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Mary Elizabeth Galvan

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**CRAM DOWN UNDER THE NEW FEDERAL
BANKRUPTCY CODE: THE EFFECT OF DEEMED
ACCEPTANCE ON THE CONFIRMATION
STANDARDS OF CHAPTER 11**

On October 1, 1979, the new Federal Bankruptcy Code of 1978¹ replaced the old Bankruptcy Act of 1898² as the vehicle for bankruptcy procedures in the United States. For the most part, the new Bankruptcy Code is the result of a two year study conducted by the Commission on the Bankruptcy Laws of the United States.³ Its purpose was to inquire into the ability of the bankruptcy system as it then existed to manage the increasing burden of bankruptcy cases which resulted from the expansion of credit since World War II.⁴ The Commission concluded that the system which had evolved under the old Act was poorly adapted to providing either debtor relief or protection of creditors' interests.⁵

First enacted in 1898,⁶ revised in 1938⁷ and significantly modified by the Rules of Bankruptcy Procedure in the 1970's,⁸ the Bankruptcy Act had been described as a "hodgepodge"⁹ whose sections were "out of date as well as out of style"¹⁰ by the late 1960's. A significant problem lay in the area of interpreting bankruptcy court procedure and practice, which had been completely revised by the Supreme Court's Rules of Bankruptcy Procedure. Since the Rules superseded any procedural provision of the Act which

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1. An Act to establish a uniform law on the subject of bankruptcies, Public L. No. 95-598, 92 Stat. 2549 (November 6, 1978) codifies and enacts title 11 of the United States Code, 11 U.S.C. §§ 101 *et. seq.* (Supp. II 1978).
2. The Bankruptcy Act of 1898, 11 U.S.C. § 1 *et. seq.* (1976), which has been replaced by the Federal Bankruptcy Code, *supra*, note 1. [hereinafter cited as the Bankruptcy Act or as the "Act."]
3. Congress established the Commission on the Bankruptcy Laws of the United States to analyze and evaluate the Bankruptcy Act in 1970. Pub. L. 91-354, 84 Stat. 468 (1970). The Commission consisted of nine members, three appointed by the President and two each by and from the Senate, House and Judiciary. *Report of the Commission on the Bankruptcy Laws of the United States, H.R. Doc. No. 93-137, 93rd Cong., 1st Sess. (1973), Part I, at 2.* [hereinafter cited as *Commissioners' Report.*] Trost, Treister, Forman, Klee, and Levin, *The New Federal Bankruptcy Code*, ALI-ABA Resource Materials, at 1 (1979) [hereinafter cited as Trost, *et. al.*]
4. *Commissioners' Report, supra* note 3, at 2.
5. *Id.* at 3.
6. The Bankruptcy Act of 1898, ch. 575, 30 Stat. 544 (1898), *supra* note 2.
7. Chandler Act of 1938, ch. 575, 52 Stat. 883, revised the Bankruptcy Act of 1898.
8. Bankruptcy Rules and Official Bankruptcy Forms. 28 U.S.C. § 2075 (1964).
9. Trost, *et al.*, *supra* note 3, at 7.
10. *Id.*

was inconsistent with them, much of the Bankruptcy Act had been effectively repealed. However, since the inconsistent provisions remained in the statute even after promulgation of the Rules, it was often unclear which portions of the Bankruptcy Act were "substantive" and therefore unaffected by the Rules.¹¹

The substantive law in the Act, with the exception of the dischargeability sections, were at least 40 years old¹² and were, for the most part, ill-equipped to deal with post-war shifts in bankruptcy focus and caseload.¹³ Interpretation of the substantive law was further complicated by the fact that it was often controlled by state law, which had itself changed significantly over the years, leaving an open question as to whether the principles of the Act were being served,¹⁴ and contributing to the general lack of uniform application of the bankruptcy law in the various federal districts.¹⁵

The Commission's study also questioned the efficiency of the actual administration of bankruptcy cases under the old Act.¹⁶ Far too much of the time, energy and expense of bankruptcy administration was being consumed on cases whose liquidated estates realized only enough money to cover administrative costs, or less.¹⁷ These estates, as well as larger estates, were being further reduced by the costs of attorneys' fees for what was too often an unnecessary adversary procedure, and the employment of attorneys to do tasks which did not require legal skills. The Commission also noted the lack of simplified procedures to record actions in routine cases and the redundancy of paperwork involved

11. *Id.* at 5.

12. *Id.*

13. *Commissioners' Report, supra* note 3, at 3. The number of bankruptcies increased 1000% between 1950 and 1970. *Id.* at 1.

14. *Trost, et al., supra* note 3, at 7.

15. *Commissioners' Report, supra* note 3, at 4.

16. *Id.* at 3.

