

Legislative Update

BY ROBERT J. KEACH

ABI Testifies on Family Farmers and Small Business Reorganizations

Editor's Note: This month's Update features testimony excerpts from a June 25 hearing before the House Judiciary Subcommittee on Antitrust, Commercial and Administrative Law. Video of the testimonies is available at judiciary.house.gov/legislation/hearings/oversight-bankruptcy-law-and-legislative-proposals.



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Robert Keach is chair of the Business Restructuring and Insolvency Practice Group with Bernstein Shur in Portland, Maine. He is a past ABI president and co-chaired the ABI Commission to Study the Reform of Chapter 11. He delivered ABI's statement. Both bills were approved by the House Judiciary Committee on July 11.

Thank you for inviting me to present the views of [ABI] in support of several bipartisan bankruptcy measures now pending before the subcommittee. ABI is the world's largest association of professionals practicing in the area of corporate restructuring and personal bankruptcy, with nearly 11,000 members worldwide....

I served as president of ABI from 2009-10 and later as co-chair of ABI's Commission to Study the Reform of Chapter 11.... The 400-page report of the Chapter 11 Commission was the product of three years of study by two dozen thought leaders in the community on how best to improve and modernize a U.S. Bankruptcy Code that was nearly 40 years old at the time. Since its issuance in 2014, the Chapter 11 Commission report has been an influential resource for stakeholders and cited by numerous federal courts, including the U.S. Supreme Court....

Family Farmer Relief Act of 2019 (H.R. 2336; S. 897)

This bipartisan and bicameral legislation would increase the debt limits for the filing of chapter 12 cases from the existing limits ... to \$10 million.

Since its enactment in the midst of the severe farm crisis in 1986, chapter 12 has been a useful and durable support for the cyclical economic challenges faced in American agriculture, roiled by fluctuating land values, swings in commodity prices, weather calamities and adverse trade policies made by government.... Chapter 12 has not only assisted family farmers in their efforts to successfully reorganize debts in bankruptcy court, it has perhaps more significantly provided a framework that encouraged stakeholders to reach agreement on debt restructuring outside the expense of the formal bankruptcy process....

At the outset in 1986, Congress established a debt limit of \$1,500,000 for eligibility.... In 1986, the vast majority of farms were owned and operated by members of a single or extended family.... However, today's farming operations are much larger and operated by fewer families than in the

1980s. Farming has progressed from intense labor with small equipment in the 1980s to limited labor but much more expensive technology, including computers using expensive GPS capability. Debt amounts are much larger today, given capital requirements for farm land, equipment and inputs.

Relative to 1986, and in nominal dollars, production expenses in agriculture have increased by 198 percent and farm debt has increased by 182 percent, while net cash income has experienced only half of that growth, according to the American Farm Bureau. As a result, the liability cap under chapter 12 does not align with the modern credit and risk environment associated with family farming....

The Family Farmer Relief Act of 2019 would allow more family farmers to seek relief under the program by raising the chapter 12 operating debt cap to \$10 million. Lifting the liability cap and giving more farmers an opportunity to qualify for chapter 12 bankruptcy provides the restructuring and seasonal repayment flexibility that many farmers need in today's lagging farm economy and will help to align bankruptcy law with the scale and credit needs of U.S. agriculture....

[W]hile there certainly have been years where farmers faced greater immediate financial challenges than 2019, uncertainties in both the trade and commodities markets make this an ideal time to reset chapter 12 before a crisis arrives. ABI supports this legislation and urges its enactment in this Congress.

Small Business Reorganization Act of 2019 (H.R. 3311; S. 1091)

Chapter 11 ... has long been of great value in preserving going-concern value [and] jobs, and maximizing creditor recoveries for many businesses. But as the Chapter 11 Commission found, the law no longer works well for businesses of smaller size. Small businesses are the entities that produce job creation and a dynamic economy, but are also most likely to experience financial distress....

The deficiencies in existing U.S. bankruptcy laws were highlighted and examined extensively during a three-year study process undertaken by [ABI's] Chapter 11 Commission.... The Commission endeavored to include all perspectives and stakeholders in the conversation, including businesses of all sizes, secured lenders, bondholders, unsecured trade creditors, and employees. Consequently, the Commission's findings and rec-



Mr. Keach (second from left) is pictured with other ABI members who either testified or attended the June 25 hearing in Washington, D.C., which also covered the Honoring American Veterans in Extreme Need Act of 2019 (H.R. 2938; S. 679), Puerto Rico Recovery Accuracy in Disclosures Act of 2019 (H.R. 683; S. 1675) and student loan debt treatment in bankruptcy.

ommendations are the result of a holistic study that seeks to improve the U.S. bankruptcy system for all stakeholders....

[T]he testimony before the Commission suggested that the chapter 11 process simply does not work at all for small and medium-sized businesses. Witnesses testified how small and medium-sized businesses no longer use chapter 11 to try to save their businesses; rather, for the most part, these companies file bankruptcy knowing the business will not survive.... For example, for fiscal years 2008-15, [more than] 18,000 small businesses filed a chapter 11 case; only about 27 percent of those companies confirmed a reorganization plan. Notably, these numbers do not account for the small businesses that are struggling but do not even try to reorganize under chapter 11 because the Bankruptcy Code is seen as broken and unworkable for those kinds of businesses.¹

Chapter 11 doesn't work for small and medium-sized businesses because the Bankruptcy Code (a) places unrealistic and artificial deadlines on small and medium-sized businesses, which do not give these companies an opportunity to restructure; (b) imposes substantial and costly disclosure and reporting requirements on these companies; (c) does not provide any tools that can help small businesses — whose owners may be unsophisticated in finance, business plans

¹ In FY 2018, there were only 1,335 small business chapter 11 cases filed nationwide. The number of cases filed under the current small business chapter 11 has declined for eight consecutive years.

or restructuring issues — create and implement an effective reorganization plan; and (d) makes it difficult for a small business owner to maintain an ownership interest in the business under the current chapter 11.

Providing a small or medium-sized debtor with the time and the tools to reorganize under the Bankruptcy Code allows individuals to retain businesses they have worked hard to build, while preserving the value of secured creditors' collateral. It keeps that business operating and acting as a customer or supplier to other small businesses, and it saves jobs. It also encourages owners of struggling businesses to seek the help they need or to enter into financing and other arrangements that may mitigate short-term problems, rather than deepening the company's longer-term financial or operational difficulties through delay. It also protects the rights of creditors in terms of notice, due process and fair and equitable treatment — rights not present in potential state law alternatives.

The SBRA could address many of the difficulties experienced by small business debtors.... However, the SBRA as currently proposed would apply to cases where a debtor has aggregate liabilities that do not exceed \$2,566,050.... This debt limit, borrowed from the current definition of "small business debtor" in § 101(51D) of the Code, is simply too low to provide meaningful help for small and medium-sized companies.

As in the case of family farms, most small businesses will have more than \$2.7 million in total debt.... For example, in times of distress, a business will actually increase borrowings secured by the business assets in an attempt to remain afloat.... Accordingly, we think the debt limit proposed for a remodeled chapter 12 (\$10 million, as found in H.R. 2336) should be adopted as part of SBRA.

The ABI Chapter 11 Commission considered several analyses and empirical studies of chapter 11 debtors' assets and liabilities found in the schedules of filed cases. The data revealed a natural breaking point at a \$10 million threshold....

The Commission agreed that while public companies should be excluded from small business treatment no matter the size ... entities with \$10 million or less in assets or liabilities corresponded most closely with businesses not well served by current U.S. bankruptcy law. We support this change to the SBRA. **abi**

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