

NEWS & INSIGHTS

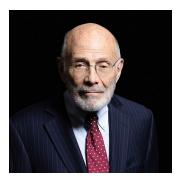
ALERTS

Second Circuit Holds That Senior Creditors' "Gifting" of Value to Existing Shareholder Under Reorganization Plan Violates Absolute Priority Rule

February 10, 2011

The U.S. Court of Appeals for the Second Circuit, on Feb. 7, 2011, held that senior creditors could not "gift" part of their reorganization plan recovery to existing shareholders of the debtor. In re DBSD N. Am., Inc., _ F.3d __, 2011 WL 350480 (2d Cir. Feb. 7, 2011) (2-1) (Lynch, J.) (explaining *In re DBSD* N. Am., Inc., 627 F.3d 496 (2d Cir. 2010) (summary opinion)). Its extensive 62-page opinion explained the court's previous two-page summary ruling of Dec. 9, 2010, which held, among other things, that the Chapter 11 debtor's reorganization plan violated the established "absolute priority" rule. As we described in a prior article, the Second Circuit's two-page ruling had also affirmed the bankruptcy court's designation (i.e., disqualification) of a secured lender's vote when the lender voted "not as a traditional creditor seeking to maximize its return on the debt it holds, but ... 'to establish control over [the debtor, as a] strategic asset." In re DBSD N. Am., Inc., 421 B.R. 133, 137 (Bankr. S.D.N.Y. 2009), quotedinDBSD, 2011 WL 35048, at *3. See Michael L. Cook and Joseph E. Bain, Second Circuit Affirms Designation of Secured Lenders' Vote and Effective Cram Down: Warning to Vultures, Bankruptcy Strategist (February 2011).

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