Summary of SBRA and select CARES Act provisions

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**This summary discusses certain aspects of recently enacted laws. It is not intended to indicate how the court may resolve any contested matter.*

The Small Business Reorganization Act of 2019 (SBRA) became effective on February 19, 2020. It creates Subchapter V, a new subchapter within chapter 11 of the Bankruptcy Code. Subchapter V eliminates some of the more expensive components of traditional chapter 11 relief. It also puts into place more expedited procedures similar to those used in chapter 12 and chapter 13 cases.

Many chapter 11 provisions apply in Subchapter V cases, but some do not. New section 1181 (11 U.S.C. § 1181) lists the sections of chapter 11 that are completely inapplicable and others that are inapplicable unless the court orders otherwise.

Only a "small business debtor" may use Subchapter V, and the SBRA changed the definition of a small business debtor under the Code. Generally speaking, to be an eligible small business debtor, the debtor must be engaged in commercial or business activities and -- as enacted in the SBRA -- cannot have more than $2,725,625 of secured and unsecured debt. In addition, at least 50% of the debtor's pre-petition debt must have been generated from commercial or business activities.

The CARES Act, enacted on March 27, 2020, amended some of the SBRA's provisions. Most notably, the CARES Act changed the definition of a small business debtor further by increasing the debt cap up to $7,500,000 for new cases filed on or after the date of the CARES Act's enactment. The debt limit increase is effective for one year unless Congress takes further action.

Only a small business debtor that elects to have Subchapter V apply may be a debtor under the subchapter. In other words, the use of Subchapter V is voluntary. Federal Rule of Bankruptcy Procedure 1020(a) provides that a debtor shall elect in their petition whether to proceed under Subchapter V.

There are several perceived benefits to eligible debtors under Subchapter V. This summary addresses some of them.

Unless the court orders otherwise, there will be no unsecured creditors committee and the debtor will not have to file a disclosure statement. However, a Subchapter V plan must contain some information traditionally contained in disclosure statements, such as a brief history of the debtor's business operations, a liquidation analysis, and projections of the debtor's ability to make payments under the proposed plan. (11 U.S.C. § 1190.)

The debtor will not incur quarterly U.S. Trustee fees in a Subchapter V case. (28 U.S.C. § 1930(a)(6)(A).) In addition, administrative expense claims may be paid over time through the debtor's plan rather than as a condition to confirmation. (28 U.S.C. § 1191(e).)

With respect to case administration, the U.S. Trustee's office will appoint a Subchapter V Trustee in every case. (11 U.S.C. § 1183.) In our District, there will not be a standing trustee.

Typically, the Subchapter V Trustee will not operate the debtor's business. (11 U.S.C. § 1183(b)(5).) The Trustee will not take possession of the debtor's assets and has no ability to sell them. Rather, the Trustee will serve a role akin to a Chapter 12 Trustee or Chapter 13 Trustee in disbursing plan payments. (11 U.S.C. § 1194.) The Trustee's role is to be a facilitator between the debtor and their creditors. Their duties specifically include helping the debtor formulate a consensual reorganization plan. (11 U.S.C. § 1183(b)(7).)

There must be a status conference in every Subchapter V case held within 60 days of the petition date unless the court orders otherwise. (11 U.S.C. § 1188.) The Subchapter V Trustee will participate in that status conference. (11 U.S.C. § 1183(b)(3).) The debtor must file a status report at least 14 days before the conference. (11 U.S.C. § 1188(c).) At the status conference, the parties will discuss the debtor's efforts to formulate and present a consensual plan of reorganization.

The debtor must file a plan within 90 days of the petition date (11 US.C. § 1189(b)), but there is no requirement that the confirmation hearing be concluded within 45 days (as in chapter 12 cases). Also, the plan does not have to be confirmed within 45 days (as in non-Subchapter V small business chapter 11 cases) (11 U.S.C. § 1189(b)). Only a debtor can file and modify a Subchapter V plan (11 U.S.C. §§ 1189(a) and 1193).

There are two ways to confirm a Subchapter V plan: consensually (11 U.S.C. § 1191(a)) and non-consensually (11 U.S.C. § 1191(b)). The court may confirm a non-consensual plan of reorganization if it does not "discriminate unfairly" and is "fair and equitable" as to each class of impaired creditors that has not accepted the plan, so long as the debtor commits all projected disposable income to making payments under the plan over a three- to five-year period. This projected disposable income commitment substitutes for the absolute priority rule, meaning the SBRA has eliminated the absolute priority rule with respect to unsecured creditors in a non-consensual plan (11 U.S.C. § 1191(b) and (c)). This makes it easier for business-owner debtors to retain their stake in the business.

In a confirmed consensual plan, the debtors receive a discharge at plan confirmation; but, in a confirmed nonconsensual plan, the debtor's discharge is delayed until after all plan payments are made. (11 U.S.C. §§ 1141(d), 1181(c), 1192). There is no "hardship" or early discharge in a Subchapter V confirmed non-consensual plan, although a debtor may seek to modify a confirmed non-consensual plan. (11 U.S.C. § 1193(c).)

A Subchapter V plan may modify the rights of a secured lender with a lien on the debtor's principal residence if the new value received in granting the security interest was not used primarily to acquire the real property and was used primarily in connection with the

debtor's small business. (11 U.S.C. § 1190(3).) This will enable some Subchapter V debtors to modify the terms of certain home equity loans and second mortgages.

Our court has prepared a new form of operating order that will be used in Subchapter V cases. The court also will enter a scheduling order in each Subchapter V case that, among other things, sets the date of the required status conference and sets deadlines for the filing of proofs of claim.

In addition to adding Subchapter V into chapter 11 of the Code, the SBRA made changes to preference law that are applicable in all cases. First, a debtor or trustee now must perform "reasonable due diligence" under the circumstances and take into account a party's "known or reasonably knowable affirmative defenses" before commencing a preference action. (11 U.S.C. § 547(b).) Second, the SBRA has amended the law regarding the proper venue for preference cases. As amended, claims under $25,000 must be brought in the district where the defendant resides (as opposed to where the bankruptcy case is pending). (28 U.S.C. § 1409(b).) The threshold amount to bring claims where the bankruptcy case is pending had been $13,650.