

CARES Act Expands Bankruptcy Protections for Small Businesses

March 26, 2020

On August 23, 2019, Congress enacted the Small Business Reorganization Act (“SBRA”), which became effective on February 19, 2020. In light of the economic impact of the COVID-19 virus on businesses, particularly small businesses, Congress is expected to expand the relief to such businesses under the SBRA, as well as other provisions of the Bankruptcy Code.

The “Coronavirus Air, Relief and Economic Security Act” (CARES Act) passed by the Senate on March 25, 2020 (the House of Representatives is expected to vote on the CARES Act on March 27, 2020), amends the SBRA to increase the debt limit for debtors filing under sub-chapter V from \$2,725,625 to \$7.5 million (the original limit will return after one year). This change will substantially increase the number of businesses in the Tri-State area that are eligible for relief under the SBRA.

As enacted, the SBRA permits businesses with debts of less than \$2,725,625 (both secured and unsecured) to file a chapter 11 case under a new sub-chapter (sub-chapter V) provided that 50% or more of those debts arise from business or commercial activities. The SBRA seeks to provide a quicker and less expensive reorganization for eligible debtors and sub-chapter V contains certain provisions not otherwise available under chapter 11, including:

- No creditors’ committee would be appointed in a case unless ordered by the court, thereby significantly reducing administrative costs for their counsel fees;
- No United States Trustee fees, which are fees based on a company’s disbursements, would need to be paid, which would also reduce the costs of administration;
- A sub-chapter V trustee will be appointed in the case to facilitate the company in restructuring its debts by helping, if needed, the debtor to formulate a consensual plan and by monitoring distributions in accordance with the terms of the plan;
- The bankruptcy court will hold a mandatory status conference within 60 days of the bankruptcy filing “to further the expeditious and economical resolution of the Subchapter V case”;
- Only the debtor may file a plan and a separate disclosure statement does not need to be filed or approved to confirm a sub-chapter V plan, which will lower the costs of proposing a plan;
- The debtor can file a plan which would not require voting by creditors, and therefore would have a greater chance of confirmation;
- A debtor’s plan can modify a mortgage against a principal residence (unlike under a non-SBRA chapter 11 plan or a chapter 13 plan), provided that the mortgage loan was not used primarily to acquire the residence (*i.e.*, a collateral mortgage) (this provision was subject of one of our prior alerts -

<https://www.cullenllp.com/blog/new-small-business-reorganization-act-of-2019-may-permit-small-business-debtors-to-modify-their-residential-mortgages/>); and

- A debtor must file its plan within 90 days of the bankruptcy filing (subject to extension under limited circumstances), which will reduce the time in bankruptcy and, as a result, the cost of administration.

Notably, although titled the “Small Business” Reorganization Act, the SBRA is available to individuals as well, who may not otherwise meet the requirements of a filing under chapter 13 of the Bankruptcy Code.

In addition to the increase of the SBRA debt limit, the CARES Act provides that any chapter 7 and chapter 13 bankruptcy provisions based on the “income” of a debtor will not include coronavirus-related payments from the federal government. For debtors who are currently making payments under confirmed chapter 13 plans, under certain circumstances a debtor will also have the ability to extend their plan payments from the standard 3 to 5 years, to 7 years after the initial payment was due. The CARES Act modifications will only be in effect for a period of one (1) year.

It is too soon to determine the extent of economic damage to the country’s businesses based on COVID-19, but it is anticipated that the changes made to the Bankruptcy Code through the CARES Act will significantly increase bankruptcy filings by small businesses under the SBRA.

Please note that this is a general overview of developments in the law and does not constitute legal advice. Nothing herein creates an attorney-client relationship between the sender and recipient. If you have questions regarding these provisions, or any other aspect of bankruptcy law, please contact Bonnie Pollack (bpollack@cullenllp.com) or Michael Kwiatkowski (mkwiatkowski@cullenllp.com) at (516) 357-3700.

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