17. It cost \$17 million to operate the bankruptcy system in 1972. Of this amount, \$6.7 million was spent on cases whose estates when liquidated resulted in no assets or nominal assets sufficient to cover only the administrative costs of the bankruptcy procedure. In 80% of these cases, the amount realized in a single case was less than \$1000. *Commissioners' Report, supra* note 3, at 3.

in bankruptcy administration.¹⁸ As did an earlier study,¹⁹ the Commission concluded that the bankruptcy system was run more for the convenience (and profit) of official participants, than for efficient management.²⁰

BUSINESS REHABILITATION UNDER THE OLD ACT: CHAPTERS X-XII

The business rehabilitation chapters of the old Act are characteristic of the general disorganization and archaic structure of the old bankruptcy system.²¹ Business debtors who chose rehabilitation instead of liquidation had to determine which of three separate chapters were applicable to their cases.²² In general, Chapter X²³ governed the reorganization of large corporate debtors. Chapter XI²⁴ provided for the adjustment of unsecured debts owed by corporations, partnerships or individuals. Chapter XII²⁵ dealt with the adjustment of secured debt of individuals or partnerships.

Each chapter had detailed and often overlapping rules governing its availability to a particular business debtor, which frequently generated pointless and wasteful litigation in determining the applicable chapter. Furthermore, even

18. *Id.*

19. The Brookings Institute conducted a study of the bankruptcy system in the late 1960's. Their study was published as Stanley, Girth, *et al.*, *BANKRUPTCY: PROBLEMS, PROCESS, REFORM*, (1971) and was relied upon in the study conducted by the Commission on the Bankruptcy Laws. *Commissioners' Report*, *supra* note 3, at 4.

20. *Id.*

21. *Trost, et al.*, *supra* note 3, at 241.

22. *Id.* at 237.

23. Bankruptcy Act of 1898, *supra* note 2, §§ 101-276, 11 U.S.C. §§ 501-676 (1976). Chapter X was generally available for the reorganization of larger corporations having publicly held securities and requiring a readjustment of their secured debts. Chapter X was also available to close corporations, but the difficulty of demonstrating that reorganization was feasible generally precluded small corporations from attempting reorganization under that chapter. 6 COLLIER ON BANKRUPTCY ¶ 0.09 at 101 (14th ed. 1978); Nachman, *Chapter X Corporate Reorganization* in *BANKRUPTCY AND THE CHAPTER PROCEEDINGS* 204 (G. W. Holmes ed. 1976).

24. Bankruptcy Act of 1898, *supra* note 2, at §§ 301-399, 11 U.S.C. §§ 701-799 (1976). Chapter XI cases enabled an individual, partnership or corporation to file a plan for the composition or extension of unsecured debts. Hertzberg, *Chapter XI Arrangement Proceedings* in *BANKRUPTCY AND THE CHAPTER PROCEEDINGS*, *supra* note 23, at 233 (1976).

25. Bankruptcy Act of 1898, *supra* note 2, at §§ 401-526, 11 U.S.C. §§ 801-926 (1976). Chapter XII dealt generally with real property arrangements by individuals or partnerships where the sole creditor or creditors were real estate mortgages.

though more than one chapter might appear to be applicable in a particular case, just as often, no one chapter seemed to be precisely suited to the debtor's needs in many other common business situations.²⁶ The result was often the net reduction of the proceeds which were to be shared by the competing interests.

CHAPTER 11 REORGANIZATION UNDER THE FEDERAL BANKRUPTCY CODE

The new Federal Bankruptcy Code eliminates much of this confusion by consolidating the treatment of all classes of business debt and debtors into a single reorganization chapter, Chapter 11 of Title 11 of the United States Code.²⁷ Underlying this consolidation is an attempt to balance substantively the competing interests of the debtor, secured and unsecured creditors, and ownership interests, and to expedite the reorganization procedure itself in order to avoid the waste of money and effort apparent under the Act.²⁸ To this end, Chapter 11 of the new Code combines those aspects of Chapter XI of the old Act aimed at facilitating the negotiation process with those of Chapter X which were designed to protect the public interest. Still other aspects of Chapter 11 are new.²⁹

26. *Commissioners' Report*, *supra* note 3, at 23.

27. Federal Bankruptcy Code, *supra* note 1, at §§ 1101-1146 (1978). Former Chapter VIII from the Bankruptcy Act, which involved railroad reorganizations is included under Chapter 11 as Subchapter IV. Chapter 11 is subject to the general provisions of the Bankruptcy Code: Chapters 1 (definitions), 3 (case administration) and 5 (trustees avoiding powers). In those jurisdictions designated pilot districts, Chapter 15 also applies. Note also that the debtor retains the option of choosing liquidation under Chapter 7, subject to certain limitations. Federal Bankruptcy Code, *id.* at § 1112. In liquidation, the debtor's property is gathered into an estate, liquidated and the proceeds are distributed to creditors. In reorganization, the debtor rearranges its debt structure under a reorganization plan and continues in business. Klee, *All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code*, 53 AM. BANKR. L. J. 107 (1979).

