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INITIAL EFFECTS OF SUBCHAPTER V OF CHAPTER 11 BANKRUPTCY DURING COVID-19

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by
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Abstract

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On February 19, 2020, the Small Business Reorganization Act of 2019 went into effect, ushering in the use of Subchapter V by small business debtors. Lawmakers crafted Subchapter V with the intent to make the reorganization process more streamlined and cost effective than the standard Chapter 11 was for these debtors. With features such as the Subchapter V trustee, cramdown provisions, filing deadlines, lack of a creditors' committee, and relaxed disclosure requirements, small business debtors should in theory be better positioned to emerge from bankruptcy as viable entities. Through quantitative analysis and qualitative research, this Article explores initial observations on Subchapter V by seeking to reconcile the lens of current research and theory and the viewpoint of practitioners. It also suggests further areas of research.

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INTRODUCTION

In the wake of COVID-19, small businesses struggled to finance their operations and keep afloat.[1] Fortunately, on February 19, 2020, the Small Business Reorganization Act of 2019 (the "SBRA") went into effect, preceding the pinnacle of COVID-19-induced business closures. Before the enactment of this statute, businesses had only two paths of recourse once they had arrived at the last resort of bankruptcy: Chapter 7 or Chapter 11. Chapter 7 bankruptcy forces liquidation of the business's assets, and the proceeds are distributed to creditors; owners cannot continue operating the business. In contrast, Chapter 11 bankruptcy allows the business's owners to continue operating the business concurrently with bankruptcy proceedings, but the business must expend significant costs to restructure the existing debt of the firm to the satisfaction of its creditors and the court. Historically, Chapter 11 bankruptcy costs have been so high that small businesses simply cannot afford the expenses and must opt for liquidation instead.[2] Previous congressional acts, including amendments from the Bankruptcy Abuse Prevention and Consumer Protection Act (the "BAPCPA")[3] meant to buoy small businesses in standard Chapter 11, have largely proven to be ineffective.[4]

With the enactment of the SBRA, however, small businesses with less than approximately $2.7 million—and temporarily $7.5 million under the CARES Act—in liabilities can file for bankruptcy under Subchapter V of Chapter 11.[5] This type of filing has unique requirements that should, in theory, eliminate the

[1] *See generally* Small Business Pulse Survey: Tracking Changes During the Coronavirus Pandemic, https://www.census.gov/data/experimental-data-products/small-business-pulse-survey.html.
[2] Arturo Bris, Ivo Welch & Ning Zhu, *The Costs of Bankruptcy: Chapter 7 Liquidation versus Chapter 11 Reorganization*, 61 J. OF FIN. 1253 (2006).
[3] The Bankruptcy Abuse Prevention and Consumer Protection Act, passed in 2005, was the last major overhaul to the Bankruptcy Code. It added provisions that were specifically meant to aid Chapter 11 small business cases. *See generally* 1 COLLIER ON BANKRUPTCY ¶ 20.04 (Richard Levin & Henry J. Sommers eds., 16th ed. 2020) (discussing major bankruptcy legislative highlights, including BAPCPA, since the Code's 1978 enactment).
[4] Lei Lei Wang Ekvall & Timothy Evanston, *The Small Business Reorganization Act: Big Changes for Small Businesses*, A.B.A. BUS. L. TODAY (2020), https://www.americanbar.org/groups/business_law/publications/blt/2020/02/small-business-reorg/.
[5] Shari L. Heyen & David B. Kurzweil, *The Small Business Reorganization Act of 2019 and the CARES Act: Expanded Restructuring Opportunities for Small Business Debtors*, 11 NAT'L L. REV. (Feb. 2021) https://www.natlawreview.com/article/small-business-reorganization-act-2019-and-cares-act-expanded-restructuring.

costliest and most stringent aspects of Chapter 11 bankruptcy, thus enabling small businesses to undergo restructuring and continue operating.[6] The SBRA went into effect merely months prior to the writing of this thesis, but small businesses are already taking advantage of its theoretically helpful features. Since small businesses are a driving force in the American economy—99.9% of United States businesses are small businesses, employing in total 60.6 million people,[7] the potential efficacy of the SBRA is crucial to softening the hard-hitting impacts of economic downturns.[8]

This study reveals quantitative and qualitative evidence tentatively supporting scholarly theories that characteristics of the SBRA are effective for reducing costs and minimizing time spent in the bankruptcy process.[9] However, the Subchapter V process is not without weakness. Debtor attorneys and creditor attorneys have pinpointed several issues in the Subchapter V process since its introduction, and these issues should be addressed and resolved to facilitate a more streamlined debtor and creditor experience.

Certain characteristics of Subchapter V—namely, the Subchapter V trustee role, cramdown provision, filing deadlines, lack of a creditors' committee, and lack of the disclosure statement requirement—can be benefits to the small business debtor, and preliminary reports indicate they are indeed helpful for shepherding the debtor through the process. The Subchapter V trustee's role is especially critical in determining whether the above-mentioned characteristics are beneficial or detrimental, so the lack of uniformity in trustee guidelines and compensation structure is, among other concerns, especially concerning. This Article proposes that lawmakers make expectations more explicit for Subchapter V trustees and that the debt limit for Subchapter V election be permanently raised from the $2.7 million figure.

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[6] Hon. Paul W. Bonapfel, *A Guide to the Small Business Reorganization Act of 2019*, 93 AM. BANKR. L. J. 571 (2019), http://www.gamb.uscourts.gov/USCourts/sites/default/files/pdf/SBRA_Guide.pdf.
[7] 2020 Small Business Profile, U.S. SMALL BUS. ADMIN. OFF. OF ADVOCACY, https://cdn.advocacy.sba.gov/wp-content/uploads/2020/06/04144224/2020-Small-Business-Economic-Profile-US.pdf.
[8] Michael C. Blackmon, *Revising the Debt Limit for "Small Business Debtors": The Legislative Half-Measure of the Small Business Reorganization Act*, 14 BROOK. J. CORP. FIN. & COM. L. 339 (2020), https://brooklynworks.brooklaw.edu/cgi/viewcontent.cgi?article=1335&context=bjcfcl.
[9] *See* Ed Flynn, *Subchapter V's First 1,000 Cases*, AM. BANKR. INST. J. (Nov. 2020), https://www-proquest-com.erl.lib.byu.edu/docview/2462500914?accountid=4488. ("It is too early to determine whether subchapter V has met its goal of providing small business debtors a more streamlined path for restructuring their debt, but all in all, it seems to be off to a pretty good start.")

Section I of this Article describes the characteristics of this study, including how quantitative and qualitative data were compiled. Section II of this Article explains the results of this study, enumerating the effects of Subchapter V to each of the involved parties by way of distinct Subchapter V characteristics. Section III of the Article explores other considerations—namely, Subchapter V's effect on creditors and characteristics extrinsic to Subchapter V that have affected case outcomes. Section IV of this Article highlights key areas of concern within the Subchapter V process. Section V of this Article discusses suggested improvements that can be made to Subchapter V moving forward.

I. CHARACTERISTICS OF THE STUDY

The findings highlighted in this Article are grounded primarily in data gathered from interviews with debtors, bankruptcy attorneys representing creditors and debtors, and Subchapter V trustees. These interviewees were all involved in recently filed Subchapter V cases and Chapter 11 cases from the same time period. I identified these interview subjects by searching on Lexis CourtLink and the PACER court docket for debtors with liabilities around the amount of the statute-imposed cut-off of $7.5 million. An ideal study would randomize which firms are able to use Subchapter V in order to minimize the effects of confounding variables. However, this is unrealistic when applied to bankruptcy research; I cannot randomly assign certain companies to Subchapter V and other similar companies to Chapter 11 in order to observe the focused effects of the SBRA. Such randomization is impossible, but the minimization of confounding variables may still be simulated by identifying debtors with liabilities slightly above and slightly below the arbitrary threshold of $7.5 million. These companies are likely to be most similar in size and other variables.

This study includes companies in Subchapter V with liabilities within $1.0 million below the threshold and companies in standard Chapter 11—filed since February 2020—with liabilities within $1.0 million above the threshold. These relevant bankruptcy cases are from a variety of districts, and the debtor companies span various industries. Within this pool of debtors, none are public companies. With Subchapter V being meant to benefit primarily small businesses, this trait is helpful in evaluating Subchapter V's efficacy outside the scope of shareholders' interests and focusing on businesses with a single or handful of owners.

For each bankruptcy case, I recorded dates and deadlines for each milestone of the bankruptcy process (e.g. holding an initial status conference, filing a plan of reorganization, holding a confirmation hearing, etc.). This helped in analyzing the speediness of and the results of the processes side-by-side.

After doing so, I interviewed the debtors, bankruptcy attorneys representing debtors and creditors, and Subchapter V trustees involved in these related cases. With the debtors, I gleaned general information about their experience in the Subchapter V proceedings and whether they or their attorney had suggested Subchapter V.[10] With the bankruptcy attorneys representing debtors, I asked for what they observe as the key differences between Subchapter V and Chapter 11; possible confounding variables with the debtor companies that might skew the Subchapter V result; and improvements to help make Subchapter V more streamlined. With the bankruptcy attorneys representing creditors, I surveyed their experiences within Subchapter V and asked if they'd seen lower creditor recovery rates through the process. With the Subchapter V trustees, I also asked if they'd seen lower creditor recovery rates, and I recorded their observations of their assigned Subchapter V case and their perception of the Subchapter V trustee's role.

This study relies heavily on qualitative evidence to reveal insights into the Subchapter V process. Personal interviews infuse academic research with increased depth and nuance, and this qualitative tool can greatly clarify key information not otherwise discernible from quantitative evidence—for instance, the observations gleaned from individuals actively involved in Subchapter V proceedings. The interviews conducted in this study cannot produce unqualified conclusions; nevertheless, they offer worthwhile and actionable insights into Subchapter V as it currently stands.[11] They also add boots-on-the-ground perspective to existing academic literature and theories on this topic.

A. Empirical Findings

While recognizing the limited set of relevant cases, initial factual analysis indicates that Subchapter V does facilitate more streamlined proceedings when compared to Chapter 11. Simply analyzing filing dates, confirmation or

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[10] This was helpful in determining whether some small business debtors already had some expertise in handling the process compared to others and whether SBRA was more successful for them as compared to Chapter 11 because of this inherent competence. All debtors I spoke to did not know what Subchapter V was before hiring their attorneys, and Subchapter V was initially suggested by their attorneys.

[11] *See* Brook E. Gotberg, *Relational Preferences in Chapter 11 Proceedings*, 71 OKLA. L. REV. 1013, 1019-20 (2019).

conversion dates, and status conference dates, the relevant cases show a marked difference between Subchapter V and Chapter 11.[12]

Within the 22 Subchapter V cases, two had confirmed plans of reorganization within 189 days and 191 days from filing, respectively; three were converted to Chapter 7 bankruptcy in 67, 126, and 83 days. The remaining cases have moved speedily, with many having filed a plan of reorganization and awaiting a confirmation hearing. Multiple status conferences have already been held.

Within the 8 Chapter 11 cases, only two have had a final result, both without a confirmed plan of reorganization—a conversion to Chapter 7 bankruptcy in 189 days, and a dismissal in 52 days. Remaining cases, except one, have failed to hold a status conference, and only one case has filed a plan of reorganization.

This analysis reveals some questions: Is the relatively slower movement of the Chapter 11 cases indicative of the process's ineffectiveness, or do these cases still reach appropriate conclusions but at a relatively slower pace? Can the rapid movement of the Subchapter V cases be seen as a success for SBRA lawmakers, or is it simply the result of more stringent deadlines? Does this process lower the recovery rates of unsecured creditors? And perhaps most urgently, has the rapid movement actually helped small businesses in their quest to quickly reorganize, re-emerge, and continue operating?

B. Personal Interviews (Qualitative Studies)

As stated before, this study relies on personal interviews to explain its findings. I conducted interviews with the debtors in Subchapter V and Chapter 11 themselves, their attorneys, and Subchapter V trustees. In this section, I discuss unique characteristics of Subchapter V and their effects, as gleaned from these interviews, on debtors, unsecured creditors, and Subchapter V Trustees.

To conduct these interviews, I obtained the email addresses and contact information of each related party from the case docket on PACER and sent a brief email detailing who I am, what kind of research I am conducting, how I obtained their information, the principal questions I was hoping to ask them, and an invitation for an interview by phone call. In each phone call, I followed a set script depending on if the interviewee was a debtor, debtor's attorney, creditor's

[12] *See* Table 1

attorney, or Subchapter V trustee. I recorded each interview for later accurate transcribing.

In my interviews with debtors, I asked two main questions: (1) How would you characterize your experience in the bankruptcy process? (2) How did you come to file under Subchapter V?

In my interviews with debtor's attorneys—both those involved with Subchapter V cases and normal chapter 11 cases, I asked these questions: (1) Do you have experience with both the normal Chapter 11 process and the Subchapter V process? (2) What are they key differences between the Subchapter V and normal Chapter 11 processes? (3) Are there characteristics of a business itself that make it more suited to Subchapter V or normal Chapter 11? (4) What, if anything, can be improved about the Subchapter V process? (5) Do clients usually choose whether they file under Subchapter V or Chapter 11, or will you generally make that determination?

In my interviews with creditor's attorneys, I asked two questions: (1) How do recovery rates for creditors compare under Subchapter V versus the normal Chapter 11 process? (2) What, if anything, can be improved about the Subchapter V process?

