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Numerosity Unwound: Counting Votes on a Chapter 11 Plan

By Stephen D. Zide, Joseph A. Shifer, and Benjamin S. Sieck

I. Introduction

The voting by creditors on a Chapter 11 plan is a critical component of the Chapter 11 confirmation process. For a plan to be confirmed, it must either be accepted by each class of impaired creditors[1] or satisfy the stringent "cram-down" standards under section 1129(b) of the Bankruptcy Code, including carrying the vote of at least one class of impaired creditors.[2] To determine whether a class of creditors has voted in favor of a plan one must look to section 1126(c) of the Bankruptcy Code. It requires that the plan be accepted by "creditors . . . that hold at least two-thirds in amount ***and*** more than one-half in number of the allowed claims of such class held by creditors . . . that have accepted or rejected such plan."

The "at least two-thirds in amount" requirement is relatively straightforward. The debtor must tabulate the votes of a given class and determine whether the accepting claims in a class constitute more than two-thirds of the amount of all allowed claims in the class that were voted. The "more than one-half in number" requirement (commonly referred to as the "numerosity" requirement), is not as straightforward. The plain text of the statue indicates that the test looks to claims, not creditors, and every case to address this issue has followed the clear wording of the statute. Therefore, one creditor can have—and vote—more than one claim.

Still, this initial observation gives rise to numerous other questions, such as what constitutes a claim for voting purposes and how broadly or narrowly is it defined? If a creditor has multiple contractual relationships with a debtor, does each relationship translate into a separate claim or does the creditor have one claim for all amounts it is owed? Relatedly, can a single creditor acquire and then vote additional claims within a class to ensure it will sway the vote? Moreover, what happens if a creditor sells a portion of its claim - does the buyer gain a vote for purposes of the numerosity requirement while the seller retains a vote for the unsold portion? The answers to each of these questions are obviously very important. If a creditor can assert or acquire multiple claims or split its claims, it may have an outsized voice in the voting process.

Given the centrality of these questions to the plan confirmation process, it is surprising how little case law there is on these topics. All told, the authors of this article have been able to identify only a handful of cases since the enactment of the Bankruptcy Code in 1978 that address the intricacies of the numerosity requirement.[3] To fill the gap on what little guidance there is, this article describes the purpose and precursors to the numerosity requirement,

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provides an overview of the limited case law addressing issues that have arisen with respect to the numerosity requirement, and concludes with a series of observations.

II. The Purpose and History of the Numerosity Requirement

The purpose of the numerosity requirement is to prevent a single creditor or small group of creditors that control the required two-thirds in claim amount of a given class from accepting a plan over the objection of a greater number of creditors who hold lesser amounts.[4] Although this requirement is intended to be protective of smaller creditors, the statute has shortfalls, particularly if a larger creditor holds multiple claims within the same class because the plain text of section 1126(c) refers to one-half of the "number of the allowed claims" held by creditors in a class rather than holders of claims (i.e., creditors).

The phrasing of "number of the allowed claims" in section 1126(c) is a departure from other formulations in the Bankruptcy Code that focus on the holders of claims. For example, section 303 of the Bankruptcy Code requires a vote by three or more entities that hold claims to commence an involuntary case against a debtor.[5] By using the term "claims" in section 1126(c), it appears the drafters of the Bankruptcy Code purposefully drafted the statute so that a plan must enjoy the support of a majority of claims rather than a majority of creditors.

The wording of section 1126(c) is the product of the gradual evolution of bankruptcy law. The Bankruptcy Act of 1898, for example, required voting approval by a "majority in number of all creditors whose claims have been allowed, which number must represent a majority in amount of such claims."[6] Under this construct, it was required that a plan enjoy the support of a majority of *all* creditors with allowed claims (not just those voting) and the majority in amount of allowed claims.

The corporate reorganization provisions of the Bankruptcy Act, first enacted in 1934 and amended by the Chandler Act in 1938, contained no numerosity requirement. Instead, plan confirmation required acceptance by creditors holding two-thirds in amount in each class affected by the plan.[7] Section 179 of the Chandler Act provided as follows (emphasis provided):

> After a plan has been accepted in writing, filed in court, by or on behalf of creditors holding ***two-thirds in amount of the claims filed and allowed of each class***, . . . the judge shall fix a hearing . . . for the consideration of the confirmation of the plan and of such objections as may be made to the confirmation.[8]

Notably, this standard did not focus on the number of creditors or claims, but solely on the amount of claims. Furthermore, it continued the Bankruptcy Act's requirement to take into account all allowed claims, rather than claims that were actually voted.

It was not until the Bankruptcy Code was enacted in 1978 that the current version of the voting requirement was instituted. Section 1126(c) combined and modified the concept of a "majority in number" from the Bankruptcy

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Act of 1898 with the concept of "two-thirds in amount" from the Chandler Act. However, only claims—not creditors—satisfy the majority in number requirement. In addition, the Bankruptcy Code added an important new feature, requiring that only the claims and creditors who actually vote on a plan are to be tallied in determining whether the relevant thresholds have been met.

The rest of this article is available in the February 2022 issue of the
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