

# 2019 Bankruptcy Reform

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# Overview

- ▶ Family Farmer Relief Act (Pub. L. 116-51)
- ▶ Honoring American Veterans in Extreme Need (HAVEN) Act (Pub. L. 116-52)
- ▶ National Guard and Reservists Debt Relief Extension Act (Pub. L. 116-53)
- ▶ Small Business Reorganization Act (SBRA) (Pub. L. 116-54)

# Purpose of the SBRA

- ▶ Streamline the process of small business reorganization by making it faster and more cost-effective
- ▶ As indicated by the House Committee Report for the SBRA, approximately 4 out of 5 businesses survive their first year. Only 1 out of 2 businesses survive five years. Only 1 out of 3 businesses survive to their tenth-year anniversary. See H.R. Rep. No. 116-171, at 2 (2019) (citations omitted)
- ▶ While most chapter 11 business cases are filed by small businesses debtors, they are the least likely to successfully reorganize. *Id.*, at 3
- ▶ The SBRA also made changes to the preference law (§ 547(b) and 28 U.S.C. § 1409(b)) requiring trustees in all cases to use “reasonable due diligence” and to take into account a party’s “known or reasonably knowable affirmative defenses” when pursuing preference claims

# Definition of Small Business Debtor

- ▶ Revised § 101(51D): “small business debtor” is a chapter 11 debtor that is engaged in commercial or business activities and has no more than \$2,725,625 (excluding debts owed to affiliates or insiders) in noncontingent liquidated secured and unsecured debt, not less than 50% of which arose from the commercial or business activities of the debtor.
- ▶ No single-asset real estate debtors.
- ▶ Requirement that no committee exists is deleted.
- ▶ Now excludes debtors subject to reporting requirements of Securities Exchange Act.

# Election

- ▶ 11 U.S.C. § 103(i): Small business debtor must elect Subchapter V for it to apply
- ▶ Proposed amendments to bankruptcy rules and official forms

# Election

## Proposed Amendment to BR 1020(a)

1 **Rule 1020. ~~Small Business~~ Chapter 11 Reorganization**

2 **Case for Small Business Debtors**

3 (a) SMALL BUSINESS DEBTOR

4 DESIGNATION. In a voluntary chapter 11 case, the debtor

5 shall state in the petition whether the debtor is a small

6 business debtor and, if so, whether the debtor elects to have

7 subchapter V of chapter 11 apply. In an involuntary chapter

8 11 case, the debtor shall file within 14 days after entry of the

9 order for relief a statement as to whether the debtor is a small

10 business debtor and, if so, whether the debtor elects to have

11 subchapter V of chapter 11 apply.

Except as provided in

12 ~~subdivision (c), the~~ The status of the case as a small business

13 case or a case under subchapter V of chapter 11 shall be in

14 accordance with the debtor's statement under this

15 subdivision, unless and until the court enters an order finding

16 that the debtor's statement is incorrect.

# Election

## Revised Official Form 101 (Voluntary Petition for Individuals); Paragraph 13

**13. Are you filing under Chapter 11 of the Bankruptcy Code and are you a *small business debtor*?**

For a definition of *small business debtor*, see 11 U.S.C. § 101(51D).

*If you are filing under Chapter 11, the court must know whether you are a small business debtor so that it can set appropriate deadlines. If you indicate that you are a small business debtor, you must attach your most recent balance sheet, statement of operations, cash-flow statement, and federal income tax return or if any of these documents do not exist, follow the procedure in 11 U.S.C. § 1116(1)(B).*

- No. I am not filing under Chapter 11.
- No. I am filing under Chapter 11, but I am NOT a small business debtor according to the definition in the Bankruptcy Code.
- Yes. I am filing under Chapter 11, I am a small business according to the definition in the Bankruptcy Code, and I do not choose to proceed under Subchapter V of Chapter 11.
- Yes. I am filing under Chapter 11, I am a small business debtor according to the definition in the Bankruptcy Code, and I choose to proceed under Subchapter V of Chapter 11.

# Election

## Revised Official Form 201 (Voluntary Petition for Non-Individuals); Paragraph 8

8. Under which chapter of the  
Bankruptcy Code is the  
debtor filing?

Check one:

Chapter 7

Chapter 9

Chapter 11. *Check all that apply.*

Debtor's aggregate noncontingent liquidated debts (excluding debts owed to insiders or affiliates) are less than \$2,725,625 (amount subject to adjustment on 4/01/22 and every 3 years after that).

The debtor is a small business debtor as defined in 11 U.S.C. § 101(51D). If the debtor is a small business debtor, attach the most recent balance sheet, statement of operations, cash-flow statement, and federal income tax return or if all of these documents do not exist, follow the procedure in 11 U.S.C. § 1116(1)(B).

The debtor is a small business debtor as defined in 11 U.S.C. § 101(51D), and it chooses to proceed under Subchapter V of Chapter 11.

A plan is being filed with this petition.

Acceptances of the plan were solicited prepetition from one or more classes of creditors, in accordance with 11 U.S.C. § 1126(b).