28. King, *Chapter 11 of the 1978 Bankruptcy Code*, 53 AM. BANKR. L. J. 107 (1979).

29. *Id.* Chapter X provided for the substitution of the independent trustee for debtor control, the absolute priority rule, the active participation of the Securities and Exchange Commission, the requirement of court approval of a plan before solicitation of its acceptance and the ability to deal directly with stockholders. Under Chapter XI, the "best interests of creditors test" provided a more flexible basis for negotiation of a plan, permitted the plan and acceptances to be filed with the petition, permitted stockholders to retain their interests even though creditors' interests were affected and generally permitted the retention of debtor management. Trost, *et al.*, *supra* note 3, at 237-239; King, *supra* note 28, at 107-108. Chapter 11 expedites the process by eliminating the different treatment

The central issue in a reorganization procedure is, of course, the reorganization plan. A basic premise of the new Chapter 11 is that the parties involved should be able to negotiate a plan which promotes their interests with a minimum of court intervention.³⁰ This represents a major departure from Chapter X of the old Act, which required court approval of a plan before acceptance by creditors could be solicited.³¹ Court approval was contingent on a finding that the plan satisfied the "absolute priority rule" and met and survived the "fair and equitable" test,³² which required that the claims of all senior interests be paid in full before any junior interest was allowed to participate in the plan.³³ The major drawback³⁴ to this requirement was that a determination of whether a plan was fair and equitable had to be based on a valuation hearing to determine the value of the business on a going concern basis. Valuation hearings were criticized as time consuming and expensive and as resulting in little more than a manipulated estimate³⁵ which determined whether a class would participate in the distribution or be eliminated from participation altogether.³⁶

Under Chapter 11, however, the court is not bound to the absolute priority rule and its concomitant fair and

available to private and public corporations and thus the ambiguity involved in the initial selection of the chapter under which a business debtor was going to proceed, as well as the need for conversion proceedings to move a case from one chapter to another and the resulting uncertainty as to how a case might be handled. *Trost, et al., supra* at 239, *King, supra* at 119. The role of the S.E.C. is modified. *Id.* at 108. Innovations in Chapter 11 include provisions for appointment of official creditors committees, the full disclosure requirement, mandatory court confirmation upon approval of the reorganization plan by a majority in each class of creditors and a finding that the plan meets the best interests of creditors test, but with a complex cram down provision based on the "fair and equitable" test in the event a class of interests or claims rejects the plan. *Id.* at 107-108.

30. *Id.* at 108.

31. Bankruptcy Act of 1898, *supra* note 2, at § 176, 11 U.S.C. § 576 (1976).

32. Bankruptcy Act of 1898, *supra* note 2, at § 221(2), 11 U.S.C. § 621 (1976).

33. 6A COLLIER'S ON BANKRUPTCY ¶ 11.06 at 216 (14th Ed. 1977).

34. This is aside from the fact that a court could not approve a plan not meeting the fair and equitable test, even if all affected classes had been willing to accept it.

35. *E.g., Commissioners' Report, supra* note 2, at 27; *King, supra* note 28, at 109; *Bell, Valuation and the Probability of Bankruptcy in Chapter X*, 52 AM. BANKR. L. J. 1 (1978).

36. *King, supra* note 28, at 109.

equitable test. So long as the requisite majority³⁷ of each class accepts³⁸ the plan on the basis of full disclosure³⁹ of the debtor's financial condition, and certain other prerequisites are met,⁴⁰ the court must confirm the plan upon a finding that all holders will receive at least as much as they would have received on liquidation,⁴¹ and that the plan is feasible and unlikely to result in liquidation.⁴² Only when a court is required to confirm a plan over the dissent of a class must the plan meet the fair and equitable test,⁴³ with its requirement of a valuation hearing.⁴⁴ Thus, Chapter 11 builds in a mechanism for the parties in interest to reach agreement prior to the submission of the plan to the court.⁴⁵ Senior interests can avoid the necessity of a valuation hearing if they can obtain the consent of junior interests to the plan,⁴⁶ thereby avoiding a possible reduction in the distribution proceeds because of the expense involved in holding valuation hearings. Junior interests will ordinarily have a better chance of participating in the final distribu-

37. Federal Bankruptcy Code, 11 U.S.C. § 1126(c) provides that a class of claims has accepted a plan if it has been accepted by holders of two-thirds in amount and one-half in number of the allowed claims of that class. 11 U.S.C. § 1126(d) (Supp. II 1978) provides that a class of interests has accepted a plan if the plan has been accepted by holders of at least two-thirds in amount of the allowed interests of such class.

38. A class of claims or interests which are not impaired under Federal Bankruptcy Code, 11 U.S.C. § 1124 (Supp. II 1978) is deemed to have accepted the plan and solicitation of acceptances from that class is not required. 11 U.S.C. § 1126(f) (Supp. II 1978).

