

Confirmation of a Plan Under Chapter 11 of the Bankruptcy Code and the Effect of Confirmation on Creditors' Rights

EDWARD B. HOPPER, II*

I. INTRODUCTION

Despite the fact that the Bankruptcy Code¹ has been in effect since October 1, 1979, the ambiguities and areas of concern involving a Chapter 11 plan of arrangement or liquidation and the effect of the confirmation of that plan on creditor's rights is still a fertile area for speculation among bankruptcy practitioners and judges. By its very nature, Chapter 11 involves an often complex attempt to save a business through reorganization, which at a minimum usually requires one to two years. Due to this time lapse, there are few court decisions dealing with the problem areas that will be discussed in this Article. Therefore, we are relegated for the most part to the statute, legislative history, the prior Bankruptcy Act,² where applicable, and the cases under the Act, as well as a smattering of law review articles which have been written on new Chapter 11.

Because of the significant effect that the plan has on creditors, it is necessary to have an understanding of the steps leading to confirmation and how a debtor can affect creditor's rights, as well as how creditors' attorneys can and should protect their clients prior to confirmation. Chapter 11 of the Code is the reorganization chapter for partnerships, corporations, proprietorships, unincorporated associations and individuals.³ Chapter 11 of the Bankruptcy Code contains attributes of the prior Bankruptcy Act Chapters X, XI and XII. Chapter 11 is correlative to the object of the old Chapters X, XI,

*Edward B. Hopper, II, Attorney, Partner in firm of Hopper & Opperman, Indianapolis, Indiana. Admitted to bar, 1964, Tennessee; 1967, Indiana. Education: Vanderbilt University, B.A., 1961; LL.B., 1964. Memberships: Indianapolis (Member, Board of Managers), Indiana State, Tennessee State, Federal and American Bar Associations, Bar Association of Seventh Circuit and Bar Association of the U.S. Supreme Court.

¹Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified at 11 U.S.C. §§ 1101-151326 (Supp. IV 1980)) [hereinafter cited as the Code].

²Bankruptcy Act of 1898, 11 U.S.C. §§ 1-1103 (1976) (repealed October 1, 1979, Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, § 401(a), 92 Stat. 2549) [hereinafter cited as the Act].

³11 U.S.C. § 109 (Supp. IV 1980) defines who may be a debtor in a Chapter 11 proceeding, generally following former Act § 11(a)(1). See S. REP. No. 989, 95th Cong., 2d Sess. 31 (1978). See also *In re Woodhouse*, 11 Bankr. 322 (S.D. Ohio 1981) for the proposition that debtors as individuals are not prohibited from seeking relief under Chapter 11.

and XII in its application to beleaguered debtors seeking court protection from creditors attempting to force the liquidation of assets. Under Chapter 11, if reorganization is impossible at the outset of the case or is discovered to be impossible during the course of the attempt to reorganize, new Chapter 11 provides for a plan of liquidation without the necessity of converting the proceeding, as was necessary under the old Act.⁴

Often it is more economical from a creditor's standpoint to liquidate under Chapter 11 rather than to convert to a Chapter 7 proceeding for the reason that the creditor does not have to wait six months for claims to be filed as required in Chapter 7,⁵ nor is there the expense of the trustee, his counsel, and possibly, accountants. In addition, the entities already involved in the proceedings, the debtor and the creditors' committee, control the liquidation subject to court approval without the interjection of a new party, the trustee, who must be educated concerning the debtor's affairs.

In the case of an operating business, once the Chapter 11 petition is filed, regardless of the voluntary or involuntary nature of the petition,⁶ a new entity, the debtor-in-possession, is created and enters into the operating phase of the business.⁷

After the petition is filed and the operational phase of the case is underway, the object of the proceeding is usually to determine whether the debtor can operate the business involved paying its day-to-day costs of operation and generating cash to apply towards debt service required under secured creditors' contracts. Additionally, under close monitoring by the creditors' committee,⁸ the debtor at-

⁴11 U.S.C. § 1123(a)(5)(D) (Supp. IV 1980) provides for a liquidating plan in a Chapter 11 case. Under the Act, there were cases which indicated that the trustee could liquidate under a Chapter X plan but no statutory provision existed for such a plan. See S. REP. NO. 1916, 75th Cong., 3d Sess. 34 (1938). *In re American Bantum Cart Co.*, 193 F.2d 616 (3d Cir. 1952). This area of controversy is now put to rest in the Code.

⁵Bankruptcy Rule 302 wherein generally a claim must be filed within six months of the first date set for the first meeting of creditors. This rule continues to apply under the new code. See S. REP. NO. 989, 95th Cong., 2d Sess. 61, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5787, 5847.

⁶11 U.S.C. § 706(a) (Supp. IV 1980) provides for a conversion from Chapter 7 to Chapter 11 of the Code. Pursuant to 11 U.S.C. § 303(b) the creditors may file an involuntary Chapter 11 petition against a debtor. See also *In re All Media Properties, Inc.*, 5 Bankr. 126 (S.D. Texas 1980), *aff'd*, 646 F.2d 193 (5th Cir. 1981).

⁷The powers and duties of a debtor in possession are defined in 11 U.S.C. § 1107(a) (Supp. IV 1980). For fiduciary responsibilities imposed by *id.* § 1107, see *In re Antilles Yachting Inc.*, 4 Bankr. 470 (D.V.I. 1980). It is of consequence that the powers, rights, and duties of a debtor in possession are generally all rights of a trustee in a Chapter 7 proceeding.

⁸11 U.S.C. § 1102(a)(1) (Supp. IV 1980) provides the statutory authorization for

tempts to operate the business without losses on a weekly basis. Typically, if there is a positive cash flow, the debtor can determine what can be applied towards service on the secured debt and can approach the secured creditor or creditors with an interim proposal.⁹

The third phase of the Chapter 11 proceeding is the promulgation of the plan of arrangement. It is possible for the plan to be developed early in the case, which would allow the debtor-in-possession to accomplish phases two and three at the same time. The Code contemplates that the plan of arrangement typically be proposed by the debtor.¹⁰ The plan is the debtor's program for settling with its creditors. After the exclusive debtor period has elapsed without an

the formulation of a creditors' committee. The rights, powers, and duties of the creditors' committee are set forth in *id.* § 1103(c). *In re Western Management, Inc.*, 6 Bankr. 438 (W.D. Ky. 1980), succinctly defined the duties of the committees:

Further, there is no indication in the record that the unsecured creditors' committee has met, investigated, monitored or in any other manner attempted to fulfill its statutory responsibility. It was envisioned by the drafters, when they removed the bankruptcy judge as overseer of a Chapter 11 case, that the committee would fill the void. Without the recommendations and findings of the creditors' committee, the Court, in ruling on a plan of reorganization, is confronted with a difficult, if not impossible, task in fulfilling its statutorily prescribed duties. It is vitally important that the Court be fully and accurately informed by independent reliable evidence. Neither the Court nor the creditors should be required to rely entirely on the evidence produced by the proponents of the plan.

Id. at 443. Judges in both the Southern District and Northern District of Indiana have adopted procedures which will become a local rule requiring the reporting of income and receipts for the 90 days preceding the filing of the petition and bi-monthly from the date of filing, using the form found in the Addendum at 544-46. The same form is used for the 90-day and bi-monthly reports.

The purpose of the reporting requirements is two-fold. Initially they protect the administrative creditor who can review the reports in the record in the bankruptcy court clerk's office to determine if it is in the best interest of a creditor to advance credit to the debtor in possession. Secondly, the reporting requirements allow the creditors' committee to determine whether the debtor's equity, if any, is deteriorating.

Additional protection is afforded the creditor who advances credit to a Chapter 11 debtor or a trustee for a Chapter 11 debtor under 11 U.S.C. § 364 (Supp. IV 1980) which gives the creditor an administrative claim and *id.* § 364(c) which authorizes the granting of a super priority over all other administrative creditors.

⁹11 U.S.C. §§ 361-364 (Supp. IV 1980) provides that creditors must be adequately protected during the pendency of the proceeding. Adequate protection can be a portion of the regular payment which compensates the creditor for the use of its collateral. *See also* Metropolitan Life Ins. Co. v. Murel Holding Corp. (*In re* Murel Holding Corp.), 75 F.2d 941 (2d Cir. 1935).

¹⁰11 U.S.C. § 1121(b) (Supp. IV 1980) gives the debtor the exclusive right to file a plan within 120 days from the date of the petition provided no trustee is appointed, and further, when read in connection with *id.* § 1121(c)(3), grants the debtor an additional 60 days to obtain confirmation.

extension by the court, any party in interest may file the plan.¹¹

The practice of negotiating a plan with the creditors' committee, which was prevalent under Chapters X, XI and XII of the Bankruptcy Act, is carried on under new Chapter 11. In a case in which there is no trustee, once the plan has been negotiated to the satisfaction of the debtor-in-possession and the creditors' committee, the plan is then circulated among the creditor body. The use of a disclosure statement under the Bankruptcy Code serves to prevent circulation of so-called "blind plans" in which the creditors really do not know on what they are voting. The disclosure statement is devised to provide the creditor body with sufficient information so that a prudent decision can be made on whether acceptance of the plan is in the interest of a particular creditor.¹²

The next step involves the solicitation of votes from the creditor body for the purpose of obtaining confirmation of the plan.¹³ Confirmation extinguishes all creditor rights beyond the terms of the plan itself against the debtor as those rights existed at pre-confirmation, with a few Code-defined exceptions discussed below.¹⁴

II. THE PROPOSED PLAN OF CONFIRMATION—A QUICK OVERVIEW

Assuming that there is no trustee in the case, the debtor has the exclusive right to file a plan within 120 days after the filing of the case.¹⁵ If a trustee is appointed in the Chapter 11 proceeding or if the debtor's proposed plan is not accepted within 180 days following the filing of the case,¹⁶ any party in interest may file a plan.¹⁷ It

¹¹Pursuant to *id.* § 1121(c), after the exclusive period of time for filing the plan by the debtor, any party in interest may file a plan.

¹²*Id.* § 1125(a)(1) provides that a disclosure statement must contain information of a kind, and in sufficient detail, as far as is reasonably practicable in light of the nature and history of the debtor and the condition of the debtor's books and records, that would enable a hypothetical reasonable investor typical of holders of claims or interests of the relevant class to make an informed judgment about the plan. . . .

¹³See *id.* § 1126 for the requirements of acceptance of plan.

¹⁴See *id.* § 1141.

¹⁵See *id.* § 1121(b).

¹⁶The 180-day period includes 60 days for acceptance of the plan after the 120-day filing period.

¹⁷11 U.S.C. § 1121(c) (Supp. IV 1980) provides as follows:

(c) Any party in interest, including the debtor, the trustee, a creditors' committee, an equity security holders' committee, a creditor, an equity security holder, or any indenture trustee, may file a plan if and only if—

- (1) a trustee has been appointed under this chapter;
- (2) the debtor has not filed a plan before 120 days after the date of the order for relief under this chapter; or
- (3) the debtor has not filed a plan that has been accepted, before 180

should be noted that on request of a party in interest, normally the debtor, and after notice and a hearing, the court may reduce or increase the 120-day period or the 180-day period.¹⁸

In most cases there should be no objection to the increase of the 120-day period if the creditors' committee realizes that the debtor is not in a position to file a plan at that time, but that there is a real possibility of a workable plan being filed in the future based on, for instance, refinancing or a sale, and there is no competing plan under consideration. The 180-day period should normally be extended when the debtor is not in a position to confirm the plan due to lack of funds or when the event which is to serve as the means for the execution of the plan, for example, a sale, cannot be closed for some reason. The only comment in the legislative history on the extension of the period appears at page 406 of the House Report where it is noted that "[c]ause might include an unusually large or unusually small case, delay by the debtor, or recalcitrance among creditors."¹⁹ The Senate Report indicates that an extension should be granted only on the showing of some promise of probable success and not as a tactical device to pressure one of the parties negotiating the plan to yield and accept a plan they consider less than adequate.²⁰

During this phase of the Chapter 11 case, the parties in interest, which typically include the debtor-in-possession and the creditors' committee, seek to formulate and work out a plan which specifies how much the creditors will be paid, the form of payment, and other details involving the reorganized debtor's business, such as interest that the stockholders will retain, who will manage the business, and in what form the reorganized debtor will continue.²¹

days after the date of the order for relief under this chapter, by each class the claims or interests of which are impaired under the plan.