In my interviews with Subchapter V trustees, I asked three main questions: (1) How would you characterize your role as a Subchapter V trustee? (2) Do you feel the "correct" outcome occurred in this case—meaning the business either exited viably or was converted mainly because of reasons intrinsic to the company itself rather than the Subchapter V process? (3) What, if anything, can be improved about the Subchapter V process?

Lawmakers' overarching goal with Subchapter V was to minimize debtors' bankruptcy-related expenses and time spent in the process. Most of the debtors, debtors' attorneys, creditors' attorneys, and Subchapter V trustees whom I interviewed indicated that the goal has been met in most cases, and that specific characteristics unique to Subchapter V could be directly traced to these successes. These findings are explained in more detail below.

II. EFFECTS OF SUBCHAPTER V SINCE FEBRUARY 2020

Lawmakers crafted Subchapter V based on two insights: that the duration and complexity of the traditional Chapter 11 process destroy value, and that creditors are the principal beneficiaries of that value.

What, then, might be altered to prevent the confirmation of a reorganization plan from being overly cumbersome and destructively expensive? This Article discusses five distinct characteristics of Subchapter V[13] that, in theory, should streamline the bankruptcy process for business debtors seeking to reorganize under Chapter 11: (1) the role of a Subchapter V trustee, (2) the lack of the absolute priority rule and the option of cramdown provisions, (3) the introduction of filing deadlines, (4) the absence of a creditors' committee, and (5) the elimination of the disclosure statement requirement.

This study supports the predictions and analyses of scholars that the Subchapter V process can indeed be more streamlined and cost effective than the standard Chapter 11 process.[14]

A. The Subchapter V Trustee

All participants in this study indicated that the most impactful change in Subchapter V was the introduction of the Subchapter V trustee. Instead of a U.S. Trustee, a Subchapter V trustee is assigned by the United States Trustee to each Subchapter V case.[15] As a result of the SBRA, the Office of the United States Trustee has compiled a list of 250 new trustees to assist with these cases, some

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[13] This study recognizes that there are more characteristics of the Subchapter V process that make it distinct from the standard Chapter 11 process. However, for the purposes of this paper, only five are discussed.

[14] *See* Clifford J. White III, *Small Business Reorganization Act: Implementation and Trends*, AM. BANKR. INST. J. (Jan. 2021), https://www.justice.gov/ust/page/file/1350736/download. (Finally, although there is not yet sufficient data to determine conclusively whether the law has affected fees, both anecdotally and from our own observations, the subchapter V trustees are resolving disputes prior to litigation, which should further reduce or eliminate unnecessary costs.")

[15] Jeffrey Barber, *Small Business Reorganization Act of 2019 Goes into Effect February 2020*, NAT'L L. REV. (Oct. 3, 2019), https://www.natlawreview.com/article/small-business-reorganization-act-2019-goes-effect-february-2020.

with prior trustee experience and many with some professional business or finance-accounting experience.[16]

Although the purpose of assigning a Subchapter V trustee is not immediately apparent from the statute, lawmakers likely intended to create a position of oversight to facilitate the speedy and successful reorganization of these smaller, less-sophisticated businesses.[17] The role is purported to be a cross between a Chapter 7 trustee and a Chapter 11 trustee with some adjustments, and some guidance but much flexibility has been given to these newly appointed trustees.[18] Interviewees generally agreed that the Subchapter V trustee operated in a different role than other trustees, but they also voiced considerable uncertainty regarding the parameters of the trustee's role, raising concerns that this approach may also lead to great harm in some cases—to be explored further in Section IV.

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[16] Alex Wolf, *Small Business Bankruptcy Law Rolls Out with New Trustees*, BLOOMBERG L. (Feb. 19, 2020, 3:31 PM), https://news.bloomberglaw.com/bankruptcy-law/small-business -bankruptcy-law-rolls-out-with-new-trustees.

[17] *See* Christopher G. Bradley, *The New Small Business Bankruptcy Game: Strategies for Creditors Under the Small Business Reorganization Act*, 28 AM. BANKR. INST. L. REV. 251, 260 (2020). ("Subchapter V trustees' duties are not well-specified, but at a minimum trustees are supposed to help 'facilitate the development of a consensual plan of reorganization."); *see also* Donald L. Swanson, *SBRA: Frequently Asked Questions and Some Answers*, AM. BANKR. INST. J. (Nov. 2019), https://www.abi.org/sbra/faqs. ("The primary difference is a small business chapter 11 provision in § 1183 (b) (7), which states that 'The trustee shall ... (7) facilitate the development of a consensual plan of reorganization.' This provision is unique; in no other place does the Bankruptcy Code (1) authorize a trustee to help a debtor in possession develop a plan of reorganization, or (2) suggest the goal of a 'consensual plan' when the absolute-priority rule does not apply. …The SBRA trustee could also fill a mediation role: The statutory 'facilitator' role of the small business trustee, combined with the statutory goal of a 'consensual plan,' seems to suggest a mediation-type role. After all, that's what mediation does: It 'facilitates' a process of achieving a 'consensual' result.")

[18] THOMAS J. SALERNO ET AL., ADVANCED CHAPTER ELEVEN BANKRUPTCY PRACTICE § 1.2B (2020) A Subchapter V trustee's duties include:

> Accounting for all of the property received by the company; examining and rejecting any claims against the company; conducting a review of the company's financial conditions and business operations; reporting any fraud or misconduct to the bankruptcy court; appearing at the status conference and materially significant hearings; producing a final report of the case for the bankruptcy court; assisting as necessary the facilitation of a plan of reorganization; distributing certain company property in accordance with the plan of reorganization; and confirming the company's adherence of the court-approved plan of reorganization during the payment period.

Although the purpose of a Subchapter V trustee is not explicitly stated, the U.S. Bankruptcy Code Chapter 11 §1183 (b)(7) does clearly charge that "the [Subchapter V] trustee shall facilitate the development of a consensual plan of reorganization."[19] Other experts have acknowledged this charge as the trustee's primary pre-confirmation task.[20] And this mandate has indeed been observed in the motives of Subchapter V trustees themselves. One Subchapter V trustee, with years of experience acting as a trustee in other standard Chapter 11 cases, asserted that his role as a trustee in pre-Subchapter V Chapter 11 cases was mainly to represent creditors' interests.[21] However, his role in Subchapter V is different. He explained,

"[I]n a SubV, …the SubV Trustee is the bankruptcy liaison—working with the creditors towards a consensual plan, making sure that the reports are filed by the debtor, or working with the debtor's counsel, making sure that happens. But, really, it's a hybrid position, where you not only need to have the creditors' interests at heart but you're almost walking the debtor through the bankruptcy aspects of the case—so a lot more education, and 'here's why you do things'…provided to the debtor and, in some cases, debtor's counsel as well, but primarily to debtors. It's a little bit different. It's a lot more debtor-friendly than a normal trustee position would be."[22]

Another Subchapter V trustee noted,

"<u>What I see most important for me is that my goal is to get a consensual plan of reorganization confirmed</u>, which means going out to all the [debtors] and making sure that they are complying with Subchapter V provisions, and assuming that's the case, then going out to the creditors and getting their thoughts about whether they agree with the plan or they have some problems with it, and trying to negotiate a deal from there….The policing stuff—'Did you file this report on time?' Or, 'How are you spending money?'"[23]

Subchapter V trustees aren't the only parties who are aware of their shifted mandate. Most debtors and creditors are observing the effects of this new duty first-hand, describing a notable shift between their traditional Chapter 11

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[19] Bradley, *supra* note 17, at 260-61. ("Subchapter V trustees' duties are not well-specified, but at a minimum trustees are *supposed* to help 'facilitate the development of a consensual plan of reorganization.'")
[20] White, *supra* note 14.
[21] Telephone Interview with TN (Dec. 28, 2020).
[22] *Id.*
[23] Telephone Interview with GJ (Dec. 29, 2020).

experiences and those in Subchapter V. In light of the Subchapter V trustee's explicit duty to "facilitate the development of a consensual plan of reorganization," many debtors believe the trustee's responsibilities extend beyond that of a neutral party. They must actively facilitate. One debtor's attorney explained,

"Subchapter V is supposed to create some kind of new dynamic with the trustee that wasn't there before. …The trustee is someone who understands what's going on in the case. If one party is being completely unreasonable, and you're talking about what's in the best interest of the estate and trying to accomplish something that's in the best interest of the estate, eventually the trustee needs to get out of the mediator role and take a side. The trustee can be called on to say if he supports the plan or not. The trustee can be called on to say if that the debtor should be removed from possession. The trustee can be called on to say if the case should be converted to Chapter 7 or should be dismissed. …I don't think the trustee should remain neutral because you do have situations where creditors are pushing too hard, or where debtors are being dishonest and taking advantage of the process."[24]

Two other debtor's attorneys agreed,

"[T]he bankruptcy administrator in our jurisdiction has kind of charged the Subchapter V trustees as a mediator to a degree—in part because the goal of Subchapter V is to get a consensual plan, to be quick and dirty, in and out, more efficient and more cost-effective than the regular Chapter 11. So in order to do that, <u>the trustees that are appointed are really trying to lean on the debtor, but also the creditor in trying to get forward a consensual plan.</u>"[25]

They were careful not to place too much responsibility on the Subchapter V trustee, though, asserting,

"The driving ship is still the debtor. We're the one that created the ship; we're driving the ship. Now we have to make sure the ship gets where it needs to go. <u>The trustee is just the assistant in all of it.</u> I still feel like it's the debtor's job to work towards a consensual plan."[26]

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[24] Telephone Interview with JF (Dec. 14, 2020).
[25] Telephone Interview with JW and DD (Dec. 11, 2020).
[26] *Id.*

These interviews suggest that all parties involved in the Subchapter V bankruptcy process are somewhat aware of the trustee's shifted role. Subchapter V trustees are integrating this new charge into their adjusted role as facilitators, and debtors' attorneys who are aware of these trustees' new responsibility actually expect the Subchapter V trustees to increase their involvement in these cases accordingly. Attorneys observed that this new involvement likely makes the Subchapter V process more streamlined and cost-efficient in attributable ways: gaining creditors' approval and lowering burdensome administrative fees.

1. Subchapter V trustees help gain creditors' approval

A goal of Chapter 11, Subchapter V is to confirm a consensual plan of reorganization.[27] For a consensual plan of reorganization, creditors must approve of a debtor's proposed plan of reorganization, but this is one of the most time-consuming, expense-producing aspects of a Chapter 11 case—convincing creditors to approve of a proposed plan of reorganization.[28] Small businesses in a normal Chapter 11 case rarely receive the approval they need before costs become overbearing and, as a result, rarely exit bankruptcy as a viable entity.[29] With the Subchapter V trustee as one of the extra tools in a debtor's toolbox, however, debtors are likely to have a greater chance of successfully reorganizing and continuing business operations.[30] Interviews support this theory.

In one Subchapter V case, after a plan of reorganization was successfully confirmed, the debtor's attorney opined,

"The SubV Trustee was very helpful in getting the creditor to agree to a cash collateral order. And I think the fact that a third party came in and said, 'Hey, look, I'm looking at this objectively,' and that this third party is the SubV trustee that everyone

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[27] SBRA Legal Manual 1 (Jan. 2020), https://www.justice.gov/ust/file/sbra_legal_manual.pdf/download. ("The legislative purpose of the SBRA was to provide a fast track for small businesses to confirm a consensual plan with the assistance of a private trustee."
[28] Bris, Welch & Zhu, *supra* note 2.
[29] Edward R. Morrison, *Bankruptcy Decision Making: An Empirical Study of Continuation Bias in Small-Business Bankruptcies*, 50 J. of L. & Econ. 381 (2007).
[30] White, *supra* note 14. ("Finally, although there is not yet sufficient data to determine conclusively whether the law has affected fees, both anecdotally and from our own observations, the subchapter V trustees are resolving disputes prior to litigation, which should further reduce or eliminate unnecessary costs.")

respects,…'looking at this from a non-interested perspective, there should be an agreement here.'"[31]

In another case, the debtor's attorneys shared,

"[H]e was very helpful to the estate from the perspective of doing financial projections and helping creditors understand the evaluation behind the debtor's assets, debt, etc., but also the projection. It kind of immediately gave some credibility to the creditors."[32]

These debtors' attorneys' answers support the notion that Subchapter V trustees are resolving disputes between debtors and creditors. With their experience and expertise, trustees are able to mediate the incentive disparity between the two parties, enabling them to come to a consensus more quickly.

Concerns still remain regarding partiality, however. Some researchers believe that fortunately for the debtor but unfortunately for the creditor, Subchapter V trustees are more likely to be debtor friendly. The trustees' statutory duty incentivizes them to focus on debtor interests and to appease the U.S. Trustee and the court. Compensation structure—by billable hours per the current non-standing trustee structure—may incentivize the trustees to hear creditor interests and investigate any potential wrongdoing by the debtors, but gaining the favor of the U.S. Trustee by keeping the plan confirmation process streamlined and smooth (even deceptively so) is more likely to incentivize trustees to ignore objections by creditors.[33] This will be explored further in Section III(A) of this Article.

While the debtors' attorneys may have some bias in their explanation of the Subchapter V trustee's actions, it is a fact that Subchapter V trustees have been involved in both debtor and creditor discussions. By negotiating with and explaining the proposed plan of reorganization to the creditors, Subchapter V trustees have already successfully facilitated the confirmation of several consensual (note: but not necessarily unanimous) plans of reorganization, complying with their statutory mandate.

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31 Telephone Interview with LP (Dec. 11, 2020).
32 Telephone Interview with JW and DD (Dec. 11, 2020).
33 Bradley, *supra* note 17, at 269.