39. Federal Bankruptcy Code, 11 U.S.C. § 1129(a) (5) (Supp. II 1978).

40. The requirements for confirmation when each class of claims or interests accepts the plan are specified in Federal Bankruptcy Code, 11 U.S.C. § 1129(a) (Supp. II 1978). For an explanation of the import of these conditions see Klee, *supra* note 27, at 136-138.

41. Federal Bankruptcy Code, 11 U.S.C. § 1129(a) (7) (A) (Supp. II 1978).

42. Federal Bankruptcy Code, 11 U.S.C. § 1129(a) (11) (Supp. II 1978).

43. Federal Bankruptcy Code, 11 U.S.C. § 1129(b) (1) (Supp. II 1978) provides that if all of the requirements of § 1129(a) are met except for the conditions imposed in (a) (8), the court shall confirm the plan on request of the proponent of the plan if the plan does not discriminate unfairly and is fair and equitable with respect to each class that is impaired under and has not accepted the plan.

44. Federal Bankruptcy Code, 11 U.S.C. § 1129(b) (2) (Supp. II 1978) specifies the conditions under which a plan will be found to meet the fair and equitable test.

45. In the majority of cases in which plans are confirmed, it will be with the consent of all parties in interest. Klee, *supra* note 27, at 133.

46. Since the Federal Bankruptcy Code, 11 U.S.C. § 1126(g) (Supp. II 1978) provides that any class which receives nothing under the plan will be deemed to have rejected it and since the existence of one dissenting class allows the proponent to invoke the cram down provisions of 11 U.S.C. 1129(b) (see 11 U.S.C. § 1129(a) (i)), senior classes have an incentive to approve plans providing for distribution to junior classes which would otherwise receive nothing in order to avoid the valuation hearing requirement.

tion of proceeds if they accept a plan instead of forcing uncertain valuation hearings which may preclude them from receiving any of the proceeds if senior interests cannot be satisfied in full. Finally, the proponent of the plan is encouraged to propose a plan which will be readily acceptable to all classes of claims or interests in order to avoid the valuation hearings⁴⁷ and to expedite the resolution of the proceedings.

To this end, the Code provides that a class which receives nothing under the plan is deemed to have rejected it.⁴⁸ This provides an incentive for the proponent of the plan and the participating parties to negotiate a plan under which all classes receive something⁴⁹ even though a class might not have received anything under the fair and equitable test or on liquidation, since the presence of even one dissenting class is sufficient to require a valuation hearing for confirmation of the plan over its dissent.⁵⁰ Conversely, any class which is unaffected under the plan is deemed to have accepted it,⁵¹ and the proponent of the plan need not go to the time and expense of soliciting its acceptance.

The relationship between section 1126(f),⁵² which provides for deemed acceptance, and the confirmation standards of section 1129(a)⁵³ creates an ambiguity which is certain⁵⁴ to become a point of contention in future bank-

47. King, *supra* note 28, at 109, Klee, *supra* note 27, at 134.

48. Federal Bankruptcy Code, 11 U.S.C. 1126(g), (Supp. II 1978).

49. King, *supra* note 28, at 109.

50. Federal Bankruptcy Code, 11 U.S.C. § 1129(b) (Supp. II 1978) is the cram down provision of the Chapter and allows a plan to be confirmed over the objection of dissenting classes of creditors so long as the requirements of § 1129(a) are met, with the exception of § 1129(a) (8), which requires unanimous acceptance.

51. Federal Bankruptcy Code, 11 U.S.C. § 1126(f) (Supp. II 1978) specifies that a class which is unimpaired under the plan is deemed to have accepted the plan.

52. Federal Bankruptcy Code, 11 U.S.C. § 1126(f) (Supp. II 1978).

53. Federal Bankruptcy Code, 11 U.S.C. § 1129(a)(10) (Supp. II 1978) requires that at least one class of claims or interests has accepted the plan for confirmation. 11 U.S.C. § 1129(a) (8) specifies that all classes must be either unimpaired or must have accepted the plan.

54. Commentators are unevenly divided on the question of whether deemed acceptance of an unimpaired class under § 1126(f) fulfills the § 1129(a) (10) requirement. 5 COLLIER ON BANKRUPTCY ¶ 1129.02, at 1129-32 (15th Ed. 1979). Klee, *supra* note 27, at 137 maintains that the requirement is satisfied where there is a class of claims that is not impaired, excluding any class of insider claims. King, *supra* note 28, at 126 seems to agree with this construction, but argues that it vitiates the seeming protection

ruptcy litigation. The key portion of section 1129(a) appears to be subsection 1129(a)(8),⁵⁵ which sets as the minimum requirement for court confirmation of a plan under the less stringent "best interests of creditors" test that every class either accept the plan or be unimpaired by it. Subsection 1129(a)(8) is the only condition of section 1129(a) which is not an absolute prerequisite under the fair and equitable test.⁵⁶ Should the proponent of a plan which has met all of the other conditions of section 1129(a) fail to obtain unanimous acceptance of the plan, he may request that the court confirm the plan over the dissent of one or more classes of claims or interests so long as one class has accepted the plan.⁵⁷ If the plan does not discriminate unfairly and meets the fair and equitable test, the court has no authority⁵⁸ to reject the plan unless the requirements of section 1129 are met with respect to more than one submitted plan, in which case the court must consider the preferences of creditors and holders of equity securities in choosing among plans.⁵⁹

