SURVEY OF TEXAS BANKRUPTCY COURT OPINIONS ADDRESSING THE APPLICABILITY OF *TILL* IN CHAPTER 11 CASES

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I. Overview

This paper is presented as an accompaniment to the June 1, 2011 presentation of Kevin Lippman, of Munsch Hardt Kopf & Harr, P.C., and Paul French of Lain, Faulkner & Co., P.C., before the Bankruptcy and Commercial Law Section of the Dallas Bar Association. The purpose of this paper is to summarize—not analyze—the United States Supreme Court plurality decision of *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004), and the relevant Courts of Appeal and Texas bankruptcy court decisions[1] addressing *Till*'s applicability in the context of Chapter 11 cases.

II. *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004)

In order to identify the appropriate cramdown rate of interest which allows a secured creditor to receive the "present value" of its claim through a stream of payments proposed in a plan, such analysis must necessarily begin with the Supreme Court's plurality opinion in *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004). *Till* represents the Supreme Court's effort to identify the methodology that should be utilized by courts in calculating an appropriate interest rate in Chapter 13 cramdown situations involving a secured creditor. Beyond Chapter 13, however, *Till* arguably provides guidance in other situations—including instances of cramdown arising in Chapter 11 cases—where a secured creditor is entitled to the "value" of its claim as of a date certain, but the debtor instead proposes to satisfy the creditor's claim through a stream of future payments.

In *Till*, the Supreme Court was faced with the specific issue of determining "the proper method . . . for discounting deferred payments to present value and what compensation the creditor is entitled to in calculating the appropriate discount rate of interest." *Till*, 541 U.S. at 486 (Thomas, J., concurring). Presented with the statutory language of section 1325(a)(5)(B)(ii) of the bankruptcy Code—commonly known as the cramdown provision of Chapter 13—and noting that "[p]lans that invoke the cramdown power often provide for installment payments over a period of years rather than a single payment[,]" the Supreme Court concluded that "[i]n such circumstances, the amount of each installment must be calibrated to ensure that, over time, the creditor receives disbursements whose total present value equals or exceeds that of the allowed claim." *Id.* at 469.

In *Till*, the Chapter 13 debtors had purchased and financed, prepetition, a used truck at an annual interest rate of 21%. *Id.* at 470. As of the commencement of the debtors' case, the debtors' owed $4,894.89 to the lender, SCS Credit Corporation, on the truck. *Id.* The debtors and SCS agreed, however, that the truck was worth only $4,000, leaving SCS undersecured. *Id.* The debtors' proposed plan provided that the debtors would submit their future earnings to the supervision and control of the bankruptcy court for a period of three years. *Id.* at 471. In addition, the debtors proposed to pay interest on the secured portion of SCS' claim at 9.5% per year. *Id.* The debtors "arrived at this 'prime-plus' or 'formula rate' by augmenting the national prime rate of approximately 8% (applied by banks when making low-risk loans) to account for the risk of nonpayment posed by borrowers in [the debtors'] position." *Id.* SCS objected to the 9.5% rate proposed by the debtors, arguing instead that it was entitled to a 21% interest rate "'which [was] the rate . . . it would obtain if it could foreclose on the vehicle and reinvest the proceeds in loans of equivalent duration and risk as the loan' originally made to [debtors]." *Id.*

[1] At the time of completion of this paper, there were no published decisions of the courts of the Southern District of Texas or the Western District of Texas addressing the applicability of *Till* in Chapter 11 cases.

As the debtors' case progressed through the bankruptcy court, the district court and the Seventh Circuit Court of Appeals on its way to the Supreme Court, four different methodologies for determining the appropriate cramdown interest rate were considered. *See id.* at 469. In analyzing which of the four approaches for determining the cramdown interest rate was appropriate, the plurality in *Till* began as follows:

> The Bankruptcy Code provides little guidance as to which of the rates of interest advocated by the four opinions in this case-the formula rate, the coerced loan rate, the presumptive contract rate, or the cost of funds rate-Congress had in mind when it adopted the cramdown provision. That provision, 11 U.S.C. § 1325(a)(5)(B), does not mention the term "discount rate" or the word "interest." Rather, it simply requires bankruptcy courts to ensure that the property to be distributed to a particular secured creditor over the life of a bankruptcy plan has a total "value, as of the effective date of the plan," that equals or exceeds the value of the creditor's allowed secured claim-in this case, $4,000.

Id. at 473-74. Noting the difficulty in analyzing whether a plan proposing a stream of payments over time does, in fact, provide a secured creditor with the value of its allowed claim as of the effective date of the plan, the Supreme Court stated that:

> A debtor's promise of future payments is worth less than an immediate payment of the same total amount because the creditor cannot use the money right away, inflation may cause the value of the dollar to decline before the debtor pays, and there is always some risk of nonpayment. The challenge for bankruptcy courts reviewing such repayment schemes, therefore, is to choose an interest rate sufficient to compensate the creditor for these concerns.

Id. at 474. The Supreme Court identified three important considerations governing the choice of an appropriate cramdown interest rate. *Id.* As these three considerations provided the analytical framework for the Supreme Court's decision as to which methodology would produce the appropriate cramdown interest rate, it is important that any party faced with a *Till* situation have a complete understanding of the Supreme Court's thought process. The Supreme Court began by stating as follows:

> First, the Bankruptcy Code includes numerous provisions that, like the cramdown provision, require a court to "discoun[t] . . . [a] stream of deferred payments back to the[ir] present dollar value," to ensure that a creditor receives at least the value of its claim. **We think it likely that Congress intended bankruptcy judges and trustees to follow essentially the same approach when choosing an appropriate interest rate under any of these provisions**. Moreover, we think Congress would favor an approach that is familiar in the financial community and that minimizes the need for expensive evidentiary proceedings.

Id. at 474-75 (internal citation omitted; emphasis added). The Supreme Court continued by stating:

> Chapter 13 expressly authorizes a bankruptcy court to modify the rights of any creditor whose claim is secured by an interest in anything other than "real property that is the debtor's principal residence." Thus, in cases like this involving secured interests in personal property, the court's authority to modify the number, timing, or amount of the installment payments from those set forth in the debtor's

> original contract is perfectly clear. Further, the potential need to modify the loan terms to account for intervening changes in circumstances is also clear: On the one hand, the fact of the bankruptcy establishes that the debtor is overextended and thus poses a significant risk of default; on the other hand, the postbankruptcy obligor is no longer the individual debtor but the court-supervised estate, and the risk of default is thus somewhat reduced.

Id. at 475 (internal citation omitted). Finally, the Supreme Court noted that

> from the point of view of a creditor, the cramdown provision mandates an objective rather than a subjective inquiry. That is, although § 1325(a)(5)(B) entitles the creditor to property whose present value objectively equals or exceeds the value of the collateral, it does not require that the terms of the cramdown loan match the terms to which the debtor and creditor agreed prebankruptcy, nor does it require that the cramdown terms make the creditor subjectively indifferent between present foreclosure and future payment. Indeed, the very idea of a "cramdown" loan *precludes* the latter result: By definition, a creditor forced to accept such a loan would prefer instead to foreclose. Thus, a court choosing a cramdown interest rate need not consider the creditor's individual circumstances, such as its prebankruptcy dealings with the debtor or the alternative loans it could make if permitted to foreclose. Rather, the court should aim to treat similarly situated creditors similarly, and to ensure that an objective economic analysis would suggest the debtor's interest payments will adequately compensate all such creditors for the time value of their money and the risk of default.

