23-BK-F

May 18, 2023

Submitted Via Email to: RulesCommittee_Secretary@ao.uscourts.gov

Judicial Conference of the United States
Committee on Rules of Practice and Procedure
Advisory Committee on Bankruptcy Rules
Washington, DC 20544

Re: Proposed Amendment of Federal Rule of Bankruptcy Procedure 3018(c)

Ladies and Gentlemen:

The National Bankruptcy Conference ("NBC") is a voluntary, non-partisan, not-for-profit organization composed of about 60 of the nation's leading bankruptcy judges, professors, and practitioners. The NBC has provided advice to Congress regarding bankruptcy legislation for approximately 80 years. We enclose a Fact Sheet providing further information about the NBC.

We write on behalf of the NBC to propose an amendment of Federal Rule of Bankruptcy Procedure 3018(c). We begin by summarizing the problem motivating our proposal and then provide specific proposed language for an amendment that would solve this problem.

Summary of the Problem

Rule 3018 covers acceptance or rejection by creditors of a debtor's plan in a chapter 9 municipality or chapter 11 case. Rule 3018(c), in particular, sets forth rules regarding the form of acceptance or rejection. Voting is a fundamental aspect of the plan process. The acceptance or rejection of a plan by individual creditors or a class of creditors determines, among other things, whether a plan proponent must satisfy the Bankruptcy Code's "cramdown" requirements, which permit a debtor to seek court approval of a plan over the objection of a class that has voted to reject the plan.[1] Voting has even more significance in small business cases under subchapter V of chapter 11 where the debtor is entitled to a materially more favorable postconfirmation arrangement if all impaired classes of creditors accept the plan.[2]

Under the current version of Rule 3018(c), acceptance or rejection of a plan must "be in writing, identify the plan or plans accepted or rejected, be signed by the creditor or equity security holder or an authorized agent, and conform to the appropriate Official Form" (i.e., the official ballot form). Sometimes a class of creditors fails to vote at all. Courts are split about whether an impaired class of creditors that fails to vote at all can be deemed to accept the plan.[3]

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1 *See* 11 U.S.C. §§ 1129(a)(8) & (b)(1), 943(b).

2 *See id.* §§ 1191(a)-(b), 1183(c)(1), 1186(a), 1192, 1193(b)-(d), 1194(b).

3 *See, e.g.*, American Bankruptcy Institute Commission to Study the Reform of Chapter 11, *Final Report and Recommendations*, 23 AM. BANKR. INST. L. REV. 1, 268-71 (2015) (discussing split in the case law—largely revolving around agreement or disagreement with *Heins v. Ruti-Sweetwater, Inc. (In re Ruti-Sweetwater, Inc.)*, 836 F.2d 1263 (10th Cir. 1988)—and ultimately concluding "that the better rule is to prohibit a plan from providing for 'deemed acceptance' if an impaired class of claims fails to vote on a plan").

In some jurisdictions, then, a class in which no creditor returned a ballot will be a rejecting class, which mandates cramdown of that class (if the debtor wants to proceed with approval of the plan) and, in a subchapter V case, precludes confirmation under Bankruptcy Code section 1191(a).

For whatever reason, several categories of creditors that are repeat players in chapter 11 cases—including the Internal Revenue Service, other federal agencies, and some state and local taxing agencies—have internal policies or practices never or very rarely to return ballots regarding bankruptcy plans, even in scenarios in which those creditors do not oppose or affirmatively support confirmation of a plan.[4] Since these creditors' claims often must be separately classified, their institutional inability or unwillingness to return ballots means that, at least in some jurisdictions, there inevitability will be a rejecting class. This result is particularly problematic in the context of subchapter V debtors—which often are small businesses that owe some overdue federal or state tax—since the rejection of a plan by even one impaired class precludes confirmation under Bankruptcy Code section 1191(a). Subchapter V debtors are thus given a difficult choice between (i) unimpairing a class of creditors that is unable or unwilling to return a ballot (which likely will provide the nonresponsive class with more favorable treatment than impairment coupled with cramdown would, which in turn could have negative implications for the debtor's reorganization) or (ii) accepting the less-favorable track of confirmation under Bankruptcy Code section 1191(b) despite the lack of substantive opposition to the plan by the rejecting-solely-as-a-function-of-its-inaction class. We can think of no policy supporting this construct, particularly in instances when the subchapter V debtor has done everything it should do and negotiated an agreed result with the nonvoting class.

We submit that existing Rule 3018(c) is unduly formalistic in mandating a written ballot as the only possible means of evidencing creditor acceptance of a plan.[5] This rigid requirement creates unnecessary problems for chapter 11 plan proponents—and especially for subchapter V debtors—in scenarios where, as a matter of substance and reality, everyone supports the plan.

Proposed Solution to the Problem

We propose that Rule 3018(c) be amended thusly:

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[4] *See, e.g.*, *In re King Mt. Tobacco Co.*, Case No. 20-01808, ECF No. 629, Audio File at 30:01–33:10 (Bankr. E.D. Wash. Sept. 14, 2022) (counsel for federal Alcohol and Tobacco Tax and Trade Bureau explaining that the agency has an internal "practice" preventing it from returning a ballot regarding a $77,208,411 secured claim, despite the fact that the agency actively negotiated the proposed plan and was urging its confirmation).