Section 1129(a)(10),⁶⁰ therefore, sets the minimum standard for confirmation, which is that at least one class of claims or interests must accept the plan. This avoids a stalemate between the parties by serving as an additional motivation to dissenting classes to avoid the cram down provisions of section 1129(b) by accepting a plan which at least one class of creditors has found acceptable. The prerogative of the proponent of a reorganization plan to use the cram down provisions so long as at least one class

afforded the creditor by § 1129(a)(10). 5 COLLIER ON BANKRUPTCY, *supra* at 1129-32 points out that a requirement of affirmative acceptance can be easily circumvented. See test accompanying note 72 *infra*.

55. Federal Bankruptcy Code, 11 U.S.C. § 1129(a)(8) (Supp. II 1978).

56. Federal Bankruptcy Code, 11 U.S.C. 1129(b) (Supp. II 1978) specifies that if all the requirements of subsection (a) other than paragraph (8) are met, the court must confirm the plan on the request of the proponent, provided that the plan does not discriminate unfairly and is fair and equitable with respect to each impaired class.

57. Federal Bankruptcy Code, 11 U.S.C. § 1129(b) (Supp. II 1978); 11 U.S.C. § 1129(a)(10) (Supp. II 1978).

58. Federal Bankruptcy Code, 11 U.S.C. § 1129(b) (Supp. II 1978) states that the court *shall* confirm the plan subject to the limitations described at note 52, *supra*.

59. Federal Bankruptcy Code, 11 U.S.C. § 1129(c) (Supp. II 1978).

60. Federal Bankruptcy Code, 11 U.S.C. § 1129(a)(10) (Supp. II 1978) excludes the acceptance of a plan by a class of insiders.

accepts the plan, however, raises the question of whether section 1129(a)(10) is intended to require the affirmative acceptance by an impaired class, or whether the deemed acceptance of an unimpaired class under section 1126(f) is sufficient.

The conditions under which classes of claims or interests may accept a plan are specified in section 1126.⁶¹ An impaired class of creditors may accept a plan only if it is acceptable to a majority of that class in number and amount of claims.⁶² An impaired class of ownership interests may accept a plan only on the approval of the holders of a majority in amount of interests of that class.⁶³ However, any class of either claims or interests which is not impaired⁶⁴ under the plan is deemed to have accepted the plan, so that the proponent of the plan is not required to solicit acceptances from that class.⁶⁵

The question, then, is whether or not the deemed acceptance by a class which will lose nothing under the proposed plan ought to be sufficient to force an otherwise unacceptable plan on classes of claims or interests whose positions will be altered by the plan. The requirement that at least one class accept the plan before the proponent can resort to cram down suggests that he be able to "sell"⁶⁶ the plan to at least one class, implying something more than merely satisfying one class in full and thereby obtaining its passive acceptance. Certainly equating deemed acceptance with the active acceptance of impaired classes under these circumstances seems to give the proponent of the plan power over dissenting classes which seems to contradict the underlying purpose of the codified bankruptcy reform to balance

61. Federal Bankruptcy Code, 11 U.S.C. § 1126 (Supp. II 1978).

62. Federal Bankruptcy Code, 11 U.S.C. § 1126(c) (Supp. II 1978).

63. Federal Bankruptcy Code, 11 U.S.C. § 1126(c) (Supp. II 1978).

64. Federal Bankruptcy Code, 11 U.S.C. § 1124 (Supp. II 1978) specifies the situations in which a class is not impaired under the plan.

65. Federal Bankruptcy Code, 11 U.S.C. § 1126(f) (Supp. II 1978).

66. Certainly there is some doubt that the requirement that at least one class accept the plan can be satisfied by the passive acceptance of a class whose position remains unaltered by the plan. Curiously, the rationale that § 1129(a)(10) places a responsibility on the proponent to sell the plan to impaired classes has not been addressed by any of the commentators (see note 54 *supra*) even though King and Klee participated in drafting the code and in drafting the COLLIER section.

more equitably the competing rights of the various parties in interest. Nevertheless, nothing in the language of Chapter 11 clearly suggests that the deemed acceptance of an unimpaired class is not intended to be the functioning equivalent of an affirmative acceptance by an impaired class. Indeed, except for the somewhat ambiguous language of section 1129(a)(8), the Code consistently equates a deemed status with an actual status throughout its chapters.⁶⁷

