

The Small Business Prepack: How Subchapter V Paves the Way for Bankruptcy's Fastest Cases

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ABSTRACT

America has long styled itself as a place where entrepreneurs can dream big and—if things go well—make it big, too. But when small businesses fail, does the U.S. bankruptcy system provide a real opportunity to preserve value and try again? For decades, bankruptcy professionals, judges, and lawmakers have tried various approaches to small business bankruptcies, none of which worked particularly well. But in 2019, Congress passed the Small Business Reorganization Act (“SBRA”), one of the most significant amendments to the Bankruptcy Code in a generation. As practitioners, scholars, and judges work out the contours of the rules, we shine new light on one strategy for creditors and debtors that has gone unexplored so far: the small business prepack. Prepackaged bankruptcies, or “prepacks,” are an aggressive and controversial approach for chapter 11 debtors that prioritize speed and certainty. Prepack debtors develop their reorganization plans, solicit votes, and prepare all necessary filings before entering court. At their fastest, some debtors have managed to get in and out of bankruptcy court in less than twenty-four hours. Filing a prepack reduces costs, lowers unpredictability, and keeps the debtor out of the public eye. Although stringent notice, disclosure, and voting requirements make prepack bankruptcies challenging and contentious under regular chapter 11, we argue that subchapter V provides a more hospitable procedural outlet for the strategy. Although the SBRA did not address prepacks expressly, the SBRA facilitates prepacks for small businesses, paving the way for bankruptcy’s fastest cases both theoretically and practically. This Article walks through what a small business prepack would look like and analyzes which small businesses would benefit most from this strategy. It concludes with several proposals to

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refine subchapter V to make small business prepacks more predictable, efficient, and fair. Not all bankruptcy cases can be fast, but the SBRA may now make it easier for some small businesses to reorganize at rocket speed.

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[The] case will move fast and that alone will reduce costs.

–Hon. A. Thomas Small¹

[T]he primary benefits . . . are speed, cost, and value.

–Sarah Borders & Steven M. Blank²

INTRODUCTION

Bankruptcy professionals and their clients have long valued expediency and efficiency. Yet throughout much of bankruptcy’s history in the United States, financially distressed small businesses often found themselves trapped in protracted and intricate bankruptcy cases or attempting to survive outside the auspices of the Bankruptcy Code.³ Recognizing the incongruence of these options with the objectives of bankruptcy, and in the wake of numerous judicial and legislative attempts to solve the problem, Congress tried a new approach in 2019 by creating a new subchapter tailored to small businesses.⁴

The Small Business Reorganization Act (“SBRA”)⁵ is one of the most significant amendments to the Bankruptcy Code in a generation.⁶ It adds a new process for small business bankruptcies—subchapter V—within chapter 11 of the Bankruptcy Code.⁷ Subchapter V removes many of the complex requirements that had made bankruptcy unapproachable

¹ *Oversight of Bankruptcy Law and Legislative Proposals: Hearing Before the Subcomm. on Antitrust, Com., & Admin. L. of the H. Comm. on the Judiciary*, 116th Cong. 5 (2019) [hereinafter Small Testimony] (revised testimony of Hon. A. Thomas Small, U.S. Bankr. J. E.D.N.C., on behalf of the Nat’l Bankr. Conf. in support of H.R. 3311), <https://www.congress.gov/116/meeting/house/109657/witnesses/HHRG-116-JU05-Wstate-SmallT-20190625.pdf> [https://perma.cc/4SBB-CV92].

² Sarah Borders & Stephen M. Blank, *1-Day Prepackaged Bankruptcy*, BLOOMBERG L. (Aug. 2021), <https://www.bloomberglaw.com/external/document/X36CBBNO000000/bankruptcy-professional-perspective-1-day-prepackaged-bankruptcy> [https://perma.cc/65HE-S79R].

³ 11 U.S.C. §§ 101–1532.

⁴ See *infra* Section I.A (describing historical changes to the Bankruptcy Code to benefit small business debtors).

⁵ Small Business Reorganization Act of 2019, Pub. L. No. 116-54, 133 Stat. 1079 (codified as amended at 11 U.S.C. §§ 1181 *et seq.*).

⁶ See, e.g., David A. Mawhinney, *Saving the Stakeholders*, 61 JUDGES’ J. 26, 28 (2022) (describing the bipartisan legislation as “ushering in the most radical changes to federal bankruptcy law in 40 years”). As Mawhinney points out, the SBRA had mustered impressive support. See *id.* The bill was signed into law only fifty-six days after it was introduced in the U.S. House of Representatives, and Congress debated it for only four minutes. See *id.* at 28 n.5.

⁷ 11 U.S.C. §§ 1181–1195.

for small businesses.⁸ It shortens the length of the bankruptcy process, lowers costs, reduces the number of seats at the negotiating table, and offers entrepreneurs the chance to start afresh by keeping a stake in their company after three to five years of making payments out of disposable income.⁹ By implementing these changes, the SBRA creates a more accessible and streamlined framework for small businesses.

Subchapter V's innovations for small businesses arise at the culmination of a decades-long experiment by debtors' counsel to speed up chapter 11 cases by soliciting votes for a plan of reorganization before even filing the case. Debtors who file a prepackaged bankruptcy, or "prepack," enter bankruptcy court with their exit plan already set.¹⁰ So, although the plan of reorganization stands as the natural climax of a business bankruptcy and is typically filed six to nine months after the petition date, in a prepack case, the debtor seeks the initial protection of the bankruptcy court and final endorsement of its plan in the same breath—right as it walks into court.¹¹ Judges do not close a bankruptcy case after confirming a plan, but plan confirmation represents the definitive end to what are usually the most controversial and contested matters in a chapter 11 reorganization case, leaving subsidiary and administrative matters for further resolution.

Over the past two decades, prepack debtors have strategized to enter and exit court under this approach more and more quickly.¹² For many bankruptcy attorneys, a longstanding goal was the twenty-four-hour prepack: a bankruptcy petition filed at night and a confirmed plan the next day.¹³ In 2019, preeminent debtor-side firm Kirkland & Ellis broke the record, confirming the first-ever twenty-four-hour prepack.¹⁴

⁸ *See id.*

⁹ *See infra* Section I.B (describing the SBRA's adjustments to the Bankruptcy Code that make the process smoother for small businesses).

¹⁰ *See* Borders & Blank, *supra* note 2 ("[A] Prepack is a bankruptcy filing in which a debtor fully negotiates the terms of a chapter 11 plan . . . before the actual bankruptcy filing.").

¹¹ If that endorsement requires creditor votes, then the debtor has formally sought acceptance of its plan before filing for the bankruptcy. *See, e.g.,* Aurelio Gurrea-Martinez, *The Rise of Pre-Packs as a Restructuring Tool: Theory, Evidence and Policy*, 24 EUR. BUS. ORG. L. REV. 93, 96 (2022); Lynn M. LoPucki & Joseph W. Doherty, *Bankruptcy Survival*, 62 UCLA L. REV. 970, 994 (2015).

¹² *See* Jonathan M. Seymour & Steven L. Schwarcz, *Corporate Restructuring Under Relative and Absolute Priority Default Rules: A Comparative Assessment*, 2021 U. ILL. L. REV. 1, 9 (2021).

¹³ *All in a Day's Work. Belk Achieves Confirmation of Pre-Packaged Plan in Record Time*, PATTERSON BELKNAP (Mar. 3, 2021), <https://www.pbwt.com/bankruptcy-update-blog/all-in-a-days-work-belk-achieves-confirmation-of-pre-packaged-plan-in-record-time> [<https://perma.cc/QKU5-GGAU>].

¹⁴ *See generally In re FullBeauty Brands Holding Corp.*, Case No. 19-22185 (Bankr. S.D.N.Y. Feb. 3, 2019). *See also* David I. Swan & Thuc-Doan Phan, *Prepackaged Plans in 24 Hours*, AM. BANKR. INST. J., Sept. 2019, at 28–29, 60, https://s3.amazonaws.com/abi-org-corp/journals/news_09-19.pdf [<https://perma.cc/JJ86-WB86>]. In numerous cases, debtors' counsel have successfully pushed a chapter 11 case from petition filing to plan confirmation in just a few days or less.

The two quotes at the outset of this Article endorse the twin values of expediency and efficiency. Yet the first statement refers to subchapter V, and the second refers to a chapter 11 prepack. Despite sharing a common objective, these two mechanisms operate quite differently. Subchapter V accomplishes speed through explicit, congressionally approved provisions that shorten timelines and promote negotiation between the debtor and its creditors.¹⁵ In stark contrast, ultra-expedited prepacks are a development of zealous advocacy—to some, overzealous—by bankruptcy attorneys, greenlit by bankruptcy judges who approve the model by collapsing the default deadlines set forth in the Bankruptcy Code.

These two phenomena should be analyzed together. The rise of prepacks¹⁶ and the creation of subchapter V¹⁷ each generated professional and scholarly discussion. Many of the reasons debtors choose to file prepacks—increased speed, reduced uncertainty, and decreased costs—can be accomplished for many small business debtors through a small business prepack. This Article, however, is the first piece of

See, e.g., Order Approving the Debtors' Disclosure Statement for, and Confirming, the Debtors' Joint Prepackaged Chapter 11 Plan, *In re Belk, Inc.*, No. 21-30630 (Bankr. S.D. Tex. Feb. 24, 2021), ECF No. 61 (less than twenty-four hours); Order (I) Approving the Disclosure Statement and Confirming the Joint Prepackaged Plan of Reorganization of SunGard Availability Services Capital, Inc. and Its Debtor Affiliates Pursuant to Chapter 11 of the Bankruptcy Code and (II) Granting Related Relief, *In re SunGard Availability Servs. Cap., Inc.*, No. 19-22915 (Bankr. S.D.N.Y. May 2, 2019), ECF No. 46 (less than twenty-four hours).

¹⁵ *See* Small Business Reorganization Act of 2019, Pub. L. No. 116-54, 133 Stat. 1079 (codified as amended at 11 U.S.C. § 1181 *et seq.*). A consensual plan is a reorganization plan under chapter 11 that has been agreed to and approved by the various classes of creditors involved in the bankruptcy case. *See* 11 U.S.C. § 1129(a)(8).

¹⁶ Some of the most prominent critics of the super-fast prepack strategy include Professor Lynn LoPucki, who describes the *Belk* prepack as part of “[c]hapter 11’s [d]escent into [l]awlessness,” and Professor Adam Levitin, who describes the super-fast prepacked bankruptcy case as a “24-[h]our [d]rive-[t]hru [b]ankrupt[y].” *See* Lynn M. LoPucki, *Chapter 11’s Descent into Lawlessness*, 96 AM. BANKR. L.J. 247, 247 (2022); Adam J. Levitin, *Purdue’s Poison Pill: The Breakdown of Chapter 11’s Checks and Balances*, 100 TEX. L. REV. 1079, 1099–1103 (2022).

¹⁷ For example, in 2020, then-Professor, now-Bankruptcy Judge Christopher G. Bradley published an incisive assessment of strategies for creditors under subchapter V. 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 (2020). Bradley focused on the creditors’ perspective, concluding (among other things) that they should resist delay and avoid holding general unsecured claims. *See id.* at 254–56. Due to the focus on creditor-driven strategies, Bradley’s assessment does not cover whether a small business prepack is possible or desirable. For other excellent treatments of the SBRA, see Brook E. Gotberg, *Reluctant to Restructure: Small Businesses, the SBRA, and COVID-19*, 95 AM. BANKR. L.J. 389 (2021) (cataloguing and analyzing results of interviews with forty-three small business owners or managers in Columbia, Missouri in the first few months of the COVID-19 pandemic), and Nicole C. Cipriano, Note, *The Big Short: How the Big Step of the Small Business Reorganization Act Fell Short*, 50 HOFSTRA L. REV. 145 (2021) (discussing the SBRA and advocating for improvements).

scholarship—of which the Authors are aware—to analyze how the two might interrelate.

This scarcity of scholarship may be in part because, despite many thousands of subchapter V cases filed since its inception, bankruptcy courts have yet to see a prototypical subchapter V prepack. But change may be on the horizon. In 2023, a restructuring group at Akerman LLP achieved what this Article dubs a “functional prepack” under subchapter V.¹⁸ In *In re BPI Sports*,¹⁹ the debtor “locked up” most of the votes through a restructuring support agreement (“RSA”) before filing bankruptcy. After filing, the debtor solicited votes and successfully confirmed its plan in just thirty-three days.²⁰ This approach, what one might call a “functional” or “lock-up” prepack because votes were cast after entering court, heralds the arrival of the small business prepack.

Still, no other debtor has attempted a prepack under subchapter V.²¹ Part of this is because not every small business debtor fits the mold for a prepack. Another chunk of this void is because bankruptcy practitioners are still coming to understand subchapter V. Conversely, the central promise of the prepack is certainty and speed. Without these elements, parties will hesitate to commit upfront to a prepack strategy. As the contours of subchapter V have become clearer, the bankruptcy bar is inching toward the true small business prepack. Small business debtors are pushing for faster and faster confirmation of their plans. And some debtors have filed plans of reorganization alongside their petitions as a sort of initial offer for negotiations.²² For certain debtors, the prepack strategy represents the cutting edge of subchapter V practice—or so this Article argues.

The legislative innovations of subchapter V clear the way for small business prepack bankruptcies and address the most serious concerns of the prepack’s detractors. Beyond that, small businesses are already less susceptible to some of bankruptcy’s other problems, most notably forum and judge shopping.²³ As numerous scholars have underscored,

¹⁸ See *In re BPI Sports*, Case No. 23-17463 (Bankr. S.D. Fla. Oct. 20, 2023). To our knowledge, *In re BPI Sports* is the first subchapter V prepack to date. See *infra* Section IV.B for more about this case.

¹⁹ Case No. 23-17463 (Bankr. S.D. Fla. Oct. 20, 2023).

²⁰ See *infra* Section I.C.

²¹ At least to our knowledge.