Query, is the court a party in interest? No provision of the Code has been read to place the court in that posture.

¹⁸*Id.* § 1121(d).

¹⁹H.R. REP. NO. 595, 95th Cong., 2d Sess. 406, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5963.

²⁰S. REP. NO. 989, 95th Cong., 2d Sess. 118, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5787.

²¹See Addendum at 523-45 for sample plan and disclosure statement.

It is at this stage of the proceeding that a well represented creditor body has the most influence over the debtor. The committee has reviewed the financial reports with the debtor and has an estimation of the percentage which they would receive on their claims should they seek a conversion to Chapter 7. This knowledge is used both by the committee and the debtor in formulating a plan that the debtor can meet and that allows the creditors to maximize their recovery. Assume, for example, that the debtor proposed \$0.20 settlement to unsecured creditors payable on confirmation. The creditors' committee is of the opinion that in liquidation creditors will receive 20 percent of their claims. The debtor's plan contemplates continuation of stock ownership as

After the negotiation of a satisfactory plan by the parties in interest, the next step is to solicit acceptances, which is the subject of section 1125 of the Code involving the preparation and circulation of a disclosure statement. The disclosure statement should contain sufficient information to enable the creditor to make an informed judgment whether to accept or reject the plan.²²

There are some situations in which a disclosure statement would not be required, such as when a plan does not contemplate the solicitation of votes, leaving the secured creditors unimpaired, and proposing to cram down all other classes.²³ Additionally, a statement may not be required when the plan, in the opinion of the court, contains enough information to constitute adequate disclosure.²⁴

There is an unsettled area involving the disclosure statement in a liquidating proceeding when a sale of the bulk of the assets of the debtor is proposed. The question arises whether the court should require an approved disclosure statement before the sale. One point of view is that the disclosure statement should be required because the sale is in reality the sole means for execution of the liquidation plan.²⁵ The contrary view is that a disclosure statement would be premature because creditors cannot be informed about the sum they are being offered in the liquidating plan until after the sale.²⁶

With the intervention of the element of the disclosure statement in the proceeding, the Code also supplies the parties with insulation against future actions based on the disclosure statement, provided that the statement is approved by the court and is the sole basis upon which acceptance of the plan is solicited.²⁷

it existed pre-petition. This may be the time to demand a percentage of the stock so that creditors share in any future success of the reorganized debtor.

²²11 U.S.C. § 1125(b) (Supp. IV 1980). Regarding the contents of the disclosure statement, see *Valley National Bank v. Trustee*, 609 F.2d 1274 (9th Cir. 1981) in which the court refused to take a technical approach used in Securities and Exchange Commission proceedings to a disclosure statement in the bankruptcy proceeding. *But see In re Cyr Bros. Meat Packing, Inc.*, 2 Bankr. 620 (D. Me. 1980) which requires that full disclosure be made.

There is also a question as to whether a notice fixing hearing on the approval of the disclosure statement need only provide that the disclosure statement is on file with the clerk of the court and may be reviewed there by any creditor.

²³See *In re Union County Wholesale Tobacco*, 8 Bankr. 442 (D.N.J. 1981).

²⁴See *In re BelAir Assocs.*, 4 Bankr. 168 (W.D. Okla. 1981).

²⁵See *In re D.M. Christian Co.*, 7 Bankr. 561 (N.D. W.Va. 1981) (disclosure statement must be filed and approved prior to sale).

²⁶See *In re Whet*, 12 Bankr. 743 (D. Mass. 1981) (sale permitted without disclosure statement).

²⁷11 U.S.C. § 1125(e) (Supp. IV 1980) contains the well known "safe harbor" provision which insulates any person engaging in solicitation from possible violation of the securities act provided that the approved disclosure statement is relied upon.

After the disclosure statement has been approved, the plan, disclosure statement, and a ballot, which the court also typically approves, are circulated to the creditor body for voting. A class of claims as set forth in the plan will be deemed to have accepted the plan if the members of the class accept the plan by at least two-thirds in dollar amount, and more than one-half in number, of the allowed claims in the class.²⁸ If the rights of a class are deemed unimpaired by the debtor and the court accepts the debtor's position, the acceptance of that class is not required and the unimpaired class is deemed to have accepted the plan.²⁹ The claims of creditors who neither accept nor reject the plan are not considered in the vote. If objections to the disclosure statement or confirmation of the plan are not advanced by an individual member of a class, the member will be bound by the class vote.³⁰ If the proponent of the plan is not relying on section 1129(a)(8), which is the "cram down" provision discussed in greater detail below, every class deemed impaired under the plan must accept the plan by the requisite vote or have been deemed to have accepted the plan in order for the plan to be confirmed.³¹

The plan may be modified pre-confirmation by the proponent of a plan. The plan, as modified, becomes the confirmed plan only if, after notice and hearing, the court confirms the plan.³²

III. STEPS IN THE CONFIRMATION PROCESS

Assuming proper classification of claims or interests in the plan under section 1125 of the Code, and assuming the absence of an objection to confirmation under section 1128 of the Code, the court must find that the plan, in general, meets the following requirements:

1. that the plan and debtor comply with applicable provisions of Chapter 11;
2. all payments made in connection with or incident to the plan have been fully disclosed;

²⁸*Id.* § 1126(c). See also *In re Northwest Recreational Activities, Inc.*, 4 Bankr. 43 (N.D. Ga. 1980).

²⁹11 U.S.C. §§ 1126(f) & 1129(a)(8) (Supp. IV 1980).

³⁰*Id.* § 1126(c). This section enforces the principle that creditors should respond to the solicitation notice.

³¹*Id.* § 1126(f).

³²*Id.* §§ 1127, 1128. Immaterial modification may not require notification of all claims. *Id.* § 1127(c). Under *id.* § 1129(b) the court may allow confirmation if the plan is fair and equitable and does not discriminate unfairly. This provision was not a part of the Act and is a major change of the reorganization section of the Code. *In re Winston Mills Inc.*, 1 C.B.C. 121 (S.D.N.Y. 1979). For the best interest of creditors test see treatment under the "cram down" section at text accompanying notes 45-56, *infra*.

3. principals and/or officers of the reorganized debtor have been disclosed;
4. that the plan has been proposed in good faith and not by any means prohibited by law;
5. the plan meets the best interest of creditors test;
6. each class has accepted the plan or is not impaired by the plan;
7. priority creditors are receiving the present market value of their claims;
8. at least one class of claims has accepted the plan;
9. confirmation is not likely to be followed by liquidation or further reorganization except as set forth in the plan.³³

The debtor's disclosure requirements at confirmation, which are not to be confused with the disclosure statement discussed above, are set forth in section 1129(a)(4)(A) and (B). The proponent of the plan is obligated to disclose to the court any payment made or promise of payment to be made to any one connected with the issuance of securities under the plan or acquiring property under the plan for services or costs in connection with the plan or incident to the bankruptcy case. It is also required that the proponent of the plan indicate what compensation is to be paid to certain officers and key personnel of the debtor as a result of the plan.³⁴

The four key steps in the above-described confirmation process are feasibility, good faith, best interest tests, and cram down.

A. Feasibility

The court must find that the debtor's plan is feasible. Under this standard, the court must determine from the evidence that the debtor can make its payments under the plan or perform under the plan. This is a significant juncture in the confirmation process for creditors. Counsel for the creditors' committee and individual creditors should be leery of plans which promise payments over time without a successful "track record" in the past, or on the basis of less than reliable projections. In the event that a debtor defaults under the confirmed plan, the creditor's sole remedy is to pursue the debtor

³³11 U.S.C. § 1129(a)(1)-(11) (Supp. IV 1980); *id.* § 1129(a)(2) indicates that Chapter 11 provisions have been complied with which would, for example, include the disclosure provisions. *Id.* § 1129(a)(3) indicates that the plan has been proposed in good faith and not by any means forbidden by law. For example, the plan cannot be proposed for the purpose of avoiding taxes or avoiding the Securities Act of 1933 as set forth in *id.* § 1129(d).

³⁴*Id.* § 1129(a)(5). See also H.R. REP. NO. 95-595, 95th Cong., 1st Sess. 408 (1977).

for the balance due *under the plan* through use of a new involuntary proceeding or normal non-bankruptcy collection remedies.³⁵

B. Good Faith

The requirement that the proponent of the plan propose the plan in "good faith" is found in 11 U.S.C. § 1129(a)(3).³⁶ The good faith requirement is derived from sections 766(4)³⁷ and 621(3)³⁸ of the previous Act.³⁹ The requirement was interpreted under Chapter X to mean that there exists a real possibility of consummation of the plan.⁴⁰ The plan must also escape a finding by the court that it is part of a scheme to defraud creditors or other interest holders.⁴¹

The most scholarly description of the good faith requirement under the Act now applicable to the Code is found in the writings of the eminent jurist Judge John K. Rickles⁴² in his article on good faith in Chapter X proceedings.

One of the safest and soundest rules of construction of statutes is to consider the purposes of the legislation and not be lost in a cosmic nebula of theory. Judges are realistic men and matters common to mankind are not foreign to them. In approving a Chapter X petition, a district judge will be governed by the information furnished him by the debtor, secured and unsecured creditors, stockholders, bondholders and other parties in interest. He will inquire as to how and why the business came into difficulty, what the difficulty was, the present condition of the business and the property,

³⁵11 U.S.C. § 1129(a)(11) (Supp. IV 1980) stipulates that "[c]onfirmation . . . is not likely to be followed by liquidation, or the need for further financial reorganization, of the debtor or any successor of the debtor under the plan, unless such liquidation or reorganization is proposed in the plan." *Id.* § 1129(a)(11) provides a new feasibility standard. *See also In re Northwest Recreational Activities, Inc.*, 4 Bankr. 43 (N.D. Ga. 1980). *Consolidated Rock Products Co. v. Du Bois*, 312 U.S. 510 (1941), indicated that evidence which could be presented by the debtor if the debtor was the proponent of the plan included past earnings history, change in policies, operations, financial projections with supportive assumptions, and appraisals. In *In re Landmark Plaza Park Limited*, 7 Bankr. 653 (D.N.J. 1981), the court refused to confirm a plan on the finding that the projection of future income necessary to make the payments was unduly optimistic.

³⁶11 U.S.C. § 1129(a)(3) (Supp. IV 1980).

³⁷11 U.S.C. § 766(4) (1976) (repealed 1978).

³⁸*Id.* § 621(3).

³⁹28 U.S.C. § 764(4) (old Act Chapter XI); 28 U.S.C. § 621(3) (old Act Chapter X).

⁴⁰6A COLLIER ON BANKRUPTCY ¶ 11.08, at 243 (14th ed. L. King 1977).

⁴¹*See Price v. Spokane Silver & Lead Co.*, 97 F.2d 237 (8th Cir.), *cert. denied*, 305 U.S. 626 (1938), for an early view of the principle.

⁴²United States Bankruptcy Court of the Southern District of Indiana.

whether there is a fair prospect that the business can be continued, what other proceedings are pending, etc. That information will be the basis of his findings of good faith, or the lack of it.⁴³

Under the provisions relating to the good faith requirement, this requirement must be distinguished from the principle that the petition be filed in good faith.⁴⁴

C. *The Best Interest of Creditors Test*

The best interest of creditors provisions are set forth in 11 U.S.C. § 1129(a)(7). The best interest of creditors test parallels in part the requirements of the provision for "cram down," treated below, and the provision known as the absolute priority rule under Chapter X. The test as set forth under the Code appears to have been interpreted as requiring a higher standard than that required under Chapters X or XI of the Act in that the creditors must receive at least as much as they would receive in liquidation (under Chapter 7), and creditors of a senior class must receive proper treatment before a junior class can share in distribution under the plan.

In the case of *In re Winston Mills, Inc.*⁴⁵ the bankruptcy judge examined section 1129(a)(7) in comparison to the requirements under the Act and concluded that the Code's standard is more stringent:

"When a plan of arrangement offers creditors considerably less than they would realize through liquidation, the plan should not be regarded as being in the best interests of the creditors." . . .

