a) of this title, if all of the applicable requirements of subsection (a) of this section other than paragraph (8) are met with respect to a plan, the court, on request of the proponent of the plan, shall confirm the plan notwithstanding the requirements of such paragraph if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interest that is impaired under, and has not accepted, the plan.

This is known as "cram down" because the plan is forced on a dissenting class. House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 17,420.

69 (Popup)
66. See note 7 supra.

70 (Popup)
67. In determining whether the plan does not discriminate unfairly and is fair and equitable with respect to a particular dissenting class, often it will be necessary to evaluate the treatment of other classes under the plan. However, neither standard will apply directly with respect to other classes unless they too have dissented. This represents a sharp departure from the traditional interpretation of the fair and equitable test under 77 and chapters IX and X of the Bankruptcy Act which applies the absolute priority rule to the plan as a whole, i.e., to every class. House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 17,420.

71 (Popup)
68. House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 17,420.

72 (Popup)
69. In many cases some or all of the creditors of a business will enter into an agreement to subordinate their claims to the claims of a creditor supplying new money to the business. The subordination agreement binds existing creditors who consent to subordinate but will not affect future creditors who do not agree to be bound by it. It is not unusual for one group of unsecured creditors ("junior debt") to be subordinated to another group of unsecured creditors ("senior debt") but for both groups to be on a par with the remaining unsecured creditors ("trade debt"). Whether any particular group is senior or junior to another group for purposes of determining priority under a plan depends on the perspective from which the issue is viewed. Thus, for example, the senior debt is senior to the junior debt but equal to trade debt; the trade debt is equal with both the senior and junior debt; and the junior debt is junior to the senior debt but equal to the trade debt. This is what is meant by relative priority. See House Report, note 40 supra, at 416-17. See Examples 13 & 14 infra.
As a general proposition a subordination agreement is enforceable in a reorganization case to the same extent it is enforceable under non-bankruptcy law. 11 U.S.C. § 510(a). However the confirmation standard of 11 U.S.C. § 1129(b)(1) applies "notwithstanding section 510(a)." This means that to the extent a class of senior claims chooses not to enforce the subordination agreement, the minority in the class will be bound notwithstanding section 510(a). On the other hand, if the senior class insists on its rights by dissenting to the plan, then the subordination agreement will be enforced through the fair and equitable test. The additional requirement that the plan does not discriminate unfairly protects the senior class, the subordinated class, and classes not involved in the subordination agreement from being treated unfairly. See note 69 supra. See also House Report, note 40 supra, at 416-17.

The Code contains a rule of construction that "includes" is not limiting. 11 U.S.C. § 102(3). This implies that the use of the term "includes" is intentionally open ended.

House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 17,420.

House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 17,420.


This was omitted from the Code as a matter of style and not substance. House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 17,420.

78. 11 U.S.C § 1129(b)(2)(B), note 84 infra.

83 (Popup)
79. 11 U.S.C § 1129(b)(2)(C), note 96 infra.

84 (Popup)
80. As described in the legislative history, the relaxed standard differs from the traditional absolute priority rule by permitting senior classes that accept the plan "to give up value to junior classes as long as no dissenting intervening class receives less than the amount of its claims in full." House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 17,420.

85 (Popup)

86 (Popup)
82. 11 U.S.C § 1129(b)(2)(A), note 135 infra.

87 (Popup)
83. Under present law a plan may be confirmed over the dissent of a secured creditor as long as the creditor is given "adequate protection", which includes an appraisal of the collateral and payment in cash of the appraised amount. See § 216(7)(c) & 461(11)(c) of the Bankruptcy Act, 11 U.S.C. §§ 616(7)(c) & 861(11)(c) (1976). See also In re Pine Gate Assoc., 2 Bankr. Ct. Dec. 1478 (N.D. Ga. 1976).

88 (Popup)
84. 11 U.S.C § 1129(b)(2)(B) provides as follows:

§ 1129 Confirmation of Plan

* * *

(b)(2) For the purpose of this subsection, the condition that a plan be fair and equitable with respect to a class includes the following requirements:

(B) With respect to a class of unsecured claims:

(i) the plan provides that each holder of a claim of such class receive or retain on account of such claim property of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or

(ii) the holder of any claim or interest that is junior to the claims of such class will not receive or retain on account of such junior claim or interest
any property.

89 (Popup)
85. The concept of "property" is very broad and includes securities. House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 14,721.