²² In his testimony to the Subchapter V Task Force, Attorney Daniel Etlinger noted that a growing number of debtors are filing “first day plans” that they “present[] as an opening offer to the creditors anticipating there will be negotiated modifications.” Daniel Etlinger, *Post Hearing Written Statement of Daniel Etlinger*, AM. BANKR. INST. 2 (Sept. 8, 2023), https://abi-subv.s3.amazonaws.com/statements/Daniel_Etlinger_Post-Hearing_Statement.pdf?VersionId=xkdJcJozw93YHlr7L-cWJyK0zp1eIMGLp [https://perma.cc/36J9-5SS7].

²³ For an overview of forum shopping, see, for example, Sarah Jones, Note, *Ameliorating Bankruptcy’s Forum Shopping Crisis Through Abstention and Venue Transfer*, 76 FLA. L. REV. 405 (2024); Adam J. Levitin, *Judge Shopping in Chapter 11 Bankruptcy*, 2023 U. ILL. L. REV. 351 (2023).

bankruptcy's loose venue rules allow national conglomerates to file in almost any district they like,²⁴ leading to a proverbial "race to the bottom."²⁵ Although big businesses can file almost anywhere, small businesses are much more likely to file for bankruptcy where they are headquartered or incorporated.

This Article proceeds in four parts. Part I delves into the historical underpinnings of subchapter V and explores its unique procedures that make it an ideal choice for small business debtors seeking to restructure quickly. Part II analyzes how chapter 11 prepacks have reshaped chapter 11 cases despite certain limitations they may pose. Part III steps back to provide a theoretical lens on subchapter V and prepacks, elucidating why the speed of a prepack can best be achieved within the subchapter V framework. The new subchapter helps assuage the concerns of critics of ultra-expedited prepacks, most notably Professor Lynn LoPucki. Finally, Part IV walks through what a small business prepack would look like and proposes concrete suggestions to further streamline prepacks under subchapter V so that the model adheres to the subchapter's legislative goals.

American small businesses, their founders, and their creditors deserve a bankruptcy model that works for them. Subchapter V is the best solution to date. At the same time, the intense pace of the prepack strategy has put pressure on the bankruptcy system, streamlining the process but undermining its legitimacy and transparency. This Article argues that subchapter V presents an appropriate channel for fast-track bankruptcies and sketches out how the bankruptcy bench and bar can best take advantage of it.

I. A NEW ERA FOR SMALL BUSINESS BANKRUPTCY

Small businesses and their founders face challenges from the onset: intense competition, limited resources, evolving markets, and more. When small businesses fall into economic or financial trouble, they can face acute and persistent financial distress. During these periods of

See generally LYNN M. LOPUCKI, *COURTING FAILURE: HOW COMPETITION FOR BIG CASES IS CORRUPTING THE BANKRUPTCY COURTS* (2005).

²⁴ 28 U.S.C. § 1408(1) allows a business debtor to file in either its state of incorporation or the state where its principal place of business is located. 28 U.S.C. § 1408(1). On its own, that provision might lead to a concentration of bankruptcy cases in Delaware, where many businesses are incorporated, but it would not allow forum shopping otherwise. *See id.* But 28 U.S.C. § 1408(2) allows a debtor to file in the district where a case of its affiliate is pending. *Id.* § 1408(2). Thus, a large corporate family can select (or incorporate) a subsidiary almost anywhere it likes, file the subsidiary into bankruptcy, then follow with the rest of the corporate family on the basis of subsection (2). *See id.*

²⁵ *See, e.g.,* LoPucki, *supra* note 16, at 250; Levitin, *supra* note 16, at 1128–50; Brook E. Gotberg, *The Market for Bankruptcy Courts: A Case for Regulation, Not Obliteration*, 49 *BYU L. REV.* 647 (2024).

financial instability, entrepreneurs or subsequent owners may turn to bankruptcy for a potential solution to their companies' financial woes,²⁶ which are often entwined with the owners' own financial futures. The United States bankruptcy system—long admired around the globe—can preserve the value of a small business as a going concern, giving the company breathing room to negotiate with creditors and a chance to restructure its financial obligations.

Until recently, though, small businesses in financial distress had two options under the Bankruptcy Code—filing for chapter 7 or chapter 11 bankruptcy relief. And neither option was attractive to small businesses or their owners. Filing a petition in bankruptcy under the Code creates an estate comprising the debtor's assets.²⁷ In chapter 7, creditors elect a trustee to liquidate these assets and use the proceeds to repay the debtor's debts.²⁸ Since the assets will be sold, chapter 7 liquidation cannot satisfy the evergreen optimism of a founder who hopes to retain control of her business and continue operating after the bankruptcy.²⁹

Chapter 11 offers a different path, allowing a debtor to restructure its debts through a court-approved plan while retaining control over its business operations during the case and possibly afterward as the “debtor in possession.”³⁰ But chapter 11 is inhospitable to many small businesses for other reasons. The bankruptcy court supervises the restructuring process, and the debtor must follow stringent guidelines to have its plan confirmed and a discharge granted. As a result, chapter 11 is time- and labor-intensive—as well as expensive.³¹ This practical reality left small businesses as “bankruptcy misfits,” as Professor Laura Coordes terms them.³²

²⁶ See David A. Mawhinney, *Written Statement of David A. Mawhinney*, AM. BANKR. INST. 7 (June 9, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/David_Mawhinney_State-ment.pdf [<https://perma.cc/N9BH-A2U2>] (“[B]ankruptcy relief remains the best tool we have to truly repair and restore the nodes in our economy.”).

²⁷ 11 U.S.C. § 541(a).

²⁸ *Id.* §§ 702, 704(a)(1) (“The trustee shall . . . collect and reduce to money the property of the estate for which such trustee serves, and close such estate as expeditiously as is compatible with the best interests of parties in interest.”).

²⁹ *Id.* § 541(a)–(b) (describing which property is included in the estate). Individual debtors (who are not the focus of this Article) can also exempt certain property from the estate under section 522(b). *See id.* § 522(b).

³⁰ *Id.* § 1107 (allowing the debtor to step into the shoes of the chapter 11 trustee as the “debtor in possession”); *see also* Grant M. Hayden & Matthew T. Bodie, *Codetermination in Theory and Practice*, 73 FLA. L. REV. 321, 348 (2021) (noting that the U.S. bankruptcy system relies on a “debtor-in-possession running the show”).

³¹ *See* Laura N. Coordes, *Bespoke Bankruptcy*, 73 FLA. L. REV. 359, 378 (2021) (“Chapter 11, designed primarily with large businesses in mind, was often too expensive and demanding for a small business debtor.”).

³² *Id.* at 377 (“Small business debtors were bankruptcy misfits because the available Bankruptcy Code chapters did not work well for them.”).

In 2019, Congress enacted the SBRA to help small businesses navigate bankruptcy more effectively.³³ The SBRA created a new subchapter V within chapter 11 of the Bankruptcy Code, another form of what Coordes calls “bespoke bankruptcy,” and what one of the Authors (riffing off of Coordes) has called “tailored bankruptcy.”³⁴ Subchapter V was designed to simplify the complex requirements of chapter 11, shorten the length of cases, and reduce associated costs.³⁵ This Part sets out the origins and framework of subchapter V, showing its promise for a streamlined insolvency proceeding for small business debtors.

A. *The Origins of Subchapter V*

Congress has long wrestled with the problem of expediting a bankruptcy case while ensuring consistency, fairness, and accessibility.³⁶ Chapter 11 bankruptcy was intended to establish “a framework for reorganizing a bankrupt business.”³⁷ Since over 99.7% of businesses with paid employees in the United States are small businesses,³⁸ it would make sense for the Bankruptcy Code to account for their lack of resources and need for speed compared with large enterprises. Unfortunately, this has not been the case. Chapter 11 takes too much time and money for it to be a viable solution for many small businesses. Before the SBRA, bankruptcy judges and federal legislatures tried several times to solve this problem—all of which were incomplete solutions.

Shortly after the Bankruptcy Code’s enactment in 1978,³⁹ bankruptcy judges realized the need for quick bankruptcies for small business

³³ Small Business Reorganization Act of 2019, Pub. L. No. 116-54, 133 Stat. 1079 (codified as amended at 11 U.S.C. §§ 1181 *et seq.*).

³⁴ See Coordes, *supra* note 31, at 359, 377–78; Christopher D. Hampson, *Bespoke, Tailored, and Off-the-Rack Bankruptcy: A Response to Professor Coordes’s ‘Bespoke Bankruptcy’*, 73 FLA. L. REV. F. 15, 19 & n.33 (2023).

³⁵ See Paul W. Bonapfel, *A Guide to the Small Business Reorganization Act of 2019*, 93 AM. BANKR. L.J. 571, 574 (2019); see also *In re Keffer*, 628 B.R. 897, 910 (Bankr. S.D. W. Va. 2021) (“It is a brave new world for bankruptcy courts following enactment of the SBRA. SubChapter V is a valuable tool for qualifying debtors and will facilitate reorganizations that were not possible before.”).

³⁶ H.R. REP. NO. 116-171, at 3 (2019).

³⁷ *Mission Prod. Holdings, Inc. v. Tempnology, LLC*, 587 U.S. 370, 373 (2019).

³⁸ *Frequently Asked Questions*, U.S. SMALL BUS. ADMIN. OFF. OF ADVOC. (Oct. 2020), <https://advocacy.sba.gov/wp-content/uploads/2020/11/Small-Business-FAQ-2020.pdf> [<https://perma.cc/JEH3-9K22>].

³⁹ Small business reforms predate the Bankruptcy Code, of course. They were a major part of the bankruptcy reforms of the 1938 Chandler Act. See DOUGLAS G. BAIRD, *THE UNWRITTEN LAW OF CORPORATE REORGANIZATIONS* 109 (2022). Under the Act, small businesses would generally reorganize under Chapter XI, which gave more control to prebankruptcy directors. See *id.* at 103, 109. Although Congress initially required absolute priority in Chapter XI, it eventually dropped the requirement. See *id.* at 77, 107, 109.

debtors.⁴⁰ Judges used their discretionary power to speed up cases for small businesses.⁴¹ They set early deadlines for the debtor to file its bankruptcy plan while simultaneously reviewing the debtor's disclosure statement.⁴² And by consolidating the final disclosure approval with the plan confirmation hearing, their innovations seemed to work for some debtors.⁴³ But the sporadic adoption of these processes sparked concerns about consistency, transparency, and legitimacy.⁴⁴

In 1994, Congress responded with the Bankruptcy Reform Act of 1994 ("BRA").⁴⁵ This act codified the fast track option for small businesses in chapter 11 that allowed a court to conditionally approve the disclosure statement, combine the disclosure statement hearing with the plan confirmation hearing, or even determine that "the plan itself provides adequate information and that a separate disclosure statement is not necessary."⁴⁶ Under the BRA, a debtor could file a chapter 11 petition and begin soliciting votes on a plan immediately after filing.⁴⁷

Approximately three years later, however, the National Bankruptcy Review Commission found the modified small business bankruptcy procedures under the BRA inadequate.⁴⁸ To be sure, small businesses benefited from various provisions of the "fast track" option, including the automatic stay and retention of business operations.⁴⁹ But too often, a business's ability to delay filing its chapter 11 plan only prolonged

⁴⁰ Brian A. Blum, *The Goals and Process of Reorganizing Small Businesses in Bankruptcy*, 4 J. SMALL & EMERGING BUS. L. 181, 206 (2000).

⁴¹ *Id.*

⁴² Cipriano, *supra* note 17, at 153. A plan confirmation hearing is where the bankruptcy judge reviews and approves or denies a proposed repayment plan for a debtor's debts. See 11 U.S.C. §§ 1128–1129.

⁴³ Cipriano, *supra* note 17, at 153; see also 11 U.S.C. §§ 1128–1129.

⁴⁴ See Blum, *supra* note 40, at 208 (noting that "the creation by courts of an innovative discretionary procedure raises a more general policy concern: A discretionary process, not mandated or regulated by the Code, is not universally adopted and, even where it is used, can vary quite significantly in the details of its scope and nature").

⁴⁵ Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 217, 108 Stat. 4106.

⁴⁶ 11 U.S.C. § 1125(f).

⁴⁷ See Jeffrey T. Kucera, Margaret R. Westbrook, David A. Mawhinney & Javier A. Roldan Cora, *Small Business Debtor Reorganization: An Overview of Chapter 11's New Subchapter V*, K&L GATES (Sept. 23, 2019), <https://www.klgates.com/Small-Business-Debtor-Reorganization-An-Overview-of-Chapter-11s-New-Subchapter-V-09-23-2019> [<https://perma.cc/EA2F-DGTS>].

⁴⁸ See James B. Haines Jr. & Philip J. Hendel, *No Easy Answers: Small Business Bankruptcies After BAPCPA*, 47 B.C. L. REV. 71, 74–75 (2005); see also Daniel O'Hare, Note, *The Long and Winding Road to the Small Business Reorganization Act: Why Our Next Stop Should Be Simplicity and Accessibility*, 124 W. VA. L. REV. 567, 578 (2022).

⁴⁹ See Haines Jr. & Hendel, *supra* note 48, at 74.

its ultimate failure.⁵⁰ Even with some incremental successes, the BRA left much to be desired for small businesses and was the catalyst for an additional wave of legislative reform—the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (“BAPCPA”).⁵¹

In addition to its other goals, BAPCPA attempted to streamline chapter 11 reorganizations for small businesses.⁵² BAPCPA retained a small business debtor’s ability to “fast track” its chapter 11 case and further tightened the deadlines in such cases.⁵³

It was not enough. From 2008 to 2015, only 27% of the 18,000 small businesses that filed for chapter 11 had a successful reorganization.⁵⁴ Those figures do not include the small businesses that never filed a bankruptcy petition in the first place “because the Bankruptcy Code [was] seen as broken and unworkable.”⁵⁵ It was clear bankruptcy was still impractical for many small businesses.⁵⁶ Even if a small business wanted to circumvent the small business provisions, a standard “[c]hapter 11 [was] . . . too slow and too costly for the majority of

⁵⁰ See O’Hare, *supra* note 48, at 578.