The debtor is required to file periodic reports (for example, 10K and 10Q) with the Securities and Exchange Commission according to § 13 or 15(d) of the Securities Exchange Act of 1934. File the *Attachment to Voluntary Petition for Non-Individuals Filing for Bankruptcy under Chapter 11* (Official Form 201A) with this form.

The debtor is a shell company as defined in the Securities Exchange Act of 1934 Rule 12b-2.

Chapter 12

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# Election

New Official Form 309E2 (Notice of Ch 11 BK Case for Individuals or Joint Debtors under Subchapter V)

New Official Form 309F2 (Notice of Ch 11 BK Case for Corporations or Partnerships under Subchapter V)

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**5. Bankruptcy Trustee**

Contact phone

Email

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**10. Filing a Chapter 11 bankruptcy case**

Chapter 11 allows debtors to reorganize or liquidate according to a plan. A plan is not effective unless the court confirms it. You may receive a copy of the plan and a disclosure statement telling you about the plan, and you may have the opportunity to vote on the plan. You will receive notice of the date of the confirmation hearing, and you may object to confirmation of the plan and attend the confirmation hearing. The debtor will generally remain in possession of the property and may continue to operate the debtor's business.

# Debtor as Debtor in Possession

- ▶ The DIP remains in possession of assets of the estate. § 1186(b)
- ▶ The DIP has the same rights, powers and duties of a trustee as a DIP in a non-Subchapter V case, including operation of the business. § 1184
- ▶ The court may terminate the debtor's status as DIP. § 1185(a)
  - ▶ The trustee will then have expanded powers, including operation of the business. § 1183(b)(5)
- ▶ The court may reinstate the debtor as DIP. § 1185(b)

# Duties of a Debtor in Possession

- ▶ Debtor must file documents required of a small business case under § 1116(1)(A) and (B). § 1187(a)
- ▶ Debtor has a duty to file § 308 periodic reports. § 1187(b)
- ▶ Debtor must comply with the other duties of a DIP in a small business case specified in § 1116(2)-(7). § 1187(b)
- ▶ DIP has the duties of a trustee under § 1106(a), except those specified in paragraphs (2), (3) and (4). § 1184
- ▶ Only the Debtor may file a plan. § 1189(a)

# Administrative & Procedural Features

- ▶ No Committee - Amended § 1102(a)(3)
- ▶ § 1181(b): other provisions of § 1102 (1102(a)(1), (2), and (4) and 1102(b)) and § 1103 don't apply in Subchapter V
- ▶ No Disclosure Statement
  - ▶ § 1181(b): 1125 is inapplicable unless court orders otherwise; however, plan must contain some things disclosure statement would normally contain - See § 1190(a)(1) - plan must contain (1) brief history; (2) liquidation analysis; and (3) projections.

# Administrative & Procedural Features - Continued

- ▶ Required Status Conference & Debtor Report

- ▶ § 1181(a): 105(d) doesn't apply
- ▶ § 1188(a): status conference is mandatory and must be held not later than 60 days after order for relief; can be extended if beyond debtor's control (See § 1188(b))
- ▶ § 1188(c): debtor must file and serve report regarding its efforts taken to obtain a consensual plan no later than 14 days prior to the status conference
- ▶ § 1183(3): trustee has duty to appear and be heard at the status conference

# Administrative & Procedural Features - Continued

- ▶ Time for Filing Plan
  - ▶ § 1189(a): only the debtor may file a plan
  - ▶ § 1189(b): must file within 90 days after order for relief; deadline can be extended if beyond debtor's control
  - ▶ § 1193(a): permits pre-confirmation modification of plan
- ▶ No Quarterly UST Fees - Amended 28 USC § 1930(a)(6)(A)
- ▶ Modification of Disinterestedness Requirement for Debtor Professionals
  - ▶ § 1195: not disqualified from employment under § 327(a) solely because professional holds pre-petition claim of less than \$10,000

# Contents of Subchapter V Plan

- ▶ The required contents of a Subchapter V plan are contained in §§ 1122, 1123 (with exceptions) and 1190
- ▶ Highlights
  - ▶ Under § 1190(1), a Subchapter V plan shall include (1) a brief history of the business operations of the debtor; (2) a liquidation analysis; and (3) projections with respect to the ability of the debtor to make payments under the proposed plan
  - ▶ Under § 1190(2), a Subchapter V plan must provide “future” earnings or income to the supervision of the trustee as is required for execution of the plan
  - ▶ Under § 1190(3), a plan may modify the rights of a holder of a claim secured by the principal residence of the debtor if the new value received in connection with the granting of the security interest (1) was not used primarily to acquire the real property; and (2) was used primarily in connection with the small business of the debtor

