

March 28, 2020



CARES Act expands restructuring options for small businesses

By Victor Milione, Richard Pedone, and Christopher Fong

What happened and how does it open new options for distressed businesses, their lenders and investors?

On March 27, 2020, H.R. 748 (the “[CARES Act](#)”) was enacted to provide emergency assistance and a healthcare response for individuals, families, and businesses affected by the 2020 coronavirus pandemic. The CARES Act modifies the Small Business Reorganization Act (“[SBRA](#)”) and greatly expands the restructuring options available to businesses with less than \$7.5 million in debt through March 27, 2021. It is effective immediately. Previously, only businesses with up to \$2.7 million in debt could use the SBRA’s expedited provisions.

Small businesses of every type that are negotiating with creditors need to understand the power of these changes. The expedited restructuring possible under the SBRA will now be available to thousands more businesses. Importantly, it appears that the debt limit will be calculated on an entity-by-entity basis. As a result, corporate groups such as restaurant chains, multi-unit franchisees, nursing home chains, and others may now have a tremendous new tool available to them. In addition, even where the debt limit appears to render a group member ineligible because each member is liable on a common debt to a bank or other lender, careful pre-bankruptcy planning and restructuring could render the entity eligible. For example, a lender that wants to work cooperatively with a group of borrowers might agree to restructure its debt for purposes of successful filing under the SBRA by limiting the joint-and-several nature of its claims for purpose of the restructuring.

How could the change benefit you and your small business?

Small business debtors have traditionally been wary of a reorganization process under Chapter 11, despite its well-acknowledged benefits, due primarily to the potential cost and disruption it often causes. For those businesses that qualify, the SBRA is intended to alleviate those concerns and to make small business bankruptcies proceed under a faster timeline and at reduced cost.

- **Streamlining the process.** Under the SBRA, only the debtor enjoys the opportunity to propose a plan of reorganization, which is due within 90 days of the bankruptcy filing. Neither separate approval of a disclosure statement nor solicitation of votes is required to

confirm a plan. Instead of soliciting plan acceptances, the small business submits a plan to the bankruptcy court containing a brief history of the business's operations, a liquidation analysis, and projections with respect to the debtor's ability to make payments under the proposed plan. The requirement that a debtor pay administrative expense claims on the effective date of the plan is also eliminated.

- **Maintaining control.** The SBRA provides for the appointment of a standing trustee to help oversee the development and confirmation of the plan; the bankruptcy court may not appoint a traditional Chapter 11 trustee or examiner in such a case. Moreover, unless the court orders otherwise for cause, an unsecured creditors' committee will not be appointed. Finally, the SBRA removes the requirement that equity holders of the small business debtor provide "new value" to retain their equity interest in the debtor without paying creditors in full. Instead, the SBRA allows small business owners to retain ownership in their businesses after emerging from bankruptcy by allowing them to pay creditors over a longer period of time. Generally, the debtor must identify its "disposable income," and the plan of reorganization must explain how the disposable income will be distributed during a three- to five-year period to effectuate payments to creditors under the plan.

The SBRA can be a valuable tool for small businesses needing to reorganize or that may benefit from the bankruptcy process. We expect that countless businesses that were formerly ineligible for the SBRA, or that ruled out bankruptcy restructuring due to the significant costs, may benefit from a lower-cost bankruptcy restructuring under the SBRA, especially now with the increase of eligible debt levels provided under the CARES Act.

For more information about the Small Business Reorganization Act and the changes passed in the COVID-19 stimulus bill, please contact our [Coronavirus Response team](#), your regular Nixon Peabody attorney, or:

- Victor Milione, 617-345-1215, vmilione@nixonpeabody.com
 - Richard Pedone, 617-345-1305, rpedone@nixonpeabody.com
 - Christopher Fong, 212-940-3724, cfong@nixonpeabody.com
-