⁵¹ Pub. L. No. 109-8, 119 Stat. 23, 59. BAPCPA had an enormous impact when it went into effect. See Richard M. Hynes, *Broke but Not Bankrupt: Consumer Debt Collection in State Courts*, 60 FLA. L. REV. 1, 29 (2008) (“[BAPCPA] went into effect in October 2005 and had an immediate and dramatic effect on the number of bankruptcy filings.”).

⁵² Robert J. Landry III, *Subchapter V and the COVID-19 Disruption: Did Congress Get Small Business Bankruptcy Reform Right This Time?*, 16 OHIO ST. BUS. L.J. 66, 72 (2021).

⁵³ See David L. Bury Jr., *ABI Commission Report—Small and Medium-Sized Debtor Enterprises*, PLAN PROONENT (Aug. 18, 2015), www.planproponent.com/2015/08/abi-commission-report-small-and-medium-sized-debtor-enterprises [<https://perma.cc/3Q2C-AJJB>]. Under BAPCPA, a small business debtor had the exclusive right to file a plan during the first 180 days of the case (compared with 120 days for non-small-business debtors) and had to file a plan within 300 days of filing its petition. 11 U.S.C. § 1121(b), (e)(1)–(2). Additionally, the court was required to confirm a small business plan (so long as it met all the requirements) within forty-five days after the debtor filed it. *Id.* § 1129(e). Courts could grant extensions to these timelines only if the debtor could demonstrate that it would “more likely than not” get a plan confirmed within the enlarged period. *Id.* § 1121(e)(3).

⁵⁴ *Oversight of Bankruptcy Law and Legislative Proposals: Hearing Before the Subcomm. on Antitrust, Com., & Admin. L. of the H. Comm. on the Judiciary*, 116th Cong. 52 (2019) (statement of Robert J. Keach), <https://docs.house.gov/meetings/JU/JU05/20190625/109657/HHRG-116-JU05-Wstate-KeachR-20190625.pdf> [<https://perma.cc/BV37-BQRF>].

⁵⁵ *Id.* at 52.

⁵⁶ See Small Testimony, *supra* note 1, at 1. Unlike regular chapter 11 cases where creditors play an oversight role that is crucial for a case’s success, creditors in small business cases are largely absent because “creditors in these smaller cases do not have claims large enough to warrant the time and money to participate actively in these cases.” H.R. REP. NO. 116-171, at 3 (2019).

middle market companies to do anything other than sell its going concern assets in a 363 sale⁵⁷ or to simply liquidate the company.”⁵⁸

In 2009, the National Bankruptcy Conference (“NBC”) formed a group to study small business bankruptcies.⁵⁹ The group found that “chapter 11 generate[d] exorbitant administrative costs, and chapter 11 include[d] requirements such as a high voting threshold and elaborate disclosures” that presented “roadblocks to reorganization.”⁶⁰ The NBC proposed adding a subchapter to chapter 11 that was specifically tailored to the needs of small businesses.

Similarly, in 2012, the American Bankruptcy Institute (“ABI”) formed a commission to study and recommend a reform of chapter 11 for small businesses.⁶¹ The commission drafted a report that mirrored many of the NBC’s concerns about the chapter 11 provisions hindering successful reorganizations.⁶²

⁵⁷ Section 363 of the Code allows the bankruptcy trustee to sell assets of the estate (up to the entire company) and use the proceeds to pay claims. See 11 U.S.C. § 363. Section 363 sales have become so prevalent that two prominent bankruptcy scholars announced that they spelled the “[e]nd of [b]ankruptcy.” See Douglas G. Baird & Robert K. Rasmussen, *The End of Bankruptcy*, 55 STAN. L. REV. 751, 751–55, 777–78, 787 (2002). For a description of 363 sales, see, for example, Kimon Korres, *Bankrupting Bankruptcy: Circumventing Chapter 11 Protections Through Manipulation of the Business Justification Standard in § 363 Asset Sales, and a Refined Standard to Safeguard Against Abuse*, 63 FLA. L. REV. 959, 960 (2011) (“Section 363(b) of the Bankruptcy Code authorizes a Chapter 11 debtor-in-possession . . . to ‘use, sell, or lease’ estate property outside the ordinary course of business. Section 363 sales tend to be cheaper and more time efficient than reorganization alternatives.”). Whether section 363 sales produce values sufficiently close to market value has been the subject of intense debate. See, e.g., Jean-Marie Meier & Henri Servaes, *The Bright Side of Fire Sales*, 32 REV. FIN. STUD. 4228, 4231 (2019); James J. White, *Bankruptcy Noir*, 106 MICH. L. REV. 691, 692 (2008); Lynn M. LoPucki & Joseph W. Doherty, *Bankruptcy Fire Sales*, 106 MICH. L. REV. 1, 3–4 (2007).

⁵⁸ Dan Dooley, *Dan Dooley Comments to ABI Commission Studying Chapter 11 Reform* (Apr. 18, 2013), <https://commission.abi.org/sites/default/files/statements/19apr2013/ABI%20Testimony.pdf> [<https://perma.cc/JEV3-F4QT>]; see also Elizabeth Warren & Jay Lawrence Westbrook, *The Success of Chapter 11: A Challenge to the Critics*, 107 MICH. L. REV. 603, 636 (2009) (“[T]he costs of Chapter 11 are sufficiently high that many small companies were squeezed out of the system, forcing the managers to liquidate the business quickly in Chapter 7 or die quietly completely outside the bankruptcy system.”); Michael St. James, *Statement for ABI Subchapter V Task Force*, AM. BANKR. INST. (June 9, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/Michael_StJames_Statement.pdf [<https://perma.cc/Y3UY-EJRW>] (“I had never seen a successful Chapter 11 that did not incur at least \$100,000 in Chapter 11 attorney’s fees and . . . a ‘fast’ reorganization would still likely take at least 8 months.”).

⁵⁹ Small Testimony, *supra* note 1, at 1.

⁶⁰ *Id.* at 117.

⁶¹ See AM. BANKR. INST., COMMISSION TO STUDY THE REFORM OF CHAPTER 11 at 2 (2014), <https://abiworld.app.box.com/s/vvircv5xv83aav14dp4h> [<https://perma.cc/396R-KK4E>].

⁶² See *id.*

Congress used the ABI and NBC reports as a framework for the SBRA, which took effect on February 19, 2020.⁶³ Although the SBRA differed slightly from the ABI's proposed procedures, Congress's intent remained consistent with the ABI's recommendation to streamline bankruptcy for small business debtors.⁶⁴

B. *New Framework for Small Businesses*

Congress created subchapter V to provide small business debtors with a more efficient, less expensive, and more obtainable path to a chapter 11 discharge.⁶⁵ The subchapter contains several key innovations that streamline the process. Some of those innovations—the ones that made headlines—make subchapter V more attractive for entrepreneurs. Under the subchapter, debtor companies can receive a discharge if they pay off their secured debt and pay their disposable income to unsecured creditors for three to five years. After the discharge, the founder of the company can retain ownership and control of the company. This innovation makes bankruptcy more palatable to ever-optimistic founders and represents a departure from bankruptcy's famous absolute priority rule.⁶⁶ Less dramatically, but no less important, subchapter V also gets rid of the required quarterly fees to the Office of the United States Trustee (“U.S. Trustee”), a division of the Department of Justice and bankruptcy's watchdog.⁶⁷

The following discussion, however, emphasizes how subchapter V might pave the way for a small business prepack. Specifically, the SBRA (1) set forth broad debtor eligibility, (2) compressed early case deadlines, (3) reduced the cast of estate professionals, and (4) gave the debtor in possession tighter control over the plan confirmation process. Each is covered in turn.

⁶³ *Subchapter V Small Business Reorganizations*, U.S. DEP'T JUST. (Mar. 5, 2024), <https://www.justice.gov/ust/subchapter-v> [<https://perma.cc/WW4X-ZH9Y>]; *President Signs Small Business Reorganization Act into Law*, AM. BANKR. INST. (Aug. 23, 2019), <https://www.abi.org/newsroom/press-releases/president-signs-small-business-reorganization-act-into-law> [<https://perma.cc/JMC3-YPSX>].

⁶⁴ The key term here is *debtors*. As attorney Michael St. James artfully framed it, “Congress has appropriately established two reorganization regimes. In traditional Chapter 11, fairness to creditors takes precedence over expense and delay. In Sub V, access for small businesses and the concomitant requirements of speed and inexpensiveness take precedence over some creditor rights.” St. James, *supra* note 58.

⁶⁵ H.R. REP. NO. 116-171, at 1 (2019).

⁶⁶ The absolute priority rule requires that the plan pay senior creditors in full before junior creditors can receive any distribution. *See infra* Section I.B.4.

⁶⁷ 28 U.S.C. § 1930(a)(6) (excepting cases under subchapter V from quarterly U.S. trustee fees based on disbursements from the estate).

1. Broad Debtor Eligibility

First, subchapter V is available to a wide swath of financially distressed firms.⁶⁸ Although subchapter V is only available to small business debtors, the statutory definition is more capacious than many people realize.⁶⁹ Professor Robert Lawless calculated that approximately 40% of chapter 11 debtors in cases filed after October 2007 would have qualified.⁷⁰

To qualify, a debtor must be “engaged in commercial or business activities”⁷¹ and have “aggregate noncontingent liquidated secured and unsecured debts” as of the date of the petition of no more than

⁶⁸ See Craig Goldblatt, *Remarks of Craig Goldblatt*, AM. BANKR. INST. 1 (July 14, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/Craig_Goldblatt_Written_Statement.pdf [<https://perma.cc/TL9S-GLBL>] (“Is every subchapter V case that files before us the kind of case that Congress had in mind when it enacted the Small Business Reorganization Act of 2019—the corner grocer or local dry cleaner, run by a hard-working entrepreneur who has hit a bump in the road and is looking to save his small business? No.”).

⁶⁹ Subchapter V requires a qualifying debtor to elect its application. FED. R. BANKR. P. 1020 (requiring a voluntary debtor to state in its petition, and an involuntary debtor to state within fourteen days of the order for relief, whether it is a small business debtor and whether it is electing to proceed under subchapter V of chapter 11). A qualifying debtor who does not elect subchapter V will proceed under chapter 11’s regular rules, unless it is small enough to fit within the definition of a “small business debtor” under the BRA, which has a much lower cap of \$2 million in qualifying debt. See 11 U.S.C. § 101(51D)(A).

⁷⁰ Bob Lawless, *How Many New Small Business Chapter 11s?*, CREDIT SLIPS (Sept. 14, 2019, 4:28 PM), www.creditslips.org/creditslips/2019/09/how-many-new-small-business-chapter-11s.html [<https://perma.cc/35UF-ALU3>]; see also Paul W. Bonapfel, *A Guide to the Small Business Reorganization Act of 2019*, U.S. BANKR. CT. N.D. GA. 3 (June 2022), https://www.ganb.uscourts.gov/sites/default/files/sbra_guide_pwb.pdf [<https://perma.cc/NG87-BGLX>]. Professor Lawless made his calculation when the debt limit for a subchapter V debtor was \$2.7 million.

⁷¹ 11 U.S.C. § 1182(1)(A). For a thorough overview of the developing case law of the phrase “commercial or business activities,” see Christopher G. Bradley, “*Commercial or Business Activities*” and *Subchapter V Eligibility*, 43 BANKR. L. LETTER 1 (2023). Some commentators believe that the statutory language requiring a subchapter V debtor to be engaged in a “commercial or business activity” does not limit debtors to those engaged in business or commercial activities when they file for bankruptcy. See, e.g., *In re Wright*, Case No. 20-01035, 2020 WL 2193240, at *3 (Bankr. D. S.C. Apr. 27, 2020) (“The definition of a ‘small business debtor’ is not restricted to a person who at the time of the filing of the petition is presently engaged in commercial or business activities and who expects to continue in those same activities under a plan of reorganization.” (quoting 2 COLLIER ON BANKRUPTCY ¶ 101.51D (16th ed. 2020))). Numerous courts have addressed the issue and reached differing opinions. Compare *In re Vertical Mac Constr., LLC*, No. 6:21-BK-01520, 2021 WL 3668037, at *3 (Bankr. M.D. Fla. July 23, 2021) (holding that debtor was eligible for subchapter V despite not having business operations because the inclusion of “activities” under the statute includes “maintaining bank accounts, having accounts receivable, analyzing claims and winding down its business”), and *Wright*, 2020 WL 2193240, at *2–3 (holding debtor who sold all assets and was no longer operating a business met the statutory definition of a small business debtor because he was “‘engaged in commercial or business activities’ by addressing residual business debt”), with *In re Thurmon*, 625 B.R. 417, 422 (Bankr. W.D. Mo. 2020) (reasoning that “[t]he plain meaning of ‘engaged in’ means to be actively and currently involved. . . . ‘engaged in’ is written not in the past or future but in the present tense”), and *Nat’l Loan Invs., L.P. v. Rickerson* (*In re Rickerson*), 636

a statutorily defined limit,⁷² “excluding debts owed to . . . affiliates or insiders,” most of which must arise “from the commercial or business activities of the debtor.”⁷³ That definition sounds more restrictive than it really is: it does not include contingent debts, unliquidated debts, or debts owed to affiliates or insiders.⁷⁴ As an illustration, Imagine GatorCo is a retail store with estimated liabilities of \$40 million, far above the nominal limit for subchapter V, which, for our purposes, we will set at \$7.5 million, the debt limit for most of subchapter V’s existence so far. GatorCo is a defendant in a slip-and-fall case where it estimates its liability will be \$8 million. It has a \$12 million mortgage note owed to its parent company, a \$15 million secured note also owed to its parent company, and a \$5 million outstanding balance owed to its suppliers.

Although GatorCo’s total debts far exceed the \$7.5 million limit, the company may still be eligible for subchapter V because the only

B.R. 416, 423 (Bankr. W.D. Pa. 2021) (holding that eligibility requires the debtor to be engaged in commercial or business activity on the petition date).