The only section of Chapter 11, in fact, which seems to distinguish between the deemed acceptance by unimpaired classes and the active acceptance of impaired classes is section 1129(a)(8),⁶⁸ which merely specifies that every class "has accepted the plan or is not impaired under the plan." Section 1129(a)(10) contains no suggestion that only impaired classes which have affirmatively accepted the plan fulfill its conditions, although it does specifically exclude the acceptance of the plan by any class of insiders.⁶⁹ The obvious argument is that had Congress intended a distinction between the two kinds of acceptance for the purposes of satisfying section 1129(a)(10), the Code would have provided a stronger clue to that intent than the single disjunctive "or" in the earlier subsection, especially since section 1129(a)(10) provides an alternative course of action under section 1129 if the conditions of section 1129(a)(8) are not met.

Section 1126(f) does not provide that a class which has been deemed to accept the plan must receive different treatment because it is unimpaired, other than that soliciting acceptance from that class is not required. Although it has been argued that the sole purpose of providing for deemed acceptance under section 1126(f) is to specify that solicitation is not required,⁷⁰ the presumption is that if permitted

67. 5 COLLIER ON BANKRUPTCY ¶ 1129.02 at 1128-32 n.47 (15th ed. 1979).

68. Federal Bankruptcy Code, 11 U.S.C. § 1129(a)(8) (Supp. II 1978) merely states that as a condition for confirmation under § 1129(a) each class must have accepted the plan or be unimpaired, but does not elaborate as to how much of a distinction between the two kinds of classes is intended to be raised.

69. See note 60 *supra*.

70. 5 COLLIER ON BANKRUPTCY ¶ 1129.02, *supra* note 54, at 1129-32 n.47 (15th ed. 1979).

to do so, an unimpaired class would vote affirmatively for acceptance anyway, and that requiring solicitation from such a class would be redundant and burden the proponent of the plan unnecessarily.⁷¹ Furthermore, if section 1126(f) is insufficient for the purpose of section 1129(a)(10), proponents of plans could easily circumvent the requirement by only slightly impairing a class⁷² in order to create an "impaired class" which could give the requisite acceptance.⁷³ An alternative argument can be made that section 1126(f) only states that solicitation of active acceptances from unimpaired classes is *not required*, not that it is prohibited, and therefore solicitation of active acceptances for purposes of section 1129(a)(10) converts the deemed acceptance to an active acceptance for purposes of section 1129(a)(10).⁷⁴ Either way, the statute could be circumvented, but the bankruptcy procedure would suffer for it.⁷⁵

The language of section 1129(a)(8) does not clearly lend itself to an interpretation that the two categories of classes should be subjected to different treatment.⁷⁶ Certainly it can be argued that section 1129(a)(8) merely emphasizes that deemed acceptance and affirmative acceptance carry the same weight in determining whether confirmation may proceed under the best interests of creditors test of section 1129. Both categories seem to have the same effect on meeting the conditions of either section 1129(a) or section 1129(b), since even if an affirmative vote is not required, a plan may not be confirmed if every class is impaired or fails to accept.⁷⁷

71. *Id.*

72. For example, this can occur by composition and extension or by offering the "impaired class" 98% of its allowed claims. Note that 11 U.S.C. § 1124 specifies that any altering of the position of a class constitutes impairment, which is a departure from the Old Act's requirement that a class be *materially* and *adversely* affected. Bankruptcy Act of 1898, *supra* note 2, at § 107.

73. 5 COLLIER ON BANKRUPTCY ¶ 1129.02, at 1129-32 n.47 (15th ed. 1979).

74. *Id.*

75. A purpose of bankruptcy reform was to streamline bankruptcy procedure and these solutions only complicate it.

76. The note in COLLIER suggests that the distinction raised in Federal Bankruptcy Code, 11 U.S.C. § 1129(a)(8) (Supp. II 1978) is merely surplusage. 5 COLLIER ON BANKRUPTCY ¶ 1129.02, *supra* note 54, at 1129-32 (15th ed. 1979).

77. 5 COLLIER ON BANKRUPTCY ¶ 1129.02, *supra* note 54, at 1129-31 (15th ed. 1979).

This ambiguity of construction is not well clarified by the prior law. Under the Supreme Court Rules of Bankruptcy Procedure,⁷⁸ acceptance by a class which was not materially or adversely affected by the terms of the plan was not counted as an acceptance in acquiring the required number of acceptances for confirmation.⁷⁹ Until new Rules are adopted, the prior Bankruptcy Rules remain in effect, but only to the extent that they are not inconsistent with the substantive portions of the new Code.⁸⁰ Whether the courts will affirm the current Bankruptcy Rules on the question of the deemed acceptance by an unimpaired class as satisfying section 1129(a)(10) remains to be seen.