Id. at 476-77 (emphasis in the original).

Based upon the foregoing considerations, the Supreme Court identified the "formula approach" as being the appropriate methodology for determining the cramdown interest rate in the Chapter 13 context. Elaborating on its decision, the Supreme Court described the formula approach as follows:

> Taking its cue from ordinary lending practices, the [formula] approach begins by looking to the national prime rate, reported daily in the press, which reflects the financial market's estimate of the amount a commercial bank should charge a creditworthy commercial borrower to compensate for the opportunity costs of the loan, the risk of inflation, and the relatively slight risk of default. Because bankrupt debtors typically pose a greater risk of nonpayment than solvent commercial borrowers, the approach then requires a bankruptcy court to adjust the prime rate accordingly. The appropriate size of that risk adjustment depends, of course, on such factors as the circumstances of the estate, the nature of the security, and the duration and feasibility of the reorganization plan. The court must therefore hold a hearing at which the debtor and any creditors may present evidence about the appropriate risk adjustment. Some of this evidence will be included in the debtor's bankruptcy filings, however, so the debtor and creditors may not incur significant additional expense. Moreover, starting from a concededly *low* estimate and adjusting *upward* places the evidentiary burden squarely on the creditors, who are likely to have readier access to any information absent from the debtor's filing (such as evidence about the "liquidity

> of the collateral market," . . .). Finally, many of the factors relevant to the adjustment fall squarely within the bankruptcy court's area of expertise.

Id. at 478-79 (citation omitted; emphasis in original).

The Supreme Court rejected each of the "coerced loan", "presumptive contract rate", and "cost of funds" approaches on the grounds that "[e]ach of these approaches is complicated, imposes significant evidentiary costs, and aims to make each individual creditor whole rather than to ensure the debtor's payments have the required present value." *Id.* at 477. Specifically, the Supreme Court rejected the coerced loan approach because it

> requires bankruptcy courts to consider evidence about the market for comparable loans to similar (though nonbankrupt) debtors—an inquiry far removed from such courts' usual task of evaluating debtors' financial circumstances and the feasibility of their debt adjustment plans. In addition, the approach overcompensates creditors because the market lending rate must be high enough to cover factors, like lenders' transaction costs and overall profits, that are no longer relevant in the context of court-administered and court-supervised cramdown loans.

Id. at 477. The Supreme Court similarly rejected the "presumptive contract rate" approach on the grounds that it

> improperly focuses on the creditor's potential use of the proceeds of a foreclosure sale. In addition, although the approach permits a debtor to introduce some evidence about each creditor, thereby enabling the court to tailor the interest rate more closely to the creditor's financial circumstances and reducing the likelihood that the creditor will be substantially overcompensated, that right comes at a cost: The debtor must obtain information about the creditor's costs of overhead, financial circumstances, and lending practices to rebut the presumptive contract rate. Also, the approach produces absurd results, entitling "inefficient, poorly managed lenders" with lower profit margins to obtain higher cramdown rates than "well managed, better capitalized lenders." Finally, because the approach relies heavily on a creditor's prior dealings with the debtor, similarly situated creditors may end up with vastly different cramdown rates.

Id. at 477-78 (internal citation omitted). Finally, the Supreme Court rejected the "cost of funds" approach because

> it mistakenly focuses on the creditworthiness of the *creditor* rather than the debtor. In addition, the approach has many of the other flaws of the coerced loan and presumptive contract rate approaches. For example, like the presumptive contract rate approach, the cost of funds approach imposes a significant evidentiary burden, as a debtor seeking to rebut a creditor's asserted cost of borrowing must introduce expert testimony about the creditor's financial condition. Also, under this approach, a creditworthy lender with a low cost of borrowing may obtain a lower cramdown rate than a financially unsound, fly-by-night lender.

Id. at 478 (emphasis in original).

The Supreme Court found the formula approach to be the most appropriate indicator of the cramdown interest rate in the Chapter 13 context, stating that

> the formula approach entails a straightforward, familiar, and objective inquiry, and minimizes the need for potentially costly additional evidentiary proceedings. Moreover, the resulting "prime-plus" rate of interest depends only on the state of financial markets, the circumstances of the bankruptcy estate, and the characteristics of the loan, not on the creditor's circumstances or its prior interactions with the debtor. For these reasons, the prime-plus or formula rate best comports with the purposes of the Bankruptcy Code.

Id. at 479-80.

Though picking the "prime-plus" formula approach as the appropriate metric for determining cramdown interest rates, the Supreme Court declined to identify a scale of risk adjustment universally applicable to such calculations because that issue was not before the Court. *Id.* at 480. The Supreme Court did note, however, that the bankruptcy court had approved a risk adjustment in the debtors' Chapter 13 case of 1.5%. *Id.* The Supreme Court also noted that other courts had "generally approved adjustments of 1% to 3% . . . ." *Id.* The Supreme Court found, without needing to specify the appropriate rate of risk adjustment, as follows:

> It is sufficient for our purposes to note that, under 11 U.S.C. § 1325(a)(6), a court may not approve a plan unless, after considering all creditors' objections and receiving the advice of the trustee, the judge is persuaded that "the debtor will be able to make all payments under the plan and to comply with the plan." Together with the cramdown provision, this requirement obligates the court to select a rate high enough to compensate the creditor for its risk but not so high as to doom the plan. If the court determines that the likelihood of default is so high as to necessitate an "eye-popping" interest rate, the plan probably should not be confirmed.

Id. at 480-81 (internal citations omitted). Accordingly, the Supreme Court left the risk adjustment factor to the determination of the trial courts. The Supreme Court's decision, as will be seen, *infra*, has led to a somewhat heterogeneous approach to calculation of the risk adjustment factor.

Justice Thomas, in his concurring opinion, disagreed with both the plurality and the dissent's belief that a "debtor-specific risk adjustment" was required to provide a secured creditor with the value, as of the effective date of the plan, of its secured claim. *Id.* at 486. Specifically, Justice Thomas noted that section 1325(a)(5)(B) contained no explicit requirement that the proper interest rate reflect the "risk of nonpayment." *Id.* at 487. Instead, Justice Thomas noted as follows:

> The statute only requires the valuation of the "property to be distributed," not the valuation of the plan (*i.e.*, the promise to make the payments itself). Thus, in order for a plan to satisfy § 1325(a)(5)(B)(ii), the plan need only propose an interest rate that will compensate a creditor for the fact that if he had received the property immediately rather than at a future date, he could have immediately

> made use of the property. In most, if not all, cases, where the plan proposes simply a stream of cash payments, the appropriate risk-free rate should suffice.

Id. After performing his analysis, Justice Thomas agreed with the plurality that the Seventh Circuit's decision should be reversed because the debtors' proposed interest rate of 9.5%—a rate exceeding the risk-free rate—would suffice to provide SCS with the value of its secured claim over the 36-month payout proposed under the terms of the plan. *Id.* at 491.

