

MAYER, BROWN, ROWE & MAW LLP'S
SUPREME COURT DOCKET REPORT
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Today the Supreme Court granted certiorari in one case of potential interest to the business community. Amicus briefs in support of the petitioners are due on Thursday, July 31, 2003, and amicus briefs in support of the respondent are due on Thursday, September 4, 2003. Any questions about this case should be directed to Miriam Nemetz (202-263-3253) or Robert Bronston (202-263-3244) in our Washington office.

Bankruptcy — Chapter 13 — Cram Down Interest Rates. The Supreme Court granted certiorari in *Till v. SCS Credit Corp.*, No. 02-1016, to decide the methodology of calculating the interest rate payable to a secured subprime creditor objecting to a Chapter 13 plan of reorganization.

Assuming all other requirements are met, when a debtor with a secured creditor files a Chapter 13 bankruptcy petition and intends to retain the collateral, the bankruptcy court must confirm the debtor's reorganization plan if the secured creditor consents or the debtor invokes Chapter 13's "cram down" provision. 11 U.S.C. § 1325(a)(5). The cram down provision requires the plan's confirmation over the objection of a creditor with an allowed secured claim if the secured creditor retains its lien on the collateral and "the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim." *Id.* § 1325(a)(5)(B). Because the allowed amount of a secured creditor's claim is the collateral's value at the time the petition is filed, *id.* § 506(a), in order for the debtor to invoke the cram down provision the plan must give the objecting secured creditor at least the equivalent of the value of the collateral the debtor has chosen to keep. *Id.* § 1325(a)(5)(B)(ii). Typically, this equivalent is a stream of payments with a present discounted value equal to the present value of the collateral, plus interest to compensate the creditor for the time value of money and the increased risk.

Debtors Lee and Amy Till invoked Chapter 13's cram down provision to keep their automobile, which secured a subprime loan at 21 percent interest from SCS Credit Corporation. The bankruptcy court confirmed the Tills' plan to pay SCS at an interest rate of 9.5 percent, which was based on the prime rate plus a risk premium of 1.5 percent, and is the rate — adjusted to account for SCS's risk of not receiving the Tills' scheduled payments — at which SCS could borrow the amount equal to the car's present value. But the district court conceived the cram down provision as effectively forcing SCS to extend to the Tills a new line of credit. The district court therefore reversed the bankruptcy court and held SCS entitled to 21 percent interest, the rate SCS would have earned on a new loan financed by the proceeds from the sale of its collateral, as 21 percent was the market rate of equivalent subprime loans to individuals in the Tills' position.

The Seventh Circuit affirmed. *In re Till*, 301 F.3d 583 (72002). The court of appeals agreed with the district court’s “coerced loan” approach, explaining that the secured creditor receives the equivalent of collateral only if it is paid the interest obtainable by making a new loan in the same industry to a similarly situated, non-bankrupt debtor. *Id.* at 591-593. The court specified that the bankruptcy court should apply a rebuttable presumption that the interest rate in the debtor’s contract is the appropriate one unless either the creditor or debtor shows that the creditor currently receives a higher or lower interest rate for similar loans. *Id.* at 592-593.

The question of how to calculate cram down interest rates divides the federal courts. While the Seventh Circuit’s approach in *Till* aligns with that of several other circuits, the Sixth Circuit refuses to accord any weight to the contract’s interest rate and looks instead to the current conventional rate on that type of loan without considering the debtor’s credit rating. *In re Kidd*, 315 F.3d 671, 678 (2003). Several circuits eschew entirely the “coerced loan” theory in favor of a “formula” approach, and calculate the interest rate by reference to the prime rate plus a risk premium, as did the bankruptcy court in *Till*. See *In re Fowler*, 903 F.2d 694, 698 (9th Cir. 1990); *United States v. Doud*, 869 F.2d 1144, 1146 (8th Cir. 1989). The Second Circuit not only adopts the formula approach but caps the secured creditor’s risk premium over the United States Treasury Bill rate at 3 percent. *In re Valenti*, 105 F.3d 55, 64 (1997), modified on other grounds by *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997).

The Supreme Court’s resolution of this issue will have a profound economic impact, not least because of recent legislative moves to force many individual debtors to file for bankruptcy under Chapter 13 rather than Chapter 7. See Bankruptcy Abuse Prevention and Consumer Protection Act of 2003, H.R. 975, 108th Cong. (passed Mar. 19, 2003). Moreover, Chapters 11 and 12 include similar cram down provisions. See 11 U.S.C. § 1129(b)(2)(A)(i)(II); 11 U.S.C. § 1225(a)(5)(B)(ii). If the Supreme Court clarifies the methodology for Chapter 13 cram downs, that methodology will probably be applied to all secured debt subject to cram down in reorganization. This case therefore is significant for all secured creditors and borrowers.

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The Supreme Court has requested the views of the Solicitor General in the following case of interest to the business community:

Zapata Hermanos Sucesores SA v. Hearthside Baking Co., No. 02-1318: The questions presented are (1) whether attorneys’ fees and expenses qualify as a recoverable form of “loss” under the United Nations Convention on Contracts for International Sales of Goods when such fees are foreseeable to the breaching party as a possible consequence of breach at the time of contracting; and (2) whether the federal courts lack inherent power to sanction a party for bad faith conduct when such conduct is potentially sanctionable by statute or rule. Mayer, Brown, Rowe & Maw represents the petitioner.

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