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BANKRUPTCY

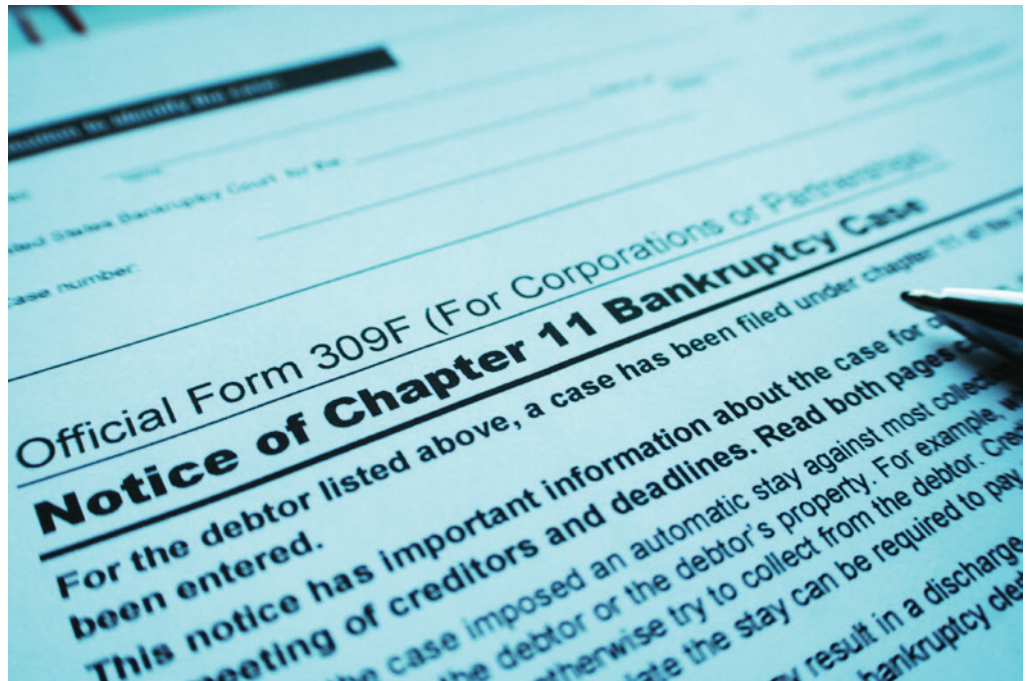
Bill Could Make Ch. 11 a Viable Option for Small Businesses



By
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In a much needed and welcomed bipartisan effort, Sen. Chuck Grassley (R-Iowa) and Sen. Sheldon Whitehouse (D-R.I.) introduced a bill last week that, if approved, would make bankruptcy a more attractive and realistic option for small businesses in financial distress. Small business debtors are companies with less than \$2.5 million of debt. The title of the bill is the Small Business Reorganization Act of 2018 and, if enacted, would create a new subchapter of title 11 of the United States Code (subchapter V, immediately following subchapter IV governing railroad reorganizations). The proposed legislation is designed to make small business bankruptcies quicker and less expensive.

So how does the proposed bill make Chapter 11 less expensive and more attractive to small



businesses? The bill shortens the time to file a plan to 90 days (as opposed to the 120 days provided for under §1121 of the Bankruptcy Code). Additionally, the bill eliminates the requirements of filing a disclosure statement and solicitation of votes of creditors. The bill truncates this two-step process by requiring only that the small business debtor propose and confirm a plan. For example, under the

proposed bill, a small business debtor would be required to file a plan within 90 days (subject to an extension based on circumstances for which the debtor should not "justly be accountable" or, in other words, based on circumstances beyond the debtor's control).

The bill contemplates that a small business debtor's plan be streamlined but must (1) include a brief history of the business operations

of the debtor; (2) contain a liquidation analysis; (3) include projections with respect to the ability of the debtor to make payments under the proposed plan; and (4) provide for the submission of all or such portion of future earnings or other future income of the debtor to the supervision and control of the trustee. Further, the bill provides that the rights of secured creditors may be modified if the claim is secured *only* by a security interest in real property that is the principal residence of the debtor and new value received in connection with such security interest was not used primarily to acquire the real property and was used primarily in connection with the small business of the debtor. This provision is almost identical to the anti-modification provisions applicable to Chapter 13 debtors and would protect purchase money mortgage lenders from modification of their rights in a small business bankruptcy but offers no protection to lenders holding collateral mortgages.

To confirm a small business debtor plan, the plan must meet all the requirements of §1129 of the Bankruptcy Code (the traditional requirements for all Chapter 11 debtors); however, the cramdown sections of §1129(b) would be modified to provide small business debtors greater flexibility in

forcing a plan upon a dissenting secured creditor (other than purchase money mortgage creditors). The cramdown provisions of the bill are premised upon the disposable income of the debtor within the plan period which can range from three to five years. Disposable income is all income of the debtor that is not reasonably necessary for the payment of expenditures necessary for the continuation, preservation or operation of the business of the debtor. The proposed bill eliminates the absolute priority rule/new value corollary from the

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cramdown requirements so business owners may be able to keep their ownership interests without having to pay senior creditors in full or provide new value through funding plan payments. Currently a small business debtor would need to either put new money into the plan or pay creditors in full to confirm a plan over the objection of creditors. The proposed bill will make small business reorganizations much more attractive to business owners looking to right-size their businesses' balance sheets while maintaining their equity stakes. Other aspects of the bill

include an expanded definition of property of the estate to include postpetition income of the debtor (similar to individual Chapter 11 debtor cases) and the absence of a formal appointment of a creditors' committee.

Traditionally Chapter 11 plans are viewed as contracts of repayment with creditors, with creditor assent to the plan obtained by satisfaction of the voting requirements contained in the Bankruptcy Code. Under the proposed bill, however, there is no solicitation and voting requirements for confirmation and, similar to a Chapter 13 individual debtor plan, creditors do not have a voting right per se, but nonetheless have a right to object to confirmation. Chapter 11 has proved unworkable for small business debtors given their size and limited financial resources. Providing small business debtors with a legislative reorganization remedy that is achievable is necessary and long overdue. The proposed bill attempts to create such a remedy and hopefully will garner full Congressional support and be enacted into law.