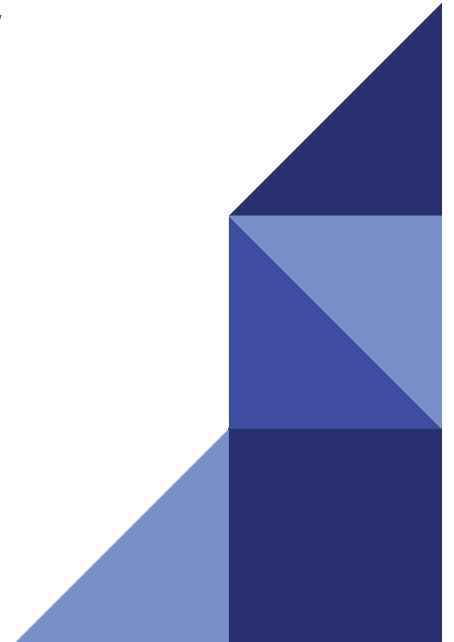


New Bankruptcy Law for Small Businesses



Small Business Reorganization Act (“SBRA”)*

- **Brand new type of Chapter 11 case (Subchapter V)** - Effective February 2020
- **Intended** to allow small business debtors to file in a timely and cost-effective manner so they can remain in business, which benefits the owners, employees, suppliers, customers and others who rely on that business.



Small Business Reorganization Act (“SBRA”)*

- **Revises and defines a “small business debtor” as:**
 1. A person or company engaged in commercial or business activities (except a person whose primary activity is in the business of owning single asset real estate);
 2. Whose total noncontingent liquidated secured and unsecured debts is no more than \$2,725,625* (excluding debts owed to one or more affiliates or insiders); and
 3. With 50% or more of the debt arising from the commercial or business activities of the person or company.

See 11 U.S.C. § 101(51D). Eligible small business debtors have to elect a Subchapter V upon filing for bankruptcy.

*The CARES Act temporarily increased the \$2,725,625 debt ceiling to \$7.5 million; however, the increase expires on or about March 27, 2021.

* There are 2 sets of provision in Chapter 11 for small business debtors: Subchapter V and small business debtors in Chapter 11 cases. SBRA does not repeal existing provisions of a small business Chapter 11.



Highlights of SBRA

Procedural Benefits (expedited process)

Streamlined requirements

- No creditor committee unless court orders
- No disclosure statement
- Administrative expenses (including trustee fees) may be paid over time through the plan
- Debtors do not pay quarterly fees to to the OUST.

Tighter timeline

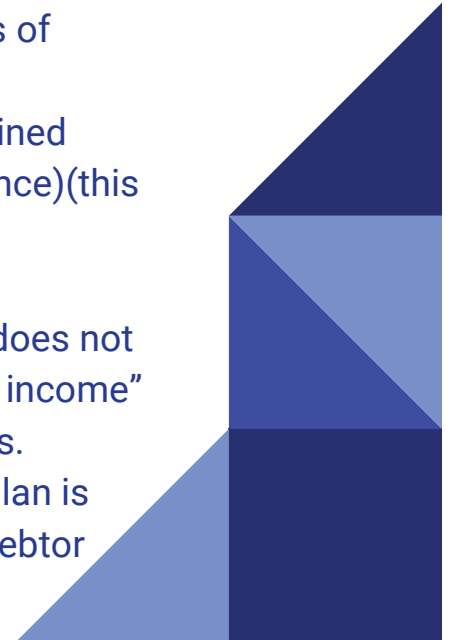
- Subchapter V Trustee appointed and 341a meeting of creditors set within 24-48 hours
- OUST conducts initial debtor interview within 10 days of case filing
- 341a meeting held approximately 21 days after filing
- Court holds status conference not later than 60 days after case is filed
- 14 days before status conference, Debtor has to file status report re efforts towards consensual plan
- Debtor shall file plan not later than 90 days after petition date