# Confirmation of Plan - Consensual - 1191(a)

- ▶ If all requirements of § 1129(a) met, court must confirm; if all requirements are met, all classes of impaired creditors have accepted the plan
- ▶ Effects of Confirmation of Consensual Plan
  - ▶ § 1183(c): trustee terminated upon substantial consummation of the plan
  - ▶ Discharge provisions of § 1141(d) apply, except § 1141(d)(5)
  - ▶ § 1141(b): confirmation vests property of the estate in the debtor, unless the plan or confirmation order provide otherwise; additional property of the estate provisions in § 1186 don't apply
  - ▶ Discharge triggers termination of automatic stay - § 362(c)(2)(C)

# Confirmation of Plan – Cramdown – 1191(b)

- ▶ § 1129(b) doesn't apply
- ▶ § 1191(b):
  - ▶ Cramdown allowed even if all impaired classes reject plan
  - ▶ Eliminates absolute priority rule
  - ▶ If all confirmation requirements met, court must confirm plan if, with respect to each impaired class that hasn't accepted the plan, the plan does not discriminate unfairly and is fair and equitable.

# Confirmation of Plan – Cramdown – 1191(b) – Continued

- ▶ § 1191(c): plan must be fair and equitable
  - ▶ § 1191(c)(1): If secured, to be fair and equitable, must satisfy § 1129(b)(2)(A)
  - ▶ If unsecured, to be fair and equitable, must meet the following:
    - ▶ § 1191(c)(2)(A): disposable income requirement - all disposable income to be received during plan must be applied to plan payments
    - ▶ § 1191(c)(2)(B): alternatively, plan may provide that value of property to be distributed under plan is not less than the projected disposable income
    - ▶ § 1191(c)(3): feasibility test - able to make all plan payments or reasonable likelihood able to make plan payments; must also include remedies if debtor defaults on payments
    - ▶ § 1191(d): definition of disposable income
- ▶ § 1191(e): permits confirmation under § 1191(b) that provides for payment through plan of administrative expense claims and involuntary gap claims

# Effects of Cramdown Confirmation

- ▶ Trustee remains and makes payments to creditors for the term of the plan (3 or 5 years) - see § 1194(b); trustee also compensated during this time
- ▶ Timing of discharge:
  - ▶ § 1181(c): discharge provisions of 1141(d) don't apply, except as provided in § 1192 (delays discharge until debtor completes payments due within first 3 years of the plan, or such longer period not to exceed 5 years)
  - ▶ Discharges all debts in § 1141(d)(1)(A) and allowed administrative expenses provided for in the plan, except doesn't discharge any debt with last payment due after plan term and doesn't discharge debt excepted under § 523(a)
- ▶ § 1186(a): property of the estate includes post-petition assets and earnings

# Post-Confirmation Modification

- ▶ Post-Confirmation Modification of Consensual Plan
  - ▶ § 1193(b): no modification after substantial consummation
  - ▶ § 1193(d): holder of any claim who voted to accept or reject the confirmed plan is deemed to have voted the same way unless the holder changes the vote
- ▶ Post-Confirmation Modification of Cramdown Plan
  - ▶ § 1193(c): can modify at any time within 3 years, or longer, but not to exceed 5 years
  - ▶ § 1191(d) requirements with regard to voting on original plan don't apply to post-confirmation modification of cramdown plan because such plan confirmed regardless of acceptances

# DIP May be Removed for Breach of Plan

- ▶ DIP may be removed “for cause.” §1185
  - ▶ Cause “includes”: fraud, dishonesty, incompetence, gross mismanagement of the debtor (pre- or post-petition), or failure to perform the debtor’s obligations under the confirmed Plan.
- ▶ If DIP is removed, the Subchapter V trustee will operate the business.
- ▶ Section 1183(b)(5) requires the trustee to:
  - ▶ File any required schedules and statements;
  - ▶ File periodic operating reports;
  - ▶ Serve as the administrator of any employee benefit plan;
  - ▶ Make reasonable efforts to transfer patients from a closing health care business to a new provider offering similar services; and,
  - ▶ For any year in which a tax return has not been filed, furnish such information as may be required by the applicable governmental entity.

# Property of the Estate

- ▶ § 1115 does not apply in a Subchapter V case
- ▶ However, § 1186(a) does apply and uses similar language to § 1115
- ▶ § 1186(a) provides that in cases where a cramdown plan has been confirmed, in addition to the kinds of property included in § 541, property of the estate includes (1) all property of the kind specified in § 541 acquired after the commencement of the case but before the case is closed, dismissed or converted; and (2) earnings from services performed by the debtor after commencement of the case but before the case is closed, dismissed or converted

# Effective Date of SBRA

- ▶ The SBRA is effective February 19, 2020
- ▶ Unlike BAPCPA, the SBRA does not specifically provide that its provisions are only applicable to cases filed after the effective date, so it is unclear whether a debtor can elect Subchapter V treatment in cases filed before February 19, 2020
- ▶ The Advisory Committee on Bankruptcy Rules has proposed interim rules for adoption which make changes to the Federal Rules of Bankruptcy Procedure
- ▶ The Western District of Washington will adopt the proposed interim rules by general order
- ▶ An additional general order will be entered modifying existing local rules to bring them in conformity with the SBRA