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Single Asset Chapter 11 Cases

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SINGLE ASSET CHAPTER 11 CASES

H. Miles Cohn*

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INTRODUCTION

Single asset Chapter 11 cases have been filed in rapidly increasing numbers in recent years. Hit by real estate recessions in the mid-1970's and mid-1980's, innumerable single asset partnerships and corporations, formed only to acquire and manage their one investment asset, have sought the protection of the bankruptcy court. Often filed with little purpose but to postpone foreclosure, and with no serious hope of reorganization, single asset cases have met harsh reactions from many courts. But single asset debtor reorganization proceedings have a long history and, on closer examination, are not fundamentally different from the more ordinary case involving multiple assets and more numerous creditors. A

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single asset debtor with a realistic plan to restructure its obligations, and with the legitimate desire and ability to do so, can sometimes overcome the many obstacles in Chapter 11 and emerge with a successful plan of reorganization.

I. THE HISTORICAL PERSPECTIVE

Single asset bankruptcy cases are not new. They first blossomed under Chapter XII of the Bankruptcy Act of 1898, which was enacted as a part of the Chandler Act in 1938. Chapter XII, entitled "Real Property Arrangements by Persons Other Than Corporations," was precipitated by the then-common situation in which an individual or partnership owned real estate for which it was obligated on bond issues secured by trust indentures and owned by large numbers of individual holders. Although Chapter XII was not limited to "single asset" cases, most debtors who sought its protection owned a single parcel of real estate, typically a developed property such as an apartment house or office building. Increasing numbers of such individuals and partnerships found themselves unable to pay their bond issues during the depression years of the 1930's, particularly in Chicago and in some northeastern cities. Chapter XII was designed for these individual and partnership debtors. Chapter XII combined the most pertinent provisions of Chapter X (corporate reorganizations) and Chapter XI (arrangements of unsecured debt), which were also enacted as a part of the Chandler Act.¹

After an initial spurt of Chapter XII cases in the late 1930's and early 1940's, Chapter XII fell into disuse for many years. Indeed, from 1938 until 1974, there were only seven reported decisions concerning confirmation of Chapter XII plans of reorganization.² But a real estate recession in the mid-1970's, "triggered by . . . tight money and substantial inflation in the construction industry and compounded around 1973 by the oil embargo and resultant inflation of 1973-74," seemed to awaken an interest in Chapter XII.³ The number of cases filed under that chapter escalated from 92 in 1973, to 172 in 1974, to 280 in 1975, and to 525 in 1976.⁴ Not surprisingly, beginning in 1974, there was "a veritable

1. See generally Weinstein, *The Debtor Relief Chapters of the Chandler Act*, 5 U. PITT. L. REV. 1, 18-20 (1938); Note, *Compositions and Extensions Under the Chandler Act*, 87 U. PA. L. REV. 837 (1939).

2. See Anderson and Ziegler, *Real Property Arrangements Under the Old and New Bankruptcy Acts*, 25 LOY. L. REV. 713, 713 n. 2 (1979).

3. *In re Pine Gate Associates*, 2 Bankr. Ct. Dec. 1478, 1480 n. 12 (Bankr. N. D. Ga. 1976).

4. *Id.*

explosion" of reported decisions analyzing plans of reorganization and other issues in Chapter XII cases.⁵

Despite the inclusion in the Bankruptcy Act of a chapter dealing primarily with single asset real estate cases, and despite the large number of such cases filed in the five years immediately preceding the enactment of the Bankruptcy Code, the drafters of the Code made little attempt to focus on single asset cases. Unlike the provisions of the Chandler Act, the Bankruptcy Code includes no separate chapter for real estate cases; indeed, the Code includes not a single provision applicable only to single asset or real estate cases.⁶

Only two issues addressed by the drafters of the Bankruptcy Code had particular relevance to the single asset case. The first was the so-called "cash out" of the undersecured creditor. The issue arose in a case in which the debtor owned real estate secured by a nonrecourse obligation; where the property was valued at an amount less than the secured obligation, the debtor could propose a plan in which the secured creditor would be paid an amount equal to the value of the property, allowing the debtor to retain the property and to discharge the nonrecourse deficiency. A single asset debtor succeeded in such a strategy in *In Re Pine Gate Associates, Ltd.*⁷ This result was thought to be unfair, since it allowed the debtor to retain all the benefits of any post-confirmation appreciation in the value of the property while paying no more than the appraised value as determined by the court at the time of confirmation.

Congress enacted section 1111(b) of the Bankruptcy Code to cure this unfairness. Section 1111(b) gives the undersecured nonrecourse creditor an option between (1) making its claim in the full amount of the secured indebtedness, or (2) making a secured claim only to the extent of the value of the property, while making an unsecured (recourse) claim for the deficiency. These provisions make it much more difficult, although not impossible, to effect a "cash out" of an undersecured creditor in a single asset real estate case.⁸

A second issue addressed by the drafters of the Bankruptcy Code had particular relevance to the single asset case: the secured creditor's

5. *Anderson and Zeigler, supra* note 2.

6. See generally *In re Greystone III Joint Venture*, 102 Bankr. 560, 562-66 (Bankr. W.D.Tex. 1989), *aff'd*, No. A-89-CA-667 (W.D.Tex. 1990, appeal filed.)

7. 2 Bankr. Ct. Dec. 1478 (Bankr. N.D. Ga. 1976).

8. See generally *In re Greystone III Joint Venture*, 102 Bankr. at 560-66; Stein, *Section 1111(b): Providing Undersecured Creditors with Post-Confirmation Appreciation in the Value of the Collateral*, 56 AM. BANKR. L. J. 195 (1982).

entitlement to relief from the automatic stay. Bankruptcy Code section 362(d) sets forth the standards under which a creditor is entitled to relief from the stay. The statute, as enacted, does not refer specifically to single asset cases, but the legislative history points to section 362(d)(2) as the focus of Congress' concern for the treatment of such cases. That provision requires the court to grant relief from the automatic stay as to property of the debtor upon a finding of two separate facts: (a) that the debtor has no equity in the property, and (b) that the property is not necessary to an effective reorganization. Although the Bankruptcy Code as adopted does not elaborate on this standard, the bill passed by the Senate included a provision stating that for the purpose of section 362(d), "property is not necessary to an effective reorganization of the debtor if it is real property on which no business is being conducted by the debtor other than the business of operating the real property and activities incidental thereto."⁹ The Senate Report accompanying the bill explained that the provision was directed at single-asset cases:

The intent of this exception is to reach the single asset apartment type cases which involve primarily tax shelter investments and for which the bankruptcy laws have provided a too-facile method to relay [sic] conditions, but not the operating shopping center or hotel cases where attempts at reorganization should be permitted.¹⁰

The effect of the Senate's proposed amendment to section 362(d)(2) was twofold: first, only properties held solely for investment or appreciation, and from which the debtor operates no ongoing business, were by definition not necessary to an effective reorganization; and second, single asset cases involving properties held solely for investment would nevertheless survive a motion for relief from stay under section 362(d)(2) if, but only if, the debtor had equity in the property.