⁷² See 11 U.S.C. § 1182(1)(A). Congress initially set the debt limit for subchapter V debtors at \$2,725,625 and then temporarily increased it to \$7.5 million under the Coronavirus Aid, Relief, and Economic Security Act. See Jeffrey Katz, *Tracking the Up(s) and Down of the SBRA Debt Limit, in FIVE SECRETS TO A MAGICAL SUB-V*, 3–4 (Oct. 2022), <https://ncbjmeeting.org/2022/materials/NCBJ%20Five%20Secrets%20to%20Magical%20Sub-V.pdf> [<https://perma.cc/B5UM-VQK4>] (discussing amendments to subchapter V’s debt limit). There is broad consensus that the subchapter V debt limit increase should be permanent. See, e.g., AM. BANKR. INST., FINAL REPORT OF THE AMERICAN BANKRUPTCY INSTITUTE SUBCHAPTER V TASK FORCE 10 (2024) [hereinafter ABI FINAL REPORT], https://abi-org.s3.amazonaws.com/Newsroom/ABI_SubV_TaskForce_FinalReport_Embargoed.pdf [<https://perma.cc/6MS7-GLEM>] (recommending that “eligibility for Subchapter V should remain at \$7,500,000 . . .”).

Unfortunately, before this Article went to print, Congress has not acted to extend or make permanent the debt limit and the relief sunsetted on June 21, 2024. See Joy Kleisinger, *The Expiration of the Increased Subchapter V Debt Limit and Its Impact on Small Business Debtors*, AM. BANKR. INST. J., Mar. 2024, at 8, 48. The debt limit has reverted to \$3,024,725 until it increases for inflation on April 1, 2025, or Congress adjusts it. See *id.* at 8, 48. Some commentators have compared subchapter V’s debt limit to chapter 12’s \$11 million debt limit for family farmers. See Coordes, *supra* note 31, at 370, 379; see also 11 U.S.C. §§ 101(18), 109(f). While subchapter V may benefit from a higher debt limit, a comparison between the two chapters cannot be straightforwardly made because the debt that qualifies in each chapter differs—the chapter 12 debt limit counts all secured and unsecured debts, whereas the subchapter V debt limit counts the more limited set of debts described above. See *id.*; *id.* at § 1182(1)(A).

⁷³ 11 U.S.C. § 1182(1)(A).

⁷⁴ See *id.* Even with the expansive definition, practitioners should remain hesitant to elect subchapter V for an ineligible debtor. See, e.g., *In re Sullivan*, 626 B.R. 326 (Bankr. D. Colo. 2021) (converting a case to chapter 7 after holding debtor filed in bad faith and finding debtor’s debt made him ineligible for subchapter V); *In re Phenomenon Mktg. & Ent., LLC*, No. 2:22-BK-10132, 2022 WL 1262001 (Bankr. C.D. Cal. Apr. 28, 2022) (converting a case to a standard chapter 11 after holding debtor was an affiliate of an ineligible corporation and not a small business). A debtor is also ineligible for subchapter V if its primary activity is the business of owning single-asset real estate, it is a corporation subject to reporting requirements under the Securities Exchange Act of 1934, or it is a member of a group of affiliated debtors of a corporation subject to the reporting requirements of the Securities and Exchange Act of 1934. 11 U.S.C. § 1182(1).

qualifying debt to establish its eligibility is the \$5 million debt owed to suppliers. GatorCo's mortgage and secured note owed to its parent company are excluded from eligibility calculations under 11 U.S.C. § 1182(a) because they are owed to affiliates. Similarly, any damages from the slip-and-fall litigation are not yet liquidated. So long as GatorCo's other debts are less than \$2.5 million, it can file for subchapter V bankruptcy.⁷⁵

With these carve-outs, the term "small business" is somewhat misleading. The businesses are not as small as they might seem, and in the aggregate, the subchapter can cover a wide swath of financially distressed firms. Small businesses in the United States account for 99.7% of all firms with paid employees.⁷⁶ From a bankruptcy perspective, "approximately 90% of all chapter 11 debtors have less than \$10 million in assets or liabilities, less than \$10 million in annual revenues, and 50 or fewer employees."⁷⁷ Even a debtor who normally would not be eligible for subchapter V may find itself in luck⁷⁸: friendly creditors may be willing to take a "pre-petition 'haircut'" to lower the debtor's debt to under the limit.⁷⁹ Similarly, a debtor could refinance some of its debt with an affiliate or insider so that the debt would not qualify toward the limit.⁸⁰

2. *Compressed Early Case Deadlines*

Second, subchapter V deviates from the chapter 11 model by accelerating deadlines.⁸¹ After a small business debtor files its bankruptcy case, deadlines follow quickly. Within ten days, the initial debtor interview

⁷⁵ 11 U.S.C. § 1182(1)(A).

⁷⁶ See U.S. SMALL BUS. ADMIN. OFF. OF ADVOC., *supra* note 38.

⁷⁷ Michelle Harner, *Rethinking "Small" Business Bankruptcies*, CREDIT SLIPS (Jan. 26, 2015, 6:48 AM), www.creditslips.org/creditslips/2015/01/rethinking-small-business-bankruptcies.html [<https://perma.cc/3SBD-FFS2>].

⁷⁸ *But see* Adam R. Prescott, *Written Statement of Adam R. Prescott*, AM. BANKR. INST. 3 (June 23, 2023), https://abi-subv.s3.amazonaws.com/statements/Adam_Prescott_Post-Hearing_Statement.pdf [<https://perma.cc/KFB6-UWHC>] ("[E]ligibility is a gating issue: Getting through the Subchapter V gate does not mean the debtor ultimately will benefit from the protections and powers of Subchapter V, as that debtor still must satisfy the many other obligations and statutory requirements in the case.").

⁷⁹ Bradley, *supra* note 17, at 265.

⁸⁰ *Id.* at 265 ("It is possible that debtors seeking subchapter V eligibility will try to game the eligibility cap. For instance, a debtor might employ mechanisms to assign debts to non-affiliate insiders . . .").

⁸¹ See *In re Rockland Indus., Inc.*, No. 21-02590, 2022 WL 451542, at *3 (Bankr. D.S.C. Feb. 14, 2022) ("Subchapter V . . . permit[s] small business debtors with the opportunity to reorganize more quickly . . ."); *In re Seven Stars on the Hudson Corp.*, 618 B.R. 333, 340 (Bankr. S.D. Fla. 2020) ("Subchapter V by its very nature is intended to be an expedited process.").

for a subchapter V case occurs.⁸² Within forty-six days, the debtor must submit a status report describing its efforts to reach a consensual plan.⁸³ Fourteen days later—a mere two months after the petition—the court must hold a status conference “to further the expeditious and economical resolution” of the case.⁸⁴ After only ninety days (three months) from the commencement of the case, a debtor must file its plan.⁸⁵ Although subchapter V contains no deadline for plan confirmation and no limit on plan amendments—features that Bankruptcy Judge Christopher G. Bradley points out debtors may use to cause delay⁸⁶—once the plan is filed, the timeline is officially in the hands of the bankruptcy judge.

Subchapter V again departs from chapter 11 by constraining a judge’s authority to grant extensions of the prescribed deadlines. In subchapter V, a judge may only grant an extension to the debtor’s ninety-day deadline to file a plan “if the need for the extension is attributable to circumstances for which the debtor should not justly be held accountable.”⁸⁷ Most courts make this standard very hard to satisfy, citing the legislative intent of subchapter V to facilitate an expedited process.⁸⁸ This standard is a big change from chapter 11, under which enlargement can be granted “for cause,” a loose standard that many bankruptcy judges grant as a matter of course.⁸⁹

Congress has compressed case timelines and hindered opportunities to extend deadlines when it enacted subchapter V. If a debtor does

⁸² See 28 U.S.C. § 586(7) (stating that the U.S. Trustee must conduct the initial debtor interview before the first meeting of creditors).

⁸³ 11 U.S.C. § 1188(c).

⁸⁴ *Id.* § 1188(a).

⁸⁵ *Id.* § 1189(b).

⁸⁶ See Bradley, *supra* note 17, at 272. Even with the notable absence of those deadlines, Bradley agrees that “the subchapter V scheme evidences an overall intention for cases to be prosecuted expeditiously by debtors.” *Id.*

⁸⁷ 11 U.S.C. § 1189(b); see also *In re Seven Stars on the Hudson Corp.*, 618 B.R. 333, 344 (Bankr. S.D. Fla. 2020) (“Based on a plain reading of this phrase, it is a clearly higher standard than the mere ‘for cause’ standard . . .”).

⁸⁸ See, e.g., *In re Trinity Legacy Consortium, LLC*, 656 B.R. 429, 434 (Bankr. D.N.M. 2023) (noting that “[c]ourts agree that § 1189(b) imposes a stricter standard than the ‘for cause’ standard set forth in § 1121(d)(1)”; *In re Online King LLC*, 629 B.R. 340, 344 (Bankr. E.D.N.Y. 2021) (denying a debtor’s motion to extend for failure to satisfy the stringent burden of demonstrating it was entitled to extension and holding that the fact no party in interest opposed debtor’s motion did not relieve the debtor of its burden to establish the extension was warranted); *Seven Stars on the Hudson Corp.*, 618 B.R. at 345 (“Congress purposefully set a short deadline for a debtor to file a plan under Subchapter V, and set a very high standard for an extension of that deadline.”).

⁸⁹ *Seven Stars on the Hudson Corp.*, 618 B.R. at 344.

not want to comply with the swift timeline of a subchapter V case, the solution is simple: do not opt in.⁹⁰

3. *Smaller Cast of Estate Professionals*

Third, subchapter V has simplified the cast of estate professionals who typically sit around the table in a chapter 11 case. This Section briefly outlines the key distinctions in a subchapter V case.

a. *Estate Professionals & Financing*

Subchapter V makes it easier for debtors to work with their long-standing attorneys, accountants, and other professionals throughout the bankruptcy case. Chapter 11 generally prevents professionals with outstanding fees from continuing to represent a debtor after the petition is filed due to the conflict arising from the professional becoming a creditor.⁹¹ Even worse, once a debtor has fallen behind on payments due to its law firm or accountant, it cannot readily avoid the conflict by paying off the debt shortly before the bankruptcy filing; such a payment would be an avoidable preference.⁹²

Large debtors solve this problem by retaining new bankruptcy counsel and paying them from a retainer.⁹³ The bankruptcy counsel releases any prepetition debt to avoid conflicts. That solution, though, requires bringing new professionals up to speed and is too expensive for many small business debtors and their professionals. For subchapter V debtors, however, prepetition professionals are not disqualified so long as their unpaid fees, as of the filing date, do not exceed \$10,000.⁹⁴ In other words, the debtor's counsel do not have to waive all their claims to avoid disqualification, making it easier for debtors to convince their

⁹⁰ See Small Testimony, *supra* note 1, at 6 (“Subchapter V is a voluntary chapter, and if a debtor does not believe it can be reorganized on the fast track . . . the debtor is not compelled to elect to be a small business enterprise debtor under subchapter V.”).

⁹¹ See 11 U.S.C. § 327(a) (providing that the trustee may retain professionals “that do not hold or represent an interest adverse to the estate”); see also Craig R. Tractenberg, John R. Gotaskie Jr. & Keith C. Owens, *Subchapter V Bankruptcy Is Available for Franchise Companies*, 24 FRANCHISE LAW. 16, 16 (2021).

⁹² An avoidable preference is a prepetition payment that improperly prefers one creditor over others similarly situated. See, e.g., *In re Ozcelebi*, 631 B.R. 629, 645 (Bankr. S.D. Tex. 2021) (finding that a \$9,999 prepetition payment to a law firm for unbilled time was allowed under subchapter V after a creditor asserted it was an avoidable preference).

⁹³ See *In re Atlas Contractors, Inc.*, 2004 Bankr. LEXIS 802, at *8 (Bankr. E.D. Ky. June 16, 2004) (“Prior to commencement of a chapter 11 case, it is common for a debtor’s professionals to obtain retainer agreements and fees to insure compensation for costs anticipated during the pendency of the case.”).

⁹⁴ 11 U.S.C. § 1195.

longstanding professionals to continue working with them through the bankruptcy case.

Similarly, subchapter V makes it easier for small business debtors to obtain financing for their case.⁹⁵ Because subchapter V allows a debtor to pay postpetition administrative expenses over a period of three to five years through the plan,⁹⁶ lenders can spread the debtor-in-possession financing repayment throughout the plan. As a result of this increased runway for repayment, subchapter V makes bankruptcy more accessible to many debtors.

b. Committees

In a regular chapter 11 case, the U.S. Trustee appoints a committee of unsecured creditors as a matter of course.⁹⁷ Not so in a case under subchapter V. In small business cases, an unsecured creditors' committee may not be appointed “[u]nless the court for cause orders otherwise.”⁹⁸ This adjustment reflects the fact that small businesses tend to have fewer creditors and a simpler financial profile.

c. Trustees

Instead of an unsecured creditors' committee, subchapter V requires a trustee to be appointed in every case.⁹⁹ The “trustee is unlike any other trustee appointed in the bankruptcy process”¹⁰⁰ because it is the only trustee whose primary function is not to operate or liquidate the estate but to promote a consensual reorganization plan.¹⁰¹ Consistent with this directive, the trustee must attend the status conference where “one function . . . is ‘to encourage and facilitate the attainment of

⁹⁵ See *id.* § 364 (authorizing debtor-in-possession financing to fund the business's ongoing operations during its bankruptcy case, which is designed for debtors that lack the capital required to retain lawyers to prepare its bankruptcy); see also Sandeep Dahiya & Korok Ray, *A Theoretical Framework for Evaluating Debtor-in-Possession Financing*, 34 EMORY BANKR. DEVS. J. 57, 60 (2017).

⁹⁶ 11 U.S.C. § 1192.

⁹⁷ *Id.* § 1102(a)(1).

⁹⁸ *Id.* § 1181(b).

⁹⁹ *Id.* § 1183(a).

¹⁰⁰ Jim White, *Understanding the Purpose of the Subchapter V Trustee*, NCBAR BLOG (Nov. 11, 2021), <https://ncbarblog.com/bk-understanding-the-purpose-of-the-subchapter-v-trustee> [<https://perma.cc/L3DA-BAPG>].