It would serve little purpose to examine with minute care the evidence offered by the debtor on the issue of satisfaction of the legal standard described above.

(Footnote 6: Section 1129(a)(7) of the 1978 Code, not applicable to this Chapter XI case . . . insures "that the dissenting members of an accepting class will receive at least what they would otherwise receive . . ." 124 Cong. Rec. [daily ed. September 28, 1978]. The 1978 Code Chapter 11 standard seems stricter than is suggested by the adverb modifier "considerably" in the quoted material in the text above.⁴⁶

⁴³Rickles, *What is "Good Faith" in Chapter X Proceedings?*, 29 J. OF THE NAT'L A. OF REFEREES IN BANKR. 60, 62 (1955).

⁴⁴*Hadley v. Victory Constr. Co. (In re Victory Constr. Co.)*, 9 Bankr. 570 (C. D. Cal. 1981).

⁴⁵1 C.B.C.2d 121 (S.D.N.Y. 1979).

⁴⁶*Id.* at 125.

It would appear that sections 1129(a)(7)⁴⁷ and 1129(b)(1) and (2), the so-called "cram down" section, will be the most controversial sections in Chapter 11 for the reason that both give rise to historically difficult questions of valuation.

D. Cram Down

"Cram down" applies to the stockholder class as well as to the classes of creditors who may be objecting to the plan. The cram down provision arises out of 11 U.S.C. § 1129(b)(1), which provides that:

if all of the . . . requirements of subsection (a) of this section other than paragraph (8) are met with respect to a plan, the court, on request of the proponent of the plan, shall confirm the plan . . . if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class"⁴⁸

⁴⁷11 U.S.C. § 1129(a)(7) (Supp. IV 1980) provides that the court can confirm only if:

With respect to each class—

(A) each holder of a claim or interest of such class—

(i) has accepted the plan; or

(ii) will receive or retain under the plan on account of such claim or interest property of a value, as of the effective date of the plan, that is not less than the amount that such holder would so receive or retain if the debtor were liquidated under chapter 7 of this title on such date; or

(B) if section 1111(b)(2) of this title applies to the claims of such class, each holder of a claim of such 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, that is not less than the value of such creditor's interest in the estate's interest in the property that secures such claims.

⁴⁸*Id.* § 1129(b)(1).

The legislative explanation of section 1129(b)(1) reads:

Subparagraph (C) applies to a dissenting class of impaired interests. Such interests may include the interests of general or limited partners in a partnership, the interests of a sole proprietor in a proprietorship, [sic] or the interest of common or preferred stockholders in a corporation. If the holders of such interests are entitled to a fixed liquidation preference or fixed redemption price on account of such interests then the plan may be confirmed notwithstanding the dissent of such class of interests as long as it provides the holders [sic] property of a present value equal to the greatest of the fixed redemption price, or the value of such interests. In the event there is no fixed liquidation preference or redemption price, then the plan may be confirmed as long as it provides the holders of such interest property of a present value equal to the value of such interests. If the interests are "under water" then they will be valueless and the plan may be confirmed notwithstanding the dissent of that class of interests even if the plan provides that the holders of such interests will not receive any property on account of such interests.

Alternatively, under clause (ii), the court must confirm the plan notwithstanding the dissent of a class of interests if the plan provides that holders of any interests junior to the dissenting class of interests will not receive or retain any property on ac-

Irving D. Labovitz indicates in his excellent article on cram down that:

"Cram Down" becomes an issue only when all necessary statutory requirements for confirmation of a plan have been achieved, except that one or more classes of claims, or other parties at interest, have refused to accept the proposed plan. It is these dissident classes that *may* become the subject of imposition of the Plan, or of a "Cram Down" of the Plan against their wishes by a debtor. The "Cram Down" tests and rules to be discussed in this outline must be distinguished from the prerequisites of confirmation otherwise incumbent upon any Chapter 11 proceeding, including compliance with statutory directives under the proposal of the Plan in a lawful and good faith manner, certain disclosure requirements, and compliance with the statutory "best interests of creditors test."⁴⁹

In a cram down situation, secured creditors must receive deferred payments totalling at least the allowed amount of their claim and the payments must be equivalent to the present market value of their claim. Unsecured creditors must either receive full compensation or deferred compensation equivalent to their claim or, if less than full compensation is provided by the plan, no junior class can receive or retain any interest in the debtor's property.

The cram down provision applies to secured creditors, unsecured creditors, and equity holders. Cram down, although new to those who worked with Chapter 11 of the Bankruptcy Act, was available under the Act in Chapter X, and as a new tool should be used sparingly. However, it should allow confirmation of plans facing recalcitrant creditors or groups.⁵⁰

Examples of cram down situations appear in several excellent law review articles.⁵¹ In reviewing these articles, consider first the

count of such junior interests. Clearly, if there are no junior interests junior to the class of dissenting interests, then the condition of clause (ii) is satisfied. The safeguards that no claim or interests receive more than 100% of the allowed amount of such claim or interests and that no class be discriminated against unfairly will insure that the plan is fair and equitable with respect to the dissenting class of interests. See 124 CONG. REC. 32408 & 34007 (1978).

⁴⁹Labovitz, *Outline of "Cram Down" Provisions Under Chapter 11 of the Bankruptcy Reform Act of 1978*, 86 COM. L.J. 51 (1981).

⁵⁰For examples of "cram down" of secured creditors in Chapter 13 cases which are analogous to Chapter 11, see *General Motors Acceptance Corp. v. Lum (In re Lum)*, 1 Bankr. 186 (D. Tenn. 1980); *In re Crockett*, 3 Bankr. 365 (N.D. Ill. 1980).

⁵¹See, e.g., Klee, *All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code*, 53 AM. BANKR. J. 133, 146-71; Labovitz, *supra* note 49, at 54-56.

following two examples based on a simple fact situation which may clarify how the relevant complex legislative authorities are to be interpreted.

Assume the "ever-present" bank holds a mortgage on the debtor corporation's real estate in the sum of \$500,000.00 and the real estate has a market value of \$450,000.00. The debtor owns equipment and inventory having a market value (on re-sale to a willing buyer) of \$100,000.00, free of liens. There are tax claims of \$60,000.00 and an unsecured trade debt of \$300,000.00.

Under 11 U.S.C. § 1129(b), a plan which proposes to pay the bank \$450,000.00 over twenty years at a current rate of interest could be "crammed down" over the bank's objection to confirmation of the plan.⁵² Tax claims can be proposed to be paid over six years, on a pro rata basis, at the statutory rate of interest and this class will be deemed to have accepted.⁵³ For unsecured creditors, if the plan offers \$40,000.00, \$20,000.00 on the date of confirmation and \$20,000.00 in notes, at the current market rate of interest to be paid over five years, the court can confirm the plan over a vote rejecting the plan since unsecured creditors are being paid not less than they would receive under a Chapter 7 liquidation.⁵⁴ Upon acceptance by one class under the plan, the other classes can be "crammed down."⁵⁵

To reiterate, the "cram down" provision applies to secured creditors, unsecured creditors, and stockholders. A rejecting class of stockholders cannot block a plan where the going concern value of the business is less than the amount of the debt.⁵⁶

⁵²See 11 U.S.C. § 1129(b)(1) (Supp. IV 1980). A "cram down" provision existed under Chapter X which defined "adequate protection". 11 U.S.C. § 616(7) (1976) (repealed 1978).

⁵³*Id.* § 1129(a)(9)(C).

⁵⁴\$100,000 (inventory and equipment) minus \$60,000 (taxes) equals \$40,000 (pot for general creditors minus expense of the Chapter 7 proceeding).

⁵⁵11 U.S.C. § 1129(a)(10) (Supp. IV 1980). *But see* Buffalo Savings Bank v. Marston Enterprises, Inc. (*In re* Marston Enterprises, Inc.), 13 Bankr. 514 (E.D.N.Y. 1981); *In re* Landau Boat Co., 13 Bankr. 788 (W.D. Mo. 1981).

⁵⁶It is determined at the hearing on the stockholder's objection to confirmation that the value of the reorganized debtor is \$5,000,000 based on the fact that earnings minus return to the investor is \$1,000,000 at a market rate of 20%. The debt then exceeds the value to the detriment of the stockholders.

Excellent discussion of cram down and examples of fact situations to which it may be applicable appear in Klee, *All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code*, 53 AM. BANKR. L.J. 133 (1979). *See also* Labovitz, *supra* note 49.

IV. EFFECT OF CONFIRMATION ON CREDITORS

Generally, confirmation does the following for the debtor:

1. Confirmation of the plan is binding on creditors of the debtor, whether or not they accept the plan or have claims which are impaired.

2. The Chapter 11 debtor, if it is a corporation, is discharged from all pre-petition debts except to the extent provided for in the plan.

3. Finally, the debtor, upon confirmation, is revested with all property of the debtor-in-possession free and clear of all claims except as provided for in the plan.

The significant change in the effect of confirmation from old Chapter XI is that the reorganized debtor is insulated from being pursued by creditors who formally asserted non-dischargeable claims. Whether the claim was scheduled or whether the debtor had committed an act giving rise to a non-dischargeable claim under Chapter 7 are matters which no longer concern the debtor post-confirmation.⁵⁷

⁵⁷11 U.S.C. § 1141 (Supp. IV 1980) provides in part:

(d)(1) Except as otherwise provided in this subsection, in the plan, or in the order confirming the plan, the confirmation of a plan—

(A) discharges the debtor from any debt that arose before the date of such confirmation, and any debt of a kind specified in section 502(g), 502(h), or 502(i) of this title, whether or not—

(i) a proof of the claim based on such debt is filed or deemed filed under section 501 of this title;

(ii) such claim is allowed under section 502 of this title; or

(iii) the holder of such claim has accepted the plan; and

(B) terminates all rights and interests of equity security holders and general partners provided for by the plan.

(2) The confirmation of a plan does not discharge an individual debtor from any debt excepted from discharge under section 523 of this title.

(3) The confirmation of a plan does not discharge a debtor if—

(A) the plan provides for the liquidation of all or substantially all of the property of the estate;

(B) the debtor does not engage in business after consummation of the plan; and

(C) the debtor would be denied a discharge under section 727(a) of this title if the case were a case under Chapter 7 of this title.

Similar provisions were found in the Act. Collier's treatise discusses section 224(1) of the Bankruptcy Act in regard to the Chapter X proceeding:

Paragraph (1) of § 224 is derived from former § 77B(h) and provides that upon confirmation of a plan, "the plan and its provisions shall be binding upon the debtor, upon every other corporation issuing securities or acquiring property under the plan, and upon all creditors and stockholders, whether or not such creditors and stockholders are affected by the plan or have accepted it or have filed proofs of their claims or interests and whether or not their claims or interests have been scheduled or allowed or are allowable".

6A COLLIER ON BANKRUPTCY ¶ 11.13 at 273 (rev. ed. 1981).

Section 1141, discharging the debtor from all pre-petition claims, makes plain sense when read in light of section 1129, which allows the court to confirm a plan over objections of creditors, provided that the plan is in the best interests of creditors and that the creditors are receiving no less than they would receive under Chapter 7.⁵⁸ In light of the foregoing, secured creditors, mortgage holders, and mechanics' lien holders should be especially wary because secured creditors' rights can be changed and terminated as a part of the plan. If the plan does not provide for preservation of the lien, and the plan is confirmed, the lien is eradicated.⁵⁹

The effect of confirmation is important to holders of non-dischargeable claims under 11 U.S.C. § 523 since these claims will not survive confirmation. The holders may be well advised to seek conversion of the proceeding to a Chapter 7 or to attempt to force the filing of a liquidation plan. The concern stems from the effect of the discharge on the creditors' rights against a co-maker, guarantor, or surety of a debt which has been extinguished by the plan.⁶⁰

A. Revocation of Confirmation

On timely request of a party in interest, the court may revoke any order of confirmation obtained by fraud, which would also revoke the discharge, leaving the remedies of creditors as they existed pre-confirmation.⁶¹ The change from prior law is that section

⁵⁸*Cf.* 11 U.S.C. §§ 371 & 476 and Bankr. R. 11-43, 12-42 (Chapters XI and XII discharges apply only to § 17 dischargeable debts). *See also* Jay Law Drug, Inc. v. United States I.R.S. (*In re* Jay Law Drug, Inc.), 621 F.2d 524 (2d Cir. 1980) dealing with the rights of the holders of non-dischargeable claims against the debtor post-confirmation. The expanded dischargeability concept does not apply to individuals or to Chapter 11 liquidations.