90 (Popup)
86. See note 140 infra. The present value is determined as of the effective date of the plan.

91 (Popup)
87. There need only be a reasonable likelihood that the present value of the property equal the allowed amount of the unsecured claims. House Record, note 53 supra, at H 11,104-H 11,105; Senate Record, note 53 supra, at S 17,421.

92 (Popup)
88. The allowed amount of an unsecured claim will vary in the case of a partially secured creditor depending on the option selected by the creditor under 11 U.S.C § 1111(b), note 167 infra. See text accompanying note 124 infra.

93 (Popup)
89. 11 U.S.C § 1129(b)(2)(B)(i), note 84 supra.

94 (Popup)
90. The concept of a "junior" claim or interest is not trivial. See note 69 supra.

95 (Popup)
91. 11 U.S.C § 1129(b)(2)(B)(ii), note 84 supra. But see note 93 infra.

96 (Popup)
92. See House Record, note 53 supra, at H 11,105; Senate Record, note 53 supra, at S 14,721. An "intermediate class" is a class with lower priority than the senior class giving up value but whose priority is not below the junior class receiving value under the plan.

97 (Popup)
93. The dissenting class has a right to prevent senior classes from being compensated more than in full and to prevent equal classes from receiving preferential treatment. House Record, note 53 supra, at H 11,105; Senate Record, note 53 supra at S 17,421.

98 (Popup)
94. 11 U.S.C § 1129(b)(1), note 65 supra.
95.  *House Record*, note 53 supra, at H 11,105; *Senate Record*, note 53 *supra*, at S 17,421. See note 92 supra.

100 (Popup)
96.11 U.S.C § 1129(b)(2)(C) provides as follows:

§ 1129 Confirmation of Plan

*  *  *

(b)(2) For the purpose of this subsection, the condition that a plan be fair and equitable with respect to a class includes the following requirements:  *  *  *

(C) With respect to a class of interests--

(i) the plan provides that each holder of an interest of such class receive or retain on account of such claim (sic) property of a value, as of the effective date of the plan, equal to the greatest of the allowed amount of any fixed liquidation preference to which such holder is entitled, any fixed redemption price to which such holder is entitled, and the value of such interest; or

(ii) the holder of any interest that is junior to the interests of such class will not receive or retain under the plan on account of such junior interest any property

101 (Popup)

102 (Popup)
98.  The value of an "interest", whether a stock interest, a partnership interest, or a proprietorship interest, necessarily varies with the fortune of the business.

103 (Popup)
99.  If a plan proposes to eliminate the interests of stockholders, the class is deemed not to accept the plan under 11 U.S.C § 1126(g). The result is that the plan cannot be confirmed under 11 U.S.C § 1129(a) because the class is impaired and has not consented. If the proponent requests confirmation under 11 U.S.C. 1129(b), then a full goingconcern valuation is required to determine the value of the interests of the former stockholders.

104 (Popup)
100.  The class may receive nothing, but the plan must otherwise be fair and equitable and not discriminate unfairly with respect to the class. See note 93 supra.

105 (Popup)
101.  11 U.S.C § 1129(b)(2)(C)(ii), note 96 *supra*. 
106 (Popup)
102. House Record, note 53 supra, at H 11,105; Senate Record, note 53 supra, at S 17,421.

107 (Popup)
103. 11 U.S.C § 521(1).

108 (Popup)
104. 11 U.S.C § 1106(a)(2).

109 (Popup)
105. 11 U.S.C § 1111(a).

110 (Popup)
106. Any creditor, indenture trustee, or equity security holder, including one who holds a claim or interest listed as disputed, contingent, or unliquidated, may file a proof of claim or interest under 11 U.S.C. § 501(a).

111 (Popup)
107. The Code specifies that a party in interest includes a creditor of a partner when the partnership to which the partner belongs is a debtor in a liquidation case under chapter 7.

112 (Popup)
108. 11 U.S.C § 502(a).

113 (Popup)
109. Certain post petition claims are determined when they arise but are then given treatment as if they were unsecured prepetition claims. 11 U.S.C. § 502(f), (g), (h) & (i).

114 (Popup)
110. Nine grounds for disallowing a claim are specified in 11 U.S.C. § 502(b)(1)-(9). For example, under 11 U.S.C. § 502(b)(1) a claim is disallowed to the extent it is unenforceable against the debtor and property of the debtor under any agreement or law, e.g., claims for deficiency on non recourse loans, claims that are usurious, and claims that are unconscionable.