Highlights of SBRA

Substantive Benefits (lower administrative costs and other beneficial rights)

- Save costs because of the streamline requirements.
- Only Debtor may propose a plan (i.e. Debtor can still propose plan if debtor has been removed as DIP).
- Debtor does not need to obtain acceptance of plan of even one impaired class of creditors.
- Plan can modify mortgage on his/her primary residence if loan proceeds obtained were used primarily for business purpose (as opposed to acquiring the residence)(this right is not available in other chapter 11, chapter 12 or chapter 13).
- Debtor has flexibility to pay administrative claims over life of the plan.
- Owners (equity holders) can retain their interests in the business even if plan does not pay unsecured claims in full so long as the Debtor uses “projected disposable income” to make payments under the plan for a minimum of 3 and maximum of 5 years.
- Debtor gets immediate discharge upon confirmation if plan is consensual. If plan is not consensual, then discharge is entered “as soon as practicable” after the Debtor completes all payments.



Chapter 11 Bankruptcy



Benefits of Chapter 11

For small businesses in financial distress, bankruptcy (whether under the SBRA or generally) can be a temporary lifeline:

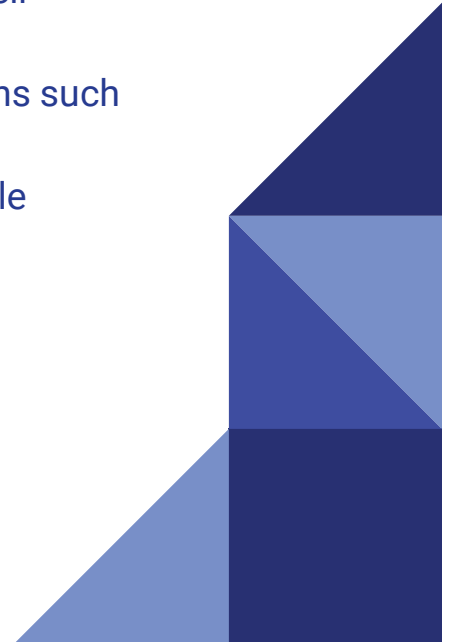
- Filing bankruptcy automatically prevents, or "stays," debt collection actions against the debtor and the debtor's property. As long as the stay ("Automatic Stay") remains in effect, creditors cannot bring or continue lawsuits, make wage garnishments, or even make telephone calls demanding payment.
- Small businesses can continue to operate.
- Management can remain in control of the business, unless the court orders otherwise.
- Management can work closely with a bankruptcy attorney and other professionals to attempt to reduce liabilities and give a company a new beginning or a "fresh start" without closing its doors.



Benefits of Chapter 11

Additional benefits:

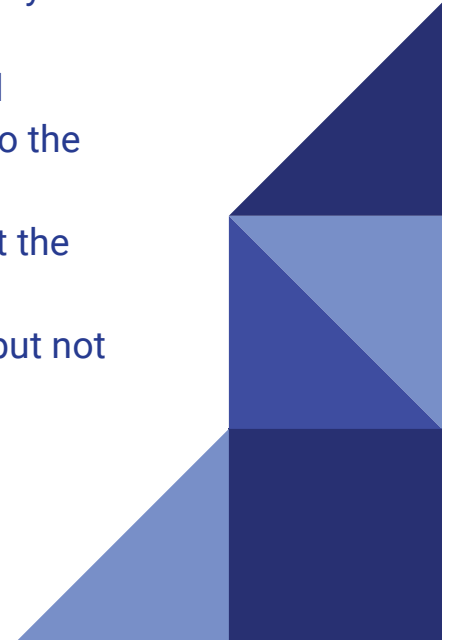
- **Deferral**: A bankruptcy filing defers the time to make certain payments on certain debts.
- **Financing**: Debtors can borrow money while in bankruptcy in order to finance their reorganization.
- **Cure Defaults**: Debtors use the chapter 11 process to cure defaults on obligations such as mortgages, taxes and other obligations.
- **Reevaluate Contracts**: The Bankruptcy Code allows a debtor to reject unfavorable contracts or unexpired leases.