2. The appointment of a Subchapter V trustee lowers administrative fees

Administrative fees associated with bankruptcy duration, U.S. Trustees, and hired professionals are lowered by the appointment of a Subchapter V trustee.

By helping to facilitate confirmation of a consensual plan of reorganization and mediating between the debtor and creditors, the Subchapter V trustee expedites the bankruptcy process, thereby keeping direct and indirect costs low—another objective of the SBRA. Administrative expenses are defined as "obligations incurred after the filing of the case and not paid in the ordinary course of business…if the expenses were actual and necessary to preserve the estate."[34] Administrative expenses may include the fees and costs incurred by professionals who are employed in the case, and the trustee's fees and expenses.[35] One Subchapter V trustee remarked, *"I liked the idea of getting a debtor though the process and helping them keep the costs down trying to expedite the process."*[36]

A majority of participating debtors' attorneys observed that their Subchapter V cases usually reached a conclusion within a fraction of the time that their Chapter 11 cases typically did. They attributed this time reduction in part to the Subchapter V trustees' active collaboration with debtors and creditors to reach a consensual plan—discussed in the previous section.

In addition to the Subchapter V trustee's role making the bankruptcy process speedier and less costly, the presence of a Subchapter V trustee removing the need for a standing U.S. Trustee also reduces bankruptcy expenses for debtors. The debtor in Subchapter V is no longer required to pay U.S. Trustee's fees.[37] Although this only slightly affects bankruptcy costs for the debtor,[38] this benefit

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[34] *See generally* 11 U.S.C. § 503

[35] Handbook for Small Business Chapter 11 Subchapter V Trustees (Feb. 2020), https://www.justice.gov/ust/file/subchapterv_trustee_handbook.pdf/download [hereinafter Trustee Handbook].

[36] Telephone Interview with JG (Jan. 12, 2021).

[37] 28 U.S.C. §1930(a)(6)(A) (2019)

[38] Bradley, *supra* note 17, at 268:

> One countervailing fact to weigh against the addition of subchapter V trustee fees is that U.S. Trustee fees will not be assessed. In larger-scale cases, these fees have become a problem for debtors, but their removal from subchapter V cases will rarely offer a material cost savings. For small business cases, the fees are manageable. In a case with quarterly disbursements of funds under $75,000, the fee as of 2020 is only $650—a sum that most hourly billers with sufficient

is significant enough to be recognized by debtors' attorneys. One debtor explained, *"You don't have [quarterly fees] in Subchapter V. To most of the debtors, that's not really critical. It's usually $975 to maybe $1400 a quarter, so it's not huge, but every little bit counts."*[39]

Most of the Subchapter V trustees selected by the U.S. Trustee have strong business acumen with occupations ranging from lawyers, CPAs, MBAs, restructuring consultants, and financial advisors.[40] Their diverse backgrounds uniquely enable these trustees to serve as their own experts in the course of negotiating a consensual plan. As such, Subchapter V trustees will likely not need to hire professionals, which in turn has reduced some costs to debtors and increased recoveries to creditors.[41]

A Subchapter V trustee discerned that this overall decrease in administrative costs, including U.S. Trustee's fees, not only removed a financial burden from the debtors but also increased the return to unsecured creditors.[42] This effect will be explored later in the Article.

B. Cramdown Provisions and No Absolute Priority Rule

Subchapter V is further equipped to streamline reorganization because the standard Chapter 11 absolute priority rule does not apply, and debtors can utilize statutory cramdown provisions to confirm a plan of reorganization.

The absolute priority rule in Chapter 11 requires the equity holders to contribute new value in order to keep their equity interest; that new value then goes to unsecured creditors.[43] Under non-Subchapter V, Chapter 11 conditions, the proposed plan of reorganization must receive the approval of a majority of creditors in each class in order to be confirmed.[44] This prolongs the negotiation

experience to serve as trustee would reach in the first morning of their appointment.

[39] Telephone Interview with JW and DD (Dec. 11, 2020).

[40] White, *supra* note 14.

[41] *Id*.

[42] Telephone Interview with TN (Dec. 28, 2020).

[43] Telephone Interview with JW and DD (Dec. 11, 2020).

[44] 11 U.S.C. 11 § 1129(a)(10).

process both before filing the proposed plan and after, greatly increasing bankruptcy expenses.[45]

One debtor's attorney with significant experience with Chapter 11 cases explained,

"If you were in a traditional Chapter 11, the two levers that creditors have that they use all the time are (1) some impaired class of creditors has to vote in favor of the plan, and (2) that equity can't get anything unless secured creditors are paid in full. Well, the case wouldn't be possible in a traditional Chapter 11….It really is like night and day. The biggest problems with Chapter 11 in my 40 years of experience is that it's a very slow process built on this premise of a negotiated solution with creditors. It's very slow, and it's very expensive. I used to tell people that I'd never seen a successful Chapter 11 that didn't end up paying $150 thousand or more in attorneys' fees, and that's no longer the case with SubV."[46]

In a typical Chapter 11, debtors often must negotiate unfair terms just to receive creditor approval, further eroding business value; otherwise, equity holders risk relinquishing their ownership stake in the business after reorganization. For a small business, that means the sole operator/business owner loses his or her stake in the company—essentially de-incentivizing the business owner from staying with the company if it emerges from reorganization.[47] This rule places the small business in danger because the company would then need to raise new equity somehow and find a new operator/owner in order to be a viable entity.[48]

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[45] Bradley, *supra* note 17, at 258. ("This requirement gives powerful creditors control over the confirmation. Here, too, a senior secured creditor with a large deficiency claim often wields veto power. These veto-holding creditors are thought to have outsized sway over the outcome of cases, often to the disadvantage of debtors and less powerful creditors.")

[46] Telephone Interview with MJ (Dec. 10, 2020).

[47] Blackmon, *supra* note 8, at 349:

> The absolute priority rule in Chapter 11 raises the issue that some small business owners may be unable to retain their ownership stake in the business after organization. A common feature of smaller businesses is a "unified ownership and management" structure that emphasizes an owner's personal stake in seeing the business thrive. Subchapter V features no absolute priority rule which essentially precludes certain creditors from receiving a distribution until higher priority creditors are paid in full.

[48] Telephone Interview with LP (Dec. 11, 2020).

In Subchapter V, debtors do not have to comply with the absolute priority rule. As two debtor's attorneys affirmed, *"That's an advantage to the debtor."*[49] The absence of the absolute priority rule should lead to an increase in successful small business reorganizations; owners can continue managing their businesses while enjoying the benefits of ownership.[50]

Subchapter V has also made available to debtors the cramdown provision—a method to get a plan of reorganization confirmed despite objections from creditors. Debtors are likely to have a significant advantage in Subchapter V because the court will confirm any plan of reorganization, regardless of objections from creditors,[51] if the debtor's plan meets a certain objective test: (1) the plan provides that all of the projected disposable income of the debtor to be received in the 3-year period, or such longer period not to exceed 5 years as the court may fix, beginning on the date that the first payment is due under the plan will be applied to make payments under the plan; or (2) the value of the property to be distributed under the plan in the 3-year period, or such longer period not to exceed 5 years as the court may fix, beginning on the date on which the first distribution is due under the plan is not less than the projected disposable income of the debtor.[52] This is an additional benefit to the small business debtor because it provides incentives for the owner to continue operating the business effectively.[53] Equity holders are able to retain additional profits above the plan's projected disposable income.

The cramdown provision can potentially markedly reduce the time that the small business spends in bankruptcy, translating to a reduction in administrative

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[49] Telephone Interview with JW and DD (Dec. 11, 2020).

[50] William L. Norton III & James B. Bailey, *The Pros and Cons of the Small Business Reorganization Act of 2019*, 36 EMORY BANKR. DEV. J. 383, 385 (2020).

[51] Bradley, *supra* note 17, at 273.

[52] 11 U.S.C. § 1191 (c)(2)(A) and (B)

[53] Bradley, supra note 17, at 275:

> The debtor's rational course of action is to project the plan period as a time when profits should be minimized in favor of putting the venture on sound footing. Thus, the entity will be in better shape when the plan is over, and the debtor's owners will once again be able to attain a return on their investment. In fact, the owners can begin to benefit from their investment during the plan period; if the projected disposable income is lower than the actual profits, there is no requirement to modify the plan to share the additional money with creditors.

costs.[54] And according to most study participants, this potential effect has become a realized benefit. As explained by one Subchapter V trustee,

"Now the company and its bankruptcy lawyer don't have to sit at the conference table trying to figure out all these different ways to try to get a plan confirmed with this veto problem from general unsecured creditors. If the general unsecured creditors won't vote to accept it, your next option is to move into something called the absolute priority rule and the new value corollary. …What Subchapter V did was say, 'No more absolute priority rule….As long as you pay projected net disposable income to unsecured creditors over the next three years, that will be enough, and that's all you need to do.'…When you have an angry creditor, it's shifted the battle away from issues about plan building and class gerrymandering, and it's put it on other issues."[55]

One debtor's attorney attributed the reduction in expenses and quick plan confirmation directly to the cramdown provision and the lack of the absolute priority rule: *"From a cramdown perspective…, it's easier; it's more streamlined, and it's less expensive because the absolute priority rule doesn't exist."*[56]

Another debtor's attorney believes that Subchapter V very effectively implements the policy decision, saying,

"We'll offer to work [priority claims] off over the next three years and pay nobody else anything, and under SubV that's perfectly permissible. And even if every general unsecured creditor—essentially, the landlord, PPP—goes against us, the court is going to approve it. So under SubV, we will merge with what's going to be PPP loans—say half a million bucks—of working capital, which ought to be able to help us weather the storms ahead. And while we project losing money for the next 3 years, it becomes smaller and smaller. By probably the fourth year, the business will be viable. We will have honored the gift certificate liability, and we'll continue to employee eighteen-ish people. <u>So if you</u>

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[54] This reduction can come from two sources: (1) preventing creditors from prolonging the negotiation process by implementing the cramdown provision; or (2) leveraging the availability of the cramdown provision to get creditors to agree to a consensual plan. Either way, small business debtors could potentially shorten bankruptcy time, saving administrative expenses that would otherwise further erode the estate. Debtors do have an incentive to choose the latter option, though, since actually implementing the cramdown provision would cause debtors to expend extra administrative fees on the trustee throughout the life of the plan—since trustees cannot be discharged before all disbursements are made on a non-consensual plan. *See* 11 U.S.C. § 1194(b) (2019).

[55] Telephone Interview with JF (Dec. 14, 2020).

[56] Telephone Interview with PT (Dec. 15, 2020).

look at those core bankruptcy values—of keeping the business alive and keeping employees paid and making some payments to creditors, all of those values are satisfied. …This case will finish in 4 months from the date of filing—probably half what a fast Chapter 11 looks like, and my fees will come in the range of $60 thousand, which again is about half what a usual Chapter 11 looks like."[57]

For even a Subchapter V case that was converted, the two debtor's attorneys confirmed the usefulness of the cramdown provision: *"Just having a much easier cramdown procedure and knowing that there's a statutory definition of fair and equitable that we can at least understand, that's certainly helpful for us, especially in this small case."*[58]

C. Filing Deadlines

Since debtors must file a plan within 90 days of initiating a Subchapter V case or run the risk of having their case dismissed, they are highly incentivized to quickly formulate a plan of reorganization to propose to creditors.[59] This naturally leads to more rapid movement towards plan confirmation.

Some scholars have warned that this new accelerated confirmation schedule may be detrimental for a debtor.[60] However, most debtor's attorneys in this study see this 90-day deadline as a characteristic that is conducive to a more streamlined, cost-reducing process. As two debtor's attorneys noticed, *"It's been quicker getting the plan on file, and I've had some informal objections, but it's a lot less complicated than the standard. …Everything in the legal world is deadline-driven, so the fact that there is a 90-day deadline to get the plan on file is the first thing."*[61]

Another debtor's attorney noted that the expectation of shorter duration was significant enough to charge a lower retainer for Subchapter V cases:

"[I]n an ordinary Chapter 11 case, I probably would have quoted a higher retainer, and I probably would have burned more of it through dancing with the Chapter 11 process,

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[57] Telephone Interview with MJ (Dec. 10, 2020).
[58] Telephone Interview with AB and JS (Dec. 14, 2020).
[59] Pursuant to 11 U.S.C. § 1189 (b), "The debtor shall file a plan not later than 90 days after the order for relief under this chapter, except that the court may extend the period if the need for the extension is attributable to circumstances for which the debtor should not justly be held accountable."
[60] Norton & Bailey, *supra* note 47, at 389-90.
[61] Telephone Interview with RG and CB (Dec. 14, 2020).

although we would have inevitably gotten to the same business outcome. And because it was a SubV, I could quote a retainer that was much lower than I would ordinarily quote and expect the case to move much more quickly than I'd expect a traditional Chapter 11. …Every day you're in bankruptcy costs money, so the longer the Chapter 11, the more expensive the process."[62]

Because a shorter timeline directly correlates with fewer administrative expenses, the same attorney observed that debtors were more optimistic about their prospects in Subchapter V, *"Basically, when you say, 'you're going to have to pay attorneys and accountants and everybody else in the whole process for a year before you get this over with,' that is a weight on any business. Whereas if you say, 'you'll be in and out in 60 or 90 days, or you'll fail, but it'll all happen within 60 to 90 days,' that is a much smaller burden."*[63]

These filing deadlines are not without downsides, though. Although this deadline urges the debtors to move more quickly, this may pose some issues and introduce more risk if they don't tread carefully. One debtor's attorney opined,

"A lot of times, debtors are their own worst enemies. …While getting in and out is good because it keeps them out of their own way, the pressure is on, and you have to move a lot quicker in a SubV. With that, sometimes things need to shake out either an investment or sale or something that's contingent, and when you don't have that contingency come to fruition, you are just hanging out there a little bit more, which maybe makes the debtor a little more vulnerable in a SubV because you have to have a pretty quick turnaround process."[64]

In short, there is great benefit in the 90-day deadline but also some risk. If a debtor's proposed plan of reorganization contains contingent provisions, this introduces a modem of complexity into the bankruptcy process. Especially because of the rapid movement expected of a Subchapter V case, even a slight delay in one provision demands immediate adjustment from the debtor. The debtor must be prepared for these risks.