115 (Popup)
111. 11 U.S.C § 502(b).

116 (Popup)
112. 11 U.S.C § 101(28) defines "lien". The Code requires the lien to encumber "property
in which the estate has an interest".

117 (Popup)

118 (Popup)

119 (Popup)
115. The method of valuation is to be "determined in light of the purpose of the valuation and of the proposed disposition or use" of the collateral. Id.

120 (Popup)
116. In lieu of "collateral" the Code refers to the "creditor's interest in the estate's interest in such property". Id. In the case of a claim subject to setoff, the claim is a secured claim to the extent of the amount subject to setoff. Id.

121 (Popup)
117. Id. If the claim is non recourse and a proper objection is made, it will be allowed only to the extent of the value of the collateral under 11 U.S.C. § 502(b)(1). House Record, note 53 supra, at H 11,093-H 11,094; Senate Record, note 53 supra, at S 17,410. Thus the allowed claim will not exceed the value of the collateral and no allowed unsecured claim will be created under 11 U.S.C. § 506(a). But see note 167 infra.

122 (Popup)

123 (Popup)
119. House Record, note 53 supra, at H 11,095; Senate Record, note 53 supra, at S 17,411.

124 (Popup)

125 (Popup)
121. 11 U.S.C. § 1111(b)(2) [hereinafter cited as "section 1111(b)(2)"], note 167 infra.

126 (Popup)
122. Section 1111(b)(1)(A)(i) of title 11 specifies the standards for an election to be made. See note 167 infra.
127 (Popup)

128 (Popup)
124. Technically it is the class of secured claims of which the creditor's claim is a part that makes the election. Unless there are multiple liens of equal priority on the same collateral, as in the case of a secured debenture issue, each secured claim will be in a class by itself. See 11 U.S.C. § 1122(a).

129 (Popup)

130 (Popup)

131 (Popup)
127. 11 U.S.C. § 1111(b)(1)(B)(ii). The collateral will be sold under 11 U.S.C. 363(k) or under the plan. In either event the recourse lender has a right to bid at the sale and to offset his full allowed claim against the purchase price. See 11 U.S.C. § 1129(b)(2)(A)(ii). The fact that a nonrecourse lender is eligible to make the election in similar circumstances is not as troublesome as it appears. If the collateral is sold, the allowed claim that becomes an allowed secured claim is equal to the value of the collateral rather than the debt and the election is of no consequence. 11 U.S.C. §§ 502(b)(1) & 1111(b)(1)(A)(ii).

132 (Popup)

133 (Popup)

134 (Popup)
130. The allowed secured claim will not equal the total amount of the debt when the allowed claim is less than the amount of the full debt. See note 61 supra.

135 (Popup)
131. There is no unsecured claim because the entire allowed claim is a secured claim. 11 U.S.C. § 1111(b)(2).

136 (Popup)

137 (Popup)

138 (Popup)
134. The requirements of 11 U.S.C. § 1129(b)(2)(A) are necessary, but not always sufficient, to satisfy the fair and equitable test. See note 72 supra.

139 (Popup)
135. 11 U.S.C. § 1129(b)(2)(A), provides as follows:

§ 1129 Confirmation of Plan
*   *   *

(b)(2) For the purpose of this subsection, the condition that a plan be fair and equitable with respect to a class includes the following requirements:

(A) with respect to a class of secured claims, the plan provides—(i)(I) that the holders of such claims retain the lien securing such claims, whether the property subject to such lien is retained by the debtor or transferred to another entity, to the extent of the allowed amount of such claims; and

(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;

(ii) for the sale, subject to section 363(k) of this title of any property that subject to the lien securing such claims, free and clear of such lien, with such lien to attach to the proceeds of such sale, and the treatment of such lien on proceeds under clause (i) or (iii) of this subparagraph; or

(iii) for the realization by such holders of the indubitable equivalent of such claims.

140 (Popup)
136. Under 11 U.S.C. § 1129(b)(2)(A)(i)(I) the lien must be retained whether the collateral is retained by the debtor or a successor to the debtor or is sold subject to the lien. If the collateral is sold free and clear of the lien, then 11 U.S.C. § 1129(b)(2)(A)(ii) is the controlling provision.
141 (Popup)
137. The "allowed amount" of a claim is not a static concept. See text accompanying note 120 supra.