It is the converse of these propositions that is important here: at least some single asset cases — those from which the debtor operates a business and those in which the debtor has equity — were not subject to attack under section 362(d)(2). The final version of the Bankruptcy Code did not, of course, contain the Senate amendment. But statements on the floors of the House and Senate by members of the Conference Committee indicate that the final version was intended to have the same effect.¹¹

9. S. 2266, 95th Cong., 2nd Sess., 354, 124 CONG. REC. 25,382 (1978).

10. S. REP. NO. 989, 95th Cong., 2d Sess. 53 (1978).

11. See 124 CONG. REC. 28,259 (1978) (remarks of Senator DeConcini).

It is therefore clear that while neither section 1111(b) nor section 362(d)(2) of the Bankruptcy Code refers specifically to single asset cases, both are of particular relevance to such cases. But these statutory provisions and the legislative history that accompanies them are perhaps more important for what they omit: neither suggests that single asset cases are to be treated any differently than the ordinary case involving multiple assets and more numerous creditors. The fact that Congress chose neither to restrict single asset cases nor to treat them separately, despite the long history of such cases under Chapter XII and the explosion of such cases that preceded the development of the Bankruptcy Code, suggests that Congress saw such cases as not fundamentally different than other individual, partnership or corporate debtor cases.¹²

II. THE TYPICAL SINGLE ASSET CASE

There are many variations of the single asset case, and some are not very different from the typical multiple asset case. Some, like the case of a debtor that owns and operates a hotel, may involve an ongoing business that has numerous employees and many classes of creditors. But one may nevertheless discern a set of facts that typifies the most common single asset cases, and which, collectively, may form a paradigm of the single asset case. Taken together, the characteristics of the typical single asset case are the following:

1. The debtor is an investment vehicle, usually a partnership but occasionally a corporation, that was formed for the purpose of holding the single asset as an investment, rather than to operate an ongoing business. As such, the demise of the debtor will not mean that a business fails and that employees lose their jobs, but rather that the particular owners of the partnership or corporation will lose their equity as creditors take over the asset.

2. The asset owned by the debtor is almost always real estate. The real estate is generally income producing, given the obvious and generally insurmountable difficulties of reorganizing a non-income-producing asset.

3. The immediate cause of the filing of the case is usually a default

12. Reviewing the legislative history of Bankruptcy Code provisions relevant to all real estate cases, whether having single or multiple assets, one court has concluded that Congress "adopted a . . . middle position on the question of single asset real estate cases in bankruptcy." In re Greystone III Joint Venture, *supra* note 8, at 566. The *Greystone* court noted a number of provisions that appear to cut in different directions, leaving the Code "rife with inconsistencies" when applied to single asset real estate cases. *Id.*

in one or more secured obligations. Unsecured obligations, typically trade debt arising from the operation of the single asset, are much less significant and generally are a small fraction of the debtor's total obligations. The case usually centers around a dispute with one or more secured creditors, because unsecured creditors (and in some cases, junior secured creditors) have little or no hope of recovering on their claims absent a successful reorganization.

4. The debtor's default in its secured obligations is generally the result of a recession or other cause that leads to a reduction in occupancy and rentals, leaving the debtor with too little cash flow to service its secured debt.

In this "typical" single asset case, the debtor's objects are easy to understand and simple to state; the debtor seeks to retain its single asset by restructuring its secured debt within the limits of its reduced cash flow. Of course, this is not to say that all single asset cases are filed for this purpose. Many cases have been filed for improper or ulterior motives, most often to retain property in which the debtor has no equity without any additional capital contribution and with no serious intent to pursue a plan of reorganization. The courts have uniformly condemned such cases as lacking the "good faith" necessary to support a bankruptcy case, and have often granted relief from the automatic stay or other relief to creditors in such cases.¹³

But here we are concerned with the legitimate Chapter 11 case, in which a single asset debtor in good faith attempts to reorganize by restructuring its obligations. Clearly, a single asset debtor may restructure its obligations under Chapter 11 of the Bankruptcy Code. Bankruptcy courts have approved plans that restructure secured debts in various ways: by adding past-due principal and interest to the restructured balance of the indebtedness; by extending the term of the indebtedness, and in some cases by reducing required principal payments for a period of time; by reducing the interest rate from a higher rate agreed at the time the indebtedness was incurred to a lower rate consistent with the market at time of confirmation; by deferring all or a portion of the interest payments for a period of time; and by separately classifying and treating the unsecured portion of an undersecured claim, in some cases paying only a portion of the unsecured deficiency and discharging the balance.¹⁴

13. See generally Cohn, *Good Faith and the Single Assets Debtor*, 62 AM. BANKR. L. J. 131, 145-47 (1988).

14. *Id.* at 146-47; see also Anderson and Ziegler, *supra* note 2, at 720-28.

III. CONFIRMATION ISSUES IN THE SINGLE ASSET CASE

A small number of issues are decisive when the typical single asset debtor attempts to confirm a plan of reorganization in a Chapter 11 case. But before reviewing these issues, it is important to clarify the subject at hand. We are here considering the usual case in which a single asset debtor legitimately and in good faith attempts to reorganize by restructuring its debts. Those cases in which single asset debtors file Chapter 11 petitions solely to delay foreclosure, with no legitimate intent to restructure their debts or otherwise reorganize, are subject to dismissal for lack of good faith and are not dealt with here. Moreover, no attempt is made to review the various confirmation requirements that must be met in all cases but are not distinctive of single asset cases. The single asset debtor must of course meet the same requirements for confirmation as must all other debtors under Chapter 11. These requirements are set forth in Bankruptcy Code section 1129, and no distinction is made in the statute between single asset cases and other types of cases. Nevertheless, a typical single asset case can be reviewed in terms of the most common issues that arise in the confirmation of plans in such cases.

A. *Bankruptcy Code Section 1129(a)(ii): The Feasibility Requirement*

Bankruptcy Code section 1129(a)(ii) requires a finding that 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." This requires the debtor to demonstrate, in short, that its plan is "feasible." This does not require the debtor to show that the plan is guaranteed to succeed. Rather, feasibility means that the debtor must demonstrate "a reasonable likelihood that the debtor will in fact be able to perform its obligations under the plan as projected."¹⁵ But proof of a reasonable likelihood of success obviously must consist of more than the debtor's optimistic hopes or speculation in the market place. The debtor must demonstrate a reasonable assurance of the commercial viability of its plan.¹⁶ The feasibility requirement is particularly troubling in a single asset real estate case, where the debtor's problems typically begin

15. *In re Wolf*, 61 Bankr. 1010, 1011 (Bankr. N.D. Iowa 1986). See also *In re Monnier Brothers*, 755 F.2d 1336, 1341 (8th Cir. 1985) ("success need not be guaranteed"); *In re Swiftco, Inc.*, 1988 W. L. 143714 (Bankr. S.D. Tex. 1988); *In re White*, 41 Bankr. 227, 230 (Bankr. N.D. Tenn. 1984).