¹⁰¹ See *id.*; U.S. DEP'T JUST., HANDBOOK FOR SMALL BUSINESS CHAPTER 11 SUBCHAPTER V TRUSTEES 1-1 (Feb. 2020) [hereinafter *SBRA Handbook*], https://www.justice.gov/ust/file/subchapterv_trustee_handbook.pdf/dl [<https://perma.cc/95SZ-KSJT>] (describing the most important duties of a subchapter V trustee); see also *In re* 218 Jackson LLC, 631 B.R. 937, 947 (Bankr. M.D. Fla. 2021) (“[T]he subchapter V trustee is the *only* trustee directed to ‘facilitate the development of a consensual plan of reorganization.’ . . . This distinction is significant.” (quoting 11 U.S.C. § 1183(b)(7))).

a consensual plan of reorganization.”¹⁰² That the subchapter V trustee’s role effectively ends upon plan confirmation—along with her fees¹⁰³—provides additional support for their facilitatory function.¹⁰⁴

4. Tighter Plan Control

Fourth, subchapter V gives the debtor tighter control over the plan proposal and confirmation process.

a. No Required Disclosure Statement

In a traditional chapter 11 case, a debtor needs to file a court-approved disclosure statement before votes on a plan can be solicited.¹⁰⁵ Disclosure statements give all parties the information necessary to make an informed vote on the plan.¹⁰⁶ But those statements also drive up the expense of chapter 11¹⁰⁷ and prolong the debtor’s exit from bankruptcy.¹⁰⁸ Subchapter V addressed these costs by eliminating the disclosure statement altogether.¹⁰⁹ Instead, the debtor’s plan must

¹⁰² Small Testimony, *supra* note 1, at 4.

¹⁰³ Subchapter V trustees bill hourly, and their fees can range from \$300 to \$600 per hour. *See* Bradley, *supra* note 17, at 258–59, 261 n.48 (emphasizing that additional administrative fees could be the difference between a plan’s success and its failure). In rare circumstances, subchapter V trustee fees may exceed what a debtor may have paid to a U.S. Trustee in a traditional chapter 11 case. *See id.* at 268 (noting that the absence of U.S. Trustee fees does not offer a material cost savings because for small business cases the fees are manageable and giving an example of a \$650 fee for cases with quarterly disbursements under \$75,000). This is more likely if there is a nonconsensual plan requiring the subchapter V trustee to persist throughout the case. *See id.* at 278.

¹⁰⁴ *See id.* at 277 (“The additional trustee fees seem to be a deadweight loss imposed to attempt to bludgeon parties into agreement.”); Ralph Brubaker, *The Small Business Reorganization Act of 2019*, 39 BANKR. L. LETTER 1, 10 (2019) (noting that “creditors will prefer to avoid the fees the Subchapter V trustee will collect from the debtor’s plan payments (before payments to creditors) if confirmation is via cram-down”).

¹⁰⁵ *See generally* 11 U.S.C. § 1125(a).

¹⁰⁶ *Id.*

¹⁰⁷ *See* Larry Ream & Nika Aldrich, *Chapter 11 Bankruptcy Is Expensive; the Small Business Reorganization Act Provides a Realistic Opportunity for Small Businesses to Reorganize*, SCHWABE (July 2, 2020), <https://www.schwabe.com/publication/chapter-11-bankruptcy-is-expensive-the-small-business-reorganization-act-provides-a-realistic-opportunity-for-small-businesses-to-reorganize> [<https://perma.cc/F2PK-NKW2>] (noting that chapter 11 bankruptcy is “notoriously expensive” because of procedural requirements including a “comprehensive disclosure statement”).

¹⁰⁸ *See* Jordan Weiss, *A More Accessible Chapter 11: Subchapter V*, MEYER, SUOZZI, ENGLISH & KLEIN (July 19, 2022), www.msek.com/blog/a-more-accessible-chapter-11-subchapter-v-by-jordan-weiss [<https://perma.cc/B49H-B6F7>]. Indeed, one side effect of removing the laborious disclosure statement is a reduced amount of time for a subchapter V debtor to stabilize its business while under the protection of the bankruptcy court. The debtor is therefore forced into working quickly and considering all reorganization options prior to filing—factors required in a prepack.

¹⁰⁹ *See* 11 U.S.C. § 1181(b) (making section 1125, which requires disclosure statements, inapplicable in subchapter V, “Unless the court for cause orders otherwise”). The express removal of

include a brief history of the debtor's business operations, a liquidation analysis, and projections of the debtor's ability to make payments.¹¹⁰

To be sure, the court can reimpose the disclosure statement rules for cause.¹¹¹ Even if it does so, the rules enacted under the BRA for small businesses still apply.¹¹² That means the court can conclude that a disclosure statement is not necessary, approve a standard form disclosure statement previously approved by the bankruptcy court, conditionally approve a disclosure statement, and consolidate a final hearing on the disclosure statement with the plan confirmation hearing.¹¹³

b. Small Business Payment Plans & Plan Exclusivity

Lastly, subchapter V gives debtors permanent plan exclusivity.¹¹⁴ This gives small business debtors the benefit of never having to compete with a creditor's plan or defend against a proposed reduction in or termination of the debtor's exclusivity period.¹¹⁵

Aside from the traditional chapter 11 rules of classes under § 1123(a)(1), a subchapter V plan must include a brief history of the debtor's operations, a liquidation analysis, and projections regarding the debtor's ability to make payments under the proposed plan.¹¹⁶ Moreover, the plan must provide a means for the debtor's future earnings to be in the subchapter V trustee's supervision and control if needed to execute the plan.¹¹⁷ If all the requirements of § 1129(a) are met and all impaired classes accept the plan, the plan will be confirmed

the disclosure statement addresses one of LoPucki's critiques of the *Belk* prepack: a disclosure statement cannot be inadequate or provided to creditors on inadequate notice if it is not required in the first place. *See* LoPucki, *supra* note 16, at 276–77.

¹¹⁰ 11 U.S.C. § 1190(a); *see also* *Subchapter V Cases—Small Business Reorganization Act of 2019*, U.S. BANKR. CT. W.D. OKLA., [www.okwb.uscourts.gov/subchapter-v-cases-small-business-reorganization-act-2019](https://perma.cc/M94A-SEA2) [https://perma.cc/M94A-SEA2].

¹¹¹ *See* 11 U.S.C. § 1181(b).

¹¹² *See id.* § 1187(c) (“If the court orders under section 1181(b) of this title that section 1125 of this title applies, section 1125(f) of this title shall apply.”); *id.* § 1125(f); *see also supra* note 46 and accompanying text. The interaction of 11 U.S.C. § 1187(c) and § 1125(f) present a neat problem in statutory interpretation. § 1125(f), by its terms, only applies in a “small business case,” which might lead one to think that the streamlined provisions for disclosure statements apply only where the subchapter V debtor also falls below the (far lower) \$2 million debt ceiling. But the term “small business case” is defined by § 101(51C) to *exclude* debtors who have elected subchapter V. Thus, for § 1187(c) to mean anything, it must mean that the streamlined provisions of § 1125(f) apply to subchapter V cases even though the text plainly says the opposite.

¹¹³ *Id.* § 1125(f)(2)–(3).

¹¹⁴ *See id.* § 1189(a).

¹¹⁵ Tractenberg, et al., *supra* note 91, at 16–17.

¹¹⁶ 11 U.S.C. § 1190(1).

¹¹⁷ *Id.* § 1190(2).

on a consensual basis.¹¹⁸ The subchapter V trustee's service is terminated when the plan is substantially consummated, reducing fees and expenses.¹¹⁹

Most radically, subchapter V departs from the absolute priority rule for cramdown cases. The absolute priority rule, unless all classes of creditors accept the plan, requires that the plan pay senior creditors in full before junior creditors can receive any distribution.¹²⁰ In regular chapter 11 cases, this rule has the effect of wiping out an entrepreneur's equity stake—the price for a nonconsensual or “cramdown” plan.¹²¹ By contrast, in a cramdown plan under subchapter V, the debtor must apply all projected disposable income¹²² received within the first three to five years of the plan to make payments under the plan, or distribute property under the plan in the first three to five years of a value that is at least the projected disposable income of the debtor.¹²³

Abandoning the absolute priority rule allows a small business debtor to confirm a nonconsensual plan by making payments to creditors and, three to five years later, having its unsecured debt wiped away.¹²⁴ This innovation solves a longstanding problem in small business cases: under the absolute priority rule, the entrepreneur has a strong incentive to avoid bankruptcy to protect her equity stake; without the absolute priority rule, the entrepreneur may consider bankruptcy a more attractive option for resolving financial distress.¹²⁵

¹¹⁸ *Id.* § 1191(a).

¹¹⁹ *Id.* § 1183(c).

¹²⁰ *See id.* § 1129(b)(2); *see also* Seymour & Schwarcz, *supra* note 12, at 2–3.

¹²¹ *See* Douglas G. Baird & Robert K. Rasmussen, *Control Rights, Priority Rights, and the Conceptual Foundations of Corporate Reorganizations*, 87 VA. L. REV. 921, 947 (2001).

¹²² Although there are various definitions of disposable income in the Bankruptcy Code, disposable income in a subchapter V case is the income the debtor receives that is not reasonably necessary to be spent on maintenance or support of the debtor, a domestic support obligation, or payments needed for the “continuation, preservation, or operation” of the debtor's business. 11 U.S.C. § 1191(d).

¹²³ *See id.* § 1191(c)(1)(2). The debtor must be able to make all payments under the plan or have a reasonable likelihood of making all payments. *Id.* § 1191(c)(3)(A).

¹²⁴ *See id.* §§ 1181, 1191(b); *see also* Coordes, *supra* note 31, at 379 (“This modification allows small business owners to retain their businesses even if they do not pay their creditors in full, provided they commit all of their disposable income to plan payments during the life of the plan.”); *In re Chip's Southington, LLC*, No. 20-21458, 2021 WL 5313546, at *4 n.5 (Bankr. D. Conn. Nov. 13, 2021) (“[A] Subchapter V plan may be crammed down on unsecured creditors even if stockholders, who are junior to unsecured creditors, retain their equity under the plan.”). Crucially, this projected disposable income rule for an individual debtor applies only when one or more classes do not accept the plan. *See* 11 U.S.C. § 1191(b). Scholars disagree about the relative merits of the absolute and relative priority rules. *Compare* Douglas G. Baird, *Priority Matters: Absolute Priority, Relative Priority, and the Costs of Bankruptcy*, 165 U. PA. L. REV. 785, 792 (2017), *with* Seymour & Schwarcz, *supra* note 12, at 4.

¹²⁵ *See, e.g.*, Baird & Rasmussen, *supra* note 121, at 947 (noting the perverse incentives created by the absolute priority rule).

C. Growing Case Law & Coming Refinements

Bankruptcy practitioners, judges, and scholars are still working out the mechanics of subchapter V and devising strategies for debtors and creditors.¹²⁶ Most commentators seem to welcome bankruptcy's newest subchapter, recognizing that the default chapter 11 rules were too complex, too expensive, and led too many small business debtors with going-concern value to eschew the bankruptcy courts altogether.¹²⁷ In 2021, Judge Michelle M. Harner, Emily Lamasa, and Kimberly Goodwin-Maigetter studied 465 subchapter V cases filed in 2020, noting that of those cases that reached confirmation, they did so in approximately six months.¹²⁸ A study of all business bankruptcies filed from 2017 to 2023 conducted by Professors Edith Hotchkiss, Benjamin Iverson, and Xiang Zheng found that subchapter V allows small businesses to reorganize when they otherwise would have liquidated.¹²⁹ Indeed, the researchers found that subchapter V doubles the odds of plan confirmation, and cases that reach confirmation get there 42% faster than nonsubchapter V cases.¹³⁰ Even more impressively, the study suggests that the subchapter does not harm expected recovery for unsecured creditors.¹³¹

A growing body of case law applying the subchapter is starting to develop over uncertain parts of the text.¹³² Even so, the bankruptcy

¹²⁶ See Bradley, *supra* note 17 (discussing creditor strategies in subchapter V). The American Bankruptcy Institute assembled a task force to review subchapter V's efficacy and evaluate whether changes are needed. See *ABI Subchapter V Task Force*, AM. BANKR. INST., <https://subtaskforce.abi.org> [<https://perma.cc/H53F-9KRB>]. The task force recently issued its final report, finding that, among other things, "Subchapter V is working as Congress intended . . . [H]owever, [there exists] certain practices and procedures that may benefit from further refinement or statutory amendment." ABI FINAL REPORT, *supra* note 72, at 1.

¹²⁷ See, e.g., Brian L. Shaw, *Written Statement of Brian L. Shaw*, AM. BANKR. INST. (June 9, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/Brian_Shaw_Statement.pdf [<https://perma.cc/ZTJ9-7BR8>].

¹²⁸ See Michelle M. Harner, Emily Lamasa & Kimberly Goodwin-Maigetter, *Subchapter V Cases by the Numbers*, AM. BANKR. INST. J., Oct. 2021, at 12, 59–60, https://s3.amazonaws.com/abi-org-corp/journals/numbers_10-21.pdf [<https://perma.cc/6WSG-5KDT>].

¹²⁹ See Edith Hotchkiss, Benjamin Iverson & Xiang Zheng, *Can Small Businesses Survive Chapter 11?*, Mar. 13, 2024, at 2, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4726391 [<https://perma.cc/LYL8-VSYH>].

¹³⁰ See *id.* at 5.

¹³¹ See *id.* at 7.