It remains to be seen whether shortened filing deadlines are a benefit to debtors or a detriment. Overall qualitative evidence suggests initial positive effects from the change, but small businesses filing in Subchapter V in the introductory phase

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[62] Telephone Interview with MJ (Dec. 10, 2020).
[63] *Id.*
[64] Telephone Interview with JW and DD (Dec. 11, 2020).

of the new bankruptcy process could be self-selecting. In this case, these small businesses would likely already be organized and prepared to file their proposed plans of reorganization. This success would not then be to the credit of the Subchapter V process itself. With time, we may see whether filing deadlines are beneficial or not—only by observing if the average small business is directly motivated by the 90-day filing deadline to move more quickly than it otherwise would and propose a plan of reorganization. But these observations are difficult and unlikely to be made, especially in the short-term.

D. No Creditors' Committee

Subchapter V does not require the formation of a creditors' committee, the absence of which contributes to streamlined proceedings. Under normal Chapter 11 proceedings, the U.S. trustee would ordinarily form a committee of unsecured creditors holding the seven largest unsecured claims again the debtor.[65] The committee has many duties, including consulting with the debtor-in-possession on case administration, investigating the debtor's conduct and operation of the business, and participating in formulating a plan.[66] Negotiating with the creditors' committee can be an incredibly time-consuming and expensive process.[67]

In standard Chapter 11, a creditors' committee can be an important safeguard to the proper management of the business by the debtor-in-possession.[68] Under Subchapter V, this duty to oversee debtor affairs mainly falls to the Subchapter V trustee. The SBRA amended section 1102(a)(3) to provide that "[u]nless the court for cause orders otherwise, a committee of creditors may not be appointed in a small business case or a case under subchapter V of this chapter."[69]

Without a creditors' committee, and especially with a Subchapter V trustee who—incentive-wise—is likely to take a more neutral or sometimes more

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[65] 11 U.S.C. § 102
[66] 11 U.S.C. § 1103
[67] Bris, Welch & Zhu, *supra* note 2.
[68] Chapter 11 – Bankruptcy Basics, https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-11-bankruptcy-basics - :~:text=Creditors' committees can play a,unsecured claims against the debtor. ("Creditors' committees can play a major role in chapter 11 cases. The committee is appointed by the U.S. trustee and ordinarily consists of unsecured creditors who hold the seven largest unsecured claims against the debtor.")
[69] SBRA deleted the existence or level of activity of a creditors' committee as a criterion for status as a "small business debtor," including a subchapter V debtor. 11 U.S.C. § 101(51D).

favorable stance towards debtor interests, debtors will presumably see their plans of reorganization negotiated more favorably. Debtors will also see cost savings from the absence of a creditors' committee.

One Subchapter V trustee explained the benefit to the debtor that this change provides: *"The default position is that there is no committee, which can be a huge cost savings to Chapter 11 because once you form a committee, then they hire counsel. Then, they may hire a financial advisor. Fees go up; with a trustee, you just have one person working on his own, not having to consult with the committee, so it's a lot more efficient and more cost effective."*[70]

Most debtors agree that eliminating the requirement for a committee of creditors streamlines costs and trims away some statute-driven complexity. Two debtor's attorneys shared, *"There's not a creditors' committee, so there are fewer potential constituencies I have to deal with. …In SubV, you don't have a committee, so you're streamlining your costs, and if you have a SubV trustee who has assumed the role of the committee, then you're losing the purpose of it."*[71]

The implied expectation from participants' responses is that although Subchapter V trustees should be conscious of the interests of these unsecured creditors, they also should be relatively more debtor-friendly than the original Chapter 11 creditors' committees were. Subchapter V trustees must find a balance between appeasing creditors and keeping the burden of bankruptcy light for debtors—acting as a built-in mediator for parties with often opposing interests.[72] Otherwise, they run the risk of reversing the intended effects of otherwise helpful changes to the debtor.

Eliminating the creditors' committee requirement seems to have decreased complexity and trimmed usual personnel from the reorganization process, but it's unclear if cost benefits are a direct function of this feature. Whether the absence of a creditors' committee is helpful or not likely hinges on the ability of the Subchapter V trustee to consolidate all duties and incentives and act as a proper mediator between creditors' interests (to maximize recovery rates) and debtors' interests (to emerge from bankruptcy as a viable entity). The overall effectiveness of Subchapter V depends on how well the two interests are

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[70] Telephone Interview with JF (Dec. 14, 2020).
[71] Telephone Interview with RG and CB (Dec. 14, 2020).
[72] *See* Bradley, *supra* note 17, at 267. ("The two most obvious potential roles are trustee as mediator and trustee as financial analyst.")

balanced to produce a consensual plan. Without a creditors' committee, creditors run the risk of lacking representation, and as such, adversarial proceedings may be more likely to occur after the confirmation of a plan.[73] This is discussed further in a later section.

E. No Disclosure Statements

One of the stated legislative intents of SBRA is to reduce "unnecessary procedural burdens and costs" by eliminating the creditors' committee and disclosure statement requirements.[74] Unless a court orders otherwise, 11 U.S.C. § 1125—which enumerates the required contents of Chapter 11 disclosure statements to be filed with a proposed plan—does not apply.[75] With the proposed plan, the debtor still must include core information that creditors and other interested parties need to evaluate the proposed plan, but the requirements are much less comprehensive and burdensome than the disclosure statement mandated by normal Chapter 11.[76]

In their Subchapter V case, two debtor's attorneys remarked, *"A lack of disclosure statements…is certainly a help for us."*[77] A Subchapter V trustee also asserted that this was a realized benefit to the debtor because the proposed plan could be sent to creditors without waiting to have the disclosure statement approved in a court hearing.[78] This reduces even more of the "unnecessary procedural burdens" that lawmakers seek to eliminate through the SBRA.

It is important to note, however, that although these reduced disclosure requirements for debtors are likely to be a benefit, this adjustment may also have the effect of keeping necessary financial information from creditors. Again, this potentially negative effect must be balanced out by the Subchapter V trustee's role in negotiation.

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[73] This happened in one such case in this study.
[74] SBRA Legal Manual, *supra* note 27, at 2.
[75] 11 U.S.C. § 1181(b)
[76] Bradley, *supra* note 17, at 260. ("But the burdens of the standard small business provisions are widely considered too onerous and are avoided by many debtors despite their being nominally mandatory.")
[77] Telephone Interview with AB and JS (Dec. 14, 2020).
[78]*See* Telephone Interview with JF (Dec. 14, 2020) ("In normal Chapter 11, you need to have a disclosure statement approved in a court process hearing before you're allowed to send out your plan to creditors and ask them to vote on it, but that doesn't exist in Subchapter V, unless the court orders that a disclosure statement is necessary.").

III. OTHER CONSIDERATIONS

Stepping away from our discussion of the intrinsic characteristics of Subchapter V and their effects on debtors, this section discusses the effects of this new process on creditors and the possibility of intrinsic debtor characteristics affecting the bankruptcy outcome. I expound the differing perspectives of scholars and practitioner accounts regarding creditors, and I speak to what debtors might avoid and might seek to practice in their courses of business and bankruptcy in order to achieve favorable outcomes.

A. Effects on Creditors

1. Possibility of Unfairness to Creditors

With all the changes made to the reorganization process by the SBRA, the Subchapter V process and resulting outcomes could potentially be unfavorable for some creditors—as mentioned in several previous sections of this thesis.[79] Powerful secured creditors have enough leverage to protect their own interests, but unsecured creditors have both fewer defense tools and less incentive to use those defense tools.[80]

For example, the Subchapter V trustee's position may have taken on some duties that previously belonged to the creditors' committee, and the trustee may mediate in some instances, thereby advocating for some creditor's interests, but the trustee is not statutorily obligated to show concern for the interests of the creditors. Subchapter V trustees are appointed case by case, and consistently attaining quick and painless plan confirmations is likely to lead the U.S. Trustee to make further appointments of that Subchapter V trustee. Thus, if anything, the

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[79] Bradley, *supra* note 17, at 254-55:

> It may be unsecured creditors such as trade and tort creditors whose interests are most affected by subchapter V, yet who are least positioned to protect themselves against such effects. For many supporters of the Act, limiting the perceived overreaching of certain creditors—in particular, undersecured creditors with both significant secured claims and large unsecured deficiency claims—has been articulated as a goal of the Act. This Article suggests the Act likely will not accomplish that goal.

[80] *Id.* at 256. ("It predicts that powerful secured creditors will not lose much ground under subchapter V, but that general unsecured creditors are likely to see their interests damaged by subchapter V."

trustee may be incentivized to only cursorily investigate the objections of creditors in order to quickly push a plan of reorganization through to confirmation. For the same reason, the trustee may ignore debtor's actions that may not be entirely appropriate but also not extremely consequential.[81]

Moreover, unsecured creditors themselves are likely to have little incentive to invest in bankruptcy proceedings. Scholars have suggested that Subchapter V further erodes protections for these creditors whose expected recoveries fail to justify active participation.[82] The theory, though, that the SBRA negatively affects unsecured creditors' recovery rates is yet to be confirmed. Initial interviews indicate that the outcomes of Subchapter V are not particularly prejudicial towards unsecured creditors despite awareness that the process might have slight bias; this is discussed in the following section.

Acknowledging or at least implying some unfairness or unbalance for the creditors, two debtor's attorneys shared,*"SubV gives the debtor incentive to move a bit faster. And the rules require him to be faster too. It not only helps them to get in and out, but <u>a quick turnaround doesn't let the creditor get their feet under them and figure out what's going on in the case</u>."*[83]

Another debtor's attorney summarized, *"We went from a regime that said, 'Negotiate with your creditors because they can prevent you from exiting if you don't reach an agreement with them,' to a regime that says, 'If you pass these objective tests, then you get out whether or not your creditors like it.'"*[84]

Fortunately, creditors can still go through the courts if they feel the plan of reorganization was unreasonable. A debtor's attorney stated, *"If there's a creditor who wants an investigation, the court's going to let the investigation occur."*[85] In one case in this study, a plan of reorganization was confirmed but is now being

[81] *Id*. at 269.
[82] *Id.* at 254-55:

> Most unsecured creditors have little incentive to act energetically in bankruptcy proceedings. They are unlikely to be paid enough to make it worth the effort. Our bankruptcy law allocates much more power to debtors and to secured claimants. This Article suggests that the Act further erodes the position of most unsecured creditors. Their expected recoveries will remain too low to justify anything other than a relatively passive attitude toward the bankruptcy proceeding, and the Act lowers the protections for passive creditors.

[83] Telephone Interview with JW and DD (Dec. 11, 2020).
[84] Telephone Interview with MS (Dec. 10, 2020).
[85] *Id*.

challenged by a creditor. Methods of recourse are thus available to creditors and are a way to protect from any inequitable treatment by the process.

The Subchapter V trustee said,*"[The case] involved a fight with a creditor…, so they've appealed the confirmation order. And the district court actually entered an order staying confirmation order pending the appeal. …I worked hard to try to bring those two together. Ultimately, we didn't get there, but I think the plan to the outcome of the case was appropriate under Subchapter V of the Bankruptcy Code."*[86]

However, appealing the confirmation order still has the undesirable effect of stretching out the bankruptcy process. This is not only undesirable for debtors but also for creditors who seek some recovery from the small business.[87] If creditors' objections are not properly addressed within the original negotiation process, and there is a possibility that the court could determine that the plan of reorganization is unreasonable, the negotiation process from then on would further increase administrative fees and possibly erode business value past a viable degree. Subchapter V would then risk losing its designed purpose of offering the small business debtor a more streamlined and cost-effective restructuring process. Again, the Subchapter V trustee is key to ensuring that all parties are satisfied and concerns properly addressed in facilitating a consensual plan.

Some scholars have theorized that Subchapter V is likely to redistribute power from junior secured and unsecured creditors to the debtor.[88] This redistribution may possibly be minimized by the courts and by the trustees, but if creditors do not voice those objections, courts and trustees are likely to devote limited energy to such cases. This is one of several reasons why lawmakers should provide trustee guidelines that more deliberately address incentives to equally represent party interests—to be explored later.

2. Minimal Difference in Recovery Rates for Creditors

Because of the possibility of unfairness to the creditors, I was interested to see if the recovery rates of creditors had fallen in Subchapter V compared to Chapter

[86] Telephone Interview with GJ (Dec. 29, 2020).
[87] Bradley, *supra* note 17, at 255. ("First, creditors should resist delay in the plan process. Debtors often seek to extend cases and delay plan confirmation, but lengthy cases are generally costly and prejudicial to creditors' interests.")
[88] *Id.* at 284.

11. The SBRA is meant to be more friendly to small business debtors, and as such, many of the traditional creditor safeguards—for example, the committee of unsecured creditors—were eliminated. This naturally tips the balance more in favor of the debtor, so my concern was whether the Subchapter V process was *overly* assisting the debtor.