While *Till* is a Chapter 13 case, dealing with a Chapter 13-specific statute (*i.e.*, section 1325 of the Bankruptcy Code), many courts—including courts in the Fifth Circuit—have relied upon the *Till* opinion in determining the appropriate cramdown interest rate applicable in Chapter 11 cases. As stated by the plurality in *Till*: "[T]he Bankruptcy Code includes numerous provisions that, like the cramdown provision, require a court to 'discoun[t] . . . [a] stream of deferred payments back to the[ir] present dollar value,' to ensure that a creditor receives at least the value of its claim." *Id.* at 474 (internal citation omitted). In footnote 10 (appended to the foregoing language from the *Till* opinion), the Supreme Court gave examples of the "numerous provisions" that require a court to discount a stream of deferred payments back to present dollar value. Among the provisions cited by the Supreme Court were (i) section 1129(a)(7)(a)(ii) of the Bankruptcy Code, which requires that, "[w]ith respect to each impaired class of claims" in a Chapter 11 plan, each holder of a claim in such impaired class "will receive or retain under the plan on account of such claim . . . property of a value, as of the effective date of the plan" equal to or exceeding the value of the creditor's claim, and (ii) section 1129(b)(2)(A)(i)(II), which states that, as one of the ways for a plan to be fair and equitable as to a class of secured claims, "each holder of a claim of such class shall receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan," equal to or exceeding the value of the creditor's claim. Because the Supreme Court found it "likely that Congress intended bankruptcy judges and trustees to follow essentially the same approach when choosing an appropriate interest rate under <u>any</u> of these provisions[,]" *id.* at 474 (emphasis added), it would be logical for one to conclude that *Till* could provide guidance in cramdown situations in Chapter 11 cases—especially in light of the Supreme Court's reference to section 1129(b)(2)(A)(i)(II), the Chapter 11 cramdown provision.

Such reliance on *Till* in the Chapter 11 context does not appear to be unwarranted. After noting the lack of a "Chapter 13 'cram down market rate of interest'" owing to the fact that "every [Chapter 13] cramdown loan is imposed by a court over the objection of the secured creditor," *id.* at 476 n.14, the Supreme Court provided the following *dictum* with respect to Chapter 11 cramdown market rates of interest:

> Interestingly, the same [*i.e.*, that there is no free market of cramdown lenders in the Chapter 13 context] is *not* true in the Chapter 11 context, as numerous lenders advertise financing for Chapter 11 debtors in possession. Thus, when picking a cramdown rate in a Chapter 11 case, it might make sense to ask what rate an efficient market would produce.

Id. (internal citation omitted; emphasis in original). Using this footnote as a guidepost, some courts have endeavored to identify the interest rate produced by a so-called "efficient market" when determining the appropriate cramdown interest rate in Chapter 11 cases. Indeed, it appears that most of the Texas bankruptcy courts addressing Chapter 11 cramdown issues have relied, at least in part, on *Till*'s guiding principles.

III. <u>Circuit Courts of Appeal Opinions Interpreting *Till*</u>

Currently, there are few opinions from the Circuit Courts of Appeal interpreting *Till*. In fact, there are only seventeen Circuit Court of Appeal opinions citing *Till* for any proposition, notwithstanding the fact that *Till* was issued by the Supreme Court roughly seven years ago. Only the Sixth Circuit has issued a published opinion discussing *Till*'s applicability in the Chapter 11 context. Following are brief discussions of the Sixth Circuit's opinion in *Bank of Montreal v. Official Committee of Unsecured Creditors (In re American HomePatient, Inc.)*, 420 F.3d 559 (6th Cir. 2005), as well the Fifth Circuit's opinion in *Drive Financial Services, L.P. v. Jordan*, 521 F.3d 343 (5th Cir. 2008) (Chapter 13 case).

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

In *Bank of Montreal v. Official Committee of Unsecured Creditors (In re American HomePatient, Inc.)*, 420 F.3d 559 (6th Cir. 2005), the Sixth Circuit heard the secured lenders' appeal of the bankruptcy court's conclusion that the appropriate cramdown interest rate for the secured lenders' claims on collateral valued at $250 million was 6.785%. *See Am. HomePatient*, 420 F.3d at 561-62.[2] Based on expert testimony, the bankruptcy court arrived at the 6.785% cramdown interest rate by taking the then-current interest rate on a six-year Treasury note and adding 3.5%. *Id.* at 562. The lenders asserted that the cramdown interest rate should have been 12.16%. *Id.*

As the bankruptcy court's decision was issued in 2003—prior to the Supreme Court's decision in *Till*—the bankruptcy court had applied the Sixth Circuit's "coerced loan" test for determining cramdown interest rates. *Id.* at 565. By the time the case had reached the Sixth Circuit in 2005, though, the *Till* decision had been on file for more than a year.

Addressing the varying viewpoints on *Till*'s applicability in the Chapter 11 context, the Sixth Circuit declined to "blindly adopt *Till*'s endorsement of the formula approach for Chapter 13 cases in the Chapter 11 context." *Id.* at 568. Instead, the Sixth Circuit concluded that it would be more appropriate for a court faced with a Chapter 11 cramdown interest rate determination to

> take [its] cue from Footnote 14 of the [*Till*] opinion, which offered the guiding principle that "when picking a cram down rate in a Chapter 11 case, it might make sense to ask what rate an efficient market would produce." This means that the market rate should be applied in Chapter 11 cases where there exists an efficient market. But where no efficient market exists for a Chapter 11 debtor, then the bankruptcy court should employ the formula approach endorsed by the *Till* plurality. This nuanced approach should obviate the concern of commentators who argue that, even in the Chapter 11 context, there are instances where no efficient market exists.

Id. at 568 (quoting *Till*, 541 U.S. at 476 n.14) (internal citation omitted).

[2] The district court affirmed the bankruptcy court's decision regarding the cramdown interest rate. *Am. HomePatient*, 420 F.3d at 562.

Based on its interpretation of *Till* and its applicability in the Chapter 11 context, the Sixth Circuit ultimately affirmed the bankruptcy court's cramdown interest rate determination, concluding that "[t]he fact that the bankruptcy court utilized the rubric of the 'coerced loan theory' that was criticized in *Till* provides no basis to reverse the bankruptcy court's decision because *Till* pointed out that, if anything, the coerced loan theory '*overcompensates* creditors . . . .'" *Id.* at 569 (emphasis in original).

B. *Drive Financial Services, L.P. v. Jordan*, 521 F.3d 343 (5th Cir. 2008)

In *Drive Financial Services, L.P. v. Jordan,* 521 F.3d 343 (5th Cir. 2008), the Fifth Circuit addressed the issue of what would constitute "the proper rate of interest to be paid on a secured claim that is paid in installments pursuant to a Chapter 13 plan." *Jordan*, 521 F.3d at 345. While *Jordan* is a Chapter 13 case, it is the only reported Fifth Circuit opinion to date addressing *Till*. Accordingly, an analysis of its holding may serve as an indicator of how the Fifth Circuit will address *Till* issues arising in the Chapter 11 context.

In *Jordan*, the debtors purchased a pickup truck prior to the commencement of their Chapter 13 case. *Id.* at 344. The debtors financed the vehicle through Drive Financial at an annual interest rate of 17.95%. *Id.* Thereafter, the debtors filed for Chapter 13 protection and sought to retain possession of the truck. *Id.* Drive Financial's claim was fully secured. *See id.* at 347. The debtors proposed in their Chapter 13 plan to pay Drive Financial's secured claim in installments with interest at the rate of 6%. *Id.* at 344. Drive Financial objected to the debtors' proposed rate of 6%, arguing that it was entitled to interest at the contract rate of 17.95%. *Id.* The debtors and Drive Financial ultimately stipulated that if *Till* were applicable, the "prime-plus" rate advanced in *Till* would be 7.5% *Id.* at 344-45 n.3. The bankruptcy court found *Till* controlling and confirmed the debtors' plan paying Drive Financial's secured claim with interest at the rate of 7.5%. *Id.* at 345.