¹³² See Bonapfel, *supra* note 35 (compiling recent subchapter V cases). There is increasing disagreement, for example, over whether the discharge exceptions in § 523(a) of the Code apply to both corporate and individual subchapter V debtors, as both the Fourth Circuit and Fifth Circuit hold, or only to individual debtors, as most bankruptcy courts to address the issue hold. Compare *Avion Funding, LLC v. GFS Indus., LLC* (*In re GFS Indus., LLC*), 99 F.4th 223, 232 (5th Cir. 2024), and *Cantwell-Cleary Co. v. Cleary Packaging, LLC* (*In re Cleary Packaging, LLC*), 36 F.4th 509, 517–18 (4th Cir. 2022), with *Lafferty v. Off-Spec Solutions, LLC* (*In re Off-Spec Sols., LLC*), 651 B.R. 862, 867 (B.A.P. 9th Cir. 2023), and *Nutrien Ag Sols., Inc. v. Hall* (*In re Hall*), 651 B.R. 62, 67–69 (Bankr. M.D. Fla. 2023). The Eleventh Circuit is now considering the issue, and nine amici

community continues to express concerns that debtors will use the subchapter to drag out resolution of cases or to avoid paying creditors.¹³³ Policymakers continue to debate the optimal debt limit for eligibility and whether it should be automatically or periodically updated.¹³⁴ Some commentators query whether the subchapter V trustee should be able to propose a plan along with the debtor.¹³⁵

And among this flurry of uncertainty, debtors continue to experiment with new strategies in subchapter V cases. A prime illustration is *In re BPI Sports*.¹³⁶ Nutritional supplement company BPI Sports filed for bankruptcy on September 18, 2023, and had its plan confirmed on October 20, 2023—just thirty-three days total. Although votes were solicited and cast postfiling, BPI Sports entered court with its plan and immediately requested confirmation of its plan since major constituencies had already committed to the plan through an RSA. This strategy marks *BPI Sports* as the first “functional” or “lock-up” prepack under subchapter V of the Bankruptcy Code.¹³⁷

have filed briefs. See *Benshot, LLC v. 2 Monkey Trading, LLC*, No. 23-90015 (11th Cir. filed July 19, 2023). Until a uniform and binding decision is reached, debtors may seek to file in jurisdictions that do not limit a business entity’s subchapter V discharge, while creditors may prefer the additional protections of a discharge exception. *But cf.* Jacob Sandler, Note, *Compelling Uniformity*, 76 FLA. L. REV. (forthcoming 2024) (“Considering uniformity throws courts into the world of policymaking as they will have to balance competing values such as predictability and correctness. It is Congress’s job to make that determination—not the courts.”).

¹³³ See, e.g., Bradley, *supra* note 17, at 271–72.

¹³⁴ Compare Sumner A. Bourne, *Written Statement of Sumner A. Bourne*, AM. BANKR. INST. 4 (June 23, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/Sumner_Bourne_Statement.pdf [<https://perma.cc/3WHK-PCVY>] (“I . . . would favor a permanent raise to \$10,000,000 . . .”), and Cipriano, *supra* note 17, at 148 (arguing that the debt limit should be raised to \$10 million), with Paul M. Black, *Statement*, AM. BANKR. INST. (June 23, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/Paul_Black_Statement.pdf [<https://perma.cc/ZV2C-DXWT>] (“[T]he current debt limit of \$7,500,000 is effective and appropriate. It should be maintained . . .”).

¹³⁵ See, e.g., Amy Denton Mayer, *Remarks of Amy Denton Mayer Regarding the Role of the Subchapter V Trustee*, AM. BANKR. INST. 8 (July 14, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/Amy_Denton_Mayer_Written_Statement.pdf [<https://perma.cc/GVC3-MQ52>] (“Should the Subchapter V trustee be permitted to file a plan if the debtor is removed from possession pursuant to Section 1185?”); Hannah L. Blumenstiel, *Written Statement of the Hon. Hannah L. Blumenstiel*, AM. BANKR. INST. 4–7 (June 9, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/Hannah_Blumenstiel_Statement.pdf [<https://perma.cc/LL7R-3FFK>] (“Where a debtor proves unable to propose a confirmable plan, whether due to feasibility concerns, bad faith, or other reasons, it might make sense to terminate the permanent exclusivity afforded by Subchapter V and to allow the SubV trustee to propose a plan.”).

¹³⁶ Eyal Berger of Akerman LLP was lead counsel on the *BPI Sports* bankruptcy.

¹³⁷ Order Confirming the Debtor’s Subchapter V Plan of Reorganization, *In re BPI Sports, LLC*, No. 23-17463 (Bankr. S.D. Fla. Oct. 20, 2023), ECF No. 121; *Akerman Uses Innovative Subchapter V Strategy to Complete Bankruptcy in 33 Days*, AKERMAN (Nov. 17, 2023), <https://www.akerman.com/en/firm/newsroom/akerman-uses-innovative-subchapter-v-strategy-to-complete-bankruptcy-in-33-days.html> [<https://perma.cc/FVQ9-6QXF>].

So, although *BPI Sports* is an exciting preview of the rise of small business prepacks, the potential of a full small business prepack remains to be fully explored. Because Congress intended for subchapter V cases to be more streamlined, the prepack approach seems like a natural fit for the subchapter. Part II explores the prepack litigation strategy.

II. HOW PREPACKAGED CASES HAVE RESHAPED CHAPTER 11

Even as Congress enacted subchapter V to streamline bankruptcy for small businesses, chapter 11 debtors and their legal counsel have been refining their own strategy to minimize the costs and publicity of being in bankruptcy court. As described above, this strategy is called a “prepackaged” bankruptcy, or a “prepack” for short.¹³⁸ The approach is counterintuitive—and controversial. To the layperson, the filing of a petition in bankruptcy might represent the end of business as usual and the beginning of a prolonged, public court process. But neither is necessarily true: under the modern U.S. bankruptcy regime, businesses reorganize under chapter 11 all the time—and some of them do so at rocket speed.

Take the case of Belk, Inc., a large department store headquartered in North Carolina that experienced financial distress in the early days of 2021.¹³⁹ On February 23, 2021, Belk filed for chapter 11 bankruptcy.¹⁴⁰ An informed observer of traditional, large retail bankruptcies might have guessed that Belk’s bankruptcy case would take somewhere between six and eighteen months.¹⁴¹ But at 10:08 AM the next morning, the bankruptcy court confirmed Belk’s reorganization plan, blessing its exit from bankruptcy.¹⁴² Nor was the plan somehow dreamed up overnight: Belk is not a small company, and the plan was complex. It reduced Belk’s debt by \$450 million, approved \$225 million in new capital, and extended maturities on its term loans by three years.¹⁴³

Belk was able to get its plan confirmed in just over twelve hours because it filed a prepack.¹⁴⁴ In addition to its regular first-day filings, a debtor filing a prepack submits its reorganization plan along with

¹³⁸ See *supra* note 14 and accompanying text.

¹³⁹ See *Sycamore Partners Reaches Agreement to Recapitalize and Retain Control of Belk*, BELK (Jan. 26, 2021), <https://newsroom.belk.com/restructuring> [<https://perma.cc/M9CY-NF45>].

¹⁴⁰ Order Approving the Debtors’ Disclosure Statement for, and Confirming, the Debtors’ Joint Prepackaged Chapter 11 Plan, *In re Belk, Inc.*, No. 21-30630 (Bankr. S.D. Tex. Feb. 24, 2021), ECF No. 61.

¹⁴¹ See, e.g., Warren & Westbrook, *supra* note 58, at 626, 629 (estimating that the average time spent in chapter 11 is approximately eleven months).

¹⁴² Transcript of First Day and Confirmation Hearing at 66, *In re Belk, Inc.*, No. 21-30630 (Bankr. S.D. Tex. Feb. 26, 2021), ECF No. 98.

¹⁴³ *Id.*

¹⁴⁴ *Id.*

its petition.¹⁴⁵ This move is a deviation from the default practice. In a traditional chapter 11 case, after filing for bankruptcy, the debtor must submit its plan, along with a disclosure statement, to the creditor body and solicit the votes of the creditors. In a prepack, the debtor has already distributed the proposed plan and disclosure statement and has already solicited votes for its plan before filing its petition. The debtor comes into court saying, in effect, here we are, this is what we want to do, our creditors have already voted, so please confirm our plan.¹⁴⁶

Prepacks have become increasingly popular,¹⁴⁷ and, for many debtors, rightfully so. A prepack minimizes the time a debtor remains in bankruptcy and thus reduces the costs of litigating through a drawn-out court process.¹⁴⁸ But prepacks have generated concern and controversy too, particularly when debtors seek plan confirmation at rocket speed. Critics of the practice, most notably LoPucki, argue that prepacks circumvent statutory periods and risk unjust results.¹⁴⁹

This Part describes the prepack litigation strategy, describes why debtors—and some creditors—choose it, and explains the limitations and risks of the approach. Part III then explains why the new rules for small business bankruptcies may be especially appropriate for prepacks.

A. *Prepacks as Litigation Strategy*

When a business enterprise files for bankruptcy, the case can proceed along several different paths, such as a liquidation under chapter 7 of the Bankruptcy Code, a plan of reorganization under chapter 11,

¹⁴⁵ See, e.g., Morris J. Massel, *The Pros and Cons of Prepackaged Bankruptcy*, SIMPSON THACHER & BARTLETT (Oct. 2, 2013, 4:58 PM), <https://www.stblaw.com/docs/default-source/cold-fusion-existing-content/publications/pub1647.pdf?sfvrsn=2> [<https://perma.cc/XJ4B-DMVF>].

¹⁴⁶ Belk's one-day prepack is an extreme example that requires the retention of many professionals and significant planning. Although a few debtors have the resources required to expedite their exit to this degree, most prepacks typically take several months to reach plan confirmation. See, e.g., David M. Hillman, *Restructuring Trend: The Ultrafast Prepack for Private Credit Deals* (Nov. 4, 2019), <https://www.proskauer.com/pub/restructuring-trend-the-ultrafast-prepack-for-private-credit-deals> [<https://perma.cc/BDU7-ZE3U>]. Nevertheless, a four-month exit remains relatively fast in the chapter 11 context, deviating from the ordinary chapter 11 timeline of approximately one year to eighteen months. See Warren & Westbrook, *supra* note 58, at 631–32.

¹⁴⁷ Indeed, there is a growing literature discussing prepacks in insolvency practice around the globe. See, e.g., Gurrea-Martinez, *supra* note 11, at 96–98 (detailing the rise of prepacks in Singapore, India, Spain, the Netherlands, and the Philippines); Anja Droegge Gagnier, *The French 'Prepack' Is Now Available*, INSOLVENCY & RESTRUCTURING INT'L, Apr. 2011, at 32–33 (analyzing the *Sauvegarde Financière Accélérée*, inspired by American chapter 11 practice); Barbara Tomczyk & Przemyslaw Wierzbicki, *Pre-Pack Under Polish Law*, INSOLVENCY & RESTRUCTURING INT'L, Sept. 2017, at 42–44 (analyzing the prepack in Polish law, inspired by American chapter 11 practice).

¹⁴⁸ See, e.g., *In re Genco Shipping & Trading Ltd.*, 509 B.R. 455, 462 (Bankr. S.D.N.Y. 2014) (“A successful prepack can cut down the duration of a bankruptcy case and, therefore, the incredible cost associated with a long, drawn out bankruptcy process.”).

¹⁴⁹ LoPucki, *supra* note 16, at 277–78.

or a sale of the business's assets under section 363.¹⁵⁰ The Code does not direct which path a debtor selects and leaves the decision to the debtor—at least in the first instance. Indeed, the Code gives the debtor a period of exclusivity during which it, and only it, may propose a plan for how to reorganize the business.¹⁵¹ Before filing, debtors considering a bankruptcy filing—at least when the case is not a “freefall” bankruptcy¹⁵²—discuss their approach to the litigation with their legal team. And, as has been the practice for several decades now, debtors generally invite their senior secured creditor, or whoever is paying for the bankruptcy case, into that discussion.¹⁵³

Debtor control of the trajectory of a bankruptcy case applies to prepack cases. In a prepack case, even as the debtor files its petition in bankruptcy, it formally proposes its chapter 11 plan and seeks confirmation of that plan. If creditor voting is required to confirm the plan, the debtor has already solicited votes. This strategy collapses the beginning and the end of the bankruptcy case into a single moment and represents a dramatic acceleration of the normal timelines in bankruptcy.

Consider the standard timeline. The Code's notice requirements contemplate a confirmation hearing no earlier than four weeks after the petition date. This is because the debtor is typically required to file a disclosure statement with its plan and provide time for creditors to vote on the plan. In its disclosure statement, the debtor must describe the plan so that creditors can understand the proposal. The debtor must obtain court approval of the disclosure statement and distribute the plan and disclosure statement to creditors four weeks (twenty-eight

¹⁵⁰ See 11 U.S.C. § 363.

¹⁵¹ See *id.* § 1121(b).

¹⁵² A freefall bankruptcy, termed for its swift and unanticipated nature, occurs when a debtor files for bankruptcy without prior negotiation or strategic planning with creditors. See Borders & Blank, *supra* note 2.

¹⁵³ Companies in financial distress usually do not have any cash available to pay for the bankruptcy process and must turn to a secured creditor, or less commonly, a new lender, to fund the bankruptcy process. See Jay Lawrence Westbrook, *Secured Creditor Control and Bankruptcy Sales: An Empirical View*, 2015 U. ILL. L. REV. 831, 835–36 (2015). The Bankruptcy Code strictly curtails the ability of debtors to use cash collateral and, in 1998, amendments to Article 9 of the Uniform Commercial Code (U.C.C.) made it easier for lenders to perfect a security interest in substantially all of their borrowers' assets, including cash and proceeds of collateral. 11 U.S.C. § 363(c)(2). See generally Cynthia Grant, *Description of the Collateral Under Revised Article 9*, 4 DEPAUL BUS. & COM. L.J. 235 (2006) (discussing the revised U.C.C. § 9-504). As a result of the U.C.C. revisions, new credit markets for distressed firms, and the eternal reluctance of American debtors to file any sooner than necessary, companies filing for bankruptcy in recent decades have tended to enter bankruptcy with their cash already serving as collateral. See, e.g., David Skeel, *Bankruptcy's Identity Crisis*, 171 U. PA. L. REV. 2097, 2102–03 (2023); David A. Skeel Jr., *Creditors' Ball: The "New" New Corporate Governance in Chapter 11*, 152 U. PA. L. REV. 917, 925 (2003); Charles J. Tabb, *Credit Bidding, Security, and the Obsolescence of Chapter 11*, 2013 U. ILL. L. REV. 103, 142 (2013). But see Westbrook, *supra* note 153, at 837–41 (2015) (presenting empirical findings challenging the prevalence of the “hog-tied” debtor in bankruptcy).

days) before a hearing on the disclosure statement.¹⁵⁴ Once the court has approved the disclosure statement, the creditor body typically has another four weeks (twenty-eight days) to vote on the plan. After the creditor body has voted, the debtor moves for plan confirmation.¹⁵⁵ Correspondingly, the period during which only the debtor may file a plan is 120 days.¹⁵⁶ The Bankruptcy Code thus contemplates plan confirmation between an inside date of two months after the petition and an outside date of four months after the petition, subject to court adjustment of those deadlines.