From my interviews with Subchapter V trustees, the general consensus is that thus far creditors' recovery rates have not suffered. The reasoning is not that the policies necessarily favor the creditors equally—although this is still a possibility—but that a portion of the administrative expenses saved by debtors are generally redistributed to creditors. This redistribution pads the creditors' recovery rates that otherwise might be eroded by the SBRA's debtor-friendly policies. This theory is supported by not only the interviewees of this study but also scholars studying Subchapter V.[89]

One Subchapter V trustee asserts,

"I would say there has been no difference in the recovery rates overall. What it allows the smaller debtors to do is to get through much more cheaply and much more quickly than ever before. But I don't know that the recovery rates to creditors have been impacted—I'm going to say—at all. And, of course, it depends on the case and that kind of thing, but what you're able to achieve in the case, in terms of recovery to creditors, may be slightly improved only from the standpoint that admin costs—admin expenses—are lower. In a true Chapter 11 case, you might see debtors' counsel's fees total 150 or 200 thousand [dollars]…here, I've seen 35 to 50 [thousand dollars]. But because they're smaller debtors, I'm going to argue those SubV cases would not have made it to a regular Chapter 11 simply because they didn't have a war chest big enough."[90]

He continues,

"It depends on the case, but of the 9 of which I've been involved in over the last 10 months or 11 months now, if there is a significant amount of unsecured credit holders, it will increase those to the unsecured. In the secured interests, most of the time there hasn't been enough of a cramdown—enough of a deleterious effect on the secured credit holders. So in this case, I guess you could say that 30 or 40 thousand-dollar decrease in trustee

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[89] White, *supra* note 14, at 2. ("As anticipated, subchapter V trustees generally have not needed to hire professionals, which has helped to reduce the cost to debtors and increase recoveries to creditors.")
[90] Telephone Interview with TN (Dec. 28, 2020).

fees—in the Office of the US Trustee fees—in [the case] made it back to the second and third secured credit holders, so it increased their return by the amount that would have gone to the admin claim to the US Trustee, but in this case, we had very little, very small unsecured creditors who—this didn't change them at all. They never would have gotten a penny in this case otherwise. <u>But in other cases I've worked on, …the decrease in administrative costs of the bankruptcy estate is how secured and, really, unsecured creditors get a bigger piece of the pie.</u> Again, the percentage overall has so far been minimal."[91]

In other words, the multi-pronged approach has had the overall effect of maintaining recovery rates for creditors while minimizing the time and costs spent by the small business debtor in bankruptcy.[92] If the SBRA had only eliminated the creditors' committee requirement or only introduced the new, more debtor-friendly Subchapter V trustee, the balances would be tipped heavily in favor of the debtor. With the decrease or elimination of some administrative fees—including attorneys' fees, U.S. Trustee's Office fees, etc.—the cash flow can be made available to compensate secured creditors.

B. Causes Intrinsic to the Debtor and Extrinsic to Subchapter V

1. What "went wrong" with converted Subchapter V cases?

Since the intent of a Subchapter V case is to confirm a consensual plan of reorganization, the reasons behind the three converted Subchapter V cases in the study's sample should be explored. The participants related to those cases in this study all referenced causes extrinsic to Subchapter V and more intrinsic to the small business itself—such as, the motive of the small business debtor, issues within the operations of the debtor entity, the number of creditors, and the history of litigation of the debtor.

In one case, the trustee explained, *"[The debtor] had two super over secured properties…In my personal opinion, that case should have never been filed as a*

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[91] *Id.*

[92] Bradley, *supra* note 17, at 277:

> Passing a consensual plan has three significant effects, all of which seem likely to motivate the debtor to seek creditors' acceptance of its plan: earlier termination of the trustee's appointment, earlier discharge, and the right to keep post-petition property free of the bankruptcy estate. Because debtors are likely to prize these incentives, there will be leverage here for creditors whose votes are necessary for plan confirmation.

reorg[anization]. It was filed simply to maximize the return to junior credit holders. …It was always going to go to pay off the creditors. …What the debtor's counsel's primary purpose was—and he achieved that—was to avoid paying the US Trustee's fees."[93]

The Subchapter V debtor in this case was using SBRA provisions to its advantage because in regular Chapter 11, the U.S. trustee would be entitled to a percentage of the final proceeds to the estate. The goal in this case was not necessarily to confirm a plan of reorganization. The outcome of this case indicates that small business debtors who have goals that do not align with Subchapter V may employ strategies inconsistent with and have outcomes that differ from statutorily defined success, but still constitute a success in the context of the debtor's goals.

In another case, the small business debtor itself had issues within the entity—management personnel, overwhelming debt relative to firm size, too many creditors, etc. One Subchapter V trustee explained,

"The case…probably should have never made it. …The court became concerned about the use of cash collateral. …<u>This debtor really did not have a good respect for debt in general, and he was very small</u>. It was a one-man operation, …so there wasn't a way to get him out of there and get someone else in there to run it. There wasn't a lot of options….This person was not remotely respectful of the rules of operating a business. He had no respect for credit. …He lost his counsel, ran out of money to pay them, ran out of money to pay me—I never got paid, and he wanted to borrow more money to fund the case. …<u>I have a feeling that if it would've been a slightly larger case, if there were some way to get him—that particular person—from running it, move him to the background, that entity might have made it</u>. …You want somebody who's going to emerge and be successful upon exit, and with him running it on his own without any help without following any financial advice…<u>Absolutely, there was a disproportionate amount of debt compared with the size of the operations of the company.</u> The SubV is different. … I really truly think it depends on the case, but they couldn't have done it without the Subchapter V provisions[;]…there was not going to be a consensual plan."[94]

The debtor's attorney spoke about the many creditors involved in this case and expounded the difficulty of shepherding the right number of creditors to confirm a consensual plan.

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[93] Telephone Interview with TN (Dec. 28, 2020).
[94] Telephone Interview with JG (Jan. 12, 2021).

"There's a litany of predators out there. We must be dealing with 20 to 25 attorneys. …A lot of times you get close, but there's a couple of things here and there, and then you need to push. …If you're really close, and you think there's a good chance you could resolve it, you're just going to continue."[95]

Another debtor's attorney shared similar sentiments: *"I'd like to think that when you have some smaller, less complicated, fewer creditor type cases, it absolutely will be more streamlined and quicker than the normal Chapter 11 cases."*[96]

In another case, the two debtor's attorneys described how previous litigation had already sullied the beginning of this Subchapter V case:

"It was an anomaly because the decision to file was made at the 11th hour, 59 minutes, 59 seconds. …Our clients were not very forthcoming or open on how to deal with their lawyers, so it was a mess, and it was the outgrowth of very bitter litigation that had begun in the state courts and was trending down fast for our client. If we had stripped away all that litigation and had had a Chief Financial Officer and Chief Executive Officer who had different personalities, it may have been successful, but that's not what we had. …Subchapter V is cost effective—probably—if you don't have a lot of litigation."[97]

Filing for bankruptcy soon after litigation invites complexity and conflict into already delicate proceedings. With the introduction of creditors who are already incensed by previous litigation, the Subchapter V process can be burdensome for the debtor—regardless of its debtor-friendly provisions. Negotiations can be stalled by ineffective mediation, and the debtor can be eaten up by the accumulation of administrative expenses that come with prolonged bankruptcy. This case failed to confirm a consensual plan of reorganization because of internal and external mismanagement.

In summary, these small businesses would probably not have been viable entities upon exit—at little or no fault to the inherent characteristics of the Subchapter V process. If they want the flexibility of the Subchapter V proceedings to work in their favor, small business should avoid poor management operations, disproportional debt, oversaturation of creditors, and filing after litigation.

[95] Telephone Interview with JW and DD (Dec. 11, 2020).
[96] Telephone Interview with PT (Dec. 15, 2020).
[97] Telephone Interview with AB and JS (Dec. 14, 2020).

2. *What additional factors extrinsic to the Subchapter V process facilitated a confirmed plan of reorganization?*

Some characteristics of small business debtors are correlated with great success in confirming a consensual plan of reorganization. As one Subchapter V trustee observed, *"The biggest problem with getting out of Chapter 11 for businesses is <u>finding a viable business that has an exit strategy</u> in the first place."*[98]

Debtors' attorneys say their debtors have a greater chance of successfully exiting the reorganization process by exhibiting a seemingly simple characteristic. Two shared,

"It's the same in any type of case. If you have good business administrators, the chances of success are so much higher. <u>Even if the business itself is rocky, just having timely, accurate information, being able to file the things in court that have to be filed, and having at least intelligent and intelligible answers when asked questions by the United States Trustee or the judge, that's the key in any type of business reorganization</u>."[99]

If small business debtors believe they can be viable after restructuring, they should formulate an exit strategy. They should have proper accounting and accurate, on-hand information. These are ways the debtors themselves can be proactive and help their attorneys and the Subchapter V trustee advocate for their interests. Otherwise, they face the possibility of fighting an already uphill battle with no preparation nor useful tools.

IV. CONCERNS ABOUT THE SUBCHAPTER V PROCESS

A. High Variability Stemming from the Subchapter V Trustee

The Subchapter V trustee can be extremely helpful, as previously discussed. However, depending on the Subchapter V trustee appointed to a certain case, there may be high variability of outcomes. This likely stems from a lack of uniformity in two characteristics of the process: (1) role perception and guidelines, and (2) compensation structure.

[98] Telephone Interview with JF (Dec. 14, 2020).
[99] Telephone Interview with AB and JS (Dec. 14, 2020).

1. Lack of Uniformity in Role Perception and Guidelines

From previous discussion in this Article, it is clear that the Subchapter V trustee plays a pivotal role in the bankruptcy process. However, although the Bankruptcy Code is relatively obvious in expecting the Subchapter V trustee to act as a facilitator for a consensual plan of reorganization, the law is decidedly less clear on how that expectation should be manifested.[100] Some guidelines are in place pursuant to the SBRA legal manual;[101] however, most participants of this study indicate varying accounts of trustee effectiveness. By their recounting, the lack of uniform guidelines for Subchapter V can have, and in some cases has had, deleterious effects. A role that should have great potential to streamline plan confirmation could likely have equal potential to distract from plan confirmation, depending on which Subchapter V trustee is appointed.[102] This high variability is demonstrated in the experiences of this study's interview subjects.

In one Subchapter V case, the trustee did not approve of the form of the proposed plan of reorganization, even though another trustee in a different Subchapter V case but in the same district had approved of the same exact form. The debtors' attorneys commented,

"We have two [Subchapter V trustees] here in Delaware, and they operate in completely different ways. [O]ne is definitely more of a facilitator and not like an active party in the actual case. …In that conference call, he commented that we should be able to work through [the issue], but he hasn't been trying to take control of the case, trying to dictate what happens or anything like that. …Our other Subchapter V trustee in our other case is inserting herself way deep into this case—objecting to my funding among others—way beyond what you would think. And she says it under the premise of fiduciary responsibility. Instead of facilitating a deal, she's been more beating us around. Because there is no real precedent, she's taking this position—maybe a more aggressive one—that

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[100] Bradley, *supra* note 17, at 267. ("No one knows how trustees will imagine or inhabit their role, and there seem to be different potential conceptions of the trustee.")

[101] SBRA Legal Manual, *supra* note 27, at 3.

[102] *Id.*

> The least predictable aspect of subchapter V is the trustee. Even if debtors qualify for subchapter V, and even if it gives them greater leverage against creditors, debtors may hesitate because of the potential costs and risks associated with the trustee. Subchapter V offers benefits to debtors, from administrative streamlining to the redistributive effects from creditors to debtors that it may bring about. But for debtors, the decision of whether to elect likely will depend on whether the advantages this subchapter offers to debtors outweigh the uncertainties and costs added by the trustee.

*she has an **obligation** to be more assertive in this role, and almost takes the function of a committee, and it's ridiculous."*[103]

In another Subchapter V case, the trustee exceeded the debtors' attorneys' expectations of his trustee role. The debtors' attorneys described the situation:

"[T]he Subchapter V trustee was wanting to get into affairs of the debtor that we didn't believe were warranted. Because in Subchapter V, the debtor is a debtor-in-possession, which by definition means there is no trustee, the Subchapter V trustee's role should necessarily be limited. We had a trustee who thought he was more like a Chapter 11 trustee under section 1104 than a Subchapter V trustee under 1181. He wanted to be on a lot of phone calls; he wanted us to run through our strategy with him."[104]

In essence, the only consensus is that there is no consensus with how Subchapter V trustees should carry out their duty. This introduces a litany of problems. If a debtor could be viable upon exit, the Subchapter V process could either aid that process or cripple the business—depending on a risky trustee lottery.[105] Furthermore, debtors' attorneys could have more difficulty estimating a bankruptcy exit timeline and related costs for a small business debtor. Perhaps most importantly, creditors and debtors alike will experience challenges in procuring a reliable strategy involving the Subchapter V trustee and learning how to work with the trustee in the Subchapter V process. Further guidelines must be introduced, or at least courts should be clear in their decisions on how a trustee should perform their duties.

2. Lack of Uniformity in Compensation Structure

Current guidelines are also unclear about the compensation structure for Subchapter V trustees. The statutory basis for compensation of Subchapter V trustees is 11 U.S.C. § 330 for case-by-case trustees and 28 U.S.C. § 586(e) for standing trustees. Because there are no standing trustees in Subchapter V, and Subchapter V trustees are appointed only on a case-by-case basis, the only statute in use that allows for compensation of Subchapter V trustees is 11 U.S.C. § 330. All Subchapter V trustees, then, claim their fees through § 330(a)(1)(A), which allows the court to award the trustee "reasonable compensation for actual, necessary services rendered by the trustee."

