

Legislative Update

BY DONALD L. SWANSON

SBRA: Frequently Asked Questions and Some Answers

Editor's Note: President Donald Trump recently signed into law several bankruptcy law changes, one of which was the Small Business Reorganization Act. Below, **Donald Swanson** answers commonly asked questions on the SBRA.

ABI was involved in the development of the package and held a live webinar to discuss the laws. The full webinar is available at abi.org/newsroom/press-releases/educational-press-briefings.

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When does the new law take effect? The Small Business Reorganization Act of 2019 (SBRA) became law on Aug. 23, 2019 (Pub. L. 116-54). However, its effective date is "180 days" later: to cases filed on or after Feb. 19, 2020.

How does the SBRA compare to chapter 12? Relief under the SBRA is modeled on chapter 12 relief. Chapter 12 came into existence in 1986 because farmers had difficulty getting plans confirmed under chapter 11. The SBRA exists today because small businesses have had difficulty getting plans confirmed under chapter 11. In both cases, the problem was the absolute-priority rule, which denies plan confirmation unless unsecured creditors agree to receive less than 100 percent. Both chapter 12 and the SBRA eliminate the absolute-priority rule. In other ways, the standards for confirmation of a plan under the SBRA follow chapter 11, not chapter 12.

Is a disclosure statement required under the SBRA? Yes, but it's a disclosure statement "lite." The SBRA retains a disclosure statement requirement (§ 1190), but only three items are required to be disclosed: a brief history of the business operations of the debtor; a liquidation analysis; and projections on the ability of the debtor to make payments under the proposed plan.

Does the SBRA eliminate any of the chapter 11 confirmation requirements? Yes. Plan-confirmation standards for chapter 11 are established in § 1129(a) and (b). Generally, the standards of § 1129(a) will still apply. However, the SBRA declares (in § 1191(a) and (b)) that the following provisions of § 1129 do *not* apply in a small business case: Unless explicitly incorporated, cramdown provisions of § 1129(b) do *not* apply; such (b) requirements take effect only when para-

graph (8) of § 1129(a) is not satisfied. Paragraph (8) of § 1129(a) does *not* apply.

Paragraph (8) requires that each class of claims has either "accepted the plan" or "is not impaired under the plan." This exclusion eliminates the absolute-priority rule, which appears in the cramdown requirements of § 1129(b). Moreover, the "at least one class" of impaired claims "has accepted the plan" requirement in paragraph (10) of § 1129(a) does *not* apply. This exclusion removes any requirement for creditor acceptance of a debtor's plan. Special provisions for "individual" debtors, under paragraph (15) of § 1129(a), do *not* apply.

Does the SBRA specifically incorporate any of the confirmation requirements in the cramdown provisions of § 1129(b)? Yes. The following confirmation requirements from § 1129(b) are explicitly incorporated into the SBRA (by § 1191(b) and (c)): The plan must not "discriminate unfairly" and must be "fair and equitable" for "each class of claims or interests that is impaired under, and has not accepted the plan" — this is a verbatim copy of the language from § 1129(b)(1).

The "fair and equitable" standard under the SBRA includes the following details: requirements of § 1129(b)(2)(A) for secured claims must be satisfied; the plan must contribute all of the debtor's "projected disposable income" to making plan payments for three to five years; the plan must be feasible (*i.e.*, there must be a "reasonable likelihood" that the "debtor will be able to make all payments under the plan"); and the plan must provide "appropriate remedies" to "protect" creditors from a failure to make payments, including "the liquidation of nonexempt assets."

Will the "contents of plan" provisions in § 1123 apply under the SBRA? The provisions of § 1123 on "contents of plan" will still apply under the SBRA, except for the following specific items (*see* § 1181(a)): the "future income from individual services" rule in § 1123(a)(8); the creditor-plan rule for an individual debtor in § 1123(c); and the "lien on principal residence" rule discussed below.

Can a lien secured only by a debtor's principal residence be avoided? It depends. The SBRA changes the existing chapter 11 rule, which prohibits modification of lien rights that are "secured only by a security interest" in a debtor's "principal residence" (*see* § 1123(b)(5)). The new rule (in § 1190(3))

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authorizes modification of such lien rights when the “new value” that a debtor received for such lien was (1) “not used primarily to acquire” the residence, and (2) instead was “used primarily” in the debtor’s small business.