142 (Popup)

143 (Popup)
139. The legislative history states that presentor deferred payments are permissible. House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at § 17,421.

144 (Popup)
140. The provision that value is measured as of the effective date of the plan requires all payments to be discounted to that date using a present value analysis. The court will determine the discount factor to be used. House Report, note 40 supra, at 468.

145 (Popup)
141. The value of the collateral will be determined on a going-concern basis which in most cases will depend on a going-concern value of the business. See id. at 414.

146 (Popup)
142. 11 U.S.C § 1129(b)(2)(A)(i)(II), note 135 supra. If the value of the collateral exceeds the amount of the debt, the present-value test operates to equate the value of consideration provided under the plan to the secured creditor's interest in the debtor's collateral.

147 (Popup)
143. A sale of collateral must be made under 11 U.S.C. § 363(k) which permits the lien holders to bid for the collateral and to offset their allowed claims that are secured by the collateral against the purchase price. 11 U.S.C. § 1129(b)(2)(A)(ii). This includes both the secured claim and unsecured claim related to the collateral. House Record, note 53 supra at H 11,093; Senate Record, note 53 supra, at § 17,409.

148 (Popup)
144. Id.

149 (Popup)

150 (Popup)
146. 11 U.S.C § 1129(b)(2)(A)(ii), n.135 supra.
151 (Popup)
147. The standard of "indubitable equivalent" is taken from the reference to "indubitable equivalence" in In re Murel Holding Corp., 75 F.2d 941 (2d Cir. 1935) (Learned Hand, J.). House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 14,721.

152 (Popup)

153 (Popup)
149. House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 17,421.

154 (Popup)
150. If the plan provides for present cash payments equal to the amount of the allowed secured claims, the class is not impaired under 11 U.S.C. §1124(3)(A) and is deemed to have accepted the plan under 11 U.S.C. §1126(f).

155 (Popup)
151. House Record, note 53 supra, at H 11,104; Senate Record, note 53 supra, at S 17,421.

156 (Popup)
152. Id.

157 (Popup)
153. It is not so much that interest per se is required. It would suffice if the principal payments exceeded the principal amount of the debt to a sufficient extent that the effective interest being paid equalled the discount factor. For example, if the plan were to pay either 20% interest on the unpaid loan balance or "principal" installments of $450,000; $400,000; $350,000; and $300,000 with "no interest" the plan would be confirmed in Example 5 assuming a discount factor of 20 %. See text accompanying note 161, infra.

158 (Popup)
154. It is unrealistic to expect the discount factor to be zero. If the plan did propose to pay interest, the plan would be confirmed as long as the interest rate equals or exceeds the discount factor.

159 (Popup)
160 (Popup)

161 (Popup)

162 (Popup)
158. 11 U.S.C § 1129(b)(2)(A), note 135 supra.

163 (Popup)
159. The class of secured claims is entitled to make the election, because the disqualifying factors of 11 U.S.C § 1111(b)(1)(B) do not apply.

164 (Popup)

165 (Popup)
161. Id. at 613.

166 (Popup)
162. There is nothing to indicate that the plan unfairly discriminates against the class of secured claims or that the plan is otherwise not fair and equitable with respect to that class.

167 (Popup)

168 (Popup)

169 (Popup)

170 (Popup)
164. 11 U.S.C § 1111(b)(1)(A)(ii) applies only to non recourse lenders. See note 167 infra.

171 (Popup)

172 (Popup)

166.  See 11 U.S.C. §§ 502(b)(1) & 506(a) and note 117 supra.

173 (Popup)

167.  11 U.S.C. § 1111(b) provides as follows:

§1111    Claims and interests

*       *       *

(b)(1)(A) A claim secured by a lien on property of the estate shall be allowed or disallowed under section 502 of this title the same as if the holder of such claim had recourse against the debtor on account of such claim, whether or not such holder has such recourse, unless-

(i) the class of which such claim is a part elects, by at least two-thirds in amount and more than half in number of allowed claims of such class, application of paragraph (2) of this subsection; or

(ii) such holder does not have such recourse and such property is sold under section 363 of this title or is to be sold under the plan.

(B) A class of claims may not elect application of paragraph (2) of this subsection if-

(i) the interest on account of such claims of the holders of such claims in such property is of inconsequential value; or

(ii) the holder of a claim of such class has recourse against the debtor on account of such claim and such property is sold under section 363 of this title or is to be sold under the plan.