⁵⁹*In re* Williams, 9 Bankr. 228, 232 (D. Kan. 1981) (once debt underlying lien is extinguished by discharge, lien is unenforceable). *See also* BANKR. SERV. (L. Ed.) § 171, at 82 (1979).

⁶⁰*See* 11 U.S.C. §§ 366(3) & 472(3) (1976) as well as Bankr. R. 11-38, 12-38 describing the circumstances which would bar confirmation under the Act if the debtor committed an act which would bar the discharge. *See also* 11 U.S.C. § 1144 (Supp. IV 1980).

⁶¹11 U.S.C. § 1144 (Supp. IV 1980) provides in part:

On request of a party in interest at any time before 180 days after the date of the entry of the order of confirmation, and after notice and a hearing, the court may revoke such order if such order was procured by fraud. An order under this section revoking an order of confirmation shall—

- (1) contain such provisions as are necessary to protect any entity acquiring rights in good faith reliance on the order of confirmation; and
- (2) revoke the discharge of the debtor.

Of special importance is the time limitation imposed of 180 days. Notice and a hearing is required. Revocation is discretionary in Chapter 11, while mandatory under Chapter 7. *Id.* § 727(d).

1144 confines the fraud to one area, specifically, fraud in obtaining confirmation of the plan, after filing. No longer is there significance to the perpetration of fraud, either pre-filing or post-filing, which would have been a bar to discharge under Chapter XI of the Act.

B. *Modification of a Plan Post-Confirmation*

Post-confirmation modification of the plan is provided for in section 1127.⁶² Section 1127(b) enables modification of the plan to take place after confirmation but before substantial consummation of the plan.⁶³ According to the Collier treatise,⁶⁴ section 1127(b) essentially incorporates into Chapter 11 Bankruptcy Rule 10-306(b) as it applied to modification of Chapter X plans. When the modification of the plan occurs, it is as if the proponent of the plan has filed a new plan. The proponent must go through the same steps required of a proponent with regard to the original plan unless the modification deals only with one class, in which case the steps need deal only with that class.⁶⁵

C. *Treatment of Tax Claims in Chapter 11*

An important change from the Bankruptcy Code occurred when Congress adopted section 1129(a)(9)(C), which allows the debtor to spread tax claims over a six year period from the date of assessment of the tax claim as a part of the plan.⁶⁶ As long as the

⁶²*Id.* § 1127 provides in part:

(b) The proponent of a plan or the reorganized debtor may modify such plan at any time after confirmation of such plan and before substantial consummation of such plan, but may not modify such plan so that such plan as modified fails to meet the requirements of sections 1122 and 1123 of this title. Such plan as modified under this subsection becomes the plan only if the court, after notice and a hearing, confirms such plan, as modified, under section 1129 of this title, and circumstances warrant such modification.

(c) The proponent of a modification shall comply with section 1125 of this title with respect to the plan as modified.

(d) Any holder of a claim or interest that has accepted or rejected a plan is deemed to have accepted or rejected, as the case may be, such plan as modified, unless, within the time fixed by the court, such holder changes such holder's previous acceptance or rejection.

⁶³*Id.* § 1127(b). *Id.* § 1101(2)(B) provides that substantial consummation means: "[a]ssumption by the debtor or by the successor to the debtor under the plan of the business or of the management of all or substantially all of the property dealt with by the plan. . . ."

⁶⁴COLLIER ON BANKRUPTCY ¶ 1127.02, at 1127-4 (15th ed. L. King 1981).

⁶⁵*Id.* ¶ 1127.03, at 1127-4. Query, does post-petition modification reopen the 180-day period under 11 U.S.C. § 1144 to revoke the original confirmation order?

⁶⁶11 U.S.C. § 1129(a)(9)(C) provides:

with respect to a claim of a kind specified in section 507(a)(6) of this ti-

reorganized debtor is making its payments under the plan, the taxing authorities cannot take action against the new entity.

D. Post-Confirmation Objections to Claims

An obvious question under the Code is that of when objections to disputed claims must be filed. Under the Bankruptcy Rules, the creditor who has a disputed claim must file the claim before the approval of the disclosure statement. Assuming that the holder of the disputed claim filed a claim pursuant to the Rule, the question is then one of when must the debtor-in-possession or the reorganized debtor file an objection to the claim. A proper interpretation of the statute seems to indicate that an appropriate objection can be lodged by the reorganized debtor after the order of confirmation has been entered. Chapters 1, 3, 5 and 11 of the Bankruptcy Code prescribe the time period in which the trustee or the entity acting as trustee in the proceeding must file objections to claims with the exception of section 502(g).

From a practical point of view, an interpretation that objections to claims must be filed before an order of confirmation is entered would render the chapter unworkable in many situations, because claims may be filed by creditors up until the time the court enters its order of confirmation. It is also conceivable that Chapter 11 proceedings may be required in order to confirm a plan which had been worked out between the creditors and the debtor prior to the filing. Some claims, such as claims of the Internal Revenue Service, require filing of the Chapter 11 proceeding in order to proceed with the program worked out between the creditors and the debtor. A plan filed with the petition could conceivably be confirmed within 45 to 60 days. With claims being filed until the date of confirmation, it is probable that the debtor would not review the claims until after confirmation. Therefore, there would be no time limitation in the chapter for the filing of objections to claims absent a court order directing the debtor to object to claims by or before a particular date.

Under the old Chapter XI, section 369 specifically provided that the court retain jurisdiction until the final allowance or disallowance of all claims. This provision was required because under old Chapter XI, claims had to be filed by all parties in interest and if claims were not filed by the date of confirmation, an additional 30 days

tle, the holder of such claim will receive on account of such claims deferred cash payments, over a period not exceeding six years after the date of assessment of such claim, of a value, as of the effective date of the plan, equal to the allowed amount of such claim.

were provided for the filing of claims. However those claims were limited by the amount scheduled by the debtor. Under the old Chapter X, neither section 196 nor Rule 10-40(f) limited the time in which the trustee could object to claims. The claim procedures under the old Chapters X and XI were merged and carried on under new Chapter 11.⁶⁷ This to some extent explains why there is no provision in the Code limiting the court's jurisdiction to hear and determine claims. The Code contains broad language directing the debtor to follow the orders of the court.⁶⁸

Traditionally, the courts have viewed the order of confirmation in a reorganization case as merely a step in the administration of the estate. Confirmation of the plan in no way interfered with the jurisdiction of the court to see that the plan was consummated.⁶⁹ Nothing divested the court of jurisdiction over the debtor's plan until the plan was consummated and a closing order entered.⁷⁰ The case terminated on the entry of the final decree.⁷¹

E. The Position of the Unscheduled Creditor Post-Confirmation

The holder of an unscheduled claim without knowledge of the Chapter 11 proceeding will probably pursue the debtor post-confirmation. Subsection (d) of section 1141 provides as follows:

(d)(1) Except as otherwise provided in this subsection, in the plan, or in the order confirming the plan, the confirmation of a plan—

(A) discharges the debtor from any debt that arose before the date of such confirmation, and any debt of a kind specified in section 502(g), 502(h), or 502(i) of this title, whether or not—

(i) a proof of the claim based on such debt is filed or deemed filed under section 501 of this title;

⁶⁷*In re Oakton Beach & Tennis Club*, 9 Bankr. 201 (E.D. Wis. 1981).

⁶⁸For post-confirmation provisions, see 11 U.S.C. § 1142 (Supp. IV 1980). There are no Chapter 11 cases known to the author on the subject of the trustee's timely objection to claims, but this question is treated in a Chapter 13 context in *In re Harris*, 2 Bankr. 369 (D.D.C. 1980).

⁶⁹See *Standard Gas & Elec. Co. v. Taylor (In re Deep Rock Oil Corp.)*, 113 F.2d 266 (10th Cir.), cert. denied, 311 U.S. 699 (1940); *Wright v. City Nat'l Bank & Trust Co.*, 104 F.2d 25 (6th Cir. 1939). See also *North American Car Corp. v. Peerless Weighing & Vending Mach. Corp.*, 143 F.2d 938 (2d Cir. 1944).

⁷⁰See *North American Car Corp. v. Peerless Weighing & Vending Mach. Corp.*, 143 F.2d 938 (2d Cir. 1944).

⁷¹See Rule 3010 of the Bankruptcy Rules of the United States Bankruptcy Court, Southern District of Indiana.

(ii) such claim is allowed under section 502 of this title;
or

(iii) the holder of such claim has accepted the plan; and

(B) terminates all rights and interest of equity security holders and general partners provided for by the plan.

2) The confirmation of a plan does not discharge an individual debtor from any debt excepted from discharge under section 523 of this title.

(3) The confirmation of a plan does not discharge a debtor if—

(A) the plan provides for the liquidation of all or substantially all of the property of the estate;

(B) the debtor does not engage in business after consummation of the plan; and

(C) the debtor would be denied a discharge under section 727(a) of this title if the case were a case under chapter 7 of this title.⁷²

Section 502(g) refers to claims arising out of a rejection of executory contract;⁷³ section 502(h) deals with the recovery of property by the debtor for an avoidable transfer or as a result of an avoidable preference;⁷⁴ and section 502(i) deals with tax claims entitled to priority which arise after the commencement of the case.⁷⁵ Section 1141(d)(3)(C) deals only with individual debtors and involves the provisions of section 727(a) which would bar a discharge of the debtor if the case arose under Chapter 7.⁷⁶

⁷²11 U.S.C. § 1141(d) (Supp. IV 1980).

⁷³*Id.* § 502(g) provides:

A claim arising from the rejection, under section 365 of this title or under a plan under chapter 9, 11, or 13 of this title, of an executory contract or unexpired lease of the debtor that has not been assumed shall be determined, and shall be allowed under subsection (a), (b), or (c) of this section or disallowed under subsection (d) or (e) of this section, the same as if such claim had arisen before the date of the filing of the petition.

⁷⁴*Id.* § 502(h). This section deals with claims which arise from property recoveries under 11 U.S.C. §§ 522(i), 550, and 553 (Supp. IV 1980). Section 522(i) deals with debtor's avoidance of a transfer or recovery of a setoff. Section 550 addresses the liability of the transferee vis-a-vis the debtor's efforts to avoid. Section 553 concerns the rights of a creditor to offset mutual debt.

⁷⁵*Id.* § 502(i).

⁷⁶COLLIER ON BANKRUPTCY, ¶ 523.03, at 523-8 to -9 (15th ed. L. King 1981) provides:

Section 523 specifically excepts certain debts from discharges granted under section 727, 1141 and 1328(b). Nine types of debts are enumerated as excepted from discharge of "an individual debtor." It must be particularly noted that section 523 applies only to individual debtors. . . . In a reorganization case under Chapter 11, while confirmation of a plan discharges the "deb-

For unscheduled claims, section 1141(d)(1)(A)(i) provides that the discharge occurs whether or not a claim was filed or deemed filed pursuant to section 501 of the Code. It is clear from this portion of the statute that an unscheduled claim is discharged under a confirmed plan, insofar as the corporate debtor, partnership, or unincorporated association is concerned. Section 523(a)(3) would, if applicable, bar the discharge of an unscheduled claim under the confirmed plan of arrangement. However, that section is not applicable to a Chapter 11 plan under the provisions of section 1141.

