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Can You Vote More Than Once? The Bankruptcy Code's Current "Numerosity" Standard Under § 1126(c) and Possible Reform

Under current law, affiliated creditors holding debt arising from the same loan transaction will not likely be lumped together when determining the number of creditors that have voted to approve or reject a plan, particularly where such affiliates held such debt prior to a bankruptcy filing and assert their claims through separate proofs of claim. Attempts to later manufacture separateness by transferring claims to affiliates for numerosity purposes will likely not, however, be respected. Recent proposals by the American Bankruptcy Institute ("ABI") seek to amend the Bankruptcy Code to collapse separate claims of affiliated entities under common investment management into one claim for voting purposes.

As the collateralized loan market begins to loosen, lenders who come to hold pieces of larger loans may choose to do so through various affiliated funds or entities, some of which may be managed by the same investment advisor. Should a bankruptcy ever occur with respect to the underlying obligor, one issue that necessarily arises in such context is whether this affiliated lender group will be treated as a single creditor, or as several different creditors, for purposes of a chapter 11 plan's numerosity requirement. This requirement, found in § 1126(c) of the Bankruptcy Code, specifies that for a chapter 11 plan to be confirmed, it must be "accepted by creditors … that hold at least two-thirds in amount **and** more than one-half in number[1] of the allowed claims of such class held by creditors …." 11 U.S.C. § 1126(c) (emphasis added). If the class accepts, and the plan is confirmed, even creditors in the class that voted against the plan, or abstained from voting, are bound by the plan. Conversely, barring a cramdown, more than one-third in amount or more than one-half in number of allowed claims may block a plan from being accepted.

Despite the fact that the level of approval required for class acceptance is often heavily scrutinized and contested,[2] there is not a great deal of jurisprudence on this specific issue. While limited, available caselaw reveals that it is the number of separate claims, not the number of creditors, which is key and that a single creditor may exercise more than one vote.[3] For example, in *In re Figter Ltd.*, 118 F.3d 635 (9th Cir. 1997), the Ninth Circuit held that a secured creditor who purchased 21 of the 34 unsecured claims was entitled to vote each of those claims against confirmation of the debtor's plan. *Id.* at 640; *see also In re Gilbert*, 104 B.R. at 211 (bankruptcy court allowed an unsecured creditor to vote a second purchased claim). Moreover, courts have tended to respect the separate nature of affiliated parties where such claims were distinct and the separateness of the underlying claims was not manufactured. *See In re Kreider*, 2006 WL 3068834 (Bankr. E.D. Pa. Sept. 27, 2006) (holding that the claims of five related American Express entities, American Express Travel Related Services Company, American Express Bank, FSB, American Express Centurion Bank (voting two claims), were each entitled to be counted for numerosity purposes).

While it is therefore possible for a single creditor or affiliates to be counted as multiple claimants, courts will also look to determine whether the underlying claims held by such creditors are sufficiently "separate" to warrant allowing multiple votes. In determining whether claims are "separate," courts have often considered two key factors: (1) whether the claims in question derive from independent transactions with the debtor, and (2) whether separate proofs of claim were (or will be) filed for the claims. *In re Gilbert, 104 B.R. at 211*.

Whether claims relate to one transaction is a factual issue. Certain types of claims, for example, trade claims or lease/contract rejection claims, are easy to distinguish as claims arising from separate transactions. *See In re Figter, Ltd.*, 118 F.3d at 640 ("[e]ach claim ar[ises] out of a separate transaction, evidencing separate obligations for which separate proofs of claim [are] filed."). It is more difficult, however, to argue that bank or bond debt arises from separate transactions (unless there is some unique characteristic to the debt that separates these claims on their face, such as a claim arising from a revolver versus a term loan or a first lien term loan versus a second lien term loan, etc.). As a result, the only method available may be to evidence various claims separateness by filing distinct proofs of claim from each affiliate.[4]

Attempts to manufacture separateness, however, by splitting pieces of a loan into various affiliates may not be permitted. To date, no court has expressly prohibited such practice or collapsed the holdings of affiliates into one vote. The Ninth Circuit, however, has stated in dicta that "of course, that is not to say that a creditor can get away with splitting one claim into many, but that is not what happened here." *In re Figter*, 118 F.3d at 641.

While current law would therefore tend to indicate that claims of affiliated lenders may be treated as separate to the extent documented by different proof of claims, allowing affiliates to count as different creditors for numerosity purposes, change may be ahead. The ABI's Commission to Study the Reform of Chapter 11 recently released its report to amend the Bankruptcy Code. Among the proposals contained therein is amending the numerosity requirements to specify that all affiliated entities under common investment management should be treated as a single creditor. Such reform is primarily directed at investment advisors and other parties that strategically purchase loans in the secondary market, often after a plan has been filed, who the Commission accuses of "significant gamesmanship" with respect to voting and classification of claims.[5]

Any amendment to the Bankruptcy Code based on such proposals is likely years away. Given the limited caselaw on this issue, however, and the importance that bankruptcy judges place on the recommendations of the ABI's Report, judges may be influenced to count claims related to a single loan transaction held by various affiliates as one claim for purposes of numerosity, notwithstanding that each party has filed a distinct proof of claim. We will continue to watch this area of law.

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1 Also known as the "numerosity" requirement.

2 Much of the jurisprudence in this area arises in the context of vote designation, whereby a creditor's vote is invalidated for, among other things, a lack of "good faith." *See In re DBSD North America*, 634 F.3d 79 (2d Cir. 2011) (holding that Bankruptcy Court did not err in designating the vote of a competitor who purchased a blocking position after the filing of a plan in order to control the bankruptcy process). Importantly, the *DBSD* court noted that "[w]e leave for another day the situation in which a preexisting creditor votes with strategic intentions." *Id*. at 105.

3 *See In re Gilbert*, 104 B.R. 206, 210 (Bankr. W.D. Mo. 1989) ("The formula contained in Section 1126(c) speaks in terms of the number of claims, not the number of creditors, that actually vote for or against the plan." *citing In re Jeppson*, 66 B.R. 269, 294 (Bankr. D. Utah 1986)); and *In re Jartran*, 44 B.R. 331, 364 (Bankr. N.D. Ill. 1984) (referring to number of ballots received based on the "amount of claims voted").

4 The Bankruptcy Code allows each creditor to file a proof of claim, even if the result is that multiple claims will be filed which all relate to the same underlying transaction. *See* Rule 3001 of the Bankruptcy Rules.

5 *See* ABI Report at 259.

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