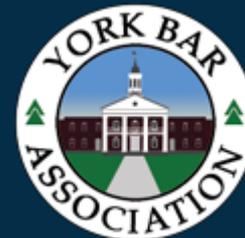


The Small Business Reorganization Act of 2019: New Chapter 11 Procedures for Small Businesses

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Meet the Panelists:



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Agenda

- Intro
- What is Chapter 11?
- Pre-filing Considerations and Analysis for Businesses
- Chapter 11 Expenses and Where the SBRA Can Help
- Core Provisions of SBRA
- Q&A
- Closing



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What is Chapter 11?

- Section of the U.S. Bankruptcy Code that allows businesses and individuals to reorganize, restructure debts, and liquidate assets
- Business remains in possession of assets and continues operating
 - Trustee is not appointed in Chapter 11 (unless ordered by court for cause)

Examples of How Chapter 11 Benefits Many Businesses

- Automatic stay - 11 USC § 362(a)
 - Stops, with some important exceptions, lawsuits and collection actions
 - Forbids creditors with pre-petition claims from seeking to recover on those claims outside of bankruptcy claim process
- Power to reject, assume, or assign executory contracts and unexpired leases at limited cost to debtor
- Ability to sell assets free and clear of liens and encumbrances
- Ability to restructure debts (and not pay some debts) through plan of reorganization, including longer amortization and new interest rate
- Time to breathe and opportunity for “fresh start” while continuing to operate and serve community now and in future



Pre-filing Considerations and Analysis for Businesses

- **Consider key stakeholders, including board, management, lenders, important vendors, and regulators**
- **Analyze loan documents and security interests**
- **13-week cash projections and upcoming expenses**
 - How much cash is needed and when does it run out?
 - Identify large expenses and timing, particularly payroll and debt service, that may drive timeframe for bankruptcy filing
 - Determine if immediate borrowing is required and sources
 - Covid-19 impact and State re-opening guidelines – What does revenue look like in a post-shutdown economy?
- **Is an out-of-court restructuring feasible?**
 - Forbearance Agreements and Loan Amendments
 - Debt Modifications
 - Receivership
 - Voluntary liquidations and wind-down



Pre-filing Considerations and Analysis for Businesses (cont'd)

- **What type of chapter 11 case will it be?**
 - Ordinary Chapter 11 case
 - Subchapter V small business case (debt less than \$7.5 million)
 - Single-Asset Real Estate (SARE) debtor
 - “Healthcare business” debtor
- **Once you are in Chapter 11, how do you plan to get out?**
 - What are the goals during and after the bankruptcy?
 - Liquidation or reorganization?
 - How long is needed to reorganize?
- **Personal / Emotional Goals**
 - Setting finances aside, is there a personal desire of ownership / management to invest in reorganization and continue operating? (time / money / employees / community)
 - Is it time to walk away in an orderly process?



Chapter 11 Expenses and Where the SBRA Can Help

- Pre-filing investigation and preparation
- Cost of getting set up in bankruptcy
 - First- and second-day motions
 - Professional retention
- Administrative / Reporting Obligations
- United States Trustee Fees
- Court approval (ordinary and non-ordinary operational issues)
- Disputes, adverse parties, and litigation
- Time from start to finish of case
- In general: limited economies of scale based on debtor's size



Core Provisions of SBRA: Who Qualifies?

- **To qualify as a small business debtor:**

The debtor must be a person or entity engaged in commercial or business activity with aggregate noncontingent liquidated secured and unsecured debts of \$2,725,625 or less (excluding debt owed to affiliates or insiders) and not less than 50 percent of which arose from the commercial or business activities of the debtor

- **But: Increased to \$7.5 Million by CARES Act for 1 Year**

- **Single-Asset Real Estate Debtors Excluded: Debtor that derives substantially all of its gross income from the operation of a single real property cannot elect into SBRA**

- **No requirement that the debtor remain engaged in the commercial or business activity post-petition**

- But: Debtor must show that at least 50% of its pre-petition debts arose from such activities
- Nonetheless, difficult to confirm plan if not operating post-petition



Core Provisions (cont'd): Debtor-in-Possession Remains

- SBRA debtor operates its business in chapter 11 as a debtor-in-possession.
 - Default is no operating trustee
- Therefore, Debtor still needs to file first-day motions typical of chapter 11 debtor in possession case, etc.
 - Professional Retention Change: No disqualifying conflict for professional to hold claim of less than \$10,000 on petition date
- Court can remove a small business debtor from debtor-in-possession status only for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor
- If that happens, the standing trustee takes over the operation of the debtor's business



