

Bankruptcy Court Rules “Make-Whole” Provision Creates Enforceable Liquidated Damages

IN SHORT

The Situation: After a ruling in *In re Ultra Petroleum Corp.* by the U.S. Bankruptcy Court for the Southern District of Texas, certain private-placement noteholders are entitled to a “make-whole” premium in excess of \$200 million, under a chapter 11 plan that had rendered the noteholders’ claims unimpaired.

The Result: In reaching the decision, the court rejected Ultra Petroleum’s argument that, because the make-whole amount represented “unmatured interest” and was not allowable under section 502(b)(2), the plan left the noteholders’ rights under the Bankruptcy Code unaltered, and the noteholders’ claims were therefore unimpaired.

Looking Ahead: Ultra Petroleum has appealed the court’s order but agreed to pay the make-whole claims and postpetition interest from its cash reserves pending the appeal.

In *In re Ultra Petroleum Corp.*, 2017 BL 335015 (Bankr. S.D. Tex. Sept. 21, 2017), the U.S. Bankruptcy Court for the Southern District of Texas ruled that certain private-placement noteholders were entitled to receive a “make-whole” premium in excess of \$200 million under a chapter 11 plan that rendered the noteholders’ claims unimpaired.

Although there have been some recent conflicting decisions on this point, the ruling is significant because the court determined that a “model form” make-whole provision triggered by a bankruptcy filing created enforceable liquidated damages. Also, the court ruled that the chapter 11 debtors must pay the make-whole amount in full (including postpetition interest at the default contract rate) to render the noteholders’ claims “unimpaired.”

Background

Ultra Petroleum Corp. (“UPC”) issued approximately \$1.5 billion in unsecured notes from 2008 to 2010. The note agreement, which was governed by New York law, provided that UPC had the right to prepay the notes at 100 percent of principal plus a make-whole amount. Events of default under the agreement included a bankruptcy filing by UPC.

UPC filed for chapter 11 protection in April 2016. Improving business conditions during the course of the case allowed UPC to seek confirmation of a chapter 11 plan that provided for the payment of all unsecured claims in full in cash. The plan designated the noteholder claims as “unimpaired” but did not provide for the payment of the make-whole amount or postpetition interest at the default rate. UPC contested the noteholders’ right to receive the make-whole amount, certain postpetition default-rate interest, and certain other related fees and expenses.



The bankruptcy court first decided that the make-whole amount was an enforceable liquidated damages provision—rather than an unenforceable penalty—under New York law.



The Court’s Decision

The bankruptcy court first decided that the make-whole amount was an enforceable liquidated damages provision—rather than an unenforceable penalty—under New York law. The court rejected UPC’s arguments that the make-whole amount was “conspicuously disproportionate to foreseeable losses at the time the parties entered” into the note agreement because it would result in a double recovery.

The court also held that UPC’s chapter 11 plan impaired the noteholder claims because the plan failed to provide for the payment of the make-whole amount and postpetition default-rate interest. The court rejected UPC’s position that, because the make-whole amount represented “unmatured interest” and was not allowable under section 502(b)(2), the plan left the noteholders’ rights under the Bankruptcy Code unaltered, and the noteholders’ claims were therefore unimpaired under section 1124(1). In support of its position, UPC relied on the Third Circuit’s ruling in *In re PPI Enterprises (U.S.) Inc.*, 324 F.3d 197 (3d Cir. 2003). In *PPI*, the court ruled that a plan proposing to pay a landlord’s lease rejection claim in an amount equal to the cap set forth in section 502(b)(6) left the landlord’s claim unimpaired.

The *Ultra Petroleum* court rejected this reasoning. According to the court, because UPC’s chapter 11 plan, and not section 502(b)(2), caused the discharge of UPC’s liability on the unpaid make-whole claim, the plan would impair the noteholders’ claims unless the plan provided for the payment of the make-

whole claim in full.

The court noted in *dicta* that UPC might have attempted to render the noteholders unimpaired without paying the make-whole amount by reinstating the notes and curing any defaults, as permitted by section 1124(2), but elected not to do so.

UPC appealed the court's order to the district court on October 5, 2017. On October 6, the bankruptcy court entered an agreed order directing that, pending resolution on appeal, UPC must pay the make-whole claims and postpetition interest no later than October 13, 2017, from a UPC reserve fund.

TWO KEY TAKEAWAYS

1. The *Ultra Petroleum* decision is noteworthy in that the court determined that a "model form" make-whole provision triggered by a bankruptcy filing did create enforceable liquidated damages.
2. The court also ruled that the chapter 11 debtors must pay the make-whole amount in full (including postpetition interest at the default contract rate) in order to render the noteholders' claims "unimpaired."

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