*F. The Tort Claim—Insurance Coverage—
Ability to Pursue the Carrier Post-Confirmation*

Consider a situation in which the debtor operated a number of convenience stores. Prior to the debtor's filing under Chapter 11, an employee of the debtor is killed during a robbery of one of the stores and the estate feels that it has a claim based upon the decedent's employer's failure to provide her with a safe place to work which would have protected the deceased from acts of violence. A Chapter 11 proceeding was filed in May of 1980 and the schedules did not include any claim, contingent or disputed, of the deceased or the estate. The administrator had no actual knowledge of the bankruptcy proceedings and seeks to bring suit against the insurance company who insured the debtor pre-petition by filing an adversary proceeding against the reorganized debtor in the Chapter 11 proceeding after confirmation. The action against the reorganized debtor is brought approximately one year after the proceeding had been initiated by a voluntary petition and eight months after the plan of arrangement had been confirmed. Query whether the order of confirmation discharging the debtor from liability to the unscheduled creditor also discharges the insurance company. Indiana Code section 27-1-13-7 seems to provide that a discharge in bankruptcy of the insured will not affect the liability of the carrier.⁷⁷

In a case in which the plaintiff in the suit against the personal injury carrier clearly prejudices the insurance company by failing to file a claim in the Chapter 11 proceeding, especially where a plan provides for fairly high dividend or perhaps 100% repayment, is the exposure of the insurance company lessened by the amount the debtor failed to collect from the Chapter 11 proceeding? There are no authorities on the subject, but clearly there appears to be exposure

tor." (which may be an individual, partnership or corporation) it is specifically provided that confirmation of a plan does not discharge an individual debtor from any debt excepted from discharge under section 523.

⁷⁷See IND. CODE § 26-1-13-7 (1976).

here created by the failure to file a claim in the Chapter 11 proceeding, regardless of the Indiana statute.

*G. Failure to Perform by the
Reorganized Debtor Post-Confirmation*

If the new entity as a result of confirmation fails to perform under the plan, what is the amount of debt due a creditor affected by the plan and what are the remedies of the creditor? The amount of debt due the creditor faced with a reorganized debtor's failure post-confirmation and pre-substantial consummation of the plan is the balance due and unsatisfied under the plan.⁷⁸

⁷⁸See 11 U.S.C. § 1144 (Supp. IV 1980); see also *In re Stratton Group, Ltd.* 12 Bankr. 471 (S.D.N.Y. 1981).

In the *Stratton* case, Judge Babbit discussed the subject of the amount due the creditor post-confirmation under Chapter XI of the Act, finding that the dissatisfied creditor's claim against the defaulting debtor now in straight bankruptcy was the balance due under the confirmed plan of arrangement. The principles set forth in *Stratton* apply to a case under the Code.

Thus, when Congress, in Section 371, defined the confirmation discharge to release the rehabilitated debtor from all his unsecured debts provided for by the plan, Congress gave meaning to its policy of affording debtors rehabilitation and a fresh start. Confirmation fixes the reach of claims that are allowed and that the debtor treats in the plan. Where the debtor effects a composition, he is relieved of his old debts and simply has the burden of achieving the promises made in the composition. The composition thus operates as an absolute settlement, and the failure to pay unpaid obligations created by the plan will not revive the old debts. *Jacobs v. Fensterstock*, *supra*, citing *In re Mirkus*, 289 F. 732 (2d. Cir. 1923). In the composition plan, the creditor receives what he bargained for there and has no right to claim more. *In re Lane*, 125 F. 772 (D.C. Mass. 1902). There is nothing in the Act to suggest that the debtor's failure to achieve promises made in a confirmed plan reinstates an original obligation. *In re Setzler*, 73 F. Supp. 314 (D.C. Cal. 1947). It would take a much clearer expression by Congress to enforce a policy wherein a debtor who unsuccessfully attempts to rehabilitate himself and benefit his creditors through a confirmed plan finds himself obligated for the original amount of the debts, whereas a straight bankrupt is discharged of all his obligations.

While the question is not entirely free from doubt, this court's conclusion finds support in the language of section 371. The phrase "unsecured debts and liabilities provided for by the arrangement" obviously means the treatment given the debts by the plan and not, as Elco would have it, the amount actually promised. The word "debt" is defined by Section 1(14), 11 U.S.C. (1976 ed.) § 1(14), to mean the totality of an obligation which may be asserted in a proceeding under the Act. These are the debts provided for in the debtor's plan and discharged by confirmation. How the debtor composes them in the plan and how the debtor achieves his promises is something else.

Accordingly, in this dispute, that something else merely means that Elco is entitled to its 35% less what it was paid. The 65% of its original debt was released by the discharge of the confirmation and the trustee in

If there is no subsequent voluntary Chapter 7 or 11 filing by the reorganized debtor, what remedies are available to the creditor to seek recovery of the balance due under the unconsummated plan? Clearly the creditor is relegated to filing suit on the debt in the appropriate non-bankruptcy forum, initiating an involuntary proceeding under Chapter 7 or 11, or seeking modification of the plan under 11 U.S.C. § 1127, which has yet to be interpreted by any court.

V. CONCLUSION

As can be seen from the foregoing discussion, the confirmation of a plan under Chapter 11 has a devastating effect on creditors' rights against a debtor. Creditors must be involved in the Chapter 11 case whether the task is palatable to them or not. They must be sure that any rights that they have under a contractual agreement are safeguarded if deemed valuable and that they understand the plan of arrangement and what is going to occur with regard to the indebtedness post-confirmation as a result of that plan.

As the discussion above also indicates, regardless of the posture of the parties prior to confirmation, the plan controls the post-confirmation posture. If creditors want to enforce their rights under the plan post-confirmation, they are relegated to their rights outside of the bankruptcy proceeding. They must proceed outside of the bankruptcy court to force the debtor to perform according to the contractual arrangement between the reorganized debtor and the creditor under the plan unless the plan provides for continuing jurisdiction of the bankruptcy court to hear such matters. Most plans do not. Should the debtor reach its goal in the Chapter 11 proceeding of reorganizing and obtaining confirmation of the proposed plan, the creditors are bound by the terms of that plan.

Chapter 11 is a useful tool which has wide ramifications that must be understood by those members of the commercial bar representing the debtor's side as well as the creditors. The Code itself contains certain safeguards for creditor's. It is incumbent upon the creditors and their attorneys to utilize these safeguards, and this requires an understanding of the entire Chapter 11 process.

bankruptcy is entitled to an order reflecting this disposition of Elco's claim in the debtor's ensuing bankruptcy. Submit such an order.
In re Stratton, Ltd., 12 Bankr. at 474-75.

ADDENDUM**UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION**

In re
JERICO, INCORPORATED,
Debtor.

NO. IP

PLAN OF REORGANIZATION*Definitions*

The following terms, when used in the Plan, shall, unless the context otherwise requires, have the following meanings, respectively:

Debtor: Jerico Incorporated, an Indiana corporation.

Chapter 11: Chapter 11 of the Bankruptcy Code.

Court: The United States Bankruptcy Court for the Southern District of Indiana, Indianapolis Division, acting in this case.

Plan: This Plan of Reorganization.

Creditors' Committee: That Creditors' Committee appointed by the court herein.

Confirmation of the Plan: The entry by this Court of an order confirming the Plan in accordance with Chapter 11.

Consummation of Plan: The accomplishment of all things contained or provided for in this Plan, and the entry of an order of consummation finally dismissing the case.

Effective Date: That date on which the order confirming the Plan becomes final and nonappealable.

Joint Venture: The relationship of Gannon Oil Co., Inc. and ABC, Inc.

Guaranteed: The unconditional joint and several guarantee of Gannon Oil Co., Inc. and ABC, Inc.

Reorganized Debtor: The status of the Debtor after confirmation of the Plan.

The official Creditors Committee and Terry Shake, Trustee, both being parties in interest propose the following plan of arrangement.

Article I

Classification of Claims and Interests

The claims and interests shall be classified as follows:

- Class 1 Unsecured claims to the extent that such claims are approved and allowed by the Court, including unsecured claims arising from the rejection of all executory contracts not assumed under this Plan.
- Class 2 Unsecured claims of The Northfield Corporation and Bank of Indiana to the extent that such claim is approved and allowed by the Court.
- Class 3 The claim of Gannon Oil Co., Inc. to the extent that such claim is approved and allowed by the Court.
- Class 4 Secured claims as such claims existed on the date of the filing of the petition for relief under Chapter 11 of the Bankruptcy Code.
- Class 5 Claim of the Bloomington Bank.

Article II

Claims and Interests not Impaired Under the Plan

There are no class of claims or interests which are not impaired under this Plan.

Article III

Treatment of Classes that are Impaired Under the Plan

Each class of claim shall be treated as follows:

- Class 1 Each member of this class shall have the option of the selection of one of the following alternatives:
 - A. A sum equivalent to fifty-six percent (56%) of the allowed claim. This payment shall be made in one cash payment at the time of the effective date of the Plan.
 - B. A sum equivalent to seventy-eight percent (78%) of the allowed claim. This payment shall be evidenced by an installment promissory note issued on the effective date of confirmation of the Plan by the Reorganized Debtor, payable in

thirty-six (36) equal monthly installments without interest commencing upon the first day of the month following the effective date of the Plan. The first twenty-four (24) monthly payments will be guaranteed by each member of the joint venture.

C. Payment of one hundred percent (100%) of the allowed claim by the Court. This payment shall be evidenced by an installment promissory note issued on the effective date of confirmation of the Plan by the Reorganized Debtor, the final payment being one hundred twenty (120) months from the effective date of the Plan. The note shall be without interest. Monthly installment payments shall commence twelve (12) months following the effective date of the Plan and shall continue in one hundred eight (108) equal installments thereafter. Each payee of the note shall have the option at the end of ninety-six (96) months to demand payment on the entire note balance. The first thirty-six (36) monthly payments will be guaranteed by each member of the joint venture.

Class 2 Payment of one hundred percent (100%) of the allowed claim by the Court. This payment shall be evidenced by an installment promissory note issued on the effective date of the confirmation of the Plan by the Reorganized Debtor, the final payment being due one hundred twenty (120) months from the effective date of the Plan. The note shall be without interest. Monthly installment payments shall commence twelve (12) months following the effective date of the Plan and shall continue in one hundred eight (108) equal installments thereafter. The payee of the note shall have the option at the end of ninety-six (96) months to demand payment on the entire note balance. The first thirty-six (36) monthly payments will be guaranteed by each member of the joint venture.

Class 3 In the same manner as Class 1 claims.

Class 4 The debt shall be paid pursuant to the terms of the debt instrument except the interest rate in each instrument shall be a fixed simple interest rate of ten percent (10%) per annum. Past due

installments existing on the effective date of the Plan will be cured first by extending the term of each debt by two months. Then the balance of any cure shall be paid at the effective date of the Plan. The holder of each claim will retain a lien on the property securing said debt.

- Class 5 The debt shall be paid pursuant to the terms of the debt instrument except the interest rate in each instrument shall be a fixed simple interest rate of ten percent (10%) per annum. Past due installments existing on the effective date of the Plan will be cured first by extending the term of each debt by two months. Then the balance of any cure shall be paid at the effective date of the Plan. The holder of each claim will retain a lien on the property securing said debt. The claim shall be guaranteed to the extent of the portion previously guaranteed to the Small Business Administration.

Article IV

Provisions for Acceptance or Rejection of Executory Real Estate Leases

A. The debtor will assume pursuant to § 365 of the Bankruptcy Code, each of the executory real estate leases set forth in Exhibit A attached hereto and made a part hereof.

B. The debtor shall assume, pursuant to § 365 of the Bankruptcy Code, the executory franchisee contracts discussed in Exhibit B attached hereto and made a part hereof.

C. The executory real estate leases set forth in Exhibit C [not attached for purposes of this Article] shall, pursuant to § 365 of the Bankruptcy Code, upon notice and hearing to any person, firm or corporation claiming an interest, be rejected and at such hearing the Court shall fix the dollar amount of damages, if any, and such person, firm or corporation shall become a Class 1 creditor.

D. The executory real estate leases set forth in Exhibit D [not attached for purposes of this Article] shall be conditionally assumed by the Debtor until August 31, 1981 pursuant to the terms of the lease. The Reorganized Debtor would have the right to either affirm or reject the executory lease by giving the lessor notice. If the Reorganized Debtor elects to reject the lease, the landlord would become a Class 1 creditor.

E. The Debtor shall assume all executory contracts with The Northfield Corporation which will be paid pursuant to the terms of the Plan.

F. Any and all other executory contracts of the Debtor not specifically set forth herein are hereby rejected and treated as Class 1 claims.