[5] The unnecessary formalism of the current rule is illustrated by another common fact pattern. Consider a scenario in which a debtor has proposed a plan that crams down a secured creditor, the secured creditor votes to reject the plan, but the parties then negotiate a revised plan that is presented to the bankruptcy court as a fully-consensual plan shortly before or at the confirmation hearing. As a technical matter under the rules, a motion should be made under Rule 3018(a) to allow the secured creditor to change its ballot (which requires "cause shown" and "notice and hearing") and a revised ballot must thereafter be submitted before Rule 3018(c) acknowledges the secured creditor's acceptance of the revised plan. In our experience, however, these steps are not formalized. Instead, the court will acknowledge the agreement between the parties and approve the plan as a consensual plan without regard to the formalisms required by the current rule.

FORM OF ACCEPTANCE OR REJECTION. An acceptance or rejection shall be in writing, identify the plan or plans accepted or rejected, be signed by the creditor or equity security holder or an authorized agent, and conform to the appropriate Official Form. The court for cause may also permit an acceptance or rejection to be set forth in a statement or representation by counsel to, or an authorized agent of, the creditor or equity security holder that is part of the record of the case, including orally at the confirmation hearing, in a stipulation, or through endorsement of a confirmation order. If more than one plan is transmitted pursuant to Rule 3017, an acceptance or rejection may be ~~filed~~ made by each creditor or equity security holder for any number of plans transmitted and if acceptances are ~~filed~~ made for more than one plan, the creditor or equity security holder may indicate a preference or preferences among the plans so accepted.

This amendment adopts a functional approach whereby acceptance or rejection of a plan may be communicated by methods other than returning a ballot. The amendment solves the problem created when certain creditors (largely governmental units) are unwilling or unable to return ballots and gives the bankruptcy court better and more complete information when all participating creditors support a plan. The amendment protects creditors' interests by requiring an on-the-record affirmative act by creditors or their counsel and a finding of cause before the court can find acceptance of a plan despite the absence of a ballot.[6]

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We urge adoption of the amendment of Rule 3018(c) proposed above or a similar revision of the rule to solve the problem detailed above. Please contact us if we can provide additional information about this proposed amendment.

Sincerely,

Whitman L. Holt

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[6] Rule 3018 applies in both chapter 11 cases and in chapter 9 municipality cases. While we have focused on chapter 11 for illustration, chapter 9 can also present similar scenarios where creditors do not or cannot submit ballots. The more functional rule we propose here would serve a similar purpose in a chapter 9 case and should apply there as well.

National Bankruptcy Conference

A non-profit, non-partisan, self-supporting organization of approximately sixty lawyers, law professors and bankruptcy judges who are leading scholars and practitioners in the field of bankruptcy law. Its primary purpose is to advise Congress on the operation of bankruptcy and related laws and any proposed changes to those laws.

History. The National Bankruptcy Conference (NBC) was formed from a nucleus of the nation's leading bankruptcy scholars and practitioners, who gathered informally in the 1930's at the request of Congress to assist in the drafting of major Depression-era bankruptcy law amendments, ultimately resulting in the Chandler Act of 1938. The NBC was formalized in the 1940's and has been a resource to Congress on every significant piece of bankruptcy legislation since that time. Members of the NBC formed the core of the Commission on the Bankruptcy Laws of the United States, which in 1973 proposed the overhaul of our bankruptcy laws that led to enactment of the Bankruptcy Code in 1978, and were heavily involved in the work of the National Bankruptcy Review Commission (NBRC), whose 1997 report initiated the process that led to significant amendments to the Bankruptcy Code in 2005. Most recently, the Conference played a leading role in developing the Small Business Reorganization Act of 2019, Pub. L. 116-54.

Current Members. Membership in the NBC is by invitation only. Among the NBC's 60 active members are leading bankruptcy scholars at major law schools, as well as current and former judges from eleven different judicial districts and practitioners from leading law firms throughout the country who have been involved in most of the major corporate reorganization cases of the last three decades. The NBC includes leading consumer bankruptcy experts and experts on commercial, employment, pension, mass tort, and tax-related bankruptcy issues. It also includes former members of the congressional staff who participated in drafting the Bankruptcy Code as originally passed in 1978 and former members and staff of the NBRC. The current members of the NBC and their affiliations are set forth on the second page of this fact sheet.

Policy Positions. The Conference regularly takes substantive positions on issues implicating bankruptcy law and policy. It does not, however, take positions on behalf of any organization or interest group. Instead, the NBC seeks to reach a consensus of its members - who represent a broad spectrum of political and economic perspectives - based on their knowledge and experience as practitioners, judges, and scholars. The Conference's positions are considered in light of the stated goals of our bankruptcy system: debtor rehabilitation, equal treatment of similarly situated creditors, preservation of jobs, prevention of fraud and abuse, and economical insolvency administration. Conferees are always mindful of their mutual pledge to "leave their clients at the door" when they participate in the deliberations of the Conference.

Technical and Advisory Services to Congress. To facilitate the work of Congress, the NBC offers members of Congress, Congressional Committees and their staffs the services of its Conferees as non-partisan technical advisors. These services are offered without regard to any substantive positions the NBC may take on matters of bankruptcy law and policy.

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