16. See, e.g., *In re Prudential Energy Company*, 58 Bankr. 857, 862 (Bankr. S.D.N.Y. 1986); *In re Trail's End Lodge, Inc.*, 54 Bankr. 898, 905 (Bankr. D. Vt. 1985).

with an inadequate cash flow to service its secured obligations. Because the debtor's single asset is usually an investment in managed real estate, there is little the debtor can do to improve its cash flow. In some cases, of course, the property has substantial deferred maintenance, and an infusion in capital to repair and rehabilitate the property may improve cash flow. But in most cases, the single asset debtor can do little but wait for the economy to recover and for occupancy and rental rates of its single asset to improve. This means that the debtor must propose some postponement of payments due to the secured creditor, and in many cases must postpone current (post-confirmation) payments of accruing interest on the secured debt. This postponement amounts to a "negative amortization" of the indebtedness, in which the secured indebtedness increases as unpaid accrued interest is added to the balance.

Where the plan proposes to defer all principal repayments and to accrue but not pay post-confirmation interest for some period of time, the feasibility of the plan necessarily depends upon a sale or refinance of the property at some point in the future; this future sale or refinance in turn is dependent upon an increase in the marketability and value of the property. The obvious problem is that the property's marketability and value in the future is difficult to predict and may be nothing more than speculation. A plan dependent upon nothing more than speculation in the value of the debtor's single asset is not feasible and cannot be confirmed.¹⁷

This does not mean, of course, that single asset plans of reorganization never can feasibly postpone the payment of principal and interest to secured creditors. A number of factors may support the feasibility of such a plan. To begin with, a debtor might demonstrate substantial current equity in its property. If the property could be liquidated at the time of confirmation for more than sufficient cash to pay the debtor's obligations, the plan is not dependent on a speculative increase in value and it may be feasible to accrue and postpone some payments. Such plans have been confirmed in *In re Pikes Peak Water Company*,¹⁸ where the court allowed a three year moratorium in payments to the secured creditor, and in *In re Nite Lite Inns*,¹⁹ where the court upheld the feasibility of a plan that provided for liquidation in three years, in the event that the

17. See, e.g., *In re Swiftco, Inc.*, *supra* note 15; *In re Hoffman*, 52 Bankr. 212, 215 (Bankr. D.N.D. 1985); *In re Stoffel*, 41 Bankr. 390, 393 (Bankr. D. Minn. 1984); *In re Landmark at Plaza Park, Ltd.*, 7 Bankr. 653, 658-59 (Bankr. D.N.J. 1980).

18. 779 F.2d 1456, 1460 (10th Cir. 1985).

19. 17 Bankr. 367, 369-70 (Bankr. S.D. Cal. 1982).

scheduled payments were not made to creditors.²⁰

Another factor that may support the feasibility of a plan that postpones payment of principal and interest is the term of such deferral. Many courts have held that the longer the extension of payments under the plan, the more difficult it will be to demonstrate feasibility, and conversely that the shorter such term, the easier it will be to demonstrate feasibility.²¹ Other factors also enter the analysis and in some cases will support the feasibility of a single asset debtor's plan to defer payments: the stability of the property's occupancy and rental rates, and current trends toward improvement in those rates; the quality of the debtor's management of the property, and its experience in managing or improving other similar properties; the court's perception of the market-place for the debtor's asset, and of the likelihood for improvement in that market in the near and long term; and the making of a capital contribution pursuant to the plan, either to supplement payments to creditors or to improve or rehabilitate the property. Obviously the court must take all of these and many more factors into consideration in making the difficult judgment call that is inherent in any feasibility determination. Feasibility may be particularly troubling in a single asset case, but in many situations the facts will point in favor of the feasibility of a single asset plan of reorganization.

B. *Bankruptcy Code Section 1129(b): The "Fair and Equitable" Requirement*

Bankruptcy Code section 1129(a) lists twelve requirements for the confirmation of a plan of reorganization. Among these is the rule stated in section 1129(a)(8), which requires a finding that each class of impaired creditors²² has accepted the plan. But this requirement is not absolute, for section 1129(b) allows the bankruptcy court under certain circumstances to confirm a plan notwithstanding the rejection of the plan by one or more classes of impaired creditors. Section 1129(b), the so-called "cram-down" provision, allows the debtor to escape the requirements of

20. Cf. *In re Landmark*, *supra* note 17, at 658-59 (holding that a three year moratorium was not feasible where the debtor did not have current equity in the property).

21. See, e.g., *In re White*, 36 Bankr. 199, 202-203 (Bankr. D. Kan. 1983), and cases cited therein.

22. A class of creditors is "impaired" unless, with respect to each creditor in the class, the plan does one of the following: (1) leaves the creditor's rights unaltered; (2) cures any default to the creditor, reinstates the maturity of the claim, and compensates the creditor for any damages caused by the default; or (3) pays the creditor, in cash at the time of confirmation, the amount of its allowed claim. Bankruptcy Code § 1124, 11 U.S.C. § 1124 (1988).

section 1129(a)(8), and thus to force the plan on rejecting impaired classes, upon a finding that 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."

The term "fair and equitable" is not defined, but the statute does set forth minimum standards that must be met by any fair and equitable plan.²³ Where the plan proposes that the debtor retain property that secures a claim, section 1129(b)(2)(A)(i) requires that to be fair and equitable with respect to a claim secured by the property, the creditor holding such a claim must retain its liens in the property and must receive cash payments over time that *both* (1) total at least the allowed amount of the claim, and (2) have a present value, at the time of confirmation, at least equal to the allowed claim.²⁴

The section 1129(b)(2)(A)(i) requirement must be contrasted with the feasibility requirement of section 1129(a)(11). Section 1129(b)(2)(A)(i) does *not* require a finding of any particular degree of probability with respect to the debtor's ability to make the payments required under the plan. The section 1129(b)(2)(A)(i) analysis requires only a mathematical calculation: either the plan provides for payments of a sufficient amount and of a sufficient present value, or it does not. Once the court determines the amount of the creditor's allowed secured claim and the appropriate interest or discount rate with which to evaluate future payments, the court need only discount the payments to be made under the

23. Bankruptcy Code § 1129(b)(2), 11 U.S.C. § 1129(b)(2) (1988), sets forth separate minimum standards for secured creditors, § 1129(b)(2)(A); unsecured creditors, § 1129(b)(2)(B); and equity interest holders, § 1129(b)(2)(C). To be "fair and equitable" with respect to a class of secured creditors, the plan must meet any one of three minimum standards defined in § 1129(b)(2)(A)(i), (ii) and (iii). Section 1129(b)(2)(A)(ii) is applicable where the plan proposes a sale of the property securing the claim, and § 1129(b)(2)(A)(iii) is applicable where the plan proposes another treatment that is "the indubitable equivalent" of the secured claim, such as abandonment of the property to the secured creditor. But where, as in the typical single asset case, the debtor proposes to *retain* the property, the plan must meet the minimum standard of § 1129(b)(2)(A)(i). See *infra* note 24.