Article V

Means for Execution of the Plan

Execution of this Plan upon its effective date shall be accomplished pursuant to an agreement entered into by and between the Joint Venture, the Trustee, and Official Creditors' Committee executed June 17, 1980. The Joint Venture, under separate agreement with the individual shareholders, will purchase the outstanding shares of the Debtor's stock prior to the effective date of the Plan.

Article VI

Provisions for Priority Claims

Each claim of the kind specified in sections 507(a)(1), 507(a)(2), 507(a)(3), 507(a)(4), and 507(a)(5) shall be paid on the effective date of the Plan cash equal to the allowed amount of such claim unless said claims are waived or payments otherwise agreed to. Each claim of the kind specified in Section 507(a)(6) shall be paid in full when due.

Article VII

General Provisions

Until the case is closed, the Court shall retain jurisdiction to insure that the purpose and intent of this Plan are carried out. The Court shall retain jurisdiction to hear and determine all claims against the Debtor and to enforce all causes of action which may exist on behalf of the Debtor. Nothing herein contained shall prevent the Reorganized Debtor from taking such action as may be necessary in the enforcement of any cause of action which may exist on behalf of the Debtor and which may not have been enforced or prosecuted by the Trustee.

DATED: July 15, 1980 .

OFFICIAL CREDITORS' COMMITTEE

by _____
ROBERT COOPER
One of Counsel

TERRY SHAKE, Trustee for
JERICO, INCORPORATED

by _____
EVERETT LINDSAY
One of Counsel

Acceptance

Gannon Oil Co., Inc. and ABC, Inc., have entered into an agreement on or about June 17, 1980 with Terry Shake, Trustee, and the Official Creditors, Committee, hereby acknowledge the Plan of Reorganization contained herein and accept its terms pursuant to said Agreement.

DATED this 15 day of July, 1980.

GANNON OIL CO., INC.

by _____

ABC, INC.

by _____

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

IN RE:

JERICO INCORPORATED,
Debtor.

NO.

DISCLOSURE STATEMENT

I

Introduction

Terry Shake, Trustee of Jerico, Incorporated, the debtor, and the Official Creditors' Committee of Jerico, Incorporated provides this Disclosure Statement to all of the known creditors of Jerico, Incorporated in order to disclose that information deemed by the Trustee and the Official Creditors' Committee to be material, important, and necessary for the creditors of Jerico, Incorporated to arrive at a reasonably informed decision in exercising their right to vote for acceptance of the Plan of Reorganization (hereinafter "the Plan") presently on file with the Bankruptcy Court. A copy of the Plan accompanies this Statement.

The Court has set August 15, 1980, at 10:00 a.m. for a first meeting of creditors and at 11:00 a.m. for a hearing on the acceptance of the Plan of Reorganization. Creditors may vote on the Plan by filling out and mailing the accompanying Acceptance Form to the Bankruptcy Court or may attend such hearing and present the Acceptance in person at that time. As a creditor, your acceptance is important. In order for the Plan to be deemed accepted, creditors that hold at least two-thirds in amount and more than one-half in number of the allowed claims of Class 1 and 5 must vote for the Plan.

NO REPRESENTATIONS CONCERNING THE DEBTOR (PARTICULARLY AS TO HIS FUTURE BUSINESS OPERATIONS, VALUE OF PROPERTY, OR THE VALUE OF ANY PROMISSORY NOTES TO BE ISSUED UNDER THE PLAN) ARE AUTHORIZED BY THE TRUSTEE OR THE OFFICIAL CREDITORS' COMMITTEE OTHER THAN AS SET FORTH IN THIS STATEMENT. ANY REPRESENTATIONS OR INDUCEMENTS MADE TO SECURE YOUR ACCEPTANCE WHICH ARE OTHER THAN AS CONTAINED IN THIS STATEMENT SHOULD NOT BE RELIED UPON BY YOU IN ARRIVING AT YOUR DECISION, AND SUCH ADDITIONAL REPRESENTATIONS AND INDUCEMENTS SHOULD BE REPORTED TO COUNSEL FOR THE TRUSTEE WHO IN TURN SHALL DELIVER SUCH INFORMATION TO THE BANK-

RUPTCY COURT FOR SUCH ACTION AS MAY BE DEEMED APPROPRIATE.

THE INFORMATION CONTAINED HEREIN HAS NOT BEEN SUBJECT TO A CERTIFIED AUDIT. THE RECORDS KEPT BY THE DEBTOR AND TRUSTEE ARE DEPENDENT UPON AN ACCOUNTING PERFORMED BY OTHERS BEYOND THE CONTROL OF THE TRUSTEE OR THE OFFICIAL CREDITORS' COMMITTEE. FOR THE FOREGOING REASONS, AS WELL AS BECAUSE OF THE GREAT COMPLEXITY OF THE DEBTOR'S FINANCIAL MATTERS, THE TRUSTEE AND THE OFFICIAL CREDITORS' COMMITTEE IS UNABLE TO WARRANT OR REPRESENT THAT THE INFORMATION CONTAINED HEREIN IS WITHOUT ANY INACCURACY, ALTHOUGH GREAT EFFORT HAS BEEN MADE TO BE ACCURATE.

II

The Plan of Reorganization

The Plan is based upon the belief of the Trustee and the Official Creditors' Committee that the present forced liquidation value of the principal assets of the debtor is so small as to offer the potential of only a minimal recovery to general unsecured creditors. The Trustee and the Official Creditors' Committee believe it is possible and in the best interest of all creditors to allow for the continued operation of the debtor as a reorganized debtor, pursuant to which, the reorganized debtor will make available to general unsecured creditors three alternatives for payment of a percentage of their claim and will allow for the normal retirement of secured indebtedness over a negotiated period of time at a negotiated rate of interest all of which are to be paid out of the future operations of the debtor-in-possession and some of which payments are to be guaranteed as hereinafter more specifically set forth. It is believed that if the debtor were liquidate, the amount realized by unsecured creditors would be minimal in relation to what is being proposed to the various classes of creditors pursuant to the Plan of Reorganization which accompanies this statement.

The Plan provides in Article I for the classification of claims and interests. The claims and interests are classified into five separate classes.

Class I claims are unsecured claims approved and allowed by the Court. Claims under this class are generally unsecured creditors who are either purveyors, suppliers of merchandise, or suppliers of services and includes unsecured claims arising from the rejection of all executory contracts not specifically assumed under the Plan. Each member of Class I, shall have the option of selecting one of the following alternatives:

(a) The sum equivalent to 56% of the allowed claim. This payment of 56% shall be made in one cash payment at the time of confirmation of the Plan. Funds for this payment will be made available by funds on hand of the debtor and by an infusion of capital of a joint venture composed of Gannon Oil Co., Inc., and ABC, Inc., the entities which are purchasing the stock of the debtor corporation.

(b) A sum equivalent to 78% of the allowed claim of each unsecured creditor. This payment shall be in the form of an installment promissory note (see Exhibit "A") issued on the effective date of confirmation of the Plan by the reorganized debtor and payable in 36 equal monthly installments without interest, commencing on the 1st date of the month following the effective date of the Plan. The first 24 monthly payments will be guaranteed by each member of the joint venture.

(c) Payment of 100% of the allowed claim by the Court. This payment shall be in the form of an installment promissory note (see Exhibit "B") issued on the effective date of confirmation of the Plan by the reorganized debtor with the final payment being 120 months from the effective date of the Plan. The note shall be without interest. Monthly installment payments shall commence 12 months following the 1st date of the month following the effective date of the Plan and shall continue in 108 equal installments thereafter. Each payee of the note shall have the option at the end of 96 months to demand payment on the entire note balance. The first 36 monthly payments will be guaranteed by each member of the joint venture.

The three methods of payment to unsecured creditors in Class I offer an alternative to each member of that class to choose the payment program which he wishes. The acceptance by the creditor of an immediate payment of 56 cents on the dollar as of the effective date of the Plan would provide no risk to any member in Class I. The acceptance of alternative (b) or (c), providing for 78% of the allowed claim over a period of 36 months or 100% of the allowed claim over a period of 120 months, provides a certain risk to an accepting unsecured creditor in Class I which will be set forth under the heading *Special Risk Factors*. A copy of the form of the note to be provided Class I creditors who choose alternative (b) or (c) is attached.

Class I further provides for unsecured claims arising from the rejection of certain executory contracts for the lease of real estate to the extent that such claim is approved and allowed by the Court. The debtor owns no real property and leases all locations where its

stores are located. The Plan sets forth in Article IV the leases which will be assumed by the reorganized debtor and the leases that will be rejected by the debtor. Article III Class I provides for the method of payment to those lessors holding leases which are rejected by the debtor. Under § 502 of the United States Bankruptcy Code, the lessor has a claim for damages resulting from a termination of the lease of real property to the extent of the rent reserved by such lease, without acceleration, for the greater of one year or fifteen percent, not to exceed three years of the remaining term of such lease, following the earlier of the date of the filing of the petition, the date on which such lessor repossessed, or the date on which the lessee surrendered the leased property, plus any unpaid rent due under such lease, without acceleration, on the earlier of such dates.

In addition to those executory contracts which are to be assumed by the reorganized debtor as set forth in Exhibit "A" to the Plan of Reorganization, and in addition to the executory real estate leases as set forth in Exhibit "C" which are to be rejected by the debtor, Article IV subparagraph (d) provides for certain executory real estate leases which are set forth in Exhibit "D" to the Plan of Reorganization and are to be conditionally assumed by the reorganized debtor until August 31, 1981, pursuant to the terms of the lease. At the termination of that period, the reorganized debtor would have the right to either affirm or reject the executory lease. If the reorganized debtor elects to reject the lease, the landlord would become a Class I creditor for its allowed claim in these proceedings. Article IV further sets forth the provision that the debtor shall assume, pursuant to § 365 of the United States Bankruptcy Code, the executory franchise contracts set forth in Exhibit "B" to the Plan of Reorganization. ANY AND ALL OTHER EXECUTORY CONTRACTS OF THE DEBTOR NOT SPECIFICALLY SET FORTH IN ARTICLE IV ARE REJECTED PURSUANT TO THE PLAN OF REORGANIZATION. CLAIMS ARISING THEREFROM SHALL BE TREATED AS CLASS I CREDITORS.

The Plan also provides for the classification of a separate class of creditors composed of the Northfield Corporation and the Bank of Indiana. This separate classification is set forth by virtue of the fact that the Northfield Corporation is not only a general unsecured creditor as a purveyor of merchandise but is also a licensor of the debtor and has guaranteed certain obligations of the debtor, including but not limited to, the obligation that is due and owing to the Bank of Indiana and any obligations for attorney fees arising out of that certain lawsuit entitled *The Northfield Corporation, plaintiff—counter-defendant v. Super Markets, Inc., defendant—counter-plaintiffs v. Jerico, Inc., counter-defendant*, pending in the United

States District Court for the Southern District of Indiana, Indianapolis Division, which is presently on appeal to the United States Court of Appeals for the Seventh Circuit. The obligation due and owing to the Northfield Corporation, licensor and purveyor of goods to the debtor, is in the approximate amount of \$395,456.00, together with an indebtedness due from debtor to the Bank of Indiana guaranteed by Northfield in the approximate amount of \$216,666.00, together with additional amounts estimated to be due Northfield in the amount of \$40,000.00, for a total amount due and owing to Northfield Corporation on all obligations in the sum of \$652,122.00. The Plan of Arrangement, as proposed, provides for the payment to creditors of Class II of 100% on the dollar of the allowed claim by the Court. The payment of 100 cents on the dollar is the same alternative offered to creditors of Class I, in that the payment of 100 cents on the dollar shall be evidenced by an installment promissory note issued on the effective date of confirmation of the Plan by the reorganized debtor, the final payment being dated 120 months from the effective date of the Plan. The note issued by the reorganized debtor shall be without interest. Monthly installment payments shall commence twelve months following confirmation and shall continue in 108 equal installments thereafter. The payee of the note shall have the option at the end of ninety-six months to demand payment of the entire note balance. The first thirty-six monthly payments will be guaranteed by the joint venture of Gannon Oil Co., Inc. and ABC, Inc. It is important to note that the treatment of Class II creditors is the offered to Class I creditors.

