The "Magic 120 Days" In Chapter 11: A Misconception?

Creditors who have served on Creditors' Committees in Chapter 11 reorganizations, or even those who have simply been involved with more than one Chapter 11 filing, know that the debtor has 120 days from the date of the Order for Relief (ordinarily the same as the date of the petition) to file a Plan. It is a common misconception, however, that the Bankruptcy Code sets a deadline for the debtor to file a Plan by that date or face some type of sanction.

The debtor can get into trouble for failing to file a Plan within the first 120 days, but the trouble will not ordinarily come from the court. Contrary to popular belief, the 120 days is merely a time period in which the debtor has the exclusive right to file a Plan.

This means that if the debtor does not file a Plan by the 120th day, anyone can file a Plan for it thereafter. If the debtor files a Plan within the first 120 days, it then has 180 days from the date of the Order for Relief to get its Plan accepted by its creditors and confirmed by the court — otherwise it faces the same threat of a third party coming forward with a competing Plan.

Of course, the Code does allow any party in interest, after notice and a hearing, to obtain a reduction or increase of either the 120 day period or the 180 day period, so long as the party requests the increase or reduction within the original 120 or 180 day time frame.

It is interesting to note that once the debtor has lost its exclusive right to file a Plan, even a complete stranger to the debtor, such as a corporate raider, is free to come forward with a Plan for the debtor's sale and/or reorganization.

There are two main reasons why a clear understanding of this 120 day period is important to creditors of the Chapter 11 debtor.

First of all, a creditor is mistaken if it expects something magic to happen by the 121st day of the debtor's reorganization procedure. Something only happens by the 121st day if a party in interest makes it happen. If a debtor's counsel knows that there is any other party or parties — whether it be the Creditors' Committee or even a competitor of the debtor — ready, willing, and able to file a Plan for the debtor, the debtor's attorney is likely to feel sharply the need for promptness in moving the reorganization effort forward.

Secondly, any creditor may file a Plan for the debtor, and the mere threat of a creditor doing so is often enough to bring concessions from the debtor and a more prompt reorganization effort. A secured creditor might, for example, file a Plan of liquidation whereby it would be able to receive the fair market value of its collateral promptly.

Although a Disclosure Statement must be approved by the Court prior to the confirmation of any Plan, the Disclosure Statement for a liquidation proceeding is relatively easy to have approved — it need only say that the Plan is to sell what the debtor has and to distribute to unsecured creditors what, if anything, is left over after the secured creditors are paid.

The filing of a Plan by a creditor is an aggressive tactic and not one to be used in every Chapter 11. It is a tactic, however, that any creditor in a Chapter 11 should keep in mind when weighing its options as to how best to maximize its recovery, or speed up the reorganization proceeding.