It has been suggested that section 1129(a)(10) is related to the Chapter XII cases under the Old Act in which some bankruptcy courts confirmed the plan by the use of the cram down provisions where no class accepted it.⁸¹ However, Chapter XII cases usually involved only one creditor, the real estate mortgagee, who retained his security interest, and was not available to corporate debtors. Furthermore, section 1129(a)(10) appears to require the acceptance of at least one class before any plan can be confirmed, apparently to protect creditors by insuring that their interests will have to be considered in a reorganization plan. Even so, that protection seems to be countered by permitting the proponent of an otherwise unacceptable

78. R. BANKR. PROC. § 10-305(a). Bankruptcy Act of 1898, *supra*, note 2 at § 179.

79. 9A AM. JUR. 2D *Rules of Bankruptcy and Official Forms* § 10-305.2 (1976). There was no deemed acceptance provision for unaffected classes in the Bankruptcy Rules. R. BANKR. PROC. 10-305(a). However, holders of claims which were "deemed allowed" under the Act were entitled to the same voting privileges as holders of claims which were actually allowed. *E.g.*, R. BANKR. PROC. § 10-401(a), 9A AM. JUR. 2D. *Rules of Bankruptcy and Official Forms* § 10-305.2 (1976).

80. Bankruptcy Reform Act of 1978 Pub. L. 95-598 § 405(d) (1978). A significant change in the bankruptcy law deals with the effect of the bankruptcy rules on the new Code. Since 1973, the Supreme Court has promulgated rules for practice and procedure under the Bankruptcy Act subject to its rule-making power under 28 U.S.C. § 2075 (1976). Under the Act, all laws in conflict with the rules were nullified. Under the Code, however, the rules may not supersede procedural provisions of the Code. *Trost, et al.*, *supra* note 3, at 74.

81. 5 COLLIER ON BANKRUPTCY ¶ 1120.02, *supra* note 54, at 1129-31 (15th ed. 1979); King, *supra* note 28, at 126.

plan to pay one class in full and thereby obtain its appearance.⁸²

Perhaps a more constructive approach should focus on the consequences of cram down to dissenting classes. Section 1129(a)(8) sets the minimum conditions under which a court must confirm a plan which, in effect, is submitted to it at the unanimous request of the parties in interest.⁸³ The section emphasizes one of the underlying motivations for corporate bankruptcy reform: that the parties themselves and not the bankruptcy courts are best able to negotiate a plan to protect their own interests. If the specified majorities of each class agree, the court must confirm the plan. Any further inquiry by the court should be directed at insuring that dissenting minorities in each class are protected and not at questioning the ability of the affirming parties to negotiate a proper plan. Members of unimpaired classes are deemed to have accepted the plan because the protection of their interests is not in issue. Members of classes which receive nothing are deemed to have rejected the plan, because the only way to determine, legally, the extent of their share in distribution of the debtors estate is through liquidation or through determination of the value of that estate through a valuation hearing.

When one or more classes (as opposed to holders of claims or interests within a class) reject a plan, the protective role of the court is broadened. Before it can confirm a plan over the dissent of even one class, it must ascertain that all the requirements of section 1129(a), other than section 1129(a)(8), have been met. Those requirements include the best interests of creditors requirement of section 1129(a)(7) that each holder in each class has either accepted the plan or will receive at least as much under the plan as it would have received under liquidation.⁸⁴ Secondly,

82. King, *supra* note 28, at 126.

83. If all classes accept the plan, they endorse the proponent's submitting it to the court, and in effect, request its confirmation.

84. Other requirements under Federal Bankruptcy Code, 11 U.S.C. § 1129(a) (Supp. II 1978) include full compliance by both the plan and the proponent of the plan with Chapter 11 (11 U.S.C. §§ 1129(a)(1) and (2) (Supp. II 1978); that the plan be legal and be proposed in good faith (11 U.S.C.

the court must determine, through valuation hearing, that every senior claim will be satisfied in full before junior interests will be allowed to participate. Because of these protections, the only way in which a dissenting class can be injured by the cram down provision of section 1129(b) is in the potential reduction of the debtor's estate through the expense of the valuation hearing, or if its members have miscalculated as to whether the amount realized under the fair and equitable test will exceed the amount the class would have received under the plan. The dissenting class can avoid these risks by consenting to the plan—a result that section 1129(a)(8) is designed to encourage. From the point of view of the dissenting class, it is irrelevant that the cram down was effected because a class had affirmatively accepted or had been deemed to have accepted the plan. The protections and risks to the dissenting class are the same whatever the nature of the accepting class. Its only concern is to ascertain whether it would be wiser to accept the proffered plan or to take its chances with the valuation hearing.