Class III of the Plan is Gannon Oil Co., Inc., since it is a purchaser of the stock of Jerico, Incorporated, and will be executing certain guarantees as the creditors in Class I may choose. Treatment afforded to Gannon Oil Co., Inc. is the same treatment that is being afforded to Class I creditors.

The Plan further provides for classification of secured creditors in Class IV. These creditors are primarily creditors who hold security on certain equipment of the debtor and include the Bank and Trust, Columbus, Indiana; the National Bank and Trust Company, Indianapolis, Indiana; the Bank and Trust, Noblesville, Indiana; the National Bank, Danville, Indiana; the Bank & Trust, Little Rock, Arkansas; and the Bank and Trust New Albany, Indiana. The debt evidenced by creditors holding claims in Class IV shall be paid pursuant to the terms of the debt instrument except that the interest rate in each instrument shall be a fixed simple interest rate of 10% per annum. Past due installments existing on the effective date of the Plan will be cured first by extending the term of each debt by two months. Then the balance of any cure shall be paid at the effective date of the Plan. The holder of each claim will retain a lien on the property securing said debt.

The remaining classification of claims is Class V which provides for a classification of the claim of the Bloomington Bank. The Bloomington Bank is set forth in a separate class by virtue of its setting off of certain obligations due and owing to the Bloomington Bank in the sum of \$173,884.92 within ninety days prior to bankruptcy. The Trustee and the Official Creditors' Committee has taken the position that said set off is a preference. Notwithstanding that fact, the Plan proposes to treat the Bloomington Bank in Class V upon repayment by the Bloomington Bank to the Trustee of the sums set off with repayment of said debt to the Bloomington Bank pursuant to the terms of the debt instrument with the bank, except that the interest rate in said instrument shall be a fixed simple interest rate of 10% per annum. Past due installments existing on the effective date of the Plan will be cured first by extending the terms of the debt by two months. The balance of any cure shall be paid at the effective date of the Plan. The Bloomington Bank will retain a lien on the property securing said debt, and the debt shall be guaranteed by each member of the joint venture for the SBA portion previously guaranteed.

THE FOREGOING IS A BRIEF SUMMARY OF THE PLAN AND SHOULD NOT BE RELIED ON FOR VOTING PURPOSES. CREDITORS ARE URGED TO READ THE PLAN IN FULL. CREDITORS ARE FURTHER URGED TO CONSULT WITH COUNSEL OR WITH EACH OTHER IN ORDER TO FULLY UNDERSTAND THE PLAN. THE PLAN IS COMPLEX INASMUCH AS IT REPRESENTS A PROPOSED LEGALLY BINDING AGREEMENT BY THE TRUSTEE, DEBTOR, AND REORGANIZED DEBTOR, AND AN INTELLIGENT JUDGMENT CONCERNING SUCH PLAN CANNOT BE MADE WITHOUT UNDERSTANDING IT.

III

Financial Information Respecting the Reorganized Debtor

The financial information hereinafter presented is to be considered in the context of the debtor's primary business activity of operating convenience food stores and making sales of gasoline. As previously stated, the debtor owns no real property. All real property utilized by the debtor is on lease, and there may or may not be any equity value in any of the leases. The machinery and equipment used in the business has been used for a period of time, and it is estimated that the depreciated value of the equipment on the books of the corporation is not its true liquidation value. Its true liquidation value in the estimates of the Trustee and the Official Creditors' Committee would be much less than the depreciated book value and

also much less than any amount owing to secured creditors on said equipment. The debtor did not own at any time any gasoline pumps or any gasoline storage tanks. That equipment was at all times owned by Gannon Oil Co., Inc. A further question arises as to whether or not gasoline in storage tanks on various premises of the debtor was in fact inventory of the debtor or belonged to Gannon Oil Co., Inc. under a consignment agreement. The Trustee and Official Creditors' Committee have taken the position that the gasoline on hand at any given date was an asset of the debtor. Gannon Oil Co., Inc. has taken the position that it was an asset of Gannon Oil Co., Inc. The treatment of Gannon Oil Co., Inc. as an unsecured creditor pursuant to the Plan of Arrangement puts that issue at rest. However, the value of the remaining machinery and equipment of the debtor, in your Trustee's opinion, is insignificant to the amount due and owing on the equipment and has no relationship to the depreciated book value of said equipment. With the exception of inventory, therefore, all of debtor's assets are encumbered by holders of prior secured claims, and accordingly, the amount of both secured claims and unsecured claims is relevant.

A statement of assets and liabilities of the debtor as of the date of the filing of the petition under Chapter 11 of the United States Bankruptcy Code on May 28, 1980, has been filed with the Bankruptcy Court as of July 9, 1980. The schedule and statement of assets and liabilities should be inspected by all interests parties. The Trustee has estimated the total debts of the debtor to be as follows:

| | |
|--|---------------------|
| Taxes owing to other than taxing authorities | \$ 20,000.00 |
| Secured claims | 712,848.59 |
| Unsecured claims without priority | <u>1,762,818.56</u> |
| Total debts of debtor corporation | 2,495,667.15 |

These are estimates only by the Trustee, and there has been no independent verification from creditors. IT IS IMPORTANT TO NOTE THAT ALL DEBTS OF THE DEBTOR WERE LISTED BY THE TRUSTEE AS BEING DISPUTED, CONTINGENT, AND UNLIQUIDATED BY VIRTUE OF THE FACT THAT THE TRUSTEE COULD NOT INDEPENDENTLY VERIFY AND HAS NOT HAD SUFFICIENT TIME TO INDEPENDENTLY VERIFY THAT THE TOTAL DEBTS AS SET FORTH ON THE SCHEDULES AND STATEMENTS OF AFFAIRS ARE ACCURATE. SINCE THE TRUSTEE HAS LISTED ALL DEBTS AS DISPUTED, CONTINGENT, AND UNLIQUIDATED, FOR ANY CREDITOR TO SHARE IN A DISTRIBUTION IN THE ESTATE AND RECEIVE A DIVIDEND FROM THE ESTATE, SAID CREDITOR *MUST* FILE A PROOF OF CLAIM IN THESE PROCEEDINGS. It is further noted by the Trustee and the Official Creditors' Committee that the amount of debts of the corporation may be increased by virtue of certain lawsuits pending, a portion of which have been removed to the Bankruptcy Court, and a portion of which are on appeal. In addition, the debts as scheduled by the Trustee do not include any amounts that would be due to lessors under rejection of executory lease contracts. Those amounts arising by the rejection of executory contracts in Arti-

cle IV (c), and those amounts arising by those executory contracts which may be rejected in one year under Article IV (d) are not included in the total debt listing of the Trustee.

The schedules and statement of affairs further reflect the property as listed by the Trustee as belonging to the debtor. That property may be summarized as follows and as appearing as of May 28, 1980, the date of the filing of the Chapter 11 petition:

| | |
|--|-------------------|
| Cash on hand | \$ 393,000.00 |
| Depreciated book value of machinery, equipment, and supplies used in business | 970,000.00 |
| Inventory on hand | 310,000.00 |
| Depreciated book value of patents and other general intangibles | 55,000.00 |
| Other liquidated debts due the debtor | <u>130,000.00</u> |
| Total property of the debtor | \$1,858,000.00 |

The cash on hand of the debtor oscillates, depending upon payment for gasoline sales made, payments to suppliers, and receipts for merchandise sold. The value of depreciated machinery, equipment, and other supplies used in the business is a depreciated book value, and it is the opinion of the Trustee and the Official Creditors' Committee that the listed value is greater than the liquidation value of said equipment, machinery, and supplies used in business, and in addition, the actual liquidation value of said machinery, equipment, and supplies used in business is less than the amount owed to secured creditors. It has been estimated by the Trustee that the true liquidation value of all machinery, equipment, and supplies used in the business owned by the debtor is the sum of \$275,000.00, not including pumps and storage tanks in the ground used for gasoline which are claimed as owned by Gannon Oil Co., Inc. The inventory value in the sum of \$310,000.00 is exclusive of gasoline and has fluctuated since the date of the filing of the petition under Chapter 11 of the United States Bankruptcy Code. The patent and other general intangibles in the sum of \$55,000.00 is the original value of the license owned by the debtor for the operation of Super Markets, Inc. and its value cannot be estimated by the Trustee. Other liquidated debts due and owing to the debtor in the sum of \$130,000.00 represent accounts receivable and notes receivable of questionable value.

It is deemed relevant by the Trustee and the Official Creditors' Committee that the total estimated liquidation value of machinery, equipment, and supplies used in business is approximately \$275,000.00, taken in light of the total indebtedness due and owing on said equipment and machinery in the sum of \$712,848.59.

The following is the Trustee's best estimates of the secured creditors holding security as set forth above:

| | |
|--|--------------|
| The Bloomington Bank security in store equipment | \$173,884.92 |
| The Bank and Trust, Columbus, Indiana security in store equipment | 46,644.66 |
| The National Bank and Trust Company security in store equipment | 166,666.70 |

| | |
|---|-------------------|
| The Bank and Trust, Noblesville, Indiana | |
| security in store equipment | 28,679.04 |
| The National Bank, Danville, Indiana | |
| security in store equipment | 84,503.00 |
| The Bank and Trust, Little Rock, Arkansas | |
| security in store equipment | 92,532.00 |
| The Bank and Trust, New Albany, Indiana | |
| security in store equipment | <u>123,551.58</u> |
| Total secured indebtedness | \$716,461.90 |

The total amount due and owing to tax creditors are personal property taxes for assessments made March of 1979 and 1980 payable in May and November, 1980, in Monroe County, Marion County, Bartholomew County, Hamilton County, Madison County, Hendricks County, Hancock County, Floyd County and Clark County in the total sum of \$20,000.00.

According to the best estimates of your Trustee, the amount of claims held by general unsecured trade creditors who would be affected by the treatment of Class I creditors is in the sum of approximately \$700,000.00. Amounts due Northfield and the Bank of Indiana approximate \$652,000.00, and the debt due to Gannon Oil Co., Inc. approximates \$191,000.00. Additional claims included in the total unsecured claims without priority represent contingent lawsuits and other claims.

It is estimated that the amount of the allowed claims of lessors on the rejection of executory contracts is in the sum of \$89,493.00. In addition, certain executory contracts which are set forth in Exhibit "D" to the Plan of Arrangement will be conditionally assumed by the reorganized debtor for a period of one year, pursuant to the terms of the lease, and at the termination of one year from the effective date of the Plan, the reorganized debtor would have the right to either affirm or reject the executory leases. If the reorganized debtor elects to reject the leases, the estimated amount of unsecured liability on those leases is in the sum of \$138,915.00.

To your Trustee's knowledge, and the knowledge of the Official Creditors' Committee, the debtor owns no stock in any other entity but does hold a note in the sum of \$25,000.00 from Uptown Realty Corporation secured by property located at 21st and Vine, Indianapolis, Indiana.

The Plan provides that the joint venture of Gannon Oil Co., Inc. and ABC will purchase the issued and outstanding stock held by officers of Jerico Corporation for the sum of \$5,000.00 plus forgiveness of a \$25,000.00 note due from Steven Harold to the debtor which the joint venture deems uncollectible. Gannon Oil Co., Inc., and ABC, Inc., have been operating the debtor corporation under a manage-

ment agreement with the Trustee since June 17, 1980. The continued operation by Gannon Oil Co., Inc., and ABC, Inc., will allow for a continued and uninterrupted chain of management through the new reorganized debtor.

Said stock purchase will be consummated subsequent to acceptance of the Plan of Arrangement and prior to the confirmation of said Plan.

All priority claims will be paid in full upon consummated of the Plan of Arrangement unless waived or otherwise agreed to. Those claims include all claims set forth in sections 507(a)(1), 507(a)(2), 507(a)(3), 507(a)(4), and 507(a)(5). More specifically, those claims include administrative claims of the Trustee, the Trustee's counsel, the Official Creditors' Committee, and attorney for the debtor all of which shall be paid in full upon confirmation, and all expenses of doing business, including payments for merchandise received, shall be paid according to terms of payment, or if administrative claims are past due as of that time, they shall be paid in full. Claims of all secured creditors shall be paid pursuant to the provisions for payment of secured creditors, and the payments of all obligations under leases being assumed by the reorganized debtor shall be cured and paid in full upon confirmation. In addition, each claim of the kind specified in section 507(a)(6), tax claims of the debtor, shall be paid in full when due.

