

Top 15 Features of New Subchapter V

11 U.S.C. §§ 1181–1195

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These materials provide a summary of the Small Business Reorganization Act of 2019 that are discussed in more detail in *A Guide to the Small Business Reorganization Act of 2019*, available on Judge Bonapfel’s chambers website, <http://www.ganb.uscourts.gov/content/honorable-paul-w-bonapfel>, under “General Information.” References to the “*Guide*” are to that paper.

Introduction

The Small Business Reorganization Act of 2019 (“SBRA”), effective February 19, 2020, enacts a new subchapter V of chapter 11 and makes conforming changes in several provisions of the Bankruptcy Code and title 28. (*Guide* Part I).

New § 1181(a) states the sections of the Bankruptcy Code that do not apply in a subchapter V case, and new § 1181(b) states sections that do not apply unless the court orders otherwise. (*Guide* Appendix A). New § 1181(c) states that § 1141(d) (which deals with the effects of confirmation and discharge) does not apply if the court confirms a “cramdown” plan, except as stated in new § 1192, which governs timing and scope of the discharge in cramdown cases.

Interim Bankruptcy Rules and new Official Forms will apply in subchapter V cases. (*Guide* Appendix B).

1. ***New definitions of “small business debtor” and “small business cases” and election of subchapter V.*** New subchapter V of chapter 11 is available for a small business debtor who elects its application. § 103(i). The small business provisions of chapter 11 apply to a small business debtor who does not make the election. (*Guide* Part III).

§ 101(51D) has a revised definition of a “small business debtor.” It retains the debt limit, currently \$ 2,725,625, but now requires that 50 percent or more of the debt arise from commercial or business activities of the debtor. A debtor engaged in owning or operating real property may now be a small business debtor, unless the debtor owns or operates single asset real estate. It is no longer a requirement that no committee of unsecured creditors exist in the case.

§ 101(51C), as amended, provides that a “small business case” is a case in which the debtor is a “small business debtor” and has not elected application of subchapter V. (Thus, a subchapter V case is not a “small business case.”)

The debtor must state in its petition whether it is a small business debtor and whether it elects application of subchapter V. Interim Rule 1020(a).

2. **Appointment of trustee.** The U.S. Trustee will appoint a subchapter V trustee whose primary duties are to monitor and supervise the case and to facilitate confirmation of a consensual plan. New § 1183. (*Guide* Part IV).

The debtor remains in possession of assets and operates the business with the same rights and duties as an ordinary chapter 11 debtor in possession. New § 1184. (*Guide* Part V).

The court may remove the debtor from possession for cause. If it does, the trustee operates the business of the debtor. The court may also remove the debtor for failure to perform the obligations of the debtor under a confirmed plan. New § 1185(a). (*Guide* §§ IV(B)(3), V(C)).

The U.S. Trustee will appoint trustees on a case-by-case basis. (*Guide* § IV(A)). It appears that the trustee is entitled to reasonable compensation under § 330(a). (*Guide* § IV(E)). A possible issue is whether a trustee should or must employ an attorney or other professional. (*Guide* §§ IV(F)).

3. **No committee of unsecured creditors.** No committee of unsecured creditors will be appointed unless the court orders otherwise. SBRA amends § 1102(a)(3) to make the same rule applicable in a small business case (*i.e.*, the case of a small business debtor that does not elect subchapter V). (*Guide* § VI(A)).

4. **No U.S. Trustee fees.** The debtor does not pay U.S. Trustee fees. 28 U.S.C. § 1930(a)(6)(A), as amended. (*Guide* § VI(E)).

5. **Subchapter V debtor has the same reporting requirements as small business debtor under existing law.** New § 1187 specifies the duties and reporting requirements of a subchapter V debtor. Although § 1116 does not apply in a subchapter V case (new § 1181(a)), new § 1187 incorporates all its requirements. (*Guide* § V(B)).

6. **Required status conference and debtor report.** The court must hold a status conference within 60 days after the order for relief. New § 1188. The debtor must file a report not later than 14 days before the status conference that “details the efforts the debtor has undertaken and will undertake to attain a consensual plan of reorganization.” New § 1188(c). (*Guide* § VI(C)).

