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Creditors' Rights and Bankruptcy Practice Group

GOODSILL ALERT

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NINTH CIRCUIT HOLDS THAT CRAMDOWN APPLIES ON A "PER PLAN" RATHER THAN A "PER DEBTOR" BASIS

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In the case of *JPMCC 2007-C1 Grasslawn Lodging, LLC v. Transwest Resort Properties Incorporated (In re Transwest Resort Properties, Inc.), 16-16221 (9th Cir. January 25, 2018)*, the U.S. Court of Appeals for the Ninth Circuit held that section 1129(a)(1) of the Bankruptcy Code, which requires that at least one impaired class of creditors accept a "cramdown" plan, applies on a "per plan" basis, rather than a "per debtor" basis.

BACKGROUND FACTS

In 2007, five separate companies (collectively, the "Debtors"), Transwest Hilton Head Property, LLC, Transwest Tucson Property, LLC (the "Operating Debtors"), Transwest Hilton Head II, LLC, Transwest Tucson II, LLC (the "Mezzanine Debtors"), and Transwest Resort Properties, Inc. (the "Holding Company Debtor") acquired the Westin Hilton Head Resort and Spa and the Westin La Paloma Resort and Country Club (collectively, the "Resorts"). Id. at 4-5.

The acquisition of the Resorts was financed by (1) a $209 million mortgage loan to the Operating Debtors from JPMCC 2007-C1 Grasslawn Lodging, LLC ("Lender"), secured by the Resorts (the "Operating Loan"); and (2) a $21.5 million loan from Ashford Hospitality Finance, LP (the "Mezzanine Lender"), secured by the Mezzanine Debtors' interests in the Operating Debtors (the "Mezzanine Loan"). Id. at 5.

In 2010, the Debtors filed a petition for chapter 11 bankruptcy relief. Id. The five cases were jointly-administered, but were not substantively consolidated. Id.

The Lender filed a claim in the bankruptcy proceeding for $298 million, based on the Operating Loan. Id. The Mezzanine Lender filed a $39 million claim based on the

Mezzanine Loan. Id. The Lender subsequently acquired the Mezzanine Lender's claim. Id.

The Debtors filed a joint chapter 11 reorganization plan (the "Plan"), wherein a third-party investor, Southwest Value Partners (the "Investor") would acquire the Operating Debtors for $30 million, thereby extinguishing the Mezzanine Debtors' ownership interest in the Operating Debtors. Id.

The Plan restructured the Lender's loan to a term of 21 years, and required monthly interest payments, and a balloon principal payment at the end of the term. Id. at 5-6. The Plan included a due-on-sale clause requiring the Debtors to pay the Lender the outstanding balance of the restructured loan in the event the Resorts were sold, although the due on-sale clause would not apply if the Debtors were to sell the Resorts between Plan years five and fifteen. Id. The Lender voted against the Plan but several other impaired classes of creditors voted to approve the Plan. Id.

The Lender, whose claim was undersecured, elected to have its entire claim treated as secured pursuant to 11 U.S.C. § 1111(b)(2). Id. at 5

Among other things, the Lender argued that section 1129(a)(10) of the Bankruptcy Code, which requires that at least one impaired class accept the Plan, applies on a "per debtor," not a "per plan," basis. Id. at 6. Because the Lender was the only class member for the Mezzanine Debtors and did not vote to approve the Plan, the Lender argued that the Plan did not satisfy the requirements of section 1129(a)(10). Id. Despite the Lender's objections, the Bankruptcy Court confirmed the Plan. Id. On appeal, the District Court ruled that section 1129(a)(10) applies on a "per plan" basis. Id. at 6-7.

PROCEEDINGS BEFORE THE NINTH CIRCUIT

Before the Ninth Circuit, the Lender argued that, when there is a jointly administered plan consisting of multiple debtors, "a 'per debtor' approach that requires plan approval from at least one impaired creditor for each debtor involved in the plan. . ." Id. at 11. In contrast, the Debtors argued that "the plain language of the statute contemplates a 'per plan' approach in which a plan only requires approval from one impaired creditor for any debtor involved." Id. As a matter of first impression among the circuit courts, The Ninth Circuit held that section 1129(a)(10) applies on a "per plan" basis. Id.

The Lender also argued that, while the Plan states it is "a jointly administered" plan, it was, in effect, a substantive consolidation. Id. at 13. The Ninth Circuit found that the

Lender's argument failed for two reasons: (1) the Lender never objected to the Plan on that basis, therefore it was not properly before the court on appeal; and (2) to the extent the Lender argues that the "per plan" approach would result in a "parade of horribles" for mezzanine lenders, such hypothetical concerns are policy considerations best left for Congress to resolve. Id. at 13-14.

In reaching its decision to affirm confirmation of the Plan, the Ninth Circuit explained:

> The plain language of the statute supports the "per plan" approach. Section 1129(a)(10) requires that one impaired class "under the plan" approve "the plan." It makes no distinction concerning or reference to the creditors of different debtors under "the plan," nor does it distinguish between single-debtor and multi-debtor plans. Under its plain language, once a single impaired class accepts a plan, section 1129(a)(10) is satisfied as to the entire plan.

Id. at 12. The Ninth Circuit explained that, "[b]ecause the plain language of section 1129(a)(10) indicates that Congress intended a "per plan" approach, we need not to look to the statute's legislative history or address the Lender's remaining policy concerns. Id. at 14.

Judge Friedland filed a concurring opinion in which he explained, "if a creditor believes that a reorganization improperly intermingles different estates, the creditor can and should object that the plan—rather than the requirements for confirming the plan. Id. at 20.

CONCLUSION

The *Grasslawn Lodging* should be extremely concerning to lenders who make loans to multiple debtors because of the serious risk that debtors will gerrymander an impaired accepting class in a cramdown situation. *Grasslawn Lodging* is also an important reminder for creditors' lawyers to assert proper objections to chapter 11 bankruptcy plans in the bankruptcy court, including objections to any disguised "substantive consolidation," or they risk waiving such objections on appeal.

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