

## The One-Year Anniversary of Subchapter V: What We've Learned

As many of you know, in 2019 Congress fortuitously passed the Small Business Reorganization Act, which created Subchapter V of the Bankruptcy Code ("Subchapter V") and came into effect in February 2020. We reported on it [here](#) and [here](#). Subchapter V created a form of Chapter 11 case in the United States Bankruptcy Code. Subchapter V aims to give businesses a faster and less expensive option for reorganizing under Chapter 11 and contains powerful tools for businesses in financial distress. Under Subchapter V, a business qualifies to file a case if its noncontingent liquidated debts are in the amount of \$2,725,625 or less. Section 1113 of the CARES Act of 2020, however, increased that debt limit from \$2,725,625 to \$7.5 million. This change in the debt limit applies until March 2021 and will return to \$2,725,625 absent an extension by Congress.

Highlights of Subchapter V include the small business retaining control of its affairs during the bankruptcy process; no creditors committee is appointed except in unusual circumstances; a streamlined confirmation process, with no disclosure statement requirements; relaxed requirements for confirmation of a plan; and with no absolute priority rule, existing ownership retains control of its business.

Case law is developing in Subchapter V and here is what we are seeing:

- » Courts want to allow debtors to file or proceed under Subchapter V. Many courts have allowed a process, called redesignation, to allow an existing Chapter 11 case be designated a Subchapter V case to take advantage of the benefits to debtors. E.g. In re: Tony and Melisa Easter, No. 19-12063-SDM, 2020 WL 6009201 (Bankr. N.D. Miss. Oct. 9, 2020) (allowing debtors to redesignation to Subchapter V one year after filing small business case ); In re Slidebelts, 2020 WL 3816290 (Bankr. E.D. Cal. July 6, 2020) (allowing debtor to dismiss and then re-file under Subchapter V).
- » Cases move fast. Subchapter V requires reporting by the debtor on its efforts to form a consensual plan for a conference with the judge just 60 days after filing and requires a plan be filed within 90 days. These deadlines are not likely to be moved. The plan deadline cannot be moved unless the debtor can show that the extension is needed for reasons "for which the debtor should not be justly held accountable," not a for cause standard. 11 U.S.C. § 1189(b).
- » Debtors viewed as trying to game the system do not stand much of a chance in Subchapter V. Perhaps because the subchapter is designed to be a fast-paced reorganization courts do not seem to have much tolerance for those debtors they view as not acting in good faith. E.g., In

re: Jeffrey Bernhard Wetter Debtor., No. 19-71010, 2020 WL 6128048, at \*9 (Bankr. W.D. Va. Oct. 14, 2020) (denying conversion from Chapter 7 case to Subchapter V case for debtor with “long history” in bankruptcy court and elsewhere, including prepetition transfers of estate assets); In re: Abundant Life Worship Center of Hinesville, Ga, Inc., No. 20-40959-EJC, 2020 WL 7635272, at \*19 (Bankr. S.D. Ga. Dec. 16, 2020) (confirming no automatic stay in effect where Subchapter V was the latest of many attempts to prevent foreclosure).

Key takeaways for creditors are:

- » Be ready when faced with a Subchapter V case. As noted above, the cases move fast, so the leisurely pace (in comparison) of a typical Chapter 11 case is not going to be the norm in Subchapter V. There is also not likely to be many continuances before a plan is confirmed. Know the leverage points and your tolerance for negotiations as quickly as possible. Strike a deal when possible.
- » Subchapter V can be brutal to unsecured creditors. Because of the definition of disposable income, it is possible for plans to be confirmed with very low payments to unsecured creditors. Perhaps the unsecured creditors may be in favor of a plan to allow for a customer to continue in business, but recovery on amounts owed prior to bankruptcy is going to be limited. Being a secured creditor is going to be in your interest whenever possible.
- » These cases are a different animal from the typical Chapter 11 or Chapter 13 cases that we have seen. Case law is still developing, so it remains to be seen where the battle lines will be drawn between creditors and debtors in Subchapter V. It is meant to be a consensual process, and in Maine, the Subchapter V cases we have seen have largely worked out this way (although there have only been 17 so far as of this writing).

Many groups are pushing for an extension (or even increase) in the debt limit to Subchapter V and there seems to be bipartisan support for such an extension. It is likely that at least the debt limit will be extended past the March 2021 date.

Courts and parties involved with these cases have also reported good or at least efficient results in the cases, which is helpful to creditors. We have so far not seen a flood of new bankruptcy cases as of this writing, as many commentators predict. Although not frequently used yet, Subchapter V still looks like it stands to become a popular option for debt relief.

*Prepared by Preti Flaherty attorney Anthony Manhart on behalf of Maine Bankers Association. To learn more about Anthony, you can visit his page [here](#).*