

Small Business Reorganization Act of 2019

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Commission Testimony/Findings

- **Risk of loss of ownership**
- **Cost**
 - **Time**
 - **Procedural/reporting burdens**
 - **Committee counsel/advisor costs**
 - **Tactical fights driven by §1129(a)(10), APR, new value elements**

SBRA attempts to address all of these concerns.

- **Intended to give more small businesses a chance at reorganization instead of simply liquidating**

Core Provisions of SBRA

- **To qualify as a small business debtor, the debtor must be a person or entity engaged in commercial or business activity with aggregate secured and unsecured debts of \$2,725,625 or less.**
- **SARE debtors excluded: debtor who derives substantially all of its gross income from the operation of a single real property cannot elect under Subchapter V.**
- **No requirement that the debtor remain engaged in the commercial or business activity post-petition, but the debtor must show that at least 50 percent of its pre-petition debts arose from such activities. (Nonetheless, difficult to confirm if not operating post-petition).**

Core Provisions (cont'd)

- **Small business debtor operates in chapter 11 as a debtor-in-possession.**
- **Obligated to file schedules and statements.**
- **The court can remove a small business debtor from debtor-in-possession status for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor, either before or after the commencement of the bankruptcy case or for failure to perform its obligations under a confirmed plan. If that happens, the standing trustee takes over the operation of the debtor's business.**

Core Provisions (cont'd)

- **Upon electing to file under Subchapter V, the debtor must file a copy of the business's most-recent balance sheet, statement of operations, cash-flow statement, and federal income tax return or a sworn statement that such documents do not exist. Small business debtor operates in chapter 11 as a debtor-in-possession.**
- **The SBRA does not specify when the debtor must elect to proceed under Subchapter V.**
- **Creditor's Committees: unless the court orders otherwise, no creditors committee; creditors committees will be the exception – not the rule – in SBRA reorganizations.**

Core Provisions (cont'd)

- **Subchapter V cases will have a “standing trustee” appointed by the U.S. Trustee.**
- **Standing trustee will act as a conduit for plan payments.**
- **Standing trustee has the authority to investigate the financial affairs of the debtor and object to the allowance of proofs of claim.**
- **Standing trustee will appear and be heard at plan confirmation; general obligation to “facilitate the development of a consensual plan of reorganization”.**

Core Provisions (cont'd)

- Standing trustee authorized to operate the debtor's business ONLY if the debtor is removed as a debtor-in-possession; otherwise NOT an operating trustee in any respect.
- Standing trustee is terminated upon “substantial consummation” of the confirmed plan.

Core Provisions (cont'd)

- The goals of Subchapter V are to minimize the time and expense of small business reorganization.
- Within 60 days of the filing, the bankruptcy court shall hold a status conference “to further the expeditious and economical resolution” of the case.
- 14 days prior to the conference, the debtor must file a report detailing the efforts to attain a consensual plan of reorganization.
- Debtor must file plan 90 days after the order for relief.
- The court can extend 90-day plan-filing deadline under “circumstances for which the debtor should not justly be held accountable.”

Core Provisions (cont'd)

- Only the debtor is allowed to propose a plan.
- The SBRA need not solicit plan acceptances with a separate disclosure statement. The plan must include a brief history of the business operations of the debtor, a liquidation analysis, and projections with respect to the debtors' proposed payments under the proposed plan.
- Note: An individual who qualifies as a small business debtor can modify a mortgage on his or her principal residence, provided that the mortgage loan was not used to acquire the real property but was used primarily in connection with the debtor's business.

Core Provisions (cont'd)

- Confirmation of a small business debtor plan of reorganization is pursuant to the usual criteria of section 1129(a) of the Bankruptcy Code, with the critical exception that the debtor does not need to obtain the acceptance of even one impaired class of creditors. §1129(a)(10) does not apply to the SBRA cram down option. Only the debtor is allowed to propose a plan.
- The SBRA debtor also has the flexibility to pay administrative claims over the life of the plan.
- Real Cramdown:
 - With respect to secured claims, cramdown is the same as an ordinary business entity chapter 11 case.

Core Provisions (cont'd)

- Equity holders can retain their interests in the business even if the plan does not pay unsecured claims in full, and the APR is not met (because the class did not accept the plan). As long as the plan “does not discriminate unfairly, and is fair and equitable” with respect to impaired unsecured creditors, the court must confirm the plan.
 - “Fair and equitable” means only that the SBRA debtor must commit all of its “projected disposable income” (or property of equivalent value) to make payments under the plan for a minimum of three and a maximum of five years.
 - The debtor must demonstrate a “reasonable likelihood” that it will be able to make all payments under the plan, and the plan must provide “appropriate remedies, which may include the liquidation of nonexempt assets” to protect creditors if the debtor fails to make plan payments (“Toggle to sale” provision).
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Core Provisions (cont'd)

- **“Disposable income” means income received by the debtor that is not reasonably necessary to: “ensure the continuation, preservation, or operation of the business.”**
- **If cramdown is pursuant to section 1191(b) (devotion of 3-5 years of disposable income), discharge enters “as soon as practicable” after the debtor completes all payments.**
- **Discharge does not extend to debts on which the last payment is due after the 3-5 year period (for example, long-term secured debt).**

Additional Key Takeaways:

- **Elective/Optional; not required to elect Subchapter V.**
- **The cramdown option is a default (as cramdown was always intended to be)—drives negotiated result.**
- **Efficiency/Speed/Simplicity/Low Cost.**
- **Intended to Promote Reorganization; Focus on feasibility.**

Implementation Issues:

- **The standing trustee**
 - **Transition period – likely appointed case-by-case**
 - **Long term – standing trustees like chapters 12/13**
 - **NOT an operating trustee**
 - **“Estate neutral”?**
 - **Financial advisor?**
 - **Success may depend on how UST implements and who is selected**

Implementation Issues:

- **Definition of “Projected Disposable Income”**
 - **NOI?**
 - **EBITDA?**
 - **GAAP?**
 - **Statutory definition may be more favorable than GAAP, NOI or EBITDA (“or”)**
- **Reporting**
 - **Critical to define at status conference/flexible (to fit debtor’s business); not one size fits all; utilize existing systems if adequate.**
 - **Should be the same as similar non-debtor business, not more detailed.**
 - **Should not be burdensome.**

Implementation Issues:

- **Test to Extend 90-day Plan Filing Period**
 - **Pro-restructuring interpretation given purpose of SBRA.**
 - **Flexible.**
 - **“Purchased” by good faith negotiations.**
 - **Default plan simple to file.**
- **Pro-restructuring interpretation expected**
- **Debt Limit**
 - **Will limit eligible debtors; increase in future? (See Chapter 12 amendment).**

Preference Reforms

- §547(b) amended as follows:
 - Except as provided in subsections (c) and (i) of this section, the trustee may, based on reasonable due diligence in the circumstances of the case and taking into account a party's known or reasonably knowable affirmative defenses under subsection (c), avoid any transfer of an interest of the debtor in property---
- Section 1409(b) of title 28, USC is amended as follows:
 - (b) Except as provided in subsection (d) of this section, a trustee in a case under title 11 may commence a proceeding arising in or related to such case to recover a money judgment of or property worth less than \$1,300 or a consumer debt of less than \$19,250, or a debt (excluding a consumer debt) against a non-insider of less than ~~\$12,850~~ \$25,000, only in the district court for the district in which the defendant resides.