On direct appeal to the Fifth Circuit, Drive Financial's first argument was that *Till* was superseded by Congress' subsequent enactment of BAPCPA. *See id.* at 347. Specifically, Drive Financial argued that the infamous "hanging paragraph" of section 1325(a)(9) of the Bankruptcy Code made section 506 of the Bankruptcy Code—which "permits a debtor to bifurcate a secured creditor's claim into a secured and an unsecured portion if the value of the collateral is less than the amount of the claim[,]" *id.* at 346—inapplicable to its claim, thereby rendering *Till* "distinguishable because it dealt with a lien-stripped claim." *Id.* at 347. If *Till* was distinguishable, Drive Financial argued, the court should follow its prior precedent which had favored use of the contract rate of interest in cramdown situations. *See id.*

Ultimately, the Fifth Circuit found Drive Financial's argument unpersuasive "because *Till* did not rely upon the fact that the creditor's claim had been bifurcated using section 506." *Id.* Instead, the Fifth Circuit noted that *Till* had "decided what interest rate was required to be paid on an objecting creditor's secured claim to ensure that the creditor receives value for its crammed down claim as required by section 1325(a)(5)(B)." *Id.* The Fifth Circuit concluded that it was facing the exact same issue as *Till*, the only difference being that Drive Financial had a fully secured claim while the lender's claim in *Till* was only partially secured. *Id.* The court found this to be a distinction without a difference, ultimately concluding as follows:

> BAPCPA did not amend the definition of value under section 1325(a)(5)(B), nor did it prohibit bankruptcy courts from altering the contractual terms for secured claims. Since these were the issues decided by *Till*, we hold that Congress did not supercede [sic] *Till* when it passed BAPCPA.

Id. at 347-48.

The Fifth Circuit then addressed the issue of whether *Till* was binding precedent. *Id.* at 348. The court found that the "facts of *Till* are indistinguishable from the facts of this case," but it also noted the fact that *Till* was a plurality decision. *Id.* Taking an extremely cautious approach to the precedential value of *Till*, the Fifth Circuit explained that:

> The Supreme Court has stated that "[w]hen a fragmented Court decides a case and no single rationale explaining the result enjoys the assent of five Justices, 'the holding of the Court may be viewed as that position taken by those Members who concurred in the judgments on the narrowest grounds.'"

Id. at 348 (quoting *Marks v. United States*, 430 U.S. 188 (1977)).

Noting the difference between the plurality's adoption of a "prime-plus" interest rate and Justice Thomas' belief that no risk premium was required under the Bankruptcy Code, Drive Financial argued that the Fifth Circuit was not bound by *Till* as there was "no common denominator on which the five justices agreed[.]" *Jordan*, 521 F.3d at 349. The court disagreed with Drive Financial's arguments for two reasons. First the court found that, because it was "presented with essentially the same facts that the Supreme Court was presented with in *Till*[,]" *stare decisis* mandated that the court decide the case in manner similar to that in *Till*. *See id.* at 349-50. Second, applying the so-called *Marks* test outlined above, "the narrowest grounds would be that the coerced loan or presumptive contract rate approach [could] not be used if they would yield an interest rate higher than the prime-plus approach." *Id*. at 350. As a result, the Fifth Circuit held that "the *Till* plurality's adoption of the prime-plus interest rate approach is binding precedent in cases presenting an essentially indistinguishable factual scenario. To this extent, *Till* is an intervening precedent from the Supreme Court that overrules this circuit's prior precedent of *Smithwick*."[3] *Id.* at 350.

The cautious nature of the *Jordan* opinion may indicate the Fifth Circuit's unwillingness to apply *Till*'s prime-plus approach in cases that are factually distinguishable from *Till*. This certainly raises a great deal of uncertainty as to Chapter 11 cases involving cramdown of a secured creditor.

IV. Northern District of Texas Case Law Interpreting *Till* in the Chapter 11 Context[4]

A. *In re Mirant Corp.*, 334 B.R. 800 (Bankr. N.D. Tex. 2005) (Lynn, J.)

In *In re* Mirant *Corp.*, 334 B.R. 800 (Bankr. N.D. Tex. 2005)—the first major case from the Northern District of Texas addressing *Till*—Judge Lynn discussed *Till*'s applicability in the context of the valuation of a group of Chapter 11 debtors for purposes of confirmation of a plan of reorganization. *See Mirant*, 334 B.R. at 803. In *Mirant*, a conglomeration of equity interest holders and creditors who stood to be "out of the money" absent a favorable interest rate determination on senior priority claims argued that, as a matter of law, "*Till* established a sliding scale of return payable to creditors to satisfy cram down requirements, from prime interest rate to prime plus three." *See id.* at 820. In opposition, the debtors argued that *Till* provided "no guidance for determining the going-concern value of a multi-billion dollar business" like that of the debtors. *Id.*

[3] *Green Tree Fin. Servicing Corp. v. Smithwick (In re Smithwick)*, 121 F.3d 211 (5th Cir. 1997).

[4] The cases appearing hereafter are listed in chronological order by date of opinion.

The court concluded that both sides were wrong. As stated by Judge Lynn:

> *Till* is clearly relevant to a determination of value, not solely in a case in which an interest rate is determined. Because *Till* instructs what return a secured creditor is entitled to for cram down purposes, *Till* effectively determines what cash flow is necessary to satisfy that creditor. Put another way, *Till* addresses, independently of the value of the underlying collateral, the economic characteristics of the obligation that the secured creditor is entitled to receive in a cram down context.

Id. at 821.

Besides instructing what return a secured creditor is to receive, Judge Lynn concluded that

> *Till* instructs how to derive that required return. While *Till* adopts a formula suitable to calculating the interest rate for secured claims in consumer cases, the formula approach remains valid in determining required return for cram down purposes or other obligations. Thus, the formula for determining the present value of unsecured debt or equity securities issued under a plan will be a risk-free rate plus an adjustment for risk; the numbers plugged into the formula and the manner of their selection will vary depending on the character (secured or unsecured, debt or equity) of the underlying obligation.

Id. at 821-22.

As a critical third point, Judge Lynn concluded that

> *Till* makes clear that the market in fact does not properly measure the value of an obligation undertaken in a plan. As noted in *Till*, the advantages of bankruptcy, such as the requirement of a court determination of feasibility, the benefits of court supervision, disclosure requirements and limits on debt are not given sufficient recognition by the market.

Id. at 822. Explaining the foregoing conclusion, Judge Lynn noted that it would be inappropriate to use the market to value the securities of a reorganized debtor—such valuation being the issue before the court—because "'the "taint" of bankruptcy will cause the market to undervalue the securities and future earning capacity of the [d]ebtor.'" *Id.* at 822 n.71 (quoting *In re Exide Techs.*, 303 B.R. 48, 66 (Bankr. D. Del. 2003)).

Rather than be compelled by the market in its determination of the return creditors are entitled to receive in a cramdown situation—essentially a coerced-loan approach—the court concluded instead that

> [i]t makes perfect sense that a debtor's value, creditworthiness and attractiveness as an investment be objectively assessed as of the prospective effective date of a plan. This is achieved by taking a market-accepted risk-free interest rate or rate of return and adding to that a risk premium determined *by the court* based on the specific risks shown by the evidence, in assessing which the court may look to the market at most as an item of evidence, not as a dispositive

> gauge of interest rates the debtor ought to pay or the investment return the debtor ought to provide.