In a prepack case, the debtor seeks to move as much of this process as possible back before the petition date. Working with creditor constituencies, it thus drafts the plan and disclosure statement along with its petition in bankruptcy, distributes the documents to its creditor body, solicits votes if necessary, and, in an “ultra-expedited prepack,”¹⁵⁷ even gives creditors the statutory opportunity to draft objections—all before filing the case. By the time the bankruptcy begins, key creditors are locked into supporting the plan through an RSA, a development that Professor Douglas Baird calls a “quiet revolution.”¹⁵⁸ Commercial litigation practice has no obvious parallel; it would be as if the plaintiff sent the complaint to the defendant, the parties engaged in discovery, agreed that trial would not be necessary, and filed the complaint, answer, and motions for summary judgment all on day one.

Although the prepack strategy represents an extreme departure from the standard trajectory envisioned by the Bankruptcy Code, it is not without statutory hooks. The prepack goes back at least to the beginning of today’s Bankruptcy Code.¹⁵⁹ When Congress enacted the

¹⁵⁴ See FED. R. BANKR. P. 3017(a).

¹⁵⁵ See 11 U.S.C. § 1129.

¹⁵⁶ *Id.* § 1121(b). The bankruptcy court may, for cause, extend this period up to 180 days after the petition date. Any such extensions are subject to outer limits that cannot be adjusted by the bankruptcy court. See *id.*; see also *id.* § 1121(d) (authorizing the court to “reduce or increase” the exclusivity period up to eighteen months).

¹⁵⁷ See Eric Chafetz & Myles R. MacDonald, *Ultra-Expedited Prepacks Are No Longer an Academic Curiosity*, LOWENSTEIN SANDLER LLP (Dec. 31, 2019), www.lowenstein.com/media/5419/20191230-new-york-law-journal-ultra-expedited-prepacks-are-no-longer-an-academic-curiosity-chafetz-macdonald.pdf [<https://perma.cc/Q93H-QWBX>] (defining ultra-expedited prepacks as “prepacks in which at least half of the 28-day period provided for filing objections to confirmation under Rule 2002(b) of the Federal Rules of Bankruptcy Procedure . . . has elapsed prior to the filing of the debtor’s petition . . .”).

¹⁵⁸ See Douglas G. Baird, *Bankruptcy’s Quiet Revolution*, 91 AM. BANKR. L.J. 593 (2017).

¹⁵⁹ Indeed, prepackaged cases can be traced back to nineteenth-century receivership proceedings. See, e.g., Dennis F. Dunne, Dennis C. O’Donnell & Nelly Almeida, *Pre-Packaged Chapter 11 in the United States: An Overview*, GLOB. RESTRUCTURING REV. (Dec. 11, 2019), <https://global-restructuringreview.com/guide/the-art-of-the-pre-pack/edition-1/article/pre-packaged-chapter-11-in-the-united-states-overview> [<https://perma.cc/8Q4C-YVH4>]. Bondholders could deposit their bonds with a committee that would then propose a reorganization plan and seek confirmation. *Id.* In chapter X of the old Bankruptcy Act, Congress banned this prepetition solicitation of plan

Code in 1978, it included provisions implicitly accepting prepackaged cases.¹⁶⁰ Specifically, the Code expressly authorizes a debtor to file its chapter 11 plans with its petition,¹⁶¹ as well as to solicit votes prior to the case's commencement—the quintessential feature of a prepack.¹⁶² It also provides a crucial workaround to the requirement of an official unsecured creditors' committee, allowing the bankruptcy court to deem ad hoc prepetition committees as having satisfied that statutory requirement.¹⁶³

BAPCPA, too, modified procedures of standard chapter 11 cases to facilitate prepacks.¹⁶⁴ Before BAPCPA, a debtor filing a prepack had to complete its solicitation before it filed for bankruptcy.¹⁶⁵ If the solicitation was interrupted for any reason, such as an involuntary bankruptcy

acceptances, responding to concerns that insiders were controlling the committees at the expense of bondholders. *Id.* However, in 1978, Congress got rid of chapter X's prohibition of prepetition solicitation. *Id.*

¹⁶⁰ See *id.*; *In re Genco Shipping & Trading Ltd.*, 509 B.R. 455, 462 (Bankr. S.D.N.Y. 2014) (“The Bankruptcy Code clearly contemplates the use of prepack plans.”). One of the attorneys involved in drafting the 1978 Code, J. Ronald Trost, advocated for provisions clearly allowing parties to negotiate their way to a solution before filing the case. BAIRD, *supra* note 39, at 138–39. As Professor Baird puts it, “Trost was not fashioning something out of whole cloth”: Chapter XI reorganizations had often followed this template. *Id.* at 139.

¹⁶¹ 11 U.S.C. § 1121(a) (“The debtor may file a plan with a petition commencing a voluntary case, or at any time in a voluntary case or an involuntary case.”).

¹⁶² See *id.* § 1126(b); see also *id.* §§ 341(e), 1125(g) (allowing solicitation of votes before the bankruptcy case starts); FED. R. BANKR. P. 3018(b) (setting forth procedure for equity security holders and creditors who vote on the plan before the commencement of the case); Robert K. Rasmussen & David A. Skeel Jr., *The Economic Analysis of Corporate Bankruptcy Law*, 3 AM. BANKR. INST. L. REV. 85, 97 n.54 (1995) (“Congress explicitly contemplated that some debtors would use this [prepackaged bankruptcy] strategy.”).

¹⁶³ See 11 U.S.C. § 1102(b)(1) (providing for the appointment of the official creditors' committee but allowing for the committee to consist of “the members of a committee organized by creditors before the commencement of the case under this chapter, if such committee was fairly chosen and is representative of the different kinds of claims to be represented”).

¹⁶⁴ See ANDREW M. TROOP, LISA G. BECKERMAN, MILDRED CABÁN, ERIC A.W. DANNER & MICHAEL J. PAPPONE, AM. BANKR. INST., THE MECHANICS OF PREPACKS: WHAT HAPPENS PRE-PETITION, AND HOW TO MAKE IT STICK POST-PETITION 131–32 (2014), <https://abi-org-corp.s3.amazonaws.com/cle/materials/2014/Jul/MechanicsOfPrepacks.pdf> [<https://perma.cc/UVR3-WFEF>]. Unfortunately, BAPCPA's focus on speed neglected other important considerations. See, e.g., Gerald P. Buccino, *Statement of Gerald P. Buccino to the American Bankruptcy Institute Commission to Study the Reform of Chapter 11*, AM. BANKR. INST. (Nov. 3, 2012), <https://commission.abi.org/sites/default/files/statements/03nov2012/Buccino.pdf> [<https://perma.cc/P5WG-KCQ2>] (“While BAPCPA may have sought to reduce the cost of bankruptcy by shortening the time period for developing a reorganization plan, it appears to have impaired the rehabilitative goal of bankruptcy by leaving insufficient time to rehabilitate or fix many bankruptcy businesses . . .”). BAPCPA was also “confusing, overlapping, and sometimes self-contradictory” to the extent that trying to understand its provisions was “like trying to solve a Rubik's Cube that arrived with a manufacturer's defect.” *In re Donald*, 343 B.R. 524, 529 (Bankr. E.D.N.C. 2006).

¹⁶⁵ TROOP ET AL., *supra* note 164, at 131.

being filed, the debtor had to start over.¹⁶⁶ This changed with BAPCPA's addition of sections 1125(g) and 341(e) to the Bankruptcy Code. Section 1125(g) permits a debtor to continue soliciting votes postpetition and without a court-approved disclosure statement.¹⁶⁷ Section 341(e) allows the court to order the United States trustee not to convene a meeting of creditors in a prepack case.¹⁶⁸

True, approving a chapter 11 plan so quickly runs afoul of various statutorily prescribed deadlines, something LoPucki and other critics have assailed.¹⁶⁹ The Bankruptcy Code expressly empowers the bankruptcy court to shorten those deadlines for cause, but those reduction provisions would almost never allow a bankruptcy plan to be confirmed faster than four days after the filing of the petition.¹⁷⁰ Although the Code also gives the bankruptcy court broad authority to issue any orders "necessary or appropriate to carry out the provisions" of the Code, that authority cannot be wielded to contravene anything in the Code¹⁷¹ but only to fill in statutory gaps.¹⁷²

B. Strategic Advantages for Debtors and Creditors

Prepacks provide both debtors and creditors with significant advantages. Bankruptcy courts can provide extraordinary relief, and prepacks allow business enterprises to spend a significantly reduced time in court to obtain that relief.¹⁷³

¹⁶⁶ *Id.* at 131–32.

¹⁶⁷ 11 U.S.C. § 1125(g).

¹⁶⁸ *Id.* § 341(e).

¹⁶⁹ *See generally* LoPucki, *supra* note 16 (criticizing Belk's bankruptcy case as unlawful).

¹⁷⁰ *See* FED. R. BANKR. P. 9006(b) (covering enlargement), FED. R. BANKR. P. 9006(c) (covering reduction); *see also infra* notes 224–25 and accompanying text.

¹⁷¹ *See* 11 U.S.C. § 105(a), (d)(2); *Czyzewski v. Jevic Holding Corp.*, 580 U.S. 451, 452 (2017) (holding that the bankruptcy court could not rely on § 105(a) to modify creditors' rights upon dismissal of a case, in contravention of distribution and priority rules); *Law v. Siegel*, 571 U.S. 415, 421–22 (2014) (holding that the bankruptcy court could not rely on § 105(a) to surcharge a debtor's homestead exemption in contravention of § 522); *see also* 28 U.S.C. § 2075 (providing that the Bankruptcy Rules "shall not abridge, enlarge, or modify any substantive right"); Jonathan M. Seymour, *Against Bankruptcy Exceptionalism*, 89 U. CHI. L. REV. 1925, 1981–82 (2022) (comparing § 105(a) to the All Writs Act, 28 U.S.C. § 2851, and pointing out that the former only "authorizes a limited selection of procedural remedies, such as the right to issue injunctions in order to make effective some other provision of the statute").

¹⁷² *But see* Chafetz & MacDonald, *supra* note 157, at 2 (citing *In re Blue Bird Body Co.*, No. 06-50026, 2006 Bankr. LEXIS 5223 (Bankr. D. Nev. Feb. 15, 2006)) (summarizing a prepackaged case where the court "was not certain that it had a statutory basis to confirm a plan of reorganization so quickly, [so] the court heavily relied on its equitable powers, which are themselves codified in § 105(a) of the Bankruptcy Code").

¹⁷³ *See supra* note 14 (listing several cases in which debtors' counsel successfully brought their clients from petition to plan within a matter of days).

Debtors cannot always solve their financial problems outside of bankruptcy. Although some out-of-court restructurings may provide some benefits, they cannot provide all the protections that bankruptcy offers. Most important, bankruptcy can eliminate holdouts.¹⁷⁴ Holdout problems are a common thorn in the side of financially distressed firms and occur when one creditor refuses to work with the debtor in the hopes that all the other creditors will work with the debtor to reduce *their* claims, leaving its claim unaffected.¹⁷⁵ Out-of-court restructurings do not allow modification of a creditor's claim without that creditor's consent, and so debtors face a one-by-one negotiation with every single creditor, each of whom has an incentive to "hold out" for the best deal possible. Holdouts can frustrate otherwise productive negotiations and stymie efforts by debtors and their creditors to reach consensual modification of the debtor's balance sheet. The Bankruptcy Code, however, permits a court to modify creditors' claims without their consent. This is done by classifying the claims and seeking consent within each class. If consent is not achieved, the court can enforce a "cramdown," imposing a plan on nonconsenting classes.¹⁷⁶

At the same time, bankruptcy comes at a price:

First, of course, there is the matter of sheer cost. As many commentators have noted, a chapter 11 case is expensive—with debtors required to submit monthly financial reports, pay quarterly fees to the U.S. Trustee, and retain counsel throughout the reorganization plan.¹⁷⁷ Although some of those costs parallel costs outside of bankruptcy (a distressed firm might still retain outside counsel, for example), not all of the costs of chapter 11 have nonbankruptcy parallels. In a chapter 11 bankruptcy, for example, the court appoints a statutory committee of unsecured creditors, a committee whose legal fees are usually paid out of estate assets, at least in part.¹⁷⁸ Outside bankruptcy, creditors are typically responsible for their own legal fees. All told, the difference in cost between an out-of-court workout and an in-court restructuring can create significant sticker shock.

Second, bankruptcy comes with court oversight and significant limitations on a debtor's ability to operate. Although debtors may continue to operate in the ordinary course of business, the Bankruptcy Code keeps a sharp eye on payments going out from the estate for any prepetition debts. A debtor in bankruptcy thus needs court approval for

¹⁷⁴ See, e.g., Robert K. Rasmussen & Randall S. Thomas, *Whither the Race? A Comment on the Effects of the Delawarization of Corporate Reorganizations*, 54 VAND. L. REV. 283, 288 (2001).

¹⁷⁵ See *id.*

¹⁷⁶ See 11 U.S.C. § 1126. If the debtor solicits a positive vote from a majority of creditors in each class who hold over two-thirds of the debt, that class has "accepted" the plan, even though individual creditors have not accepted the plan. See *id.*

¹⁷⁷ See, e.g., Dunne et al., *supra* note 159.