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[103] Telephone Interview with RG and CB (Dec. 14, 2020).
[104] Telephone Interview with AB and JS (Dec. 14, 2020).
[105] Bradley, *supra* note 17, at 267.

Pursuant to § 330 (a)(3), the court determines the reasonableness of such claimed compensation using four factors: (1) the time spent on such services; (2) the rates charged for such services; (3) whether the services were necessary to the administration of, or beneficial at the time at which the service was rendered toward the completion of, a case under this title; and (4) whether the services were performed within a reasonable amount of time commensurate with the complexity, importance, and nature of the problem, issue, or task addressed.

Especially because limited precedent exists on what the court deems "reasonable," Subchapter V trustees now essentially choose how they prefer to be compensated, and the debtor—though not having chosen the assigned trustee—must bear the costs. As two debtor's attorneys expressed, *"We're still trying to figure out how trustees get compensated."*[106]

Another debtor's attorney reported,

"There's no case law, and we're inventing it as we go and having to borrow from Chapter 12. In Nebraska, they appointed two Subchapter V trustees, and none of them are standing trustees. The trustees get paid depending on if there is a standing trustee, or if they're not standing. I don't believe any state has a standing Subchapter V trustee, so the non-standing, which means they're appointed on a case-by-case basis, will get paid however they ask, and there's no clarity whatsoever. It's basically an administrative expense against the estate that has to be paid. I have two more complex cases and two different Subchapter V trustees. Both of them are lawyers. Both of them are charging an hourly rate. One is in a smaller town, which is the capital of the state. He's charging $250 an hour, but he's also the standing Chapter 12 trustee; he understands how this is supposed to work—not terribly involved until he has to be. The other guy's charging $385 an hour and is treating it like a new client for him where he gets to force us into these unnecessary mediation meetings from time to time, and he's already racked up $15,000 in fees in five months. He's charging more money than me; he's basically acting as another attorney in the case. It's a huge pain. It's difficult for me as an attorney who advises clients, 'Hey, I don't know which trustee we're going to get. There's a wild swing in cost. One of them is going to be a lot more active; one of them is not.' That's been the most frustrating part so far. …<u>If they got to fix anything, they really need to explain compensation structure for these Subchapter V trustees</u>. …I think that has to be a legislative fix."[107]

[106] Telephone Interview with JW and DD (Dec. 11, 2020).
[107] Telephone Interview with PT (Dec. 15, 2020).

In their Subchapter V cases, most debtors' attorneys I interviewed are observing inconsistent fee applications from their trustees, not only in rates charged but also in time spent for trustee services. A private trustee assigned to a Subchapter V case could translate to a heavier burden on the debtor in administrative expenses—contrary to stated legislative intent. And by their own definition, these trustees may not even believe they are exacting a heavy burden. But no matter the intent of Subchapter V trustees, without further instruction or court precedent regarding "reasonable" Subchapter V trustee compensation, trustees may continue experiencing challenges in determining whether their planned work and rates are "excessive" or "reasonable."

3. Resulting High Variability of Subchapter V Trustee-Related Costs

Congress' stated intent is for Subchapter V cases to not be burdened with excessive administrative fees.[108] A large part of these administrative fees stems from the Subchapter V trustee, who charges based on (1) compensation structure and (2) level of involvement—i.e. billable hours. However, the trustees' compensation structure is highly variable, and limited guidelines exist to outline uniform trustee fees or even provide a useful measure for "excessive[ness]." Since even the trustee's level of involvement is variable, costs stemming from certain iterations of a trustee's role can be significant as well.[109]

Depending on which trustee is assigned, a Subchapter V case may see a wide range of fee charges and/or time spent in bankruptcy, which also translates to increased administrative expenses. Two debtor's attorneys expressed their frustration with the lack of uniform guidelines for trustees regarding actual application of the mandate, citing the excessive actions of one Subchapter V trustee and their direct effect on increasing expenses for the debtor: *"And our point was, that's what we as lawyers do, and why are we layering on more administrative fees? What we think he should do is help us formulate the plan and help us sell it to the various parties so that we can go under 1129A and get a consensual plan filed."*[110]

These attorneys saw the Subchapter V trustee's actions as unnecessary because they were already being performed; the trustee's actions—no matter how well-

[108] SBRA Legal Manual, *supra* note 27.
[109] Bradley, *supra* note 17, at 268. ("Whatever role they play, the costs of a trustee could be significant.")
[110] Telephone Interview with AB and JS (Dec. 14, 2020).

intentioned—were repetitive and, in the end, drove up administrative fees to be paid by the debtor. It is important to recognize here, however, that this is the perspective of the debtor's attorneys and potential for bias is high. The Subchapter V trustee could very well have been trying to fulfill the legislative mandate and doing so reasonably, as a court may later determine. The clear problem here, though, is that the parties are not reaching a consensus on expectations of both trustee actions and compensation. This decreases the ability of the trustee to "facilitate the confirmation of a consensual plan of reorganization" because this may limit the ability and willingness of the trustee and the debtor's attorney to work together amenably.

Assuming these debtors' attorneys are correct about the trustee's *over*-involvement, situations like these can be detrimental to the small business debtor. Firms with less than $7.5 million of debt—much less $2.7 million of debt—are often small margin cases, which could be overwhelmed by trustee fees. Costs could accumulate quickly with a trustee who chooses to play a more substantial role. And with the high variability of trustee's perceptions of their role, debtors may be hesitant to elect for Subchapter V, given how pivotal the Subchapter V trustee can be to the outcome of a case.[111]

Even if a Subchapter V trustee is not *overly* involved, the costs associated can still be significant. A Subchapter V trustee is statutorily obligated to charge fees for only "services [that] were performed within a reasonable amount of time commensurate with the complexity, importance, and nature of the problem, issue, or task addressed."[112] Unfortunately, this can still be insufficient to prevent unnecessary expenses. One debtor's attorney expounded an overall assessment of her Subchapter V cases:

"In cases where you really don't need them, you're still paying for them. In all fairness to the SubV trustee, they don't know if they'll be needed or not, so as soon as they get

[111] Bradley, *supra* note 17, at 268:

> Small business cases are often small margin cases. Small margin cases could be overwhelmed by trustee fees. Much of the success or failure of subchapter V will depend on what trustees actually do. If they are largely passive intermediaries, costs could be low—although the value added could be even lower. But if the trustee plays a more substantial role mediating between debtor and creditors, or if the trustee engages in serious financial analysis concerning, for instance, the debtor's financial projections, costs could rise very quickly. The very fact that this is so unclear is likely to disturb debtors facing the election decision.

[112] 11 U.S.C. § 330 (a)(3)(D)

appointed, they have to review all the pleadings; they have to attend the IDI; they have to attend the 341; they have to attend the status conference; they have to attend every hearing, so they know what's going on. But they may, frankly, never be needed. And then the debtor has to pay them thousands of dollars….In a normal Chapter 11 case, there's a US trustee, but you don't pay them by the hour….One of the biggest expenses in a SubV case could be the SubV Trustee, and <u>in a case where they're not needed, the expenses can be large and unnecessary.</u>"[113]

Because Subchapter V trustees must act as a mediator or facilitator, they need to be updated and informed on the case's progress—a responsibility that mandates a threshold level of involvement. If a case does not need a Subchapter V trustee to step in as a mediator or facilitator, though, this threshold may still be unnecessary for the small business debtor.

From this discussion, Subchapter V trustees appear to have high flexibility in determining the necessity of their involvement. Although this can be helpful, lawmakers should realize that such flexibility likely has a trade-off: Subchapter V trustees may make the wrong call. Debtors and creditors may have other paths of recourse that will be discussed later in this Article, but these options still take time and money. Increased guidance from either the Office of the U.S. Trustee or lawmakers themselves should help formulate an improved and more structured strategy for Subchapter V trustees.

B. Subchapter V Trustees' Mistaken Treatment of Small Businesses

Aside from individual trustees' variability, the overall trustee perspective may be harming small businesses in Subchapter V. Two debtor's attorneys voiced their concerns that trustees may still be treating small businesses like large firms:

"I don't think that there's a recognition among the US Trustee's office and/or the Subchapter V trustees, in some sense, that it's a small business trying to operate, make something happen with this business, keep its head above water, and do this process. They are being treated like big companies, and they just can't handle the things that they're being asked to do in the process. …I get the sense that they're being treated like the same kind of thing, and it's hampering the ability of these people to actually run their business while they're in Chapter 11."[114]

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[113] Telephone Interview with LP (Dec. 11, 2020).
[114] Telephone Interview with RG and CB (Dec. 14, 2020).

It is again important to recognize that this perspective from two debtor's attorneys may be biased, as debtors' attorneys are incentivized to advocate for their client and seek the most favorable bankruptcy conditions. However, since the very purpose of Subchapter V is to streamline the process for small businesses, lawmakers should consider what additional direction might be given to Subchapter V trustees in order to realize that vision. This certainly may introduce a moral hazard problem if the bankruptcy process is made overly simply for the small business debtor, but the abstract "line" between streamlined and excessively simplified seems not to have been reached yet, and Subchapter V trustees can certainly do more to shepherd the debtor through the process.

C. Unclear Cramdown Provisions

Although most debtors acknowledge the general effectiveness of eliminating the absolute priority rule and introducing the cramdown provision, some parties are still concerned. One creditor's attorney said, *"SubV really belongs in sort of a hybrid between Chapter 13 and some Chapter 11 procedures. Getting rid of the absolute priority rule is great for small businesses; <u>it doesn't do enough, though</u>. There're inherent problems with the individual. Individuals run small businesses basically as their alter egos. …They don't account for things very well generally."*[115]

Admittedly, this creditor's attorney's main concern is with characteristics intrinsic to the debtor—the general organization and viability of the small business. Assuming the debtor were a viable entity with optimistic exit prospects, eliminating the absolute priority rule could significantly streamline the bankruptcy process for the small business, as seen in the experiences of other aforementioned debtor's attorneys.

Others, though, were concerned with lack of court precedent on how exactly debtors should utilize the cramdown provision in their proposed plans. Pursuant to 11 U.S.C. § 1191 (c)(2)(A), the court may confirm a plan of reorganization that is "fair and equitable," even with objections from creditors. The statute defines a plan as "fair and equitable" if it provides that all of the debtor's disposable income be paid out to creditors in the following three- to five-year period.

Many of this study's participants expressed confusion regarding how disposable income is to be defined and calculated. One Subchapter V trustee expressed,

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[115] Telephone Interview with DS (Dec. 11, 2020).

"There's going to be arguments about how you calculate net disposable income. …If a creditor really wants to fight it, how much is it appropriate to pay insiders' salaries to the officers and directors? Is that market rate or not? Should it be market rate, or should they be taking a discount? What about insider debt? If there's secured debt that's owed to somebody's brother or another company that's owned by an insider, should that get too high? Is that a sign of bad faith if they're trying to take all the money out of income, leaving a small amount of net disposable income for general unsecured creditors?"[116]

Two debtor's attorneys shared,*"[I]t's a little bit confusing how to apply the cramdown provisions with respect to paying disposable income over a period of three to five years—as to how you determine if it's three or five and whether the court has any discretion to extend it beyond five years—those are things we don't know the answer to."*[117]

This concern doesn't necessarily mandate a legislative fix because with the passage of time, this could be naturally resolved through the courts. Nevertheless, debtors and creditors may benefit from the more uniform expectations facilitated by clearer guidelines. This is discussed further in Section V.

V. SUBCHAPTER V MOVING FORWARD (IMPROVEMENTS)

This Article briefly discussed concerns with some characteristics of Subchapter V. The introduction of Subchapter V is a boost for the small business debtor's plight, but the statute's provisions are far from perfect. One creditor's attorney even went so far as to say,

"Being a creditor's attorney and looking at Chapter 13 and all the debtors that would fail in Chapter 13, I looked at it as if there would only be about a 10-15% chance of somebody getting all the way through a Chapter 13 and paying my mortgage company client all of their money back. I see Subchapter V as even worse than that. It's less than 10% that we'll be able to get a confirmed plan, less than 10% we'll be able to survive. And the law itself, while it may help some, still leaves a significant [number] of small businesses out in the cold."[118]

This sentiment was not widely shared by this study's interviewees, but it does raise questions of what more might be improved about Subchapter V. Although

116 Telephone Interview with JF (Dec. 14, 2020).
117 Telephone Interview with AB and JS (Dec. 14, 2020).
118 Telephone Interview with DS (Dec. 11, 2020).

Subchapter V appears promising at this preliminary stage, all interview subjects acknowledged characteristics of the nascent process that need to be improved. They noted some negative outcomes that could be prevented if lawmakers were to amend and clarify some provisions of the SBRA. They also noted that some flaws needed—rather than a legislative fix—more of a judicial cure or simply the passage of time. In this section, some potential improvements are suggested and discussed.

A. Uniformity of Subchapter V Trustee Position

1. Uniform Trustee Role Perception and Guidelines

This study has repeatedly revealed that debtor's attorneys and creditor's attorneys have worked with Subchapter V trustees whose levels of involvement span a wide range. While there are existing guidelines in the statute's legal manual itself and the Handbook for Small Business Chapter 11 Subchapter V Trustees, they are not enough to help small business debtors minimize risk in the bankruptcy process.[119] This section discusses these potential solutions in addition to more specific trustee guidelines: (1) appointing Subchapter V trustees to cases only when necessary, and (2) introducing standing Subchapter V trustees.