Id. at 822-23 (emphasis in original).

While the court found *Till* valuable in "determining *how* to value" the debtors, it did not read *Till* as "dictating" a return in the prime to prime-plus-three range. *See id.* at 823. Accordingly, for purposes of the *Till* motion before it, the court found that *Till* did "not provide, as a matter of law, a specific range of interest rates required to satisfy unsecured claims pursuant to [Bankruptcy] Code § 1129(b)(2)(B)(ii)." *Id.* at 824.

B. *In re Northwest Timberline Enterprises, Inc.*, 348 B.R. 412 (Bankr. N.D. Tex. 2006) (Jernigan, J.)

In *In re Northwest Timberline Enterprises, Inc.*, 348 B.R. 412 (Bankr. N.D. Tex. 2006), Judge Jernigan addressed the issue of an appropriate cramdown interest rate in a somewhat unorthodox procedural setting. In that case, the court had before it motions for relief from the automatic stay filed by filed by Chevron U.S.A. Inc., the undersecured lender to the debtors. *Northwest Timberline*, 348 B.R. at 415-16. Chevron's claims were secured by substantially all of the debtors' assets—primarily gas stations and convenience stores operated by the debtors. *Id.* at 416. In each of the two debtors' cases, the court found that Chevron was undersecured by approximately $600,000. *Id.* at 417.

Approximately one year after the commencement of the debtors' cases, a Chapter 11 trustee was appointed for the somewhat limited purpose of "helping to find a businesslike resolution for these cases." *Id.* at 418. After approximately another year following the Chapter 11 trustee's appointment, however, the court noted that "no 'businesslike resolution' seem[ed] to have materialized in the cases." *Id.*

In taking up Chevron's stay relief motions, the court noted that the debtors had filed a joint plan of reorganization which contemplated a restructuring of most of the debtors' debt and a $260,000 new equity infusion. *Id.* at 420. Under the terms of the plan, the court discerned that Chevron's secured claims were to be paid through monthly payments at 8% annual interest, with a 25-year amortization and a balloon payment after 7 years. *Id.* at 421 n.13. Deeming the critical issue to the determination of the motions to lift stay to be whether the debtors' proposed plan was confirmable, the court undertook an analysis of whether the debtors' proposed cramdown interest rate of 8% was sufficient to provide Chevron with the present value of its secured claims. *See id.* at 422-23.

Following a lengthy analysis of the evidence offered by both Chevron and the debtors as to the appropriate rate of cramdown interest due on Chevron's claims, the court concluded that the debtors' plan was "patently unconfirmable" because the debtors' proposed 8% interest rate was insufficient. *Id.* at 431. Though faced with a Chapter 11 plan, the court found it "appropriate to start its analysis with regard to the interest rate being offered to Chevron with *Till* . . . ." *Id.* at 431. The court concluded that "if *Till* applies to the case at bar, this court should start with the 8% national prime rate put into evidence in these cases, and then determine what the appropriate adjustment to that rate is, based on the risks and the character of the underlying obligations owed to Chevron." *Id.* at 432. The court, however, noted the uncertainty involving *Till*'s applicability in the Chapter 11 context—especially in light of footnote 14 from *Till* and its indication that it might make sense to reference market data. *See id.* As a result, the court felt compelled to

> take the cue from *Till* and not mechanically apply the "formula approach" in the Chapter 11 cases at bar. Rather, the court here has significant evidence to explore what an efficient market might produce for loans similar to the Chevron loans proposed under the Debtors' plan and, from that, make a determination what the appropriate rate is for Chevron under the Debtors' plan.

Id. at 432. The court offered further insight into its decision-making process by stating as follows:

> This court believes that the correct discount rate for purposes of Section 1129(b)(2) should fairly consider the rate that the market would require debtors to pay for financing the amount of the secured creditor's claim, and the market rate would necessarily take into account *loan-specific and debtor-specific criteria* (*e.g.*, the amount financed, the ratio of the amount financed to the debtor's assets, the debtor's leverage, the debtor's performance history, the industry, *et cetera*). Even if the Debtors in the case at bar had credible and numerous examples of the secured loan interest rates obtained by other Chevron stations/convenience stores coming out of bankruptcy cases, or in the industry generally, these would not fairly take into account *debtor-specific criteria* which should be considered for purposes of Section 1129(b)(2). At the same time, this court does not consider the market rate all-controlling—if there were a ready market of lenders willing to make an exit loan to these Debtors similar to what is proposed for Chevron by these Debtors. The market rate would have to be *efficient* for it to be all controlling. The market might, in fact, too highly assess the risk (or unfairly put a taint on) the debtors coming out of bankruptcy.

Id. at 434 (emphasis in the original). Finding no efficient market for the type of exit loan contemplated under the debtors' plan, the court concluded it "must fall back on" the prime-plus formula advanced in *Till*. *Id.* Based upon the evidence before it, the court concluded that the proper cramdown interest rate payable to Chevron under the terms proposed by the debtors would be 13.75%. *Id.* Concluding that the plan was not confirmable, the court lifted the stay. *Id.* at 436.

C. *In re Sylvan I-30 Enterprises*, 2006 WL 2539718 (Bankr. N.D. Tex. Sept. 1, 2006) (Hale, J.)

In *In re Sylvan I-30 Enterprises*, 2006 WL 2539718 (Bankr. N.D. Tex. Sept. 1, 2006)—the first of three opinions by Judge Hale addressing the applicability of *Till* in the Chapter 11 context—the court was faced with the task of determining the appropriate cramdown interest rate payable on an oversecured creditor's claim. *Sylvan*, 2006 WL 2539718 at *7. The debtor, Sylvan I-30 Enterprises, had entered a loan agreement with Texeco Refining and Marketing, Inc., to borrow funds for the purpose of financing the construction of a gas station. *Id.* at *1. Under the terms of the loan documents, Sylvan was to repay the loan with interest at an adjustable rate.[5] *Id.* Once Sylvan defaulted on the loan, Motiva Enterprises LLC became the holder of the loan. *Id.* Motiva's lien was secured by substantially all of Sylvan's assets, and at the time of the commencement of Sylvan's Chapter 11 case, Motiva held a secured claim for at

[5] According to the court, the adjustable rate was determined by "starting with Citicorp's commercial paper rate and adding a spread of 225 basis points." *Sylvan*, 2006 WL 2539718 at *1.

least $1,918,823. *Id.* at *1. Because the debtor's property was worth approximately $2.2 million, Motiva's claim was deemed fully secured. *Id.* at *2.

Under the terms of its plan, the debtor proposed to pay Motiva's secured claim in full over 15 years with an annual interest rate of 7.55%. *Id.* at *4. At the time of the confirmation hearing on the debtor's plan, however, the contract rate of interest was 8.19%. *Id.* Motiva objected to the debtor's proposed interest rate, offering evidence which the court found "clearly indicated that the marketplace for convenience store and gas station loans does not base such loans on the prime rate of interest. . . . Rather, such loans are generally made on a variable rate tied to a commercial paper rate or a LIBOR rate." *Id.* at *5.