24. Bankruptcy Code § 1129(b)(2)(A)(i); 11 U.S.C. § 1129 (1988), provides that to be "fair and equitable" with respect to a class of claims that is secured by property not abandoned to the claimants, the plan must provide:

(i) that the holders of such claims retain the liens securing such claims, whether the property subject to such liens 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 totalling 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.

See generally Booth, *The Cram-down on Secured Creditors: An Impetus Toward Settlement*, 60 AM. BANKR. L.J. 69, 87 (1986); Klee, *All You Ever Wanted to Know About Cram-down Under the New Bankruptcy Law*, 53 AM. BANKR. L.J. 133, 155 (1979).

plan to a present value at the time of confirmation. Thus, for example, a plan providing for no payments at all during its term but providing for a single balloon payment at some distant point in the future would nevertheless meet the requirements of section 1129(b)(2)(A)(i) if the balloon payment were so large that, when discounted at an appropriate rate, the present value of the payment at the time of confirmation would be equal to the creditor's allowed secured claim.

But while a plan retaining property must meet the standard of section 1129(b)(2)(A)(i) to be "fair and equitable," it does not follow that each plan to meet this test is necessarily "fair and equitable." Section 1129(b)(2) provides that "the condition that a plan be fair and equitable with respect to a class *includes* the following requirements" Bankruptcy Code section 102(3) makes clear that the word "includes" is "not limiting." Thus the section 1129(b)(2) tests are only minimal standards, and are not intended as definitions of the "fair and equitable" requirement. As the legislative history makes clear:

Although many of the factors interpreting fair and equitable are specified in paragraph (2), others, which were explicated in the description of section 1129(b) in the House Report, were omitted from the House amendment to avoid statutory complexity and because they would undoubtedly be found by courts to be fundamental to "fair and equitable" treatment of a dissenting class.²⁵

Where a single asset plan meets the requirement of section 1129(b)(2)(A)(i) as to a secured creditor, the plan by definition proposes to pay that creditor the full amount of its allowed secured claim; and where the claim is to be paid over a period of time, the plan by definition accrues and pays interest on the claim at a rate sufficient to insure the present value of the claim. Where the court finds that this plan is feasible, therefore, it may be difficult to imagine what would not be "fair and equitable" about the plan. After all, such a plan would require payment in full of the secured creditor's allowed claim, on terms that would protect the present value of the claim and which the court found to be feasible. If the secured creditor is being paid the full present value of its claim, in a plan that has been found to be feasible, might the secured creditor still have a legitimate complaint?

In some cases, the courts have indeed found that secured creditors have legitimate objections, under section 1129(b)(2), to a single asset plan

25. 124 CONG. REC. 32,407 (1978). See *In re D & F Construction, Inc.*, 865 F.2d 673, 675 (5th Cir. 1989); *In re Spanish Lake Associates*, 92 Bankr. 875, 878 (Bankr. E.D. Mo. 1988); *In re Edgewater Motel, Inc.*, 85 Bankr. 989, 998 (Bankr. E.D. Tenn. 1988).

that provides for the payment of the secured claim on terms that are otherwise sufficient and feasible. These objections seem to fall into two categories. In the first, the plan has proposed such a substantial extension of the term of the indebtedness, or otherwise has so changed the nature of the creditor's bargain, that the result goes beyond any "fair" expectation of the creditor. This is the case in *In re Stoffel*,²⁶ where the bankruptcy court refused to confirm extensions of payments to secured creditors for periods from 24 to 26 years. A similar case is *In re Hoffman*,²⁷ where the bankruptcy court found a plan not to be "fair and equitable" where its treatment of the secured creditor called for a consolidation of loans, a substantial extension of loan terms, and a release of a portion of the liens securing the loans. The court found that the plan did not provide fair and equitable treatment of the secured claim because its provisions so "substantially vari[ed] the terms and conditions of the original agreement" with the creditor. Of course, this is not to say that the terms of the creditor's bargain cannot be substantially changed; after all, that is what plans of reorganization are all about. But it does mean that there are reasonable limits, and that at some point a plan can so substantially change the creditor's original bargain as not to be "fair and equitable" within the meaning of section 1129(b)(2).

A second, and somewhat more common, objection under section 1129(b)(2) has to do with the assumption of the risks and benefits inherent in any plan of reorganization. It is axiomatic that a plan may be "feasible" without being "guaranteed of success."²⁸ Even where the plan has "a reasonable likelihood of success," there are risks inherent in any postponement of payments to creditors. There are many such risks in any plan of reorganization, but two are foremost in the single asset case. The first risk is the plan's dependence upon the future of the debtor's single asset. Unless the debtor has provided a meaningful guaranty or additional collateral to the secured creditor, the debtor's ability to meet its obligations under the plan is entirely dependent upon the future of its single asset because it has no other business or assets out of which to pay creditors. The second risk arises from the appraisal process itself. Most single asset cases involve real estate, and most such cases arise in depressed markets where there are few sales of similar properties. No matter how convincing the expert testimony, the bankruptcy court must

26. 41 Bankr. 390, 393 (Bankr. D. Minn. 1984).

27. 52 Bankr. 212, 217 (Bankr. D.N.D. 1985).

28. See *supra* notes 15-16 and accompanying text.

recognize that "estimating the value of real estate, and especially forecasting it, is a speculative test."²⁹

What is not "fair and equitable" about some single asset plans is that they impose these downside risks on the secured creditor while retaining the upside benefits for the equity owners of the debtor. This occurs in some cases where the plan proposes no payment of the principal amount of the secured claim until some point in the future, and in some cases where the plan postpones (or "negatively amortizes") post-confirmation interest. In such a plan, the debtor will make as little payments as possible during the early years under the plan, while accruing interest and promising to pay the creditor in a "balloon" payment due five years or more in the future. Such a debtor is typically waiting for the real estate market to improve, with the hope and expectation that it can sell the property in the future, repay its creditors in full and retain equity. This may be feasible to do, especially where the court finds that the property is already worth more than debtor's obligations and where the court has confidence in the future marketability and value of the property. However, such a plan imposes the risk of failure on the secured creditor, because the creditor will receive no payments, but merely the return of its property, if the plan fails and the debtor cannot make the required balloon payment.