The trustee must appear and be heard at the status conference. New § 1183(b)(3).

In the Northern District of Georgia, the notice of bankruptcy filing will include the time for the status conference.

7. **Property of the estate.** § 1115 does not apply in a subchapter V case, but similar provisions become applicable in cases of individuals and entities if the court confirms a “cramdown” plan. (*Guide* Part XI).

§ 1115 provides that, in an individual case, property of the estate includes property that the individual acquires after the filing of the petition and earnings of the debtor from postpetition services.

New § 1186(a) provides that, if the court confirms a cramdown plan, property of the estate consists of property of the estate under § 541, property that the debtor acquired postpetition, and postpetition earnings from services.

8. Filing of plan and contents; no disclosure statement. Only the debtor may file a plan, new § 1189(a), and the debtor must do so within 90 days of the order for relief, new § 1189(b). (*Guide* § VI(D)). The plan must meet the content requirements of subchapter V. The content requirements of §§ 1122 and 1123 (with three exceptions) remain applicable in a subchapter V case, and new § 1190 states additional requirements. (*Guide* Part VII). Section 1125, which requires a disclosure statement, does not apply unless the court orders otherwise. (*Guide* § VI(B)). New § 1181(b).

The content requirements of § 1123(a)(8) and § 1123(c) do not apply. New § 1181(a). Section 1123(a)(8) requires the plan of an individual debtor to provide for payment to creditors of all or such portion of future earnings or other income as is necessary for execution of the plan. Section 1123(c) prohibits a plan filed by an entity other than the debtor from providing for the use, sale, or lease of exempt property unless the debtor consents. (*Guide* § VII(A)).

New § 1190(3) modifies the rule of § 1123(b)(5) that prohibits modification of a claim secured only by a security interest in the debtor's principal residence. New § 1190(3) permits modification of such a claim if the new value received in connection with the granting of the security interest was not used primarily to acquire the real property and was used primarily in connection with the small business of the debtor. (*Guide* § VII(B)).

New § 1190(1) requires that a plan contain: (1) a brief history of the operations of the debtor; (2) a liquidation analysis; and (3) projections regarding the ability of the debtor to make payments under the proposed plan. (*Guide* § VII(B)).

New § 1190(2) requires that the plan provide for the submission of "all or such portion of the future earnings or other future income of the debtor to the supervision and control of the trustee as is necessary for the execution of the plan." (*Guide* § VII(B)).

9. Payment of administrative expense claims under the plan. § 1129(a)(9)(A) requires that a plan must provide for the payment in full of administrative expense claims and "involuntary gap" claims, unless the holder agrees to different treatment. New § 1191(e) permits confirmation of a plan that provides for payment of such claims through the plan if the court confirms it under the "cramdown" provisions of new § 1191(b). Administrative expense claims include fees of the trustee and professionals employed by the debtor and the trustee. They also include § 503(b)(9) claims for goods received by the debtor within 20 days before the filing of the petition. (*Guide* § VIII(B)(6)).

10. **Confirmation of consensual plan.** New § 1191(a) provides that the court must confirm a plan if it meets all the requirements of § 1129(a) except the requirement of § 1129(a)(15) that, in an individual case, the debtor must pay projected disposable income to make payments under the plan for five years or the term of the plan, whichever is longer, if an unsecured creditor invokes it. (*Guide* § VIII(A)).

11. **Cramdown confirmation: no accepting class required, no absolute priority rule; projected disposable income requirement applies to all debtors.** New § 1191(b) states the rules for cramdown confirmation. Section 1129(b) does not apply in subchapter V cases. New § 1181(a). (*Guide* § VIII(B)).

The court may confirm a plan under new § 1191(b) if:

(1) all of the requirements for confirmation in § 1129(a) are met except the requirements that all creditors accept the plan ((a)(8)), that at least one impaired class accept the plan ((a)(10)), and that an individual debtor commit projected disposable income ((a)(15));

(2) the plan does not discriminate unfairly; and

(3) the plan is “fair and equitable.”

In the case of a class of secured creditors, the provisions of § 1129(b)(2)(A) govern determination of whether the plan is “fair and equitable.” (*Guide* § VIII(B)(2)).