One debtor's attorney suggested,

"It seems like they should be appointed if necessary, not from the outset. The U.S. trustee would tell you, 'Yeah, but you don't have to pay quarterly fees in a SubV.' And a quarterly fee is paid in a normal Chapter 11, and it's based on the dispersements the debtor makes, and it's a sliding scale percentage, but it depends on the case. Sometimes it actually works to your benefit, because most individual Chapter 11s, their quarterly fees are 300 bucks a quarter, so it's not a fair comparison to say, 'You don't have to pay quarterly fees, so now you pay SubV fees.'"[120]

This potential solution, though plausible, ultimately does not help the issue of non-uniformity. The Subchapter V trustees would still be appointed on a case-by-case basis with the same general guidelines that direct them now. Making the Subchapter V trustee position an optional one to be determined by either the U.S. Trustee or the court would also add another layer of complexity to the process. This simply adds yet another duty onto court dockets while providing little

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[119] *See generally* SBRA Legal Manual, *supra* note 27; Trustee Handbook, *supra* note 35.
[120] Telephone Interview with LP (Dec. 11, 2020).

additional benefit to the debtor and creditor. Debtors and creditors are likely to still experience a trustee-roulette.

Additionally, this suggestion is likely to be a significantly bias against creditors, who may already have thin representation due to the lack of a creditors' committee.

A creditor's attorney proposed the second solution—that a standing trustee structure, as opposed to the current case-by-case-appointment method, would be preferable:

"Something of a standing trustee process would probably be better. … The reason why I think a standing trustee is better is because then things would be more uniform. It would take it out of the purview of the United States Trustee. …There might be more flexibility within a standing trustee as long as they're managing the case. A standing trustee would have required documents that they're looking for that are standard. Each case I've found in dealing with different analysts at the United States Trustee's office required different documents. They have different questions. …It should be more uniform, and a standing trustee would have it be more uniform."[121]

A standing trustee could very well provide the uniformity that many bankruptcy attorneys are seeking. In 28 U.S. Code § 586, lawmakers have already outlined the option of appointing a standing trustee if the number of cases under Subchapter V of Chapter 11 in a particular region so warrant. The U.S. Trustee of that region, jointly with the approval of the Attorney General, may appoint standing trustee(s).[122] If one or more individuals were to be the appointed trustee for every Subchapter V case in a certain district, the actions of those standing trustees would be far more predictable and uniform than if the Office of the U.S. Trustee were to continue appointing professionals to the trustee position case-by-case.

All of the Subchapter V trustees I spoke to in this study had primary jobs aside from overseeing their assigned cases. Most of them had been appointed to only one or two Subchapter V cases thus far. This naturally leads to a wild swing in trustee activity. The number of cases filed under Subchapter V of Chapter 11 may not trigger the provisions of 28 U.S. Code § 586(b) and lead the U.S. Trustee to

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[121] Telephone Interview with DS (Dec. 11, 2020).
[122] 28 U.S.C. § 586(b)

appoint standing trustees, but this study indicates another compelling and arguably sufficient reason to appoint them.

A trade-off that debtors may experience as a result of this transition from case-by-case-appointed trustees to standing trustees is the change in compensation structure. Subchapter V standing trustees are compensated pursuant to 28 U.S. Code § 586(e), which sets the standing trustees' fees at a percentage rate, including overhead, of plan payments. This is a more uniform compensation structure for debtors to factor in, but the decrease in volatility also introduces the possibility and risk that debtors pay out more over the lifetime of the plan than they might to a non-standing trustee charging an hourly rate.

Appointing a standing trustee is likely to prove a solution to the lack of uniformity, but the switch from non-standing to standing trustee does mandate some trade-offs. While this decision is ultimately under the discretion of a region's U.S. Trustee and Attorney General, this Article encourages each district to take these study's findings and determine the necessary course of action for its potential bankruptcy petitioners.

2. Uniform Compensation Structure

As the statute is written, Subchapter V trustees are compensated by an hourly rate that they themselves determine, as long as the court determines that such compensation is "reasonable."[123] The debtor, creditors, and the United States Trustee can still review the trustee's fee applications and object if the requested compensation is excessive or unreasonable; however, this still places a burden on the parties involved.[124] More objections within the bankruptcy process still increase time and expenses for the debtor and creditors.

The Handbook for Small Business Chapter 11 Subchapter V Trustees reminds that "*Trustees are encouraged to keep in mind Congress' stated intent that subchapter V cases not be burdened with excessive administrative expenses when planning their work and submitting their fee applications for review and approval by the court.*"[125] However, the current compensation structure for trustees incentivizes a higher hourly rate, especially since "reasonableness" has not yet been solidified by the courts.

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[123] 11 U.S.C. § 330(a)(1)(A)
[124] Trustee Handbook, *supra* note 35.
[125] *Id.*

While this problem may be fixed through future court decisions that become precedent as Subchapter V matures, the Office of the U.S. Trustee could implement several safeguards to reduce yet another roulette of trustee-related expenses. For example, when appointing trustees on a case-by-case basis, the U.S. Trustee could research prevailing professional rates and apply that uniform hourly rate to all appointed trustees' fee applications. Or, as discussed above, a transition to standing trustees would reduce the broad variability of trustee compensation. Future studies may explore these possibilities further.

B. Increased Debt Limit

Bankruptcy is designed to give debtors "overwhelmed with unimaginable debt[,] a fresh start through meaningful relief from their debt…and give them a new pathway to economic prosperity."[126] Through the CARES Act, in response to COVID-19, lawmakers increased the original debt limit of $2.7 million to $7.5 million—meaning more businesses could file under Subchapter V of Chapter 11 in the one-year period following the CARES Act. In February 2021, the debt limit returned to its previous figure. Some have argued that lawmakers should permanently increase the debt limit to a figure above $2.7 million.[127] Pervasive judicial theory, current scholarly opinion,[128] and practitioners' opinions all support this adjustment to increasing Subchapter V election.

From judicial opinion, we learn that the courts view bankruptcy as necessary to the health and functioning of this society. In *Sturges v. Crowninshield*, the Supreme Court asserted that the power over bankruptcies was granted to Congress to exercise, and the power is necessary for the good of the community. The Court argued that "the power to grant relief in the extremities of debt and indigence is a moral necessity—it is essential for the existence and well-being of civilized and commercial society."[129] Thus, a mechanism for relief from debt must

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[126] AM. BANKR. INST., *ABI Commission to Study the Reform of Chapter 11: 2012-2014 Final Report and Recommendations*, 23 AM. BANKR. INST. L. REV. 1, 297 (2015) (statement of Rep. David Cicilline, Member, H. Judiciary Comm.) (hereinafter *ABI Final Report*).
[127] Blackmon, *supra* note 8, at 342. ("[T]he SBRA's one legislative shortcoming is its failure to raise the debt limit for small business debtors. This should be resolved with further legislation.")
[128] Bradley, *supra* note 17, at 262. ("Some commentators have suggested that there may be efforts to raise the cap on a permanent basis.")
[129] Donald L. Swanson, *Subchapter V Eligibility: Congress Needs to Permanently Extend the $7.5 Million Limit—Now!*, MEDIATBANKRY, Nov. 10, 2020, https://mediatbankry.com/2020/11/10/subchapter-v-eligibility-congress-needs-to-extend-the-7-5-million-limit-now/.

be available from a moral standpoint. That mechanism must have the ability to facilitate relief from debt, so the question must be whether standard Chapter 11 or other bankruptcy measures are sufficient to grant relief for viable small businesses with debt greater than $2.7 million.[130] The near unanimity of judicial[131] and scholarly opinion calling for an increase in the debt limit suggests the answer to be "no."

Scholarly opinion asserts that because the debt limit resides at roughly $2.7 million, the SBRA excludes many "small businesses" that could benefit from the Subchapter V process. Under pre-Subchapter V Chapter 11, small business debtors had a success rate of less than half of the success rate for non-small business debtors.[132] Robert J. Keach, a member of the ABI, claimed that the current debt limit is "simply too low to provide meaningful help for small and medium-sized companies."[133] Both the ABI and the NBC recommended a limit of $10 million,[134] but Blackmon indicates that a parred down value of $7.5 million would be more appropriate.[135] The exact figure has no scholarly consensus, but that the figure should be raised from its current level is generally agreed upon.

Most, if not all, participants in this study indicated that the debt limit should be either kept at $7.5 million or at least adjusted to a limit greater than $2.7 million.

Two debtor's attorneys stated, "*The first thing would be to increase the debt limit from $2.7 [million] to close to $7.5 [million] because $2.7 [million] for a small business can go pretty quick[ly], especially if there's related entities, or they own the dirt that they operate out of. …I think we could increase it, …and really do what Congress's intent was.*"[136]

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130 This Article does not assert that businesses that cannot conceivably survive, should survive. Bankruptcy is not meant to save a business which is beyond repair. The Code cannot, nor should it, fix a business that has no viability.

131 Hon. Jim D. Pappas, *Let's Talk Bankruptcy Reform (or How I Would "Improve" the Bankruptcy Code)*, 62 ADVOCATE (IDAHO ST. B. ASS'N) 22, 23 (2019).

132 Anne Lawton, *An Argument for Simplifying the Code's "Small Business Debtor" Definition*, 21 AM. BANKR. INST. L. REV. 55, 92 (2013).

133 ROBERT J. KEACH, AM. BANKR. INST., TESTIMONY OF AMERICAN BANKRUPTCY INSTITUTE 5 (June 19, 2019), https://docs.House.gov/meetings/JU/JU05/20190625/109657/HHRG-116-JU05-Wstate-KeachR-20190625.pdf.

134 *ABI Final Report*, *supra* note 126, at 299; NAT'L BANKR. CONFERENCE, A PROPOSAL FOR AMENDING CHAPTER 12 TO ACCOMMODATE SMALL BUSINESS ENTERPRISES SEEKING TO REORGANIZE 15 (Jan. 3, 2010), nbconf.org/wp-content/uploads/2015/07/NBC-Small-Business-Rept-Dec-17-2009.pdf.

135 Blackmon, *supra* note 8, at 343.

136 Telephone Interview with JW and DD (Dec. 11, 2020).

This Article proposes that lawmakers permanently increase the debt limit above $2.7 million due to four main reasons: (1) under a higher debt limit, more debtors can benefit from Subchapter V; (2) a nationwide limit should be lenient because debt value varies nationwide; (3) a lower debt limit would make more debtors vulnerable to the absolute priority rule in normal Chapter 11; and (4) businesses with lower debt are generally less organized, and current Subchapter V provisions wouldn't do enough for them regardless.

1. More debtors benefit

With an increased debt limit, more small to medium-sized debtors can take advantage of Subchapter V provisions. For example, a debt limit of $7.5 million would roughly cover between 78.0% and 86.7% of small to medium-sized debtors.[137] Furthermore, the Family Farmer Relief Act (the "FFRA") sets forth a compelling precedent that when a provision of the Code designed for a narrow class of debtor excludes a significant chunk of debtors who could also fit that class, then Congress should step in and modify the Code.[138]

One debtor's attorney explained,

"I don't know what the number should be. I do think it should be higher. …There's sort of a Goldilocks thing somewhere between $3 and 7 million, where I think a number of cases fall, where they could be organized, but the absolute priority rule in normal Chapter 11 is a big impediment to that. And they could otherwise stay in business. So I would be a proponent of keeping a higher debt limit for small businesses. Obviously, there are other trade-offs, but having more companies have access to what is faster and cheaper can only benefit smaller businesses."[139]

Another commented,

"In my experience $7.5 [million] is probably adequate for Subchapter V….The $2.7 million is probably inadequate for most practitioners other than perhaps an individual who owns a small business. That will be bad news if the cap actually goes back to the $2.7

[137] *ABI Final Report*, *supra* note 126, at 309-310.
[138] Blackmon, *supra* note 8, at 359.
[139] Telephone Interview with PT (Dec. 15, 2020).

million at the end of March of next year. …because most companies have more than that amount of debt. …I would say, at a minimum, you need a $5 million cap."[140]

2. Debt value varies nationwide and is easily accumulated

Advocates of a higher debt limit see the SBRA as akin to "putting a band aid on a really bad cut" because it is insufficient for today's economy, where it "doesn't take a business of much size to run up $2.7 million in debt."[141] This is especially true during times of financial distress when small businesses are likely to need debt relief the most.[142]

One Subchapter V trustee observed,

"Absolutely, I agree that the debt limit should be kept at $7.5 million. … Debts are different in different parts of the country, so $2.5 million in the Southern District of California or the Southern District of New York is not the same as $2.5 [million] in Idaho. When you have one number across the whole country, it's tough. If $7.5 [million] doesn't stay, then you're just not going to have as many cases, and it's just not going to be as effective—just because a number of companies won't be eligible for it."[143]

3. Fewer debtors vulnerable to the prohibitive and expensive absolute priority rule in normal Chapter 11

If a small business inadvertently moves beyond the $2.7 million debt limit, as it is easy to do, it will have to go through standard Chapter 11—which scholars have repeatedly stated does not work for small business debtors.[144] This includes the absolute priority rule—a prime feature of traditional Chapter 11—which is often an obstacle to prompt reorganization. In this case, if the debtor cannot confirm a plan, its creditors can propose one, which may result in the creditor taking control of the assets and case from an individual debtor or debtor-entity's owners.[145] For small businesses, the absolute priority rule serves to prolong the