This uncompensated risk led the Court of Appeals for the Fifth Circuit to hold recently, in *In re D & F Construction, Inc.*,³⁰ that a plan providing for negative amortization of interest over a period of twelve years with repayment of principal in fifteen years was not "fair and equitable." The court explained:

We do not hold that there can never be an occasion when negative amortization would be fair and equitable. We do say that this plan is not fair and equitable. Negative amortization coupled with deferring substantially all repayment of principal for fifteen years can only be considered reasonable if one speculates that the present condition of the Fort Worth, Texas real estate market will improve substantially. While this speculation may be wholly acceptable from the standpoint of the debtor and the other classes of creditors, it is an altogether impermissible speculation from the standpoint of [the secured creditor] which is effectively denied access to the security contracted for during the next fifteen years and must furnish further funding to the project.³¹

29. *In Re Swiftco, Inc.*, *supra* note 15.

30. 865 F.2d 673, 675-76 (5th Cir. 1989).

31. *Id.* at 676.

Many bankruptcy courts have refused for the same reason to confirm negative amortization plans. This was the case, for example, in *In re Memphis Partners, L.P.*,³² where the court held that a negative amortization plan was not fair and equitable because "in the early years of such financing the creditor is at risk of not receiving the present value should the plan end prematurely;" in *In re Spanish Lake Associates*,³³ where the court held that a plan requiring the secured creditor "to wait seven years before the Debtor begins paying the full 10% plan interest rate, when the figures presented suggest a risk of financial deficiency, is unduly burdensome;" in *In re McCombs Properties VIII, Ltd.*,³⁴ where the court held that any deferral of post-confirmation interest would render the plan not fair and equitable; and in *In re Gemini at Dadeland, Ltd.*,³⁵ where the court held that a negative amortizing plan required the secured creditor to "assume a risk of its implementation without having received the indubitable equivalent of its claim," and was therefore "unfair."³⁶

However the analysis is framed, the bottom line is the same: a plan is not fair and equitable where it imposes too much of the downside risk of reorganization on the secured creditor relative to the upside benefits retained for the debtor. This does not mean, of course, that single asset plans may never postpone the payment of principal or interest to secured creditors. Indeed, many courts have confirmed such single asset plans in the face of rejecting classes of secured creditors. One such case is *In re Pikes Peak Water Company*.³⁷ There the Court of Appeals for the Tenth Circuit held to be fair and equitable a plan that provided for a three-year moratorium in payments of all principal and interest to the secured creditor, with a balloon payment of the full principal and interest at the end of that period. Although this imposed some risk on the secured creditor,

32. 99 Bankr. 385, 388 (Bankr. M.D. Tenn. 1989).

33. 92 Bankr. 875, 879 (Bankr. E.D. Mo. 1988).

34. 91 Bankr. 907, 911 (Bankr. C.D. Cal. 1988).

35. 36 Bankr. 129, 131 (Bankr. S.D. Fla. 1983).

36. The same conclusion was reached in two recent decisions using a somewhat different analysis. In *In re Lakeside Global II, Ltd.*, 116 Bankr. 499 (Bankr. S.D. Tex. 1989), and *In re Swiftco, Inc.*, 1988 W.L. 143714 (Bankr. S.D. Tex. 1988), the court argued that even the minimal mathematical standard of § 1129(b) (2)(A)(i) is not met where the plan imposes the downside risk on the secured creditor while retaining the upside potential for the debtor. The court held that to meet the requirements of § 1129(b)(2)(A)(i), the plan must either *assure* the creditor that it will be paid in full, or else must *compensate* the creditor for any risk of nonpayment by giving the creditor something of value equal to the benefits of ownership that it would have obtained upon foreclosure. The court reasoned that to comply with the "absolute priority rule" as codified in § 1129(b) (2) (A) (*see supra* note 23) the secured creditor that is not assured of payment must receive the same value as would a "new buyer" of the property; such a buyer would bear the downside risk but also would receive "the potential of full benefits of any increase in value."

37. 779 F.2d 1456 (10th Cir.1985).

the court found that the debtor had substantial equity in the property (a valuation of \$3.5 million against a secured indebtedness of \$2.9 million), and that a moratorium in such context was fair and equitable.³⁸ Other courts have approved deferrals of interest where the rate of interest is sufficient to compensate the secured creditor for the additional risk imposed by the plan.³⁹ Additionally, many courts have confirmed plans that provided for the payment of current interest but postponed repayments of principal for substantial terms.⁴⁰

As to a secured creditor, perhaps it can be said that, to be fair and equitable, a single asset plan of reorganization must not impose a risk on the creditor that is out of proportion to the benefits received by the creditor under the plan. The more the plan imposes a risk on the secured creditor, by extending the payment of principal and interest over a longer period of time, the greater is the need to compensate the creditor for the risk inherent in its increasing reliance on the single asset for repayment. That compensation can take either of two forms. In the first place, the plan can provide some greater assurance of repayment, such as a guaranty by some person or entity other than the debtor, or a contribution of additional security or collateral. In the second place, the creditor can be compensated by receiving a portion of the upside potential of reorganization, either by the accrual of interest at a higher rate or by receiving an equity interest or profits participation in the eventual sale of the property. No test or formula can guide the bankruptcy judge in determining whether the creditor has been sufficiently compensated for the risk it must assume. Like feasibility, this determination is a judgment call: the court must weigh the risks imposed on the creditor against the benefits paid to the creditor in determining whether the plan is "fair and equitable" as to the secured creditor.

C. *Bankruptcy Code Section 1129(b)(2)(A)(i): The Interrelationship Between Interest Rates and Valuation*

In order to determine whether the minimum "fair and equitable"

38. See also *In re Landmark at Plaza Parks, Ltd.*, 7 Bankr. 653 (Bankr. D.N.J. 1980) (holding that a plan providing for a three-year moratorium on payments of interest and principal was fair and equitable, but nevertheless was not feasible).

39. See *In re Pinebrook, Ltd.*, 85 Bankr. 160, 162 (Bankr. M.D. Fla. 1988); *In re Orosco*, 77 Bankr. 246, 255-56 (N.D. Cal. 1987).