Analyzing the appropriate cramdown interest rate owed Motiva, the court stated as follows:

> In determining the appropriate interest rate to be applied to allowed secured claims under a plan of reorganization, the Supreme Court has expressly rejected the "presumption" that the contract rate is the appropriate interest rate. The Supreme Court's decision in *Till* addressed the proper rate of interest required to be used with regard to payments to secured creditors on a cram down loan under a proposed Chapter 13 plan. However, the *Till* decision, while helpful, may be inapplicable in a Chapter 11 case. In a footnote, the Supreme Court expressly stated that "when picking a cram down rate in a Chapter 11 case, it might make sense to ask what rate an efficient market would produce." The selection of an interest rate for a claim that recognizes the realities of the various transactions entered into by the Debtor is consistent with such approach. In this case there is no evidence that the risk of non-payment or non-performance is any greater now then [sic] it was when the loan was made. The uncontroverted testimony was that Motiva's collateral is much greater in value then [sic] the amount of its debt. In fact the current operations are mirroring those . . . when Motiva was satisfied with less than a 5% rate of interest. The interest rate required of the Debtor prepetition is a fair measure of the market's assessment of the risk associated with dealing with the Debtor. The Court finds that the variable rate in the Agreement and related loan documents provides present value for Motiva. Thus, the variable interest rate provided in the Agreement is the appropriate rate for the payment of Motiva's secured claim.

Id. at *7 (internal citations omitted). Based on the foregoing, the court concluded that the variable rate of interest provided in the contract between the debtor and Motiva was the appropriate cramdown interest rate. *Id.* at *8.

D. ***In re Vinson*, Case No. 09-36728-bjh-11 (Bankr. N.D. Tex. Apr. 29, 2010), (Houser, C. J.)**

In In *re Vinson*, an individual Chapter 11 case, Judge Houser issued an oral ruling confirming the debtors' Chapter 11 plan over the objection of secured creditor Fannie Mae. Transcript of Ruling on Confirmation [#172], *In re Vinson*, No. 09-36728-bjh-11 (Bankr. N.D. Tex. Apr. 29, 2010), ECF No. 183 (hereinafter, "Vinson Transcript"). Though Judge Houser never specifically cited to or mentioned *Till*, she did address the appropriate cramdown interest rate owed to Fannie Mae on its secured claims.

In *Vinson*, the debtors proposed to pay interest on Fannie Mae's secured claims at 6.05% and 6.08%, which were the non-default contract rates of interest on the mortgages securing Fannie Mae's loans. *See* Vinson Transcript at 13. The *Vinson* case presented an unusual situation in that Fannie Mae put on no evidence of what it believed to be the appropriate cramdown interest rate. *Id.* at 10. Instead, Fannie Mae relied on the *Good v. RMR Investments, Inc.*, 428 B.R. 249 (E.D. Tex. 2010) decision out of the Eastern District of Texas (discussed, *infra*) for the proposition that, because the debtors were solvent debtors (*i.e.*, they proposed to pay all creditors in full with interest under their plan), Fannie Mae was entitled to the contract default interest rate of 10%. *Id.* at 13-14.

After reviewing the district court's *Good v. RMR Investments* decision and the underlying bankruptcy court decision in *In re Good*, 413 B.R. 552 (Bankr. E.D. Tex. 2009), *aff'd,* 428 B.R. 249 (E.D. Tex. 2010), Judge Houser concluded that both those decisions were incorrect in using the contract default interest rate as the cramdown interest rate for purposes of section 1129(b). The court noted that the *Dow Corning* case relied on in the decisions from the Eastern District of Texas actually addressed a section 506(b) pendency interest issue—not a section 1129(b) cramdown interest issue. *Id.* at 15-16.

Though finding the debtors' evidence regarding the cramdown interest rates to be less than "robust," Judge Houser concluded that, with regard to the debtors' proposed treatment of their obligations to Fannie Mae, "the proposed terms of this new note do provide a market rate of interest and do provide . . . Fannie Mae with a stream of payments that have a present value equal to Fannie Mae's allowed secured claim." *Id.* at 10, 18. Judge Houser continued by concluding as follows: "I do not believe that the *Dow Corning* rationale or the *Southland Corporation* rationale carries over into the determination of what is a market rate of interest for purposes of cram-down in accordance with Section 1129(b)." *Id.* at 18.

As indicated *supra*, Judge Houser repeatedly referred to the "market rate of interest" in analyzing the cramdown interest rate owed by the debtors. Based on the evidence offered by the debtors, including (i) expert witness testimony that the market rate of interest would be 6% and (ii) a print-out from Fannie Mae's website which showed mortgage rates at approximately the time of the hearing to be 5.07%, the court concluded that the debtors' cramdown interest rate was the market rate of interest. *Id.* at 11-13. Accordingly, the court confirmed the debtors' plan. *Id.* at 19.

E. *In re SJT Ventures, LLC*, 441 B.R. 248 (Bankr. N.D. Tex. 2010) (Hale, J.)

In *In re SJT Ventures, LLC*, 441 B.R. 248 (Bankr. N.D. Tex. 2010)—the second of Judge Hale's opinions interpreting *Till* in the Chapter 11 context—the court addressed the issue of what would constitute "the appropriate rate of post-confirmation interest in a Chapter 11 plan for repayment of an over-secured debt backed by real-property collateral." *SJT Ventures*, 441 B.R. at 249. In *SJT Ventures*, the debtor had purchased a four-story commercial building and financed the purchase through Lehmann Brothers. *Id.* at 250. Lehmann Brothers later transferred the note to Aurora Bank. *Id.* After falling behind on its payments, the debtor filed for Chapter 11 protection. *Id.*

At the time of the confirmation hearing on the debtor's Chapter 11 plan, the building was valued at approximately $2.3 million. *Id.* Aurora's allowed secured claim was approximately $1.9 million, thereby yielding a loan-to-value ratio of approximately 82%. *Id.* at 250-51. At the confirmation hearing on the debtor's plan, the debtor proposed paying Aurora's claim at a 6.35% interest rate, amortized over 30 years, with a balloon payment to be made after 5 years. *See id.* at 250. Aurora objected to the debtor's proposed interest rate, arguing that it was instead entitled to the contract rate of interest of 8.69%. *Id.*

In support of its argument that it was entitled to the contract rate of interest, Aurora cited the Bankruptcy Court for the Eastern District of Texas' decision of *In re Good*, 413 B.R. 552 (Bankr. E.D. Tex. 2009), *aff'd,* 428 B.R. 249 (E.D. Tex. 2010) (discussed, *infra*). Like Judge Houser in *Vinson*, Judge Hale indicated an unwillingness to follow *Good*, as that case relied on Sixth Circuit case law addressing pendency interest—*i.e.*, interest assessed post-petition but pre-confirmation. *See id.* at 252. Instead, noting the Fifth Circuit's holding in *Jordan* that "*Till* forecloses the presumption that the contract interest rate automatically applies post-confirmation" and Judge Jernigan's "preference for a 'market based approach'" in determining cramdown interest rates, *see id.* at 252, Judge Hale concluded that, in the case before him, "a 'market rate,' based on a calculation indicative of the ordinary practices of commercial real-estate lenders in the area," was the appropriate metric for determining the cramdown interest rate due Aurora. *Id.* at 253.