New § 1191(c) states a “rule of construction” for determining whether the plan is fair and equitable. The rule:

(1) imposes a requirement that the debtor (whether an entity or an individual) use all of the debtor’s projected disposable income for a three-year period, or such longer period not to exceed five years as the court may fix, to make payments under the plan (*Guide* § VIII(B)(4));

(2) requires a finding that the debtor will be able to make all payments under the plan or that there is a reasonable likelihood that the debtor will be able to make them (*Guide* § VIII(B)(5)); and

(3) requires the inclusion of “appropriate remedies” in the plan in the event of default, including the liquidation of nonexempt assets (*Guide* § VIII(B)(5)).

There is no absolute priority rule.

New § 1191(d) defines disposable income in essentially the same way as chapter 12, § 1225(b).

Key issues are how the court determines disposable income, whether the projected disposable income commitment period should be longer than three years, and how long it should be. The “means test” standards do not apply. Disputes may arise if a debtor wants to reserve funds for anticipated capital improvements or wants to spend money to grow the business. If the debtor is a “pass-through” entity for tax purposes (*e.g.*, an LLC or a subchapter S corporation), a question may be whether the debtor may make distributions to its owners to enable them to pay the tax that they owe individually as a result of the debtor’s income. (*Guide* § VIII(B)(4)).

12. ***Payments under the plan.*** How creditors receive payments under the plan differs depending on whether the court confirms a consensual or cramdown plan.

If the court confirms a consensual plan, the service of the trustee terminates upon “substantial consummation.” New § 1183(c)(1). The debtor must serve notice of substantial consummation on all parties in interest. New § 1183(c)(2). Substantial consummation generally occurs when distribution under the plan commences. § 1101(2). Thus, the debtor makes payments under the plan. (*Guide* § IX(A)).

New § 1194(b) requires trustee to make payments under a cramdown plan, unless the plan or confirmation order otherwise provides. A likely issue is whether, as in chapter 13 cases, the debtor may make postpetition installment payments on long-term debts that are being cured or reinstated. (*Guide* § IX(B)).

13. ***Discharge.*** The timing of the discharge and its scope depend on whether the court confirms a consensual or cramdown plan.

If the court confirms a consensual plan, § 1141(d) applies, except for paragraph (d)(5). Paragraph (d)(5) defers the discharge in an individual chapter 11 case until the debtor completes payments under the plan and also provides for a “hardship discharge.” Because § 1141(d) applies, the debtor receives a discharge upon confirmation. § 1141(d)(1)(A). It does not discharge an individual debtor from any debt excepted under § 523(a). (*Guide* § X(A)).

If the court confirms a cramdown plan, § 1141(d) does not apply. New § 1181(c). Instead, new § 1192 governs the discharge. (*Guide* § X(B)). Significant features are:

- (1) The debtor does not receive a discharge until completion of payments due within the first three years, or such longer period not to exceed five years as the court may fix.
- (2) The discharge applies to all debts provided in § 1141(d)(1)(A) *and* all other debts allowed under § 503 (administrative expenses).
- (3) The discharge does not apply to any debt on which the last payment is due after the first three years, or such longer period not to exceed five years as the court may fix.

(4) The discharge is subject to the exceptions in § 523(a). It is not clear whether the exceptions apply to a debtor that is not an individual.

14. ***Postconfirmation modification.*** The availability of postconfirmation modification depends on whether the court confirms a consensual plan or a cramdown plan. (*Guide* § VIII(C)).

If the court confirms a consensual plan, postconfirmation modification is not permitted after substantial consummation. New § 1193(b). Postconfirmation modification is permissible only if the circumstances warrant and the court confirms it under § 1191(a).

If the court confirms a cramdown plan, the debtor may seek its modification at any time within three years, or such longer period not to exceed five years as the court may fix. § 1193(c). Postconfirmation modification is permissible only if the circumstances warrant it and the court confirms it under § 1191(b).

15. ***Prepetition debt up to \$10,000 to professional employed by debtor does not disqualify professional from representing subchapter V debtor.*** New § 1195 provides that a person is not disqualified from employment under § 327(a) solely because of a claim of less than \$ 10,000 that arose prior to commencement of the case. (*Guide* § VI(F)).