40. See *In re Adamson Co.*, 42 Bankr. 169 (Bankr. E.D. Va. 1984); *In re White*, 41 Bankr. 227 (Bankr. M.D. Tenn. 1984); *In re Hollanger*, 15 Bankr. 35 (Bankr. W.D. La. 1981).

test of Bankruptcy Code section 1129(b)(2)(A)(i) has been met, the bankruptcy court must make two separate determinations. First, the court must value the debtor's single asset; that being the security for the creditor's claim. Pursuant to Bankruptcy Code section 506(a), it is this value that determines the amount of the creditor's allowed secured claim. Section 506(a) divides the creditor's claim into two portions: an allowed secured claim to the extent of the value of the property, and an allowed unsecured claim to the extent of any deficiency.⁴¹ Second, the court must determine the appropriate interest or discount rate to apply in determining the "present value" of the stream of payments proposed in the plan. When these have been determined, it is a mere mathematical calculation to determine whether the stream of payments proposed under the plan, when discounted at the appropriate rate to a present value at the time of confirmation, is at least equal to the allowed secured claim.⁴²

Unfortunately, the Bankruptcy Code provides little guidance in determining either of these matters. With respect to the valuation of the property securing the claim, section 506(a) states only that: "Such valuation shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest." This ambiguity was intentional. As the legislative history makes clear, Congress recognized that the statute "does not specify how value is to be determined, nor does it specify when it is to be determined," and Congress left these matters "to case by case interpretation and development."⁴³ This has led the courts to consider various methods of valuing property, and in some cases the courts have distinguished between the "liquidation" value that would be attained upon an immediate sale and the "going concern" value that presupposes the debtor's retention of the property for some period of time. These distinctions are less important, however, in the typical single asset case, since the debtor owns only an investment asset and its ownership is not likely to add value to the asset.

41. Bankruptcy Code § 506(a) provides, in pertinent part, as follows:

An allowed claim of a creditor secured by a lien on property in which the estate has an interest . . . is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property. . . , and is an unsecured claim to the extent that the value of such creditor's interest . . . is less than the amount of such allowed claim.

11 U.S.C. § 506(a) (1988).

42. See *supra* note 24 and accompanying text.

43. H.R. REP. NO. 595, 95th Cong., 1st Sess. 339 (1977); S. REP. NO. 989, 95th Cong., 2d Sess. 54 (1978).

The Bankruptcy Code likewise provides little guidance for determining the appropriate interest or discount rate. The courts and commentators have therefore devised a number of different and sometimes conflicting means for determining the appropriate rate. The most common analysis is a comparison to the appropriate "market" rate of interest for similar loans. As Collier explains, the "deferred payment of an obligation under a plan is like a coerced loan and the rate of return with respect to such loan must correspond to the rate which would be charged or obtained by the creditor making a loan to a third party with similar terms, duration, collateral and risk."⁴⁴ Many courts have followed this approach.⁴⁵ Some courts have relied upon the contract rate of interest, especially where the loan is recent and the contract is the best evidence of the appropriate market rate.⁴⁶ Other courts have relied on such comparisons as the legal rate of interest on judgments under state law,⁴⁷ and federal statutory rates.⁴⁸ One commentator suggests that the analysis must begin with the rate paid on government securities or with the creditor's cost of borrowing, to which should be added only a small risk factor. This conservative approach is intended to further a perceived policy of encouraging successful reorganizations.⁴⁹

While recognizing the many different methods of valuing property and determining the appropriate interest rate, many courts and commentators seem to overlook the interrelationship between the two. The typical secured creditor will argue, in the course of a plan confirmation hearing, that the treatment of its claim under the plan should be compared with new commercial loans made by the creditor and similar lenders, and thus should bear the same interest rate as a new loan that might be made by the creditor on a similar project. Indeed, a secured creditor can be expected to argue that the interest rate should be much higher than that appropriate to an ordinary commercial loan, given the risk implicit in any bankruptcy reorganization. But this presupposes that, were it not for the reorganization, the creditor would immediately liquidate its collateral and receive cash in the full amount of its allowed secured

44. 5 L. KING, COLLIER ON BANKRUPTCY ¶ 1129.03[1] (15th ed. 1979).

45. See, e.g., *In re S. States Motor Inns, Inc.*, 709 F.2d 647 (11th Cir. 1983), *cert. denied*, 465 U.S. 1022 (1984), and cases cited therein.

46. See *In re Monnier Bros.*, 755 F.2d 1336 (8th Cir. 1985).

47. See *In re Anderson*, 28 Bankr. 628 (Bankr. S.D. Ohio 1982).

48. See *In re Fisher*, 29 Bankr. 542 (Bankr. D. Kan. 1983); *In re Nite Lite Inns*, 17 Bankr. 367 (Bankr. S.D. Cal. 1982).

49. See Carbiener, *Present Value in Bankruptcy: the Search for An Appropriate Cramdown Discount Rate*, 32 S.D. L. REV. 42 (1987). Cf. *In Re Fowler*, 903 F.2d 694 (9th Cir. 1990) (approving interest rate equal to prime rate plus risk factor).

claim, which cash would then be available for reinvestment at current "market" rates of interest. This may be so, but only if the bankruptcy court has calculated the creditor's allowed secured claim on the basis of a rapid liquidation sale for cash. "Fair market value," by contrast, presupposes a reasonable time to market the property as well as available alternative financing. As a practical matter, a real estate lender that wants to receive the full "market value" of its security in a distressed real estate market must probably sell the property itself and provide financing for the sale. The most appropriate market comparison might therefore be with the financing extended by lenders to purchasers of their own foreclosed properties. And that financing typically is made at below market rates, not at the additional premium often demanded by the creditor in the course of a confirmation hearing.

Thus a fair approach to the determination of interest rates must begin with an understanding of the method by which the property has been valued. Where the property has truly been valued on a liquidation basis, and where this value represents the cash that could actually be obtained upon the creditor's foreclosure and liquidation of its collateral, then a true "market" rate of interest is more appropriate. But where the value represents an appraised "fair market value," dependent upon longer term marketing and reasonable financing, then the appropriate interest rate should account for the lower rates that actually would be earned upon a sale of the property at that price by the lender. Obviously, there is an inverse relationship between the valuation of the asset and the appropriate interest rate: the more liberal the method of valuing the property, the lower the appropriate interest rate.

D. Bankruptcy Code Section 1129(b)(2)(B): Treatment of the Secured Creditor's Unsecured Deficiency Claim

If the court values the debtor's single asset at an amount less than the debtor's obligation to a secured creditor, then the creditor will have an unsecured deficiency claim. Pursuant to Bankruptcy Code section 506(a), this deficiency is treated as an unsecured claim, separate and apart from the creditor's secured claim.⁵⁰ Thus, the unsecured deficiency must be placed in a class separate from the secured claim and the plan must propose a separate means for its payment. This creates an opportunity for the single asset debtor, which may seek to pay less than the full amount of the unsecured deficiency. If successful, this would allow the

50. See *supra* note 41.

debtor to do what Congress sought to prevent by enacting Bankruptcy Code section 1111(b): to "cash out" the secured creditor by paying the amount of the allowed secured claim while not paying all of the unsecured deficiency.