Core Provisions (cont'd): Filing Requirements and Timing

- Upon electing to file under Subchapter V, debtor must file a copy of most-recent balance sheet, statement of operations, cash-flow statement, and federal income tax return
 - But if none, file sworn statement that such documents do not exist
- SBRA does not specify when the debtor must elect to proceed under Subchapter V. Proposed local rules and forms provide for the election at the time the petition is filed.
 - Recent cases indicate that debtor may be able to retroactively elect to be in Subchapter V under certain conditions
- Creditor's Committees: Unless the court orders otherwise, no creditors committee; creditors committees will be the exception – not the rule – in SBRA reorganizations.



Core Provisions (cont'd): Standing Trustee

- Subchapter V cases will have a “standing trustee” appointed by the U.S. Trustee.
- Standing trustee will appear and be heard at plan confirmation; *general obligation to “facilitate the development of a consensual plan of reorganization”*.
- Standing trustee will act as a conduit for plan payments in the case of nonconsensual plans or consensual plans providing for that role.
- Standing trustee has the authority to investigate the financial affairs of the debtor only if a party-in-interest requests an investigation and the Court approves.



Core Provisions (cont'd): Standing Trustee

- Standing trustee authorized to operate the debtor's business ONLY if the debtor is removed as a debtor-in-possession; otherwise NOT an operating trustee in any respect.
- Standing trustee's services are terminated upon "substantial consummation" of the confirmed plan in all cases; such services terminated upon confirmation and effectiveness of consensual plan.
- How and how much does the standing trustee get paid? (*Open question in Maine*)
- Who are the standing trustees?
- Experience to date with standing trustees



Core Provisions (cont'd): Deadlines for Fast-tracking Case

- **The goals of Subchapter V are to minimize the time and expense of small business reorganization**
- **How is that done? New Statutory Deadlines**
 - Within 60 days of the filing, the bankruptcy court shall hold a status conference “to further the expeditious and economical resolution” of the case
 - 14 days prior to the status conference, the debtor must file a report detailing the efforts to attain a consensual plan of reorganization
 - Debtor must file plan 90 days after petition date
 - The court can extend 90-day plan-filing deadline under “circumstances for which the debtor should not justly be held accountable.”
 - **NOTE: NO CONFIRMATION DEADLINE; JUST A FILING DEADLINE**



Core Provisions (cont'd): Special SBRA Plan Rules

- Only the debtor is allowed to propose a plan
- The SBRA need not solicit plan acceptances with a separate disclosure statement (*cost savings*)
 - Although no separate disclosure statement, plan must include (i) brief history of the business operations of the debtor, (ii) liquidation analysis, and (iii) projections with respect to the debtors' proposed payments under the proposed plan.
- SBRA plan can modify rights of a claim secured only by a security interest in real property that is the principal residence of the debtor if money received in connection with the granting of the security interest was (i) not used primarily to acquire the real property; and (ii) used primarily in connection with the small business of the debtor



Core Provisions (cont'd): Special SBRA Plan Rules

- **Confirmation of SBRA plan is pursuant to the usual criteria of section 1129(a) of the Bankruptcy Code, with the critical exception that the debtor does not need to obtain the acceptance of even one impaired class of creditors.**
 - §1129(a)(10) does not apply to the SBRA cram down option
 - What does cram down option mean in practice for debtors?
- **Equity holders can retain their interests even if plan does not pay unsecured claims in full, as long as plan “does not discriminate unfairly and is fair and equitable” with respect to impaired unsecured creditors**
 - “Fair and equitable” means only that the SBRA debtor must commit all of its “projected disposable income” (*or property of equivalent value*) to make payments under the plan for 3 to 5 years
 - Disposable income means income received by the debtor that is not reasonably necessary to: “ensure the continuation, preservation, or operation of the business.”



Key Takeaways

- Elective/Optional; not required to elect Subchapter V
- The plan cram down option is a default (as cramdown was always intended to be)—drives negotiated result and encourages cooperation and restructuring support agreements
- Efficiency/Speed/Simplicity/Low Cost
- Intended to Promote Reorganization; Focus on feasibility



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Subchapter V in Practice

- Subchapter V cases in Maine
- Real cost savings in some areas
- Focus on exit plan / light at end of the tunnel
- Collective effort to make Subchapter V work



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Q&A



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