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[140] Telephone Interview with AB and JS (Dec. 14, 2020).
[141] Ruiqi Chen, *Bankruptcy Bills Could be 'More Muscular,' Advocates Say*, BLOOMBERG L., (Aug. 7, 2019), https://www.bloomberglaw.com/product/blaw/document/XFP8F5H8000000?criteria_id=4136c0576cc558530973f7b3f6a56e2c&searchGuid=f7325aeb-6fd9-43d8-b95d-c2f52e2d867d.
[142] Blackmon, *supra* note 8, at 354.
[143] Telephone Interview with GJ (Dec. 29, 2020).
[144] KEACH, *supra* note 133, at 4.
[145] Pappas, *supra* note 131, at 22.

bankruptcy process—increasing costs—and erodes the position of the debtor-owner—removing incentives for the owner to operate the small business. A lower debt limit subjects more small to medium-sized businesses to standard Chapter 11 and its associated absolute priority rule. A higher limit protects them. Two debtor's attorneys confirmed,

"One of the great things about Subchapter V from our point of view as debtors' lawyers, is no absolute priority rule, which is a huge issue in any debtor case where it's relatively small. …In a small case, the concept of exchanging debt for equity usually doesn't exist, so we really do have to have the debtor's owners or the debtor…retain ownership of the business. That's why it's so important to us to want to see that $7.5 million cap, because otherwise we're going to get into businesses that have $3.0 million worth of debt, but you've got the absolute priority rules. And getting around the absolute priority rule can be done, but it just adds a whole lot of expense to the case, and that's where you get back to the initial problem. These cases cost too much money for the small business to bear."[146]

4. Businesses with lower debt are generally less organized

With a higher debt limit, Subchapter V will likely be made available to companies that have higher potential for viability upon exit. A lower debt limit might make Subchapter V available to a group of small businesses that, because of intrinsic disorganization, still might not survive. A creditor's attorney reasoned,

"From the very beginning, there's no way that these cases should have the same filing fee as a [large corporation]. Those debtors only pay $1717, but my debtor has to file a SubV case for the same filing fee. That's ludicrous. …A small corporation that is in the $15-20 million range is probably going to be much better with this kind of process than an actual small business—somebody below the absurd number that they initially put out. $7.5 [million] is actually more realistic because even companies that have $7.5 million worth of debt are still disorganized. …SubV gives them a better opportunity, but it still is very cumbersome. …It may be helpful for larger businesses, but once you go down the size scale, these businesses are just not going to survive still under SubV."[147]

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[146] Telephone Interview with AB and JS (Dec. 14, 2020).
[147] Telephone Interview with DS (Dec. 11, 2020).

5. Concerning possibility of moral hazard and tightening credit terms

However beneficial permanently raising the debt limit may be, lawmakers must still consider the ramifications of doing so. In particular, the bankruptcy system may witness a moral hazard problem—where small businesses accumulate as much debt as possible up to the raised debt limit, knowing they have the assurance of an easier Subchapter V bankruptcy process. Additionally, critics of similar propositions argue that raising the debt limit could increase borrowing costs and decrease the availability of credit for debtors as well.

Regarding the moral hazard problem, this study has not delved into the possibility of riskier behavior from small businesses due to an increase in the debt limit, as this would be difficult to study especially given the current COVID-19 environment where small businesses are scrambling to stay afloat. It does raise this concern so that further studies may be conducted to obtain plausible reassurance that any increase with the moral hazard problem will be negligible.

This study has also not delved into the possibility of tightening credit availability for small business debtors. Some scholars have expressed some hesitance for similar adjustments; for example, the American Bankers Association critiqued the FFRA that raised the debt limit for family farms. Its primary concern was that "credit terms would tighten considerably for many family farms, with a disproportionate impact on the most distressed farms in need of credit."[148] It also asserted that borrowing costs would increase and availability of credit would decrease accordingly for debtors.[149] These concerns should be properly explored before an amendment to the SBRA to raise the debt limit is passed.

C. Clear Interpretation of Disposable Income

As discussed in the preceding sections, many bankruptcy practitioners are concerned with how to interpret the statute's wording of "disposable income." Two debtor's attorneys expressed,

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[148] *See* Am. Bankers Ass'n, Statement for the Record on Behalf of the American Bankers Association Before the Subcommittee on Antitrust, Commercial and Administrative Law of the Judiciary Committee of the United States House of Representatives 5 (June 25, 2019), https://www.aba.com/-/media/documents/testimonies-and-speeches/statement-record-house-judiciary-subcommittee-chapter12-bankruptcy.pdf?rev=be9fa8b76efc45c88aacc5b775c96fd8.
[149] *Id*. at 7.

"I think clarity as in how you interpret the statute [is needed]. …In Subchapter V, this section says that the court can fix the time for three years, but to no length greater than five years. So they give the discretion to the court on determine what's fair and equitable as it relates to the length of the plan. So clarity is really going to come into play when it's, what's the standard there? Is it three or is it five? The debtor's attorney is always going to say three years, and the creditor's is always going to say five years, so that's always going to be something that we'll eventually fight over."[150]

They continued,

"[T]he statute is a little bit vague on disposable. What is disposable income? We say that disposable income is projected. So, for example, if we put forth a plan that's got a projected disposable income of 5 grand, and that gets confirmed, the debtor better pay 5 grand. But if the disposable income for that month is 10 grand, we get the windfall. Some debtor's attorneys are going with actual disposable income rather than projected, so if they do actual disposable income and then they don't have any disposable income, they don't make any plan payments. There's a little bit of a question of, what is disposable income?"[151]

Another debtor's attorney has settled into paying actual income:

"There's the aspect of disposable income as the cramdown requirements. If one person rejects, the debtor has to contribute disposable income for a three-year period—how and why you calculate that is an unknown. In my opinion, all you have to do is give actual income, which means you don't have to project a number. One of the judges has said he has concerns about that, but I don't think he'll stop me. …More uniformity in how to calculate [disposable income is needed]…because say that you project the disposable income number, and your business changes. Coming back in and amending a Chapter 11 plan is not easy to do."[152]

The first question that debtors are wrestling with is whether to plan for actual disposable income or projected disposable income. If projected disposable income, the second question is how debtors should calculate these projections. Both are difficult questions to resolve unless there is consensus within the courts. From these and more shared experiences, the courts should prioritize coming to a consensus on whether debtors may plan for actual disposable income or

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[150] Telephone Interview with JW and DD (Dec. 11, 2020).
[151] *Id.*
[152] Telephone Interview with PT (Dec. 15, 2020).

calculate projected disposable income. Otherwise, the confusion while formulating a proposed plan of reorganization may unduly prolong the bankruptcy proceedings.

D. The Passage of Time and Increased Precedent

With all the issues presented regarding the Subchapter V process, it is important to remember that its introduction was fairly recent. Given its fledgling status, many of its issues could very well be resolved simply through the passage of time and accompanying court precedent as bankruptcy courts rule on emerging Subchapter V cases.[153]

Two debtor's attorneys observed,

"I think the biggest issue right now is that there hasn't been a whole lot of precedent that's been said. To a certain degree, it's a matter of the US Trustee, the SubV Trustee, and everyone else feeling their way through the initial few cases. Once you get a precedent established, …then it becomes a lot easier. …When we're still plowing new ground, I think there's a greater level of cautiousness on the part of the US Trustee to make sure that it's done right, and no one is being criticized for getting it wrong."[154]

Others concurred, *"Clarity will come with time just because it's so new."*[155]

Some scholars have suggested that with increased precedent, the balances will tip more prejudicially against the unsecured creditor and for the small business debtor.[156] Although yet to be confirmed, this assertion is yet another reason to more sharply scrutinize current trustee guidelines and determine how to improve them.

CONCLUSION

Preliminary quantitative and qualitative data indicate that the Subchapter V process offers reduced costs and promising outcomes for debtor businesses

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[153] Bradley, *supra* note 17, at 283. ("Laws are passed by Congress, but their meanings develop over time. They take shape only gradually. Laws' scope and impact develop from the experience of actual cases and negotiations, informed by the writings and discussions of judges, practitioners, and academics.")
[154] Telephone Interview with RG and CB (Dec. 14, 2020).
[155] Telephone Interview with JW and DD (Dec. 11, 2020).
[156] Bradley, *supra* note 17, at 284.

seeking to reorganize—although bankruptcy-related costs might still be prohibitive for companies below the original $2.7 million cut-off. Its outcomes are tentatively no less favorable for creditors as well. To refine the process, legislators should consider permanently increasing the debt limit of Subchapter V debtors to a figure well above the original $2.7 million, and solidifying uniformity of the Subchapter V Trustee position. Other issues have arisen due to the process's infancy and remain beyond the scope of policymaking: how should parties interpret statutory language? What should the standard be for income calculation? Etc. In time, as with all nascent statues, bankruptcy courts should judicially resolve these issues, and precedent should clarify them. This study also suggests further areas of research, including the true recovery rates of unsecured creditors and how administrators might give Subchapter V trustees enough guidance while enabling them to maintain flexibility.

Table 1 Summary of Cases and Milestone Dates

Case Type	Case	Bankruptcy Date	Days to Meeting of Creditors	Days to First Status Conference	Days to File Plan of Reorganization	Days to Confirmation	Days to Conversion	Days to Dismissal	Secured Debt (Official Form 206D)	Unsecured Debt (Official Form 206E/F)	Total Debt
Subchapter V	A	2020-04-22	21	34	41	189			$ 3,066,333.00	$ 4,655,873.27	$ 7,722,206.27
Subchapter V	B	2020-05-26	31	44	38	191			$ 756,569.84	$ 6,689,738.07	$ 7,446,307.91
Subchapter V	C	2020-05-29	27	55	Deadline Extended				$ 3,047,048.07	$ 3,901,148.70	$ 6,948,196.77
Subchapter V	D	2020-05-29	40	54	90				$ 3,624,505.45	$ 2,964,382.55	$ 6,588,888.00
Subchapter V	E	2020-06-07	144	60	Converted		67		$ 3,666,836.60	$ 3,803,082.37	$ 7,469,918.97
Subchapter V	F	2020-06-08	22	56	92				$ 7,153,615.45	$ 228,582.65	$ 7,382,198.10
Subchapter V	G	2020-06-26	34	55	90				$ 5,358,329.23	$ 1,324,870.31	$ 6,683,199.54
Subchapter V	H	2020-07-01	51	55	75		126		$ 7,268,220.59	$ 5,064.00	$ 7,273,284.59
Subchapter V	I	2020-07-03	55	40	89				$ 5,403,130.24	$ 2,062,853.95	$ 7,465,984.19
Subchapter V	J	2020-07-15	26	49	Deadline Extended				$ 3,873,474.00	$ 3,092,308.38	$ 6,965,782.38
Subchapter V	K	2020-07-23	34	55	90				$ 1,650,153.42	$ 5,029,428.32	$ 6,679,581.74
Subchapter V	L	2020-07-28	27	37	80				$ 4,788,367.67	$ 2,523,160.03	$ 7,311,527.70
Subchapter V	M	2020-07-31	32	32	70				$ 6,107,003.80	$ 1,034,010.37	$ 7,141,014.17
Subchapter V	N	2020-08-06	33	26	90				$ 4,489,960.30	$ 2,563,476.32	$ 7,053,436.62
Subchapter V	O	2020-08-07	Not set	33	Converted		83		$ 3,015,145.36	$ 3,713,809.74	$ 6,728,955.10
Subchapter V	P	2020-08-10	24	57	88				$ 149,900.00	$ 6,758,283.32	$ 6,908,183.32
Subchapter V	Q	2020-08-19	20	35	78				$ 3,624,285.10	$ 3,453,920.44	$ 7,078,205.54
Subchapter V	R	2020-08-25	28	Continued	43				$ 1,248,742.72	$ 6,135,718.12	$ 7,384,460.84
Subchapter V	S	2020-08-25	30	49	41				$ 1,194,697.73	$ 5,765,689.66	$ 6,960,387.39
Subchapter V	T	2020-08-25	24	44	90				$ 377,378.07	$ 6,468,722.76	$ 6,846,100.83
Subchapter V	U	2020-08-28	26	Cancelled	69				$ 1,575,000.00	$ 5,625,738.08	$ 7,200,738.08
Subchapter V	V	2020-09-03	25	Continued	90				$ 2,214,951.74	$ 4,369,032.37	$ 6,583,984.11
AVERAGE			**36**	**46**	**75**	**190**	**92**	**N/A**	**$ 3,347,893.11**	**$ 3,734,949.72**	**$ 7,082,842.83**
Chapter 11	W	2020-05-12	86	Not set	Converted		189		$ 7,192,125.35	$ 865,419.76	$ 8,057,545.11
Chapter 11	X	2020-05-29	41	Not set	Dismissed			52	$ 4,440,187.57	$ 3,847,746.02	$ 8,287,933.59
Chapter 11	Y	2020-06-24	34	34	Not Submitted				$ 7,237,000.00	$ 665,096.00	$ 7,902,096.00
Chapter 11	Z	2020-07-15	Continued	Continued	Not Submitted				$ 6,087,229.83	$ 1,504,502.05	$ 7,591,731.88
Chapter 11	AA	2020-08-04	Continued	Not set	90				$ 8,177,273.12	$ 82,999.73	$ 8,260,272.85
Chapter 11	BB	2020-09-24	67	Continued	Not Submitted				$ 7,991,000.00	$ 380,521.65	$ 8,371,521.65
Chapter 11	CC	2020-03-24	46	Not set	Not Submitted				$ 8,166,817.32	$ 128,454.69	$ 8,295,272.01
Chapter 11	DD	2020-05-01	27	Not set	Missed deadline				$ 3,667,154.00	$ 4,820,519.11	$ 8,487,673.11
AVERAGE			**50**	**34**	**90**	**N/A**	**189**	**52**	**$ 6,619,848.40**	**$ 1,536,907.38**	**$ 8,156,755.78**