This might be accomplished where the unsecured deficiency is classified together with the claims of unsecured creditors willing to support the plan, in number and amount sufficient to allow for acceptance of the plan by the class as a whole notwithstanding the rejection of the plan by the holder of the unsecured deficiency claim. Bankruptcy Code section 1122(a), which sets forth the standard for classification of claims and interests, states only that the plan may place a claim in a particular class if the claim "is substantially similar to the other claims . . . of such class." Because the deficiency claim is nothing but an unsecured claim, it can ordinarily be classified together with other unsecured claims, such as trade debts, unsecured loans, and other unsecured deficiencies. The class as a whole may accept the plan, pursuant to Bankruptcy Code section 1126(c), by a vote in favor of the plan of at least two-thirds in amount and more than one-half in number of the allowed claims in the class.

In the single asset case, however, the unsecured deficiency claim commonly represents the bulk of the debtor's unsecured obligations. Classifying the deficiency together with other unsecured claims in such a case generally would not allow the debtor to force the plan on an objecting holder of an unsecured deficiency, whose vote is significant enough to force the unsecured class to reject the plan. If a class of unsecured creditors including the deficiency claim has voted to reject the plan, or if a separately classified deficiency claim has voted to reject the plan, the plan may then be forced on such an unsecured class only if it meets the requirements of section 1129(b). These require that the plan not discriminate unfairly, and that it be fair and equitable with respect to each class of claims that has not accepted the plan.

This creates two difficulties for the single asset debtor. In the first place, the requirement that the plan not discriminate unfairly may prevent the debtor from paying a smaller proportion of a separately classified deficiency claim than is paid to other unsecured creditors, such as trade debt.⁵¹ The second problem arises under section 1129(b)(2)(B), which states the minimum requirement that must be met for a plan to be

51. See *In re 222 Liberty Assoc.*, 108 Bankr. 971, 990-91 (Bankr. E.D. Pa. 1990); *In re Pine Lake Village Apartment Co.*, 21 Bankr. 478, 480 (Bankr. S.D.N.Y. 1982). Cf. *In re Greystone III Joint Venture*, 102 Bankr. 560, 571-72 (Bankr. W.D. Tex. 1989), *aff'd*, No. A-89-CA-667 (D.C.W.D. Tex. 1990, appeal filed).

"fair and equitable" as to unsecured creditors. This statutory provision is the codification of the "absolute priority rule" with respect to unsecured creditors.⁵² The rule, which was long recognized though not codified under the Bankruptcy Act, provides that a plan cannot be confirmed over the objection of a class of creditors unless (a) the class is being paid in full, or (b) no junior class of creditors or equity interest holders receives anything of value under the plan.⁵³ An exception to this rule was recognized in *Case vs. Los Angeles Lumber Products Co.*,⁵⁴ which acknowledged that a debtor might infuse capital ("money or money's worth") into a plan and thereby retain value not greater than such capital even though one or more classes of creditors had not been paid in full.

There is some dispute, however, as to whether section 1129(b)(2)(B) codified this "fresh capital" exception to the absolute priority rule. The statute provides that a plan of reorganization, to be fair and equitable with respect to a class of unsecured creditors that is not paid the full amount of its claims, must provide that no junior claim or interest "receive or retain under the plan on account of such junior claim or interest any property." Some courts and commentators read the phrase, "on account of such junior claim or interest," to allow the debtor to retain something of value in exchange for a new infusion of capital, but others decline to so read this language and instead argue that the "fresh capital" exception to the absolute priority rule was intentionally omitted by Congress when it enacted the Bankruptcy Code.⁵⁵ The Supreme Court, which considered the reach of the "fresh capital" exception to the absolute priority rule in *Ahlers* expressly chose not to reach this underlying issue.⁵⁶

52. Bankruptcy Code § 1129(b)(2)(B) provides that to be "fair and equitable" with respect to a class of unsecured claims, the plan must meet one of two tests: (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 under the plan on account of such junior claim or interest any property.

53. See *Norwest Bank of Worthington vs. Ahlers*, 485 U.S. 197 (1988).

54. 308 U.S. 106 (1939).

55. Compare *In re Rudy Debruyker Ranch, Inc.*, 84 Bankr. 187 (Bankr. D. Mont. 1988) with *In re Snyder*, 105 Bankr. 898 (Bankr. C.D. Ill. 1989).

56. *Ahlers*, 485 U.S. at 203 n.3. The issue in *Ahlers* was whether the debtor's post-confirmation labor (or "sweat equity") could qualify as "money or money's worth" and therefore constitute the "fresh capital" that would justify an exception to the absolute priority rule. The Court held that "sweat equity" was not "money or money's worth," and declined to reach what appeared to be the threshold issue: whether the Bankruptcy Code had "dropped the infusion-of-new-capital exception to the absolute priority rule." *Id.* See Powlen & Wuhrman, *The New Value Exception to the Absolute Priority Rule: Is Ahlers the Beginning of the End?*, 93 COM. L.J. 303, 314-17 (1988).

The bottom line is this: if the “fresh capital” exception to the absolute priority rule still exists, then it would seem that a single asset debtor could still “cash out” a secured creditor by contributing to the plan fresh capital in an amount at least equal to the value retained by the debtor under the plan. For example, in a case where property is valued at \$1 million and the secured creditor has a claim of \$1.5 million, the equity interest in the debtor might contribute \$100,000, to be used to pay a portion of the unsecured deficiency claim. The debtor might argue that in discharging the balance of the creditor’s unsecured deficiency claim, it is retaining an interest in property that has little or no current value, and is certainly no greater than the fresh capital contribution.⁵⁷ That being the case, the secured creditor faced with a “cash out” of its allowed unsecured (deficiency) claim would have to retreat to the protection of Bankruptcy Code section 1111(b), the provision that was enacted by Congress to protect against such a plan.⁵⁸ But section 1111(b) is an imperfect protection. Section 1111(b)(1), which gives the creditor “recourse” and thus allows an unsecured claim even where the debtor has no personal liability, does not prevent the owners of the debtor from contributing sufficient capital to meet the “fresh capital” exception to the absolute priority rule. Of course, the secured creditor might then elect the application of section 1111(b)(2), which requires the debtor to treat the entire claim as “a secured claim to the extent that such claim is allowed.” Instead of two separate claims, one secured and one unsecured, the creditor will have a single secured claim. The plan must then meet the requirements of section 1129(b)(2)(A)(i), which sets the minimum standard that a plan must meet to be fair and equitable with respect to a secured class. To meet this standard, the plan must provide for payments to the secured creditor in an amount totalling at least the amount of the secured claim, including that portion that would have been unsecured but for the section 1111(b) election. But while the payments must total the full amount of the claim, the payments may be made over time; and, pursuant to section 1129(b)(2)(A)(i), the *present value* of this stream of payments need not be greater than the “value of [the creditor’s] interest” in the property securing the claim. Thus, in the case where the property is worth \$1 million but the secured creditor has a claim of \$1.5 million, the plan might provide for payment of \$1.5 million over a long

57. Such a “cash out” of the secured creditor was allowed in *In re Greystone III Joint Venture*, *supra* note 51. The *Greystone* court confirmed a plan in which the debtor paid only three percent (3%) of both the trade debt and the separately classified deficiency claim.