Following a lengthy discussion of *Till*'s applicability in the Chapter 11 context, the court agreed "that the reasoning in *Till* applies to the basic concept of calculation of the 'present value' of secured debt for the purposes of § 1129(b)." *Id.* at 255. The court based this conclusion partly on the idea that to "require that debtors repay secured creditors at the contract interest rate going forward from confirmation would often impede successful reorganization in a staggering percentage of cases." *Id.* The court did caution against a rigid application of the prime-plus, or formula, rate adopted by the Supreme Court in *Till*, stating that "[t]o blindly apply the formula from *Till* in the present commercial lending context, beginning with the Prime rate and adding in a percentage for risk, would be . . . to use a starting point that 'no one speaks in terms of.'" *Id.*

Noting that useful guidance in determining the present value of a secured interest can be derived from the market "[w]here there is an established and efficient market, as in the case of oversecured commercial real estate lending," the court noted that it "must seek out the approach that will most fairly and accurately account for the characteristics of the debtor and the market value of the creditor's claim." *Id.* Upon this rationale, the court held that, "with regard to oversecured commercial loans, this Court will employ the formula ordinarily used by the market to derive the appropriate interest rate." *Id.* The court found that "[e]mploying such a 'market formula' will achieve the Supreme Court's underlying purpose in *Till* of ensuring that secured creditors are compensated for the 'time value of their money and the risk of default' by way of an objective assessment, while at the same time employing the on-the-ground insight of an effective market, where it exists." *Id.*

Based upon expert testimony presented by the debtor, the court ultimately concluded that the debtor's proposed interest rate, which was based on the daily 5-year Treasury Bill rate with an additional "spread" tied to the loan-to-value ratio, was the appropriate calculus for determining the cramdown interest rate owed to Aurora on its secured claim. *See id.* at 255-56.

F. *In re Maluhia Eight, LLC*, 2010 WL 4259832 (Bankr. N.D. Tex. Oct. 22, 2010) (Hale, J.)

In *In re Maluhia Eight, LLC*, 2010 WL 4259832 (Bankr. N.D. Tex. Oct. 22, 2010) (slip opinion), Judge Hale again addressed the issue of the proper cramdown rate of interest owed to slightly oversecured creditors whose claims were secured by real property in Hawaii. *Maluhia Eight*, 2010 WL 4259832 at *2. Though the full terms of the debtors' proposed payment of the secured creditors' claims were not set forth in the opinion, it is clear that the debtors proposed a "pay and accrue" interest scheme whereby the lender would receive a 4% interest payment on their claims with an additional 1% interest to be paid at final payout. *Id.* at 3. The secured creditors instead sought a cramdown interest rate akin to the "junk bond" rate. *Id.* at 1. The court found the "junk bond" rate proposed by the secured creditors to be too high, but the court also found the debtors' proposed "4+1" rate to be too low based on the approach taken in *Till. Id.* at *3. The court, without much discussion, instead found that a proper cramdown rate of interest for the type of loan involved would be "around 7%," based on the five-year treasury rate and an additional risk premium. *Id.* Based in part on this higher cramdown interest rate, the court concluded that the debtors' plan was not feasible and denied confirmation. *See id.* at *4-5.

G. *In re Texas Grand Prairie Hotel Realty, LLC*, Case No. 10-43242-rfn-11 (Bankr. N.D. Tex. Apr. 28, 2011)

In *In re Texas Grand Prairie Hotel Realty, LLC*, Judge Nelms issued oral findings and conclusions in support of his order confirming the debtors' Chapter 11 plan of reorganization.[6] Transcript of Ruling on Modified Chapter 11 Plan [#294], *In re Tex. Grand Prairie Hotel Realty, LLC*, No. 10-43242-RFN-11 (Bankr. N.D. Tex. Apr. 28, 2011), ECF No. 306 (hereinafter, "TGP Transcript"). The debtors owned and operated four hotels in the state of Texas. *See* TGP Transcript at 13. The secured lender was undersecured by collateral valued at approximately $39 million. *See id.* at 26. Under the terms of the debtors' plan, the lender's secured claim would be amortized over 20 years and repaid over a term of 7 years with a cramdown interest rate of 5%. *See id.* at 22-23, 29. While the secured lender did not argue that *Till* was inapplicable in the Chapter 11 context, *see id.* at 21, it nevertheless asserted that the appropriate cramdown interest rate should be 9.45%.

In determining the appropriate cramdown interest rate, Judge Nelms stated that "*Till* is instructive, if not controlling, in Chapter 11 cases." *Id.* However, Judge Nelms expressed his concern that too much attention was being placed on the *dictum* of footnote 14 offered by the plurality in *Till*. *See id.* at 21-22. As to the applicability of *Till* in the Chapter 11 context, Judge Nelms concluded as follows:

> In my opinion, evidence of what rate an efficient market would produce is not required by *Till*. Instead, *Till's* ruling, and the only one that caused it to enjoy a majority, is as follows, and I quote: "The court should aim to ensure that an objective economic analysis would suggest that the debtor's interest payments will adequately compensate all creditors for the time value of their money and the risk of default."

Id. at 22. Disagreeing with the contention of the lender's expert that the market should be consulted, Judge Nelms concluded as follows:

> I don't think that *Till* can be construed to require the Court to determine what rate an efficient market would produce. This is because that rate includes factors such as the lender's profit, the lender's expenses, and not only that particular lender's but other lenders' subjective analysis of risks. Those should not form any part of a *Till* analysis.

Id. at 23. The lender's expert conceded that no market existed for the type of loan being made under the debtors' plan; however, the lender's expert asserted that the market should be

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[6] The debtors are represented by the law firm of Munsch Hardt Kopf & Harr, P.C.

consulted for the type of loan nearest that proposed in the plan, with a debtor-specific adjustment made thereafter. *See id.* at 23-24. Judge Nelms rejected that assertion, stating:

> I disagree with that approach because it establishes a benchmark before adjustment that I just view to be completely inconsistent with *Till*. *Till* set that benchmark at national prime, but according to [the lender's expert], you first determine what level any portion of a loan would be financeable, and then you begin to work from there. So if we were to place that analysis in the context of *Till*, which involved a car loan, what you would do is, let's say where a Chapter 13 debtor owes $4,000 and the car is worth $4,000, [the lender's expert] would say that there's no conventional financing for that loan. But there are perhaps payday lenders who might loan $2,000 at 12 percent, so the benchmark is 12 percent, and then you add a substantial risk premium to account for the risk that the other $2,000 represents.
>
> The Court finds no support for that type of analysis in *Till*. If anything, this strikes the Court as more in the nature of a forced loan approach that the majority in *Till* expressly rejected.

Id.

Finding the debtors' expert's testimony persuasive and in line with *Till*, the court approved the debtors' proposed cramdown interest rate of 5%, representing the prime rate of 3.25% plus a 1.75% debtor-specific risk adjustment. *Id.* at 22-23.

The lender has appealed the confirmation order to the United States District Court for the Northern District of Texas.