(2) If such an election is made, then notwithstanding section 506(a) of this title, such claim is a secured claim to the extent that such claim is allowed.

174 (Popup)


175 (Popup)

169.  The claim is to be allowed or disallowed under 11 U.S.C. § 502, as if there were recourse even if recourse is prohibited by contract or applicable law. House Record, note 53 supra, at H 11,103; Senate Record, n.53 supra, at S' 17,420.

176 (Popup)

177 (Popup)
171. This special status applies only in a reorganization case under chapter 11. 11 U.S.C. § 103(f).

178 (Popup)
172. The status will not be granted, and if it has been granted it will be terminated, if the collateral is sold under 11 U.S.C. § 363 or to be sold under the plan. House Record, note 53 supra, at H 11,103; Senate Record, note 53 supra, at S 17,420.

179 (Popup)

180 (Popup)
174. Section 1111(b)(1)(A)(i) of title 11, note 167 supra, states that an election is made if the class votes, by at least two-thirds in amount and more than one, half in number of allowed claims of the class, for application of section 1111(b)(2). Note that the requisite majorities are of allowed claims and not of the claims that are voted. Undoubtedly the amount of allowed claims of the "the classy refers to a class of allowed secured claims; the interest of a class of allowed unsecured claims in the collateral is of "inconsequential value", with the result that the class of unsecured claims is ineligible to elect application of 11 U.S.C. § 1111(b)(2). 11 U.S.C. § 1111(b)(1)(B)(i).

181 (Popup)

182 (Popup)
176. Although the statute is unclear, it would seem that the allowed secured claim will equal the amount of the debt for either a recourse or nonrecourse creditor. Otherwise, the nonrecourse creditor would have nothing to gain by electing application of 11 U.S.C. § 1111(b)(2).

183 (Popup)

184 (Popup)
185 (Popup)

186 (Popup)
180. See text accompanying note 161 supra.

187 (Popup)

188 (Popup)

189 (Popup)

190 (Popup)

191 (Popup)

192 (Popup)
186. Section 1129(b)(2)(A)(i) of title 11, n.135 supra, is therefore satisfied.

193 (Popup)
187. In order to be confirmed the plan must still comply with the best-interests-of-creditors test under 11 U.S.C. 1129(a)(7). In this example the non recourse lender would receive nothing for his deficiency claim in liquidation, so the requirement is met as to it. But the plan still must meet the test with respect to the trade debt, because there has not been unanimous acceptance by the class of which they are a part. See 11 U.S.C § 1129(a)(7)(A)(i). On liquidation the trade debt is entitled to 100% of the value of the unsecured assets, because there is no deficiency claim of a non recourse lender in liquidation and the trade debt comprises the entire class of unsecured claims. Since the $600,000 they will get under the plan is less than 100% of the $1,400,000 going-concern value of the unsecured assets, it is not likely that the best-interests test will be met, unless expenses of administration are quite substantial and the liquidation value of the unsecured assets is almost worthless.
194 (Popup)
188. 11 U.S.C § 1126(c).

195 (Popup)

196 (Popup)

197 (Popup)
191. It is unclear whether the trade debt could be classified separately from the deficiency claim under 11 U.S.C § 1122(a).

198 (Popup)
192. See 11 U.S.C § 1126(c).

199 (Popup)
193. 11 U.S.C § 1126(g).

200 (Popup)
194. 11 U.S.C § 1129(b)(2)(C), note 96 supra.

201 (Popup)
195. Id.

202 (Popup)
196. The plan would not be fair and equitable with respect to the stockholders because a senior creditor would be paid more than in full. See text accompanying note 76 supra.

203 (Popup)
197. 11 U.S.C § 1129(b)(1), note 65 supra.

204 (Popup)
198. 11 U.S.C § 1129(b)(2)(B)(i), note 84 supra.

205 (Popup)
199. 11 U.S.C § 1129(b)(2)(B)(ii), note 84 supra.

206 (Popup)
200. The plan must also comply with all of the requirements of 11 U.S.C. § 1129(a) other than paragraph (8). 11 U.S.C. § 1129(b)(1).

207 (Popup)

208 (Popup)

209 (Popup)

210 (Popup)

211 (Popup)

212 (Popup)
206. 11 U.S.C. § 1126(g).

213 (Popup)

214 (Popup)

215 (Popup)