58. See *supra* notes 7-8 and accompanying text.

period of time at a low rate of interest; the rate may be so low that the present value of the income stream is only \$1 million.

This is an imperfect protection for the secured creditor, because it seems to rest on a presumption that the property will be sold before the conclusion of the plan term, requiring the debtor to pay the full face amount of the indebtedness. If, instead, the debtor retains the property for the full term of the plan, then the creditor has been "cashed out" by payments which, calculated to their present value at confirmation, do not exceed the value of the property at that time. Despite the intent of section 1111(b), such a creditor has not received any of the post-confirmation appreciation in the value of the property. A related problem is that section 1111(b) does not provide that the debtor's obligation shall not be assumable. Thus, the debtor might sell the property at a substantial profit, retaining the proceeds for itself and leaving the secured creditor with a low interest long-term loan. There does not appear to be any reported case in which such an attempt has been addressed, but the court faced with such a plan should remember that section 1129(b)(2)(A) states only a minimum requirement, not a definition of "fair and equitable." Thus the secured creditor may argue that even though such a "cash out" meets the literal terms of sections 1111(b) and 1129(b)(2), it would not be fair and equitable to allow the debtor to retain all of the post-confirmation appreciation in the value of the property.

E. *Bankruptcy Code Section 1129(a)(10): The Requirement for a Single Consenting Class*

Bankruptcy Code section 1129(a)(10) requires that so long as any class of claims is impaired, the plan may not be confirmed unless "at least one class of claims that is impaired under the plan has accepted the plan, determined without including any acceptance of the plan by any insider." This section requires a minimum level of acceptance for all plans of reorganization. The requirement that at least one class of impaired claims vote to accept the plan cannot be cured by a reliance on section 1129(b); absent the approval of at least one class of impaired claims, the bankruptcy court has no authority to confirm the plan even if it does not discriminate unfairly and is fair and equitable with respect to all classes of creditors.⁵⁹ This provision creates a problem for some single asset debtors, where the debtor has only a single secured creditor and either negligible or no noninsider unsecured debt. As a result of section

59. See L. KING, COLLIER ON BANKRUPTCY §1129.02 (15th ed. 1979).

1129(a)(10), a lone noninsider creditor possesses an "absolute veto power" over the confirmation of a Chapter 11 plan of reorganization.⁶⁰

A single asset debtor may plan its filing so as to leave at least some unsecured trade creditors to form a consenting impaired class. But if the secured creditor is left with any unsecured deficiency, the secured creditor may cause the unsecured class to vote to reject the plan.⁶¹ With this in mind, some debtors have sought to classify the unsecured trade debt separately from the unsecured deficiency claim, in order to create a small impaired but accepting class. Bankruptcy Code section 1122(a) allows claims to be classified together only if the claims are "substantially similar," but the statute does not require the converse, that is, that all "substantially similar" claims be classified together. Some courts have thus allowed separate classifications of unsecured claims, even when done to create an accepting impaired class, so long as the plan does not "unfairly discriminate" against either class.⁶² Other courts have broadly disapproved of such separate classifications.⁶³

An impaired accepting class may not be created out of the equity interests in the debtor, even if they reject all or a part of their equity interests and thereby become impaired. This was rejected as a second attempt to comply with section 1129(a)(10) in *In Re Pine Lake Village Apartment Co.*,⁶⁴ where again the court refused to confirm the plan. As the court explained, section 1129(a)(10) requires one accepting impaired class of *claims*; the interests of limited partners or other owners of the debtor do not constitute "claims" as they are defined in the Bankruptcy Code.⁶⁵ A related issue, which does not seem to have been addressed in any reported decision, is whether an impaired accepting class may be created out of a *de minimus* amount of unsecured debt. One may question, for example, whether a class of unsecured trade debt of, say, \$5,000,

60. *In re Gagel & Gagel*, 30 Bankr. 627, 629, (Bankr. S.D. Ohio 1983). See also *In re Anderson Oaks (Phase I) Ltd. Partnership*, 77 Bankr. 108, 111-12 (Bankr. W.D. Tex. 1987).

61. This assumes that the secured creditor has not elected, pursuant to Bankruptcy Code section 1111(b), to have its entire claim treated as a single secured claim. Needless to say, a secured creditor may choose to forego such election for the purpose of casting a vote against the plan in the unsecured class.

62. See *In re 222 Liberty Assoc.*, 108 Bankr. 971, 989-90 (Bankr. E.D. Pa. 1990); *In re Grey-stone III Joint Venture*, 102 Bankr. 560, 566-72 (Bankr. W.D. Tex. 1989), *aff'd*, No. A-89-CA-667 (D.C.W.D. Tex. 1990) (appeal filed); *In re Ag Consultants Grain Div., Inc.*, 77 Bankr. 665 (Bankr. N.D. Ind. 1987).

63. See *In re Waterways Barge Partnership*, 104 Bankr. 776, 783-86 (Bankr. N.D. Miss. 1989); *In re Pine Lake Village Apartment Co.*, 19 Bankr. 819, 831 (Bankr. S.D.N.Y. 1982) (refusing to allow such "gamesmanship in vote getting").

64. 21 Bankr. 478, 480 (Bankr. S.D.N.Y. 1982).

65. *Id.* See Bankruptcy Code §§ 101(4), (16), 11 U.S.C. §§ 101(4), (16) (1988).

could constitute an "accepting class" under section 1129(a)(10) in the face of a secured claim in the amount of \$1 million.

IV. CONCLUSION

Confirming a plan of reorganization in a single asset Chapter 11 case is no easy task. The debtor must overcome substantial obstacles to demonstrate feasibility, to convince the court that the plan is fair and equitable as to dissenting impaired creditors, and in some cases even to establish a consenting class of creditors. It is not surprising, therefore, that non-consensual confirmed plans in such cases are rare. In many cases, however, Chapter 11 provides the breathing spell and the framework for negotiations that makes it possible for the debtor to reach agreement with its creditors.