COVID-19 UPDATE


Shutts & Bowen LLP
CARES Act Bankruptcy Code Changes

The Coronavirus Aid, Relief, and Economic Security (CARES) Act recently made important revisions to the United States Bankruptcy Code, including an increase of debt limits for small businesses reorganizing under Chapter 11.

Small Business Reorganization Act

On February 19, 2020, the Small Business Reorganization Act (SBRA) came into effect. Commonly referred to as “Subchapter V” under Chapter 11, the SBRA was enacted to make it easier for small businesses to reorganize.

As originally enacted, Subchapter V was only to apply to firms with no more than $2,725,625 in liquidated debt. As part of the recently passed CARES Act, Congress provided for a one-year increase of the Subchapter V debt limits to $7.5 million in liquidated debt.

Under Subchapter V, the debtor is required to file a Chapter 11 plan within ninety-days of the bankruptcy filing and must also provide for plan payments for a period of three to five years.

Subchapter V also takes a page from how Chapter 13 cases under the Bankruptcy Code function in that the debtor’s projected disposable income will now be used to apply payments under the plan.
Specifics on Bankruptcy Code
Subchapter V

In order to *expedite* the plan confirmation process and make it easier for small businesses to reorganize, under Subchapter V:

1) a small business debtor is no longer required to submit its plan to a voting and disclosure statement process;

2) the debtor is no longer required to pay all administrative expense claims immediately upon plan confirmation and the debtor can stretch payments over the life of the plan; and

3) Subchapter V removes the absolute priority rule which requires that any equity holders of the small business debtor provide “new value” to be able to retain their equity interests if any of their creditors interests were impaired under the chapter 11 plan.
Specifics on Bankruptcy Code Subchapter V

Under Subchapter V, unsecured creditors lose many protections available in the traditional Chapter 11 plan process and there are no unsecured creditors’ committees allowed under Subchapter V.

To protect unsecured creditors, Subchapter V requires the appointment of a trustee with limited powers. The trustee is appointed to assist with managing and facilitating the small business debtor’s reorganization and to ensure that the debtor follows the reorganization exactly as it was presented in the plan.

From a secured creditor’s perspective, there are still similarities to the traditional Chapter 11 process. While secured creditors have fewer opportunities to raise objections to a Subchapter V plan, and many of the strategies used in a traditional Chapter 11 process may be unavailable, a secured creditor must be paid the value of their secured claim over the life of the plan. The small business debtor continues to have the right to seek a cram-down in the amount of a secured claim equal to the value of the collateral.

Takeaways

Subchapter V is still in its infancy. There are still many questions as to how cases will ultimately be administered and how the case law will develop. However, the enlargement of the debt limit will allow more businesses to take advantage of the potential benefits offered by Subchapter V.

For more information on Subchapter V of the Bankruptcy Code, please reach out to James A. Timko.

To view time-sensitive resources and learn more about the protocols Shutts & Bowen is implementing to protect its employees and clients from COVID-19 exposure, click here.