Benefits of Chapter 11

Additional benefits:

- **Reduce Interest Rate**: Debtors can adjust certain interest rates of loans secured by commercial equipment, vehicle or certain real estate.
- **Sale**: A court may approve the sale of assets “free and clear” of claims, liens and interests. The secured creditors’ claims, liens and interests would attach solely to the sale proceeds. Generally, there is no successor liability for a purchaser.
- **“Cram Down”** - A plan can be confirmed even if a class of creditors votes against the plan of reorganization and they disagree with how they are treated in the plan.
- **“Discharge”**- After confirmation and payment under the terms of the plan, most but not all debts incurred prior to the bankruptcy filing are cancelled.



Benefits of Chapter 11

While operating, a Debtor has various options to restructure financial obligations and reorganize debts in Chapter 11:

- The Bankruptcy Code provides the Debtor a host of powers to remedy operational problems (*i.e.* reject executory contracts and unexpired leases)
- The Bankruptcy Code allows a small business time and ability to propose a plan that restructures the debtor's debts and reorganizes the debtor's business allowing it to continue to operate (through a confirmed or approved plan). Some plans can be a liquidating plan.
- Other "bankruptcy powers" include imposing a plan on dissenters, holding creditors at bay (through the automatic stay) while negotiating with creditors, and getting a clean deal in one wrapped up confirmation order enforceable by a federal bankruptcy judge that is binding on all state and federal courts once it is final and non-appealable.



Benefits of Chapter 11: The Automatic Stay

- The filing of bankruptcy creates an injunction staying all actions by creditors to recover on a claim against the debtor.
- The purpose of the Automatic Stay: “Provide breathing space to the debtor, prevent harassment of the debtor, assure that all claims against the debtor will be brought in the sole forum of the bankruptcy court, and protect creditors as a class from the possibility that one or more creditors will obtain payment to the detriment of others.” *Daff v. Good (In re Swintek)*, 906 F.3d 1100, 1103 (9th Cir. 2018).
- Great tool to use to keep creditors at bay while negotiating and “restructuring” the terms with creditors.

