

# New Bankruptcy Relief Provisions for Small Businesses

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Carpentry is a trade that requires a great deal of professional skills. Just about anyone can go shopping and fill a toolbox with a variety of tools. However, it's the skilled carpenter who not only knows the purpose of each tool but also how to masterfully use the tool to complete the task at hand. While some tools are used every day, others are only needed for unique challenges. For many business owners, bankruptcy has likely been viewed as a tool of last resort. However, Congress recently added a tool to the proverbial financial toolbox that could result in small businesses taking a different view of bankruptcy.

## Bankruptcy under the Small Business Reorganization Act

The Small Business Reorganization Act of 2019 (SBRA), which went into effect on February 19, 2020, created a new subchapter V to Chapter 11 under the provisions of the United States Bankruptcy Code. In the past, many small business owners found that reorganization under the previous provisions available through Chapter 11 was too costly and time consuming. The SBRA aims to provide a faster and less costly reorganization process for small businesses – and, most importantly, may provide a lifeline for owners to keep their businesses.

### Eligibility

In order to be eligible under the SBRA, persons (both individuals and entities) must be engaged in commercial activity with total secured and unsecured debts of less than \$2,725,625, of which at least half must be related to business activity. On March 27, 2020, this limit was increased to \$7,500,000 for a 12-month period as part of the Coronavirus Aid, Relief, and Economic Security (CARES) Act. Also, the debtor's principal activity cannot be a single-asset real estate operation.

### Notable Provisions

Trustee: Under a traditional Chapter 11 reorganization, a trustee is only appointed for cause (e.g., fraud) and will take control of the debtor's business. The SBRA stipulates that a trustee is automatically appointed under Subchapter V; however, the debtor retains control of the business with the trustee acting more in the capacity of an advisor.

Process and timeline: As previously mentioned, one of the SBRA's main objectives is to expedite the reorganization process. The debtor must file a plan of reorganization within 90 days of filing. Subchapter V also excludes the necessity for a disclosure statement which is required under traditional Chapter 11. The disclosure statement is intended to provide creditors with sufficient information to assess and vote for or against a reorganization plan. Due to disputes regarding the adequacy of the disclosures, this can typically lead to prolonged delays.

Retaining equity ownership: The Absolute Priority Rule, which stipulates that equity interest holders cannot retain an ownership interest in the debtor unless all creditor claims are paid in full, does not apply to Subchapter V. This provision is a potential game-changer for many business owners as the SBRA removed the requirement that equity holders provide "new value" to retain their equity interests without paying the creditors in full. With many business owners having a substantial portion of their net worth tied up in their business, providing new value was something that may not have been possible before as many businesses confronting bankruptcy were already facing a liquidity crisis.

Plan confirmation: Unlike traditional Chapter 11, Subchapter V allows for a debtor to confirm a reorganization plan without acceptance of the creditors as long as the plan is fair and equitable – the debtor must contribute all "projected disposable income" to making plan payments for three to five years.

Discharge: If the court confirms a consensual plan accepted by creditors, the debtor will receive a discharge at confirmation. Otherwise, without a consensual plan, the debtor receives the discharge once all plan payments are made.

### **Tooling for Time**

With the economy and businesses currently facing unprecedented challenges, Subchapter V can offer businesses a cost and time-efficient option to put a hold on their obligations while negotiating with creditors and lenders to come out on the other side with stronger footing.

### **Contact Us**

If you have any questions or would like additional information to determine if taking advantage of this financial tool while it is available is right for your business, we are here to help. Please contact the partner in charge of your account or:

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