

Chapter 11 Plan Confirmation Problem

Grim Reaper Health Care Co. (“GR”) had trouble collecting insurance and Medicare payments, and the resulting cash-flow problems (along with severe marketing difficulties) forced it into Chapter 11. GR believes that selling its business to a new entity (to be called Hippocrates Health Care (“HHC”)) with a more aggressive collections department will turn the company around. It proposed the following distributions in its plan of reorganization:

Class I—the only secured claimant, Burly Bank (“Bank”), will receive a promissory note from HHC for 10% of its allowed secured claim, payable over 10 years, it will lose its liens (which cover every asset GR owns), and it will receive 75% of the stock of HHC;

Class II(A)—all doctors employed by GR (most of whom will continue to be employed by HHC) will receive payments over two years equal to 60% of their allowed unsecured claims (for unpaid wages earned during the period immediately preceding the bankruptcy filing);

Class II(B)—all nurses employed by GR (few of whom will continue to be employed by HHC) will receive payments over two years equal to 50% of their allowed unsecured claims (also for unpaid wages earned during the period immediately preceding the bankruptcy filing);

Class III—all general unsecured creditors of GR (suppliers, non-medical employees, etc.) will receive payments over two years equal to 40% of their allowed unsecured claims; and

Class IV—the 25 current shareholders of GR will receive 25% of the stock of HHC in exchange for a total contribution of \$25 million.

Bank and the current shareholders essentially crafted the plan. The structure for the new company, HHC, was the brainchild of the current shareholders, and Bank smelled money in the new HHC, which the financial press had already tentatively valued at over \$2 billion. Therefore, GR had counted on “yes” votes on the plan from Bank and the shareholders. GR had expected its doctors, who do not belong to a union, to accept the plan. It had expected to have a more difficult time with its nurses, who belong to a very aggressive national union. The vote of the general unsecured creditors, as always, was impossible to predict. Therefore, in its Disclosure Statement and other solicitation materials, GR made it very clear (truthfully) that, if GR’s assets were liquidated, no unsecured creditor would receive anything, because Bank’s liens cover virtually everything, and the debt to Bank far exceeds even a liberal valuation of GR’s assets.

As expected, Bank and the 25 shareholders voted “yes” on the plan, as did the Class II(A) doctors. Many of the nurses refused to participate in the process, so of the 200 members of Class II(B), only 100 participated in the vote. Of the 100 Class II(B) nurses actually casting ballots, 50 voted yes, and 50 voted no. The total claims owed to Class II(B) total \$3 million, of which the 100 nurses who actually voted are owed \$2 million, with “yes” ballots cast by nurses owed \$1.4 million. The Class III general unsecured creditors were also split, with only 100 of 300 creditors actually casting a ballot, of whom 75 voted “yes.” Those who voted “yes” are owed \$670,000 of the \$1 million owed to the 100 who actually voted, and the claims of the entire 300-member Class III total \$5 million.

You represent one of the Class II(B) nurses who voted “no” on the plan. She is confused and worried by the results of the close vote. Advise her as to 1) who won the vote, and 2) whether the requirements for confirmation of a Chapter 11 plan have been met here, and 3) whether she can make any objections to confirmation of the plan.