Does voting on plan confirmation still exist under the SBRA? Probably, but this appears to be ambiguous. Here’s why: For starters, “acceptance of plan” provisions in § 1126 are not mentioned in the SBRA — neither explicitly included nor excluded. Second, the SBRA explicitly eliminates § 1129(a)(8) and (10) requirements that impaired classes must accept the plan (*see* § 1191(b)). Third, § 1191(b) requires fair and equitable treatment of an impaired claim that “has not accepted” the plan. Fourth, the trustee is to facilitate the development of “a consensual plan.”

How does the role of a trustee under the SBRA compare to the role of a trustee under chapter 12 and 13? A trustee is appointed in each: under the SBRA (§ 1183), under chapter 12 (§ 1202) and under chapter 13 (§ 1302). The statutory role and duties of these three trustees are similar, particularly as between the SBRA and chapter 12.

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.

How will the small business trustee be compensated? Section 586(e)(1) and (5) allows the court to “award compensation” to the small business trustee in an amount “consistent with services performed” and limited by 10 percent of “payments made under the plan.” Such compensation is payable upon substantial consummation of the plan, conversion or dismissal of the case, or other termination of the trustee’s services. The small business trustee is expressly excluded from provisions of § 326.

What exactly are the nature and limits of this “facilitate the development” role? That remains to be determined, but here are a couple suggestions. One suggestion is that the SBRA trustee should be a financial wizard who can work with all parties on cash flows, interest rates, payment requirements and all the numbers puzzles that comprise a plan. After all, financial advisors fill a crucial role in large bankruptcy cases. Such a role is still needed — but rarely used — in small business cases because of limited resources.

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.

How does the existence of the SBRA affect representation of a client who qualifies? Before the SBRA, the first question in representing a debtor who now qualifies was this: How do we deal with the absolute-priority rule? Upon the

effective date of the SBRA, the first questions in representing a debtor who qualifies will become: (1) What are our goals, and (2) is there a credible cash flow to achieve those goals? The SBRA thus offers options to debtors and their counsel not previously available.

The Committee on Bankruptcy Rules of the U.S. Judicial Conference is considering the development of model rules.

When does the small business debtor get a discharge: upon confirmation like chapter 11, or after completion of plan payments like chapter 12 and 13? Under the SBRA, the debtor receives a discharge only “after completion” of “all payments due within” the three- to five-year term of the plan (§ 1192) — like chapters 12 and 13 — but without incorporating the hardship-discharge provisions of § 1328(b). However, if creditors consent, the debtor can receive a discharge at confirmation.

Regarding rates of interest under a plan, will the U.S. Supreme Court’s formulation for chapter 13, established in *In re Till*, 541 U.S. 465 (2004), still apply? This question probably has a district-by-district answer. Some bankruptcy courts follow *In re Till* in circumstances outside of chapter 13. However, others don’t. Future practice under the SBRA will probably follow the same course: Courts that are accustomed to following *In re Till* in chapter 11 or 12 contexts will probably continue to do so, while courts who aren’t won’t.

What impact will the SBRA have on preference claims under the Bankruptcy Code? The impact is not limited to small business cases and is twofold. Before a preference claim can be pursued, a claimant must use “reasonable due diligence” in light of “the circumstances of the case” to consider “a party’s known or reasonably knowable affirmative defenses.” However, a preference suit for less than \$25,000 against a noninsider, involving a non-consumer debt, can only be brought in the district where the defendant resides.

Why did Congress set the total debt limit for SBRA eligibility so low, at \$2,725,625? The reality is that, as with chapter 12, Congress is establishing a baseline from which to measure the SBRA’s impact. In 1986, Congress set the debt limit for chapter 12 at only \$1.5 million. Chapter 12 has worked as Congress intended. Legislation recently enacted (Pub. L. 116-53) raises the limit to \$10 million. It is hoped that the recommendations of ABI (\$10 million) or the National Bankruptcy Conference (\$7.5 million) will be considered in the near future.

Are there any federal rules or model local rules being proposed for the SBRA? The Committee on Bankruptcy Rules of the U.S. Judicial Conference is considering the development of model rules. Watch this space for more details to come. [abi](#)