Robinson+Cole

Business Reorganizations, Bankruptcy, and Creditors' Rights

October 2017

Cramdown Interest Rate Best Set Based on Market Rates

The Bankruptcy Code permits cramdown of a secured creditor but requires that the secured creditor receive deferred cash payments at least equal to the value of its collateral. This means that installment payments to the secured creditor must bear interest. But at what interest rate? This question has vexed bankruptcy courts for decades.

The U.S. Supreme Court shed considerable light on this question in *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004). *Till* was a Chapter 13 case, and the Court held that the appropriate method for determining the interest rate for secured claims in a Chapter 13 plan is what has become known as the "formula" approach. Following *Till*, bankruptcy courts have started with the prime rate, and added basis points to it to adjust for the risk going forward, in establishing cramdown interest rates.

The provisions of the Bankruptcy Code applied by the Court in *Till* are analogous to the cramdown provisions in Chapter 11. The Court noted in *Till* that the formula approach might be appropriate in Chapter 11 cases but did not decide the issue and in a footnote observed that there is no free market of willing cramdown lenders in a Chapter 13 context as there might be in a Chapter 11.

In its October 20, 2017, decision in the appeal from the U.S. Bankruptcy Court (S.D.N.Y.) confirming the Chapter 11 plan in *In re Momentive Performance Materials, Inc.*, the Second Circuit Court of Appeals (*In re MPM Silicones, L.L.C.* 2d Cir. Case No. 15-1682, Oct. 20, 2017) followed the lead of the Court of Appeals for the Sixth Circuit (*see*, *In re American HomePatient, Inc.*, 420 F.3d 559 (6th Cir. 2005)) and instructed that, if there is evidence of an efficient market for the proposed cramdown loan, the bankruptcy court should first consider the "market rate" approach before relying on the formula approach. "Efficient markets" exist where the loan contemplated under the cramdown plan can be obtained in the market with similar terms, size, and collateral. The court relied on the difference in the markets for such loan terms, which may be available in the Chapter 11 setting but typically are not available to Chapter 13 debtors, as observed in *Till*.

Notably, the Second Circuit also rejected the claims of the objecting secured creditors that they were entitled to a "make whole" premium on their loans, relying on its prior decision in *In re AMR Corp.*, 730 F.3d 88 (2d Cir. 2013). In reaching this decision, the Second Circuit adopted the reasoning of the bankruptcy court, which found that the operative indentures would trigger the make whole premium only in the case of an "optional redemption," not in the case of an acceleration brought about by a bankruptcy filing. The Second Circuit's *Momentive* decision could set the stage for a split with the U.S. Court of Appeals for the Third Circuit on the issue of the enforceability of make whole premiums. In *In re Energy Future Holdings Corp.*, 2016 U.S. App. LEXIS 20601, the Third Circuit held that a debtor's refinancing of its first and second lien notes during its Chapter 11 case triggered the obligation to satisfy the make whole payment. Of course, the determination of this issue depends largely on the precise language of the loan documentation, making it hard to compare the outcomes and reasonably predict future results.

Secured creditors who face cramdown now will have another tool available to seek better interest rates for their post-confirmation claims but may be losing their bargained-for rights under make whole premium provisions.

For more information, please contact one of the lawyers listed below or another member of Robinson+Cole's Business Reorganizations, Bankruptcy, and Creditors' Rights Group:

Patrick M. Birney | Steven J. Boyajian | Andrew A. DePeau | Michael R. Enright

For insights on legal issues affecting other industries, please visit our Thought Leadership page and subscribe to any of our newsletters or blogs.

Boston | Hartford | New York | Providence | Stamford | Albany | Los Angeles | Miami | New London | rc.com

Robinson & Cole LLP

© 2017 Robinson & Cole LLP. All rights reserved. No part of this document may be reproduced, stored in a retrieval system, or transmitted in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, without prior written permission. This document should not be considered legal advice and does not create an attorney-client relationship between Robinson+Cole and you. Consult your attorney before acting on anything contained herein. The views expressed herein are those of the authors and not necessarily those of Robinson+Cole or any other individual attorney of Robinson+Cole. The contents of this communication may contain attorney advertising under the laws of various states. Prior results do not guarantee a similar outcome.