V. <u>Eastern District of Texas Case Law Interpreting *Till* in the Chapter 11 Context</u>

A. ***In re Good*, 413 B.R. 552 (Bankr. E.D. Tex. 2009) (McGuire, J.), *aff'd*, 428 B.R. 249 (E.D. Tex. 2010) (Schell, J.)**

In *In re Good*, 413 B.R. 552 (Bankr. E.D. Tex. 2009), *aff'd*, 428 B.R. 249 (E.D. Tex. 2010), the bankruptcy court dealt with the provisions of a Chapter 11 joint plan of reorganization for a number of entities affiliated with real estate developer Kenneth Good. *Good*, 413 B.R. at 553. Under the joint plan, the debtors proposed to pay all creditors in full over a period of four years. *Id.* At the conclusion of the four years, the debtors anticipated holding a surplus of $85 million in cash. *Id.*

Prior to filing for Chapter 11 protection, one of the debtors, LCI, had entered into a loan agreement with RMR Investments, Inc., whereby RMR loaned $7,860,000 to LCI. *Id.* at 553. The RMR loan was secured by a deed of trust granting RMR a first priority security interest in a parcel of land. *Id.* at 554. The rate of interest on the loan was the higher of the prime rate plus 2.75% or 11% per annum. *Id.* at 554. Upon an event of default, the rate of interest would increase by 4%. *Id.* As of LCI's petition date, the principal balance owed to RMR was $7,760,000. *Id.* Because the land securing RMR's note was valued between approximately $9.8 million and $12 million, there was no dispute that RMR was oversecured. *See id.* at 554-55. Furthermore, there was no dispute that LCI was solvent or that it had defaulted on its contractual obligations to RMR. *Id.* at 559.

RMR objected to LCI's plan on multiple grounds, including that the plan failed to treat RMR's secured claim fairly and equitably as required under the absolute priority provisions of section 1129(b)(2). *See id.* at 555-56. Specifically, RMR contested LCI's proposed cramdown interest rate of prime plus 1%[7] (or such rate as determined by the bankruptcy court at the confirmation hearing). *Id.* at 555, 558. Noting that a number of similarly situated creditors had agreed to post-confirmation interest rates totaling between 5% and 6% under the plan, the bankruptcy court concluded that a rate of prime plus 2% would satisfy the requirement that the debtor's plan be fair and equitable. *See id.* at 555-56. Ultimately, the bankruptcy court (Judge Rhoades) confirmed LCI's plan. *Id.* at 556.

On RMR's motion for reconsideration, Judge McGuire, sitting in the absence of Judge Rhoades, framed the issue before him as being "whether, as a matter of law, RMR is entitled to receive its contractual default rate of interest from LCI rather than the Plan Rate as determined by the Court." *Id.* at 558. Relying upon the Sixth Circuit's decision in *In re Dow Corning Corp.*, 456 F.3d 668 (6th Cir. 2006), Judge McGuire noted that "[i]n cases involving solvent debtors, courts 'have overwhelmingly concluded that there is a presumption that the default interest rate should be allowed.'" *Id.* at 559 (quoting *Dow Corning*, 456 F.3d at 680). Judge McGuire continued by noting that:

> "In this context, the rational [sic] for use of the contract rate is straightforward: A debtor with the financial wherewithal to honor its contractual commitments should be required to do so. The only good reason for refusing to give a creditor in reorganization all that he bargained for when he extended credit is to help other creditors, the debtor's assets being insufficient to pay all creditors in full."

Id. at 559 (quoting *In re Dow Corning Corp.*, 244 B.R. 678, 695 (Bankr. E.D. Mich. 1999)) (internal citation omitted). Because there was "no dispute that LCI was in default of its contractual obligations to RMR when it filed for bankruptcy protection, that LCI [was] solvent, or that RMR [was] oversecured[,]" Judge McGuire concluded that "under the circumstances of this case, LCI failed to rebut the presumption that RMR is entitled to interest at the contractual default rate of 15% per annum." *Id.* at 560. Accordingly, with respect to the cramdown rate of interest payable to RMR, the court granted RMR's motion for reconsideration. *Id.* at 561.

Following the bankruptcy court's decision on RMR's motion for reconsideration, the debtor, LCI, filed its own motion for reconsideration. *Good v. RMR Investments, Inc.*, 428 B.R. 249, 250 (E.D. Tex. 2010). In its motion, LCI argued, *inter alia*, that it was no longer solvent and that there was no manifest error in the bankruptcy court's original order confirming the plan and the cramdown interest rate of prime plus 2%. *See id.* at 252. The bankruptcy court denied LCI's motion for reconsideration, and LCI appealed the bankruptcy court's conclusion that the "proper rate of 'cramdown' interest payable by LCI to RMR [was] the pre-petition default interest rate." *Id.* at 252.

Noting that "[a] bankruptcy court's calculation of an appropriate 'cramdown' interest rate for purposes of Chapter 11 plan modification is a question of fact reviewed for clear error[,]" the court concluded that "the bankruptcy court's determination of the postconfirmation interest rate should be upheld unless it strikes this court as dead wrong or completely outside the range of permissible conclusions." *Id.* at 253. In reviewing the bankruptcy court's calculation of the cramdown interest rate, the district court noted the Fifth Circuit's unwillingness to adopt a specific formula for the calculation of the post-confirmation interest rate. *Id.* at 253-54.

[7] This rate that would have totaled 4.25% at the time of confirmation.

Focusing on the case-by-case and fact-specific nature of risk levels associated with determining a cramdown interest rate, the district court stated as follows:

> Because risk analysis involves the weighing of witness' testimony, demeanor and credibility, the Fifth Circuit has declined to "tie the hands of lower courts as they make the factual determination involved in establishing an appropriate interest rate." Therefore, absent clear error, the bankruptcy court's determination will not be disturbed.

Id. at 254 (quoting *Fin. Sec. Assurance Inc. v. T-H New Orleans Ltd. P'ship (In re T-H New Orleans Ltd. P'ship)*, 116 F.3d 790, 800 (5th Cir. 1997)) (internal citations omitted). The district court further found that the bankruptcy court had "rightly relied upon Fifth Circuit precedent which permits bankruptcy courts to determine the appropriate rate of cramdown interest based on circumstances of the debtor and creditor in a particular case." *Id.*

The district court took notice that the bankruptcy court had based its decision to apply the default contract rate of interest upon the facts that (i) LCI was in default of its contractual obligations at the time it commenced its bankruptcy case, (ii) LCI was solvent, (iii) RMR was oversecured, (iv) payment of interest at the default contract rate would not reduce payments to any other creditors under the plan, and (v) payment of interest and the default contract rate would only reduce the equity available to the debtors at the conclusion of the case. *Id.* Based on the bankruptcy court's factual findings, the district court concluded that the bankruptcy court had not erred in applying the default contract rate of interest to the calculation of the cramdown interest rate payable by the debtor to RMR. *Id.* at 255.

The district court specifically rejected the debtor's argument that *Till* required the application of the prime-plus formula approach in calculating the cramdown interest rate. First, relying on footnote 14 to the *Till* opinion, the court found that while "[t]his footnote suggests that . . . the formula approach may be applied in the Chapter 11 context, its application is not required." *Id.* at 255. Second, relying on the Fifth Circuit's decision in *Jordan*, the district court concluded that

> even if this court were to ignore the implications of footnote 14, *Till* is a plurality opinion and therefore does not necessarily reflect the rule for calculating cramdown interest in all circumstances. In [*Jordan*], the Fifth Circuit only narrowly adopted the formula approach for Chapter 13 cases, noting: "[the] *Till* plurality's adoption of the prime-plus interest rate approach is binding precedent in cases presenting an essentially indistinguishable factual scenario." Therefore, in the Fifth Circuit, bankruptcy courts still enjoy some latitude in determining which method should be applied to determine the cramdown interest rate in Chapter 11 cases.

Id. at 255 (quoting *Jordan*, 521 F.3d at 350) (internal citations omitted).

Because *Good* presented an atypical factual scenario—*i.e.*, one involving a solvent debtor—it may be best to limit *Good*'s conclusion to the facts of that case. Nevertheless, parties practicing in the Eastern District of Texas should be aware of *Good* and its conclusions.