The dissenting class is not powerless to influence the nature of the plan. First, assuming that avoidance of a valuation hearing will be a major motivating factor in formulating the plan, the option of a class of claims or interests to withhold its acceptance, and thus require the proponent of the plan to seek cram down, is itself an effective instrument to encourage the proponent to propose

§ 1129(a)(3) (Supp. II 1978)); that there be full disclosure of the identities of any individual who will replace the debtor or act as a director, officer or voting trustee and that such appointment will be consistent with the interests of claimants and with public policy and that there will be full disclosure of any insiders to be employed or retained under the plan and the nature of their compensation (11 U.S.C. § 1129(a)(5) (Supp. II 1978)); that any payments made in connection with the plan be fully disclosed and that such payment be reasonable (11 U.S.C. § 1129(a)(4) (Supp. II 1978)). Furthermore, any rate changes under the plan are expressly conditioned on the approval of any regulatory commission with jurisdiction over the rates of the debtor. 11 U.S.C. § 1129(a)(6) (Supp. II 1978). 11 U.S.C. § 1129(a)(9) (Supp. II 1978) specifies that the plan provide for the specified treatment of priority claims. Finally, 11 U.S.C. § 1129(a)(11) (Supp. II 1978) conditions confirmation on a determination that the plan is not likely to be followed by liquidation or the need of further financial reorganization of the debtor unless such liquidation or reorganization is proposed in the plan. In other words, the plan must be feasible.

a plan which will be acceptable to all classes. Secondly, any party in interest, including a member or representative of a dissenting class may present an alternative plan to the court for confirmation if the debtor has not filed a plan within 120 days from the date of the order for relief⁸⁵ or if the plan has not been accepted by every impaired class of claims or interests within 180 days.⁸⁶ Furthermore, upon the request of a party in interest and after notice and hearing, a court may, for cause, increase or reduce the 120-day period or the 180-day period.⁸⁷ Although the statute does not define "cause", almost certainly a proponent's invoking the cram down of an unacceptable plan before the expiration of the 180-day period ought to be sufficient cause to allow the court to reduce that period to allow dissenting parties in interest to present an alternative plan.

The alternative plan is subject to the same restrictions of section 1129(a) and section 1129(b) as the debtor's plan. Since section 1129(a) does not require that the plan be acceptable to the debtor, it would seem that an alternative plan which is accepted by all classes of claims or interests would be preferable to a plan which would have to be "crammed down", particularly in light of the mandate in section 1129(c) that the court must consider the preferences of creditors and equity holders in deciding among plans.⁸⁸ Also, an alternative plan which met all of the requirements of section 1129(a) would have to be confirmed without a valuation hearing. Only if a class of claims or interests rejects the alternative plans must the fair and equitable test of section 1129(b) be applied.

Thus, not only do the alternative plan provisions of the Chapter safeguard the interests of a dissenting class by permitting it to file its own plan to avoid having an unacceptable plan forced on it, they provide negotiating leverage

85. Federal Bankruptcy Code, 11 U.S.C. § 1121(c) (2) (Supp. II 1978).

86. Federal Bankruptcy Code, 11 U.S.C. § 1121(c) (3) (Supp. II 1978). A party in interest can also file a plan if, after 120 days, a trustee has been appointed under Chapter 11. 11 U.S.C. §§ 1121(c) (1) and 1121(b) (Supp. II 1978).

87. Federal Bankruptcy Code, 11 U.S.C. § 1121(d) (Supp. II 1978).

88. Federal Bankruptcy Code, 11 U.S.C. § 1129(c) (Supp. II 1978).

during the 120-day period in which the debtor must file a plan. A debtor who is aware that an alternative plan may be proposed and confirmed in lieu of his is necessarily compelled to take the interests of the dissenting classes into account in formulating and proposing his plan. Again, it seems to make little practical difference whether section 1129(a)(10) acceptance is effected by affirmative acceptance of an impaired class or by deemed acceptance by an unimpaired class.

The foregoing analysis does not answer the question of why, with these additional safeguards of creditors' interests, acceptance, deemed or otherwise, should be required of any class before confirmation over the dissent of other classes is permitted. Nevertheless, before a court may consider confirmation that acceptance must be obtained. Those drafters⁸⁹ of the Code who have commented on the cram down question have concluded that deemed acceptance by an unimpaired class is sufficient for the purposes of sections 1129(a)(10) and 1129(b). Certainly the Code is structured to protect the interests of creditors in the event of cram down, and in such a way that it seems to make little practical difference how acceptance by a class has been obtained.

Chapter 11 is clearly designed to promote unanimous agreement among the parties in interest before a reorganization plan is submitted to a bankruptcy court. There seems to be universal agreement that the threat of valuation hearings constitutes considerable leverage in obtaining the consent of dissenting classes. Whether that purpose extends as far as allowing cram down where the only accepting class is a class which is not affected by the plan awaits interpretation and definition in the courts. The question will surely be raised.

Mary E. Galvan

89. See note 54 *supra*.