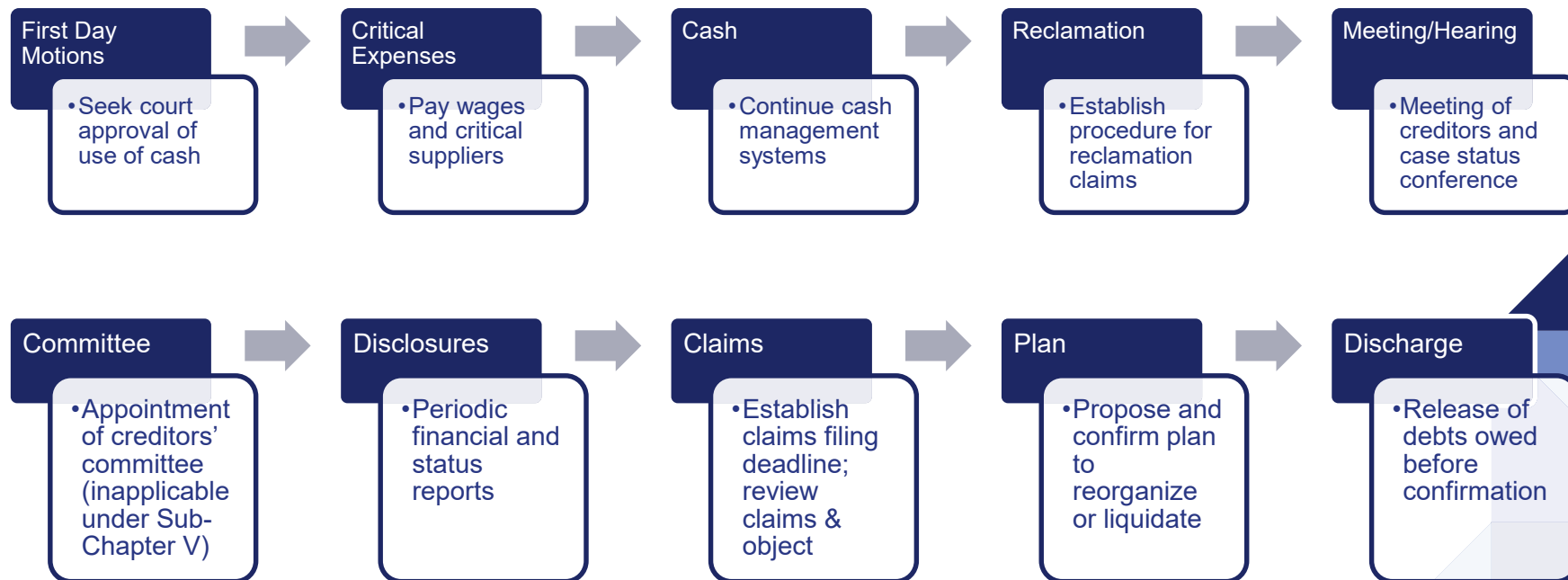


Benefits of Chapter 11: Asset Sales

- **Asset Sale:** Companies that lack the financial means or desire to undergo a reorganization have the option to quickly sell all or substantially all of their assets "free and clear" of liens, claims, and interests.
- **For Sellers:** Chapter 11 gives a company the ability to conduct an orderly sale and maximize returns by selling the company as an operating business.
- **For Buyers:** Buyers are able to acquire assets free and clear of liens, claims and interests, and take advantage of procedures that enable sales to close quickly and obtain certain protections for finality of the sale.



Typical Life of Chapter 11 Reorganization



Summary: Pros and Cons of Filing Chapter 11

Pros:	Cons:
<ul style="list-style-type: none">• Debtor-in-possession remains in control of assets.• Reduce and discharge debts/obligations during the reorganization process.• Preserve the business name, goodwill and customer base.• Continue to operate while paying off debts.• Trigger the Automatic Stay which prevents creditors from taking any collection action against assets.• Section 363 Asset Sales.• Restructure debts allowing for lower payments to be made over a longer period of time.	<ul style="list-style-type: none">• Financial record keeping and extensive oversight and scrutiny of reporting requirements, which may ultimately benefit the company.• Restrictions on the compensation of debtor's insiders/owners/officers.• Court may reject a proposed reorganization plan if it determines it is not viable, compliant or realistic.• Expensive.

Ch. 11 Small Business vs. SBRA*

	Small Business Chapter 11	SBRA
Deadline to File and Confirm Plan	300 days to file Plan; 45 days after filing to confirm Plan	90 days to file Plan; No deadline to confirm Plan
U.S. Trustee Fees	Yes, paid quarterly	No
Disclosure Statement, describing the Chapter 11 plan of reorganization	Yes	No, unless Court orders otherwise "for cause"; Plan must include a brief history of the business operations of the debtor
Creditors Committee	Possible, but unlikely	No, but a Subchapter V Trustee is appointed
Absolute Priority Rule (strict hierarchy of payment among claims of differing priorities)	Yes. To retain ownership of their business without paying creditors in full, (1) creditors must vote to accept the plan or (2) equity holder must pay "new value" to the business in a substantial amount.	No, management retains equity
Administrative Expenses (actual and necessary expenses incurred during the bankruptcy to preserve the estate)	Must be paid on Plan's effective date	Can be extended over life of the Plan

* There are 2 sets of provisions in Chapter 11 for small businesses: Subchapter V and small business Chapter 11 case. SBRA does not repeal existing provisions of a small business Chapter 11.