To accomplish the payments of all funds as above set forth, including provisions for treatment of classes, Gannon Oil Co., Inc., and ABC, Inc., shall fund the proposed Plan of Reorganization for the reorganized debtor and shall provide the monies necessary for payment to classes calling for payment upon confirmation and for the provisions for payment of priority claims.

IV

Special Risk Factors

Certain substantial risk factors are inherent in most securities issued pursuant to a Plan of Reorganization in a Chapter 11 case. If such plans are accepted, it is usually because they represent a greater hope for return than the dividend in a liquidating Chapter 7 case. ALL OF THE RISK FACTORS INHERENT IN SECURITIES ISSUED PURSUANT TO A PLAN OR REORGANIZATION ARE PRESENT IN THE PROMISSORY NOTES PROPOSED TO BE ISSUED IN THIS CASE SHOULD CREDITORS IN CLASS I CHOOSE TO ACCEPT PROMISSORY NOTES AND IN THE OTHER CLASSES WHERE PROMISSORY NOTES ARE ISSUED. While creditors in Class I, if they so choose, and creditors in Class II, III, IV and V will be accepting notes of the reorganized debtor,

and while there is a guarantee as set forth in Article III of certain portions of those notes by Gannon Oil Co., Inc. and ABC, those creditors accepting notes should realize that outside of the viability of Gannon Oil Co., Inc., and ABC, there is no guarantee that said notes will be paid in full when due. Based upon the April 30, 1980, financial statements supplied by Gannon Oil Co., Inc., and ABC, Inc., which are on file in the offices of the attorney for the Trustee and attorney for the Official Creditors' Committee, the combined unaudited net worth of both companies is approximately \$1,500,000.00. These financial statements may be reviewed at either of the above offices by any creditor during normal business hours. The Trustee and the Official Creditors' Committee make no representation or warranty of payment in full of said notes when due.

It is expected that should any Class I creditor choose to accept treatment under subparagraph (b) or (c) of Article III Class I and receive a promissory note that no market will exist for said notes issued under the Plan and realization upon them must await distributions pursuant to the terms of said note, if any, from the reorganized debtor. The notes as issued under the Plan are exempt from registration under the Securities Act of 1933 and State or local laws to the extent provided in 11 U.S.C. § 1145 (Supp. IV 1980).

DATED at Indianapolis, Indiana, this 15 day of July, 1980.

TERRY SHAKE, TRUSTEE FOR
JERICO, INCORPORATED

By _____
Everett Lindsay, One of Counsel

OFFICIAL CREDITORS' COMMITTEE OF
JERICO, INCORPORATED

By _____
Robert Cooper, One of Counsel

PROMISSORY NOTE AND LIMITED WARRANTYN O T E

\$ _____

Date: August____, 1980

For value received the undersigned promises to pay to the order of _____ the total sum of _____ Dollars (\$ _____), at _____ or at such other place as the holder hereof may direct in writing. Payment shall be in 36 equal monthly installments commencing on September 1, 1980 and each month thereafter. No interest shall be payable on any amount due hereunder.

In the event of any default in payment not cured within 15 days after receipt by maker of written notice of such default by certified mail addressed to maker at _____

_____, then the holder of this note shall have the right to declare the entire remaining balance immediately due and payable without further presentment, protest, notice of protest or dishonor. After default, upon acceleration, the holder shall be entitled to recover attorney fees and costs in collection of this note, all without relief from valuation and appraisal laws.

No delay or omission on the part of the holder hereof in the exercise of any right or remedy shall operate as a waiver of such right or remedy and no single or partial exercise of any right or remedy by the holder shall preclude further exercise of any other right or remedy.

JERICO, INC.

By _____
President

L I M I T E D G U A R A N T Y

Date: August____, 1980

In order to induce the payee of the above note to accept same, the undersigned, jointly and severally, absolutely guaranty the full and prompt payment of every indebtedness due together with reasonable attorney's fees and costs of collection to the extent allowed by the note.

Provided, however, the liability of the undersigned pursuant to this Guaranty shall be limited only to the making of the first 24 installments due upon the note and such guaranty shall not extend to any other installments. The liability of the undersigned shall arise upon acceleration of the note by the holder when effected in accordance with the terms contained in the note and payment of any remaining guaranteed amount shall be made upon demand. Such liability shall not be affected by any settlement, compromise, extension, or variation of the terms of the note.

The undersigned hereby expressly waive the following: (a) notice of (and acknowledge due notice of) acceptance of this Guaranty by payee; (b) protests, demands, pursuit of collection, and notices thereof; (c) notices of nonpayment and nonperformance and amount of indebtedness outstanding at any time; and (d) the right to remove any legal action from the Court originally acquiring jurisdiction. This agreement shall, without further consent of or notice to the undersigned, pass to, and may be relied upon and enforced by, any successor or assignee of payee.

GANNON OIL CO., INC.

By _____ Guarantor
ABC, INC.

By _____ Guarantor

PROMISSORY NOTE AND LIMITED GUARANTYN O T E

\$ _____ Date: August____, 1980

For value received the undersigned promises to pay to the order of _____ the total sum of _____ Dollars (\$ _____), at _____ or at such other place as the holder hereof may direct in writing. Payment shall be in 108 equal monthly installments commencing on September 1, 1980 and each month thereafter. No interest shall be payable on any amount due hereunder. The holder shall have the right to demand payment in full of the remaining balance at any time after September 1, 1988.

In the event of any default in payment not cured within 15 days after receipt by maker of written notice of such default by certified mail addressed to maker at _____

_____, then the holder of this note shall have the right to declare the entire remaining balance immediately due and payable without further presentment, protest, notice of protest or dishonor. After default, upon acceleration, the holder shall be entitled to recover attorney fees and costs in collection of this note, all without relief from valuation and appraisement laws.

No delay or omission on the part of the holder hereof in the exercise of any right or remedy shall operate as a waiver of such right or remedy and no single or partial exercise of any right or remedy by the holder shall preclude further exercise of any other right or remedy.

JERICO, INC.

By _____
President

L I M I T E D G U A R A N T Y

Date: August____, 1980

In order to induce the payee of the above note to accept same, the undersigned, jointly and severally, absolutely guaranty the full and prompt payment of every indebtedness due together with reasonable attorney's fees and costs of collection to the extent allowed by the note.

Provided, however, the liability of the undersigned pursuant to this Guaranty shall be limited only to the making of the first 36 installments due upon the note and such guaranty shall not extend to any other installments. The liability of the undersigned shall arise upon acceleration of the note by the holder when effected in accordance with the terms contained in the note and payment of any remaining guaranteed amount shall be made upon demand. Such liability shall not be affected by any settlement, compromise, extension, or variation of the terms of the note.

The undersigned hereby expressly waive the following: (a) notice of (and acknowledge due notice of) acceptance of this Guaranty by payee; (b) protests, demands, pursuit of collection, and notices thereof; (c) notices of nonpayment and nonperformance and amount of indebtedness outstanding at any time; and (d) the right to remove any legal action from the Court originally acquiring jurisdiction. This agreement shall, without further consent of or notice to the undersigned, pass to, and may be relied upon and enforced by, any successor or assignee of payee.

GANNON OIL CO., INC.

By _____ Guarantor
ABC, INC.

By _____ Guarantor

IN THE MATTER OF:) CASE NO. _____
)
) INTERIM FINANCIAL REPORT NO. ____
)
) _____ THROUGH _____
 _____)
 PETITION FILED: _____

(ITEMS 1 THROUGH 16 MUST BE ANSWERED)
(USE "NONE" OR "N/A" WHERE APPROPRIATE)

SUMMARY OF CASH TRANSACTIONS

1. Cash and Bank Balances at beginning of Current Reporting Period. \$ _____
2. Receipts during Current Reporting Period:
 - A. Cash Sales (ordinary courses of business) _____
 - B. Collection of Pre-Chapter 11 Receivables (Net of Discounts) _____
 - C. Collection of Post-Chapter 11 Receivables _____
 - D. Other Cash Receipts (attach schedule itemizing receipts-See Form 2D attached) _____

TOTAL RECEIPTS (2A through 2D) _____
3. Cash Disbursements during Reporting Period (exclude transfers between bank accounts for payrolls, taxes, etc.)
 - A. For ordinary operations:
 1. Net payroll other than officers, stockholders and directors. _____
 2. Net payroll, officers, stockholders and directors (attach list of salaries of officers, directors & management personnel requested only for initial report unless there are changes in salaries or personnel). _____
 3. Payroll taxes disbursed to taxing authorities. _____
 4. Other taxes disbursed to taxing authorities. _____
 5. Utilities. _____
 6. Insurance premiums (See #15) _____
 7. Rent (premises). _____
 8. Purchase of goods and materials. _____
 9. Other (itemize if over \$250.00-use separate schedule if necessary). _____

TOTAL SPENT FOR ORDINARY OPERATIONS: \$ _____
- B. Payments to secured parties (list below and indicate basis of payment, i.e., court order): \$ _____

- C. Administrative Disbursements (non-business expenses relating to Chapter 11):
1. Appraiser's fees and expenses.* _____
 2. Accountant's fees and expenses.* _____
 3. Other Administrative Disbursements (itemize) _____

TOTAL accountant fees paid to date.
 \$ _____

TOTAL ADMINISTRATIVE DISBURSEMENTS \$ _____

TOTAL DISBURSEMENTS \$ _____

4. Cash and Bank Account balances at inception of Chapter 11.
5. Total Cash and Bank Account balances at end of Current Reporting Period (items 1, plus 2, minus 3). \$ _____
6. Itemize cash and all bank balances invested funds, as of end of Reporting Period. Provide account numbers; identify payroll, tax and other special accounts. (The total must equal the balance shown in #5).
 Debtor-in-possession Accounts:

| DEPOSITORY | ACCT.NO. | TYPE ACCT. | BALANCE |
|--|----------|------------|----------|
| 1. | _____ | | \$ _____ |
| 2. | _____ | | \$ _____ |
| 3. | _____ | | \$ _____ |
| 4. | _____ | | \$ _____ |
| 5. | _____ | | \$ _____ |
| | | SUB TOTAL | \$ _____ |
| 7. Petty Cash on Hand | | | \$ _____ |
| | | TOTAL | \$ _____ |
| 8. <u>ADD:</u> Total Receipts from inception of Chapter 11 to end of Reporting Period: | | | \$ _____ |
| 9. <u>LESS:</u> Total Disbursements from inception of Chapter 11 to end of Reporting Period: | | | \$ _____ |

*Cannot be paid without Court Order.

10. Total Cash and Bank Account Balances at end of Current Reporting Period - per item #5. \$ _____
11. Total deposited into Special Tax Account this period for Payroll Taxes: (Attach Federal Deposit Receipts.) \$ _____

SUMMARY OF OPERATIONS

- 12. Total Sales of Mdse./Services during the Current Reporting Period: \$ _____
- 13. Inventory: Quantities based on physical count () visual estimate (), other () describe.
 - A. Inventory at inception of Chapter 11. _____
 - B. Inventory at beginning of Reporting Period. _____
 - C. Inventory purchased during Reporting Period. _____
 - D. Inventory sold during Reporting Period. _____
 - E. Inventory on hand at end of Current Reporting Period. _____
- 14. Accounts Receivable:
 - A. Accounts receivable at inception of Chapter 11 _____
 - B. Accounts receivable at beginning of Reporting Period. _____
 - C. Accounts receivable created during Reporting Period. _____
 - D. Accounts collected during Reporting Period: Pre-11____ Post-11____ _____
 - E. Balance accounts receivable at end of reporting period: Pre-11____ Post-11____** _____
 - F. Attach schedule of accounts receivable 90 days and over, plus any other doubtful accounts. Describe collection efforts. _____
- 15. Itemize all unpaid obligations, including accruals for utilities, rent, salaries, etc. post Chapter 11. _____

TOTAL

**State Amount Due for Liens for Post Receivables.

- 16 Status of insurance coverage, payment and proof of premium payments (see Operating Guidelines):
- 17. Remarks:

DEBTOR-IN-POSSESSION _____
 By: _____
 Position _____

DATED: _____