¹⁷⁸ 11 U.S.C. § 1102.

even mundane tasks such as paying utility bills or taxes.¹⁷⁹ Any business decision outside the ordinary course requires court approval as well,¹⁸⁰ sharply curtailing the debtor's ability to change its approach. This, too, creates a high price of admission that is reduced when a debtor exits bankruptcy quickly.

Prepacks thus allow debtors—and those creditors who support the plan—to access the protections of bankruptcy without incurring all the costs of a drawn-out bankruptcy case.¹⁸¹ Debtors filing a prepack receive these benefits of bankruptcy and the speed and privacy seen in certain out-of-court restructuring strategies. Getting in and out of court quickly reduces costs, keeps the debtor out of the public eye, allows the debtor to continue operating as usual, and instills confidence in stakeholders.¹⁸² Whether prepacks lead to success is hard to determine empirically. A 2015 study by LoPucki and Doherty determined that prepackaging a bankruptcy case was marginally more likely to result in a successful reorganization, but the authors concluded that selection bias likely explains the result: companies with a prepack in hand that suspect imminent failure decide not to file.¹⁸³

C. *Limitations, Risks, and Legitimacy of Prepacks*

With all this said, the prepack strategy comes with significant limitations, some risks, and sharp concerns about legitimacy.

Let us start with limitations. Prepacks work only for debtors with certain types of capital structures because the plan must still meet the Bankruptcy Code's stringent requirements for plan confirmation. Those requirements mean, in effect, that a prepack debtor must have a viable underlying business and plan to use the bankruptcy process to reduce the debt overhang in coordination with its secured creditors.¹⁸⁴

First, the prepack strategy cannot work for debtor companies with unsecured creditors that (1) cannot be identified in advance and

¹⁷⁹ See, e.g., *Region 21 Operating Guidelines & Reporting Requirements for Chapter 11 Debtors in Possession and Chapter 11 Trustees*, U.S. DEP'T JUST. 3 (Oct. 2022), https://www.justice.gov/ust/ust-regions-r21/file/ch11_guidelines_reporting_req.pdf/dl?inline [<https://perma.cc/M4JV-3URT>].

¹⁸⁰ See 11 U.S.C. § 363(b).

¹⁸¹ See Robert K. Rasmussen & Randall S. Thomas, *Timing Matters: Promoting Forum Shopping by Insolvent Corporations*, 94 Nw. U. L. REV. 1357, 1375 (2000) (“The prepackaged bankruptcy thus provides the firm with the benefit of class-wide voting to minimize holdout problems, while simultaneously minimizing the time the firm spends in bankruptcy.”).

¹⁸² See Dunne et al., *supra* note 159. Having votes solicited before commencing the case gives key stakeholders certainty that the company will continue business as usual. *See id.* This reduced uncertainty makes it more likely that the business will continue operating as usual. *See id.*

¹⁸³ See LoPucki & Doherty, *supra* note 11, at 995.

¹⁸⁴ See Chafetz & MacDonald, *supra* note 157, at 3 (stating that an ultra-expedited prepack requires “(1) a debtor with a healthy underlying business filing solely because of too much debt; (2) a fulcrum class of secured creditors . . . and (3) no holdouts”).

(2) stand to recover some percentage of their debt in bankruptcy. This is because the voting rules in bankruptcy require one class of creditors who will not be repaid in full to sign off on the plan.¹⁸⁵ When that role can be filled by a small set of identifiable secured creditors, they can design a plan with the debtor and vote on it in advance. If the secured creditors can be paid in full, the next class of creditors whose consent is needed becomes the class of unsecured creditors. But if those unsecured creditors cannot be identified in advance, as is usually the case for operating companies, they cannot vote on the plan before confirmation. The result is that prepacks tend to be used either by (1) operating companies that are deep enough in debt that the unsecured creditors will receive no distribution under the plan or (2) holding or mezzanine companies who, by virtue of not being operating companies, have a closed universe of unsecured creditors.

Second, even apart from voting requirements, the bankruptcy court must sign off on the plan as feasible and authorize any sales of estate property out of the ordinary course.¹⁸⁶ A debtor that proposes to sell the business or slash major business lines will be unlikely to convince a bankruptcy judge that such dramatic changes are appropriate without notice and an opportunity to hear objections—including from the U.S. Trustee. For that reason, prepack cases typically propose only balance-sheet restructuring rather than wholesale reworking of business plans.

Then there are risks to the prepack strategy. A financially distressed firm that attempts to negotiate a global resolution outside of bankruptcy does not have the benefit of bankruptcy's automatic stay, which provides helpful "breathing room" for debtors in bankruptcy.¹⁸⁷ Soliciting votes before the stay may cause creditors to attempt to collect debts or alter terms of their contract.¹⁸⁸ Bankruptcy is no small decision, and "[i]f word of an impending bankruptcy filing leaks out, . . . vendors may cease shipping, other creditors may seek to exercise remedies, competitors may seek to take away business, customers may look elsewhere, and employees may hit the street looking for a more secure job."¹⁸⁹

¹⁸⁵ 11 U.S.C. § 1129.

¹⁸⁶ *See id.* § 363(b).

¹⁸⁷ For a description of the automatic stay, see *Auriga Polymers Inc. v. PMCM2, LLC*, 40 F.4th 1273, 1277–78 (11th Cir. 2022) ("The automatic stay provides breathing room for the debtor to negotiate with its creditors and craft a plan of reorganization . . .").

¹⁸⁸ Douglas M. Foley & James E. Van Horn, *Prepacks on the Rise in Chapter 11 Bankruptcies: Renegotiated Plans Can Accelerate Reorganizations*, J. CORP. RENEWAL, Aug. 2008, at 12–13, www.mcguirewoods.com/news-resources/publications/prepacks.pdf [<https://perma.cc/L9TT-23NK>].

¹⁸⁹ John D. Ayer, Michael Bernstein & Jonathan Friedland, *The Life Cycle of a Chapter 11 Debtor Through the Debtor's Eyes*, AM. BANKR. INST. J., Sept. 2003, at 20, 50–52, <https://www.kirkland.com/siteFiles/kirkexp/publications/2455/Document1/Friedland%20-%20Life%20Cycle%20of%20a%20Chapter%2011%20Debtor%202.pdf> [<https://perma.cc/ER98-JHLV>].

And even though involuntary bankruptcy cases are rare,¹⁹⁰ circulating a proposed prepack could be used to support the propriety of a creditor-filed, involuntary bankruptcy case.¹⁹¹

Debtors may also find they have inadequate leverage when attempting to negotiate before filing a bankruptcy petition because they cannot invoke certain rights received in bankruptcy court. For example, chapter 11 allows debtors to reject certain executory contracts and leases—turning those debts into unsecured claims—and, in some instances, to cap the damages for breach of contract.¹⁹² This power gives the debtor the ability to defang certain creditors in bankruptcy court.¹⁹³

Additionally, there is no guarantee that the bankruptcy court will find the debtor's efforts adequate. If the court finds that the proposed disclosure statement or solicitations do not meet the stringent requirements set forth in chapter 11, the debtor is back at square one and has lost a lot of money from the prepetition preparation. Not only can the court raise concerns with the prepack process *sua sponte*, a single creditor or the U.S. Trustee's office can object to plan confirmation and claim the prepetition disclosure, notice, and solicitation were inadequate.¹⁹⁴ The consequences of getting it wrong can derail the chance of a consensual resolution, especially when many prepacks "are agreed to by creditors on the assumption that they will proceed through bankruptcy with the unusual speed for prepackaged plans for which the Bankruptcy Code provides."¹⁹⁵

Even where the prepackaged plan is confirmed, the speed of the case may heighten the risk that the reorganization is insufficient to solve the debtor's financial problems—resulting in a second chapter 11 case within a few years, sometimes cheekily called a "chapter 22."¹⁹⁶

¹⁹⁰ See, e.g., Richard M. Hynes & Steven D. Walt, *Revitalizing Involuntary Bankruptcy*, 105 IOWA L. REV. 1127, 1127 (2020) ("Just 0.05 percent of petitions are involuntary . . .").

¹⁹¹ A debtor in the process of negotiating a prepackaged bankruptcy when an involuntary petition is filed might simply not contest the involuntary petition and regain control of the case by converting it to chapter 11 and seeking a subchapter V designation. Under Bankruptcy Rule 1020, an involuntary debtor has fourteen days after the court rules on the involuntary petition to state whether it elects subchapter V. See 11 U.S.C. § 303(h); FED. R. BANKR. P. 1020(a).

¹⁹² See 11 U.S.C. § 365(b)(1), (3)–(4).

¹⁹³ See *id.*

¹⁹⁴ See, e.g., *In re LATAM Airlines Grp. S.A.*, 55 F.4th 377, 381, 388–89 (2d Cir. 2022) (ruling on a U.S. Trustee's objection to confirmation due to, in part, inadequate solicitation).

¹⁹⁵ See *In re Houghton Mifflin Harcourt Publ'g Co.*, 474 B.R. 122, 138 n.51 (Bankr. S.D.N.Y. 2012) ("[S]takeholders can be grievously injured, and value can be destroyed, when chapter 11 cases are not concluded quickly. . . ." (citations omitted)).

¹⁹⁶ See, e.g., Eyal Berger, *Written Statement of Eyal Berger*, AM. BANKR. INST. 2 https://abiv-subv.s3.amazonaws.com/statements/Eyal_Berger_Written_Statement.pdf [<https://perma.cc/SV8T-BNJ4>]. For example, the reorganized SunGard filed for a second chapter 11 case in 2022. See Declaration of Michael K. Robinson, Chief Executive Officer and President of the Debtors in Support of Chapter 11 Petitions and First Day Pleadings at ¶ 7, *In re SunGard AS New Holdings, LLC*,

All these risks take place against the backdrop of significant critique of the prepack strategy. The Bankruptcy Code provides for notice periods that the ultra-expedited prepacks, at best, distort and, at worst, violate.¹⁹⁷ For example, in *Belk*, “[t]he court did not give the creditors notice of the disclosure statement or plan confirmation hearings until after those hearings were held.”¹⁹⁸ The court in *Belk* attempted to assuage concerns by issuing a “due process preservation order,” which allowed parties to raise due process objections after confirmation.¹⁹⁹ Even so, for LoPucki, this approach represents part of bankruptcy’s recent “descent into lawlessness.”²⁰⁰ To be sure, other commentators do not share the same concerns. Creditors’ acceptance of prepackaged plans may indicate their approval and support the contention that the modified procedures injure no one.²⁰¹ Even so, the notion of codified rules not being followed may erode the perceived legitimacy of the Bankruptcy Code and weaken the legal footing of the prepack strategy.²⁰²

The reader may already start to see how, in subchapter V, Congress addressed many of the same risks described above for small business debtors, including inadequate leverage with creditors, the uncertainty of success, and the need to adjust the Bankruptcy Code’s standard notice provisions. The next Part shows how the prepack strategy fits neatly into Congress’s innovation for small business bankruptcies.

III. WHY PREPACKS FIT NEATLY INTO SUBCHAPTER V

A. *For Whom Are the Bankruptcy Courts Open?*

Bankruptcy law and policy have always presented a mix of public and private values—and this is no less true for prepacks. As noted in Part II, the prepack litigation strategy has generated a firestorm of

No. 22-90018 (Bankr. S.D. Tex. Apr. 11, 2022), ECF No. 7 (stating that the previous bankruptcy “did not comprehensively address the Company’s operating cost structure and capacity utilization challenges”).

¹⁹⁷ The U.S. Trustee has critiqued ultra-fast prepacks for violating due process. *See, e.g.*, Objection of United States Trustee to Debtors’ Emergency Scheduling Motion and Joint Prepackaged Plan of Reorganization, *In re Belk, Inc.*, No. 21-30630 (Bankr. S.D. Tex. Feb. 23, 2021), ECF No. 44. The U.S. Trustee’s objections did not impede the prepack.

¹⁹⁸ LoPucki, *supra* note 16, at 247.

¹⁹⁹ Due Process Preservation Order, *In re Belk, Inc.*, No. 21-30630 (Bankr. S.D. Tex. Feb. 24, 2021), ECF No. 62.

²⁰⁰ LoPucki, *supra* note 16, at 250.

²⁰¹ *But see id.* at 252 (“[T]he acceptance of a Chapter 11 plan signals approval of the plan no more than turning over one’s wallet signals approval of an armed robbery.”).

²⁰² *See id.* (“[T]he bankruptcy courts have no authority to ignore the law.”). Even with chapter 11’s premium on creditor voting, Skeel points out that flat bans on distortions (like RSAs and “deathtrap” provisions) might cause more harm than good. *See* David A. Skeel Jr., *Distorted Choice in Corporate Bankruptcy*, 130 YALE L.J. 366, 366, 370–71 (2020). The same principle might apply to prepacks.

controversy. That controversy is particularly acute because prepacks attempt to take as much of the bankruptcy process out of the public eye as possible. Whether that gambit seems evasive or prudent turns in large part on one's priorities about what bankruptcy courts are meant to accomplish. Put differently, for whom are the bankruptcy courts open?

The two major schools of thought are called traditionalist, or functionalist, and proceduralist. Each of them present both a descriptive and normative portrayal of how bankruptcy works and how it should be reformed. The differences between the two camps run deep. Indeed, after years of debate, in a 1998 law review article, Professor Baird declared an impasse, arguing that the two camps were building from different "uncontested axioms."²⁰³ Yet while each school of thought has a leading paladin or two, most bankruptcy professionals find themselves somewhere in the middle.

1. *The Traditionalist Take on Prepacks*

For the traditionalist or functionalist school, bankruptcy is a public solution to private financial distress. Championed by then-law professor, now-Senator Elizabeth Warren,²⁰⁴ the traditionalist school sees bankruptcy courts as a sort of emergency room, funded by the public and taking all comers. And, to push the metaphor perhaps too far, the goal of the system is to stabilize the patient and stop the bleeding. The bankruptcy system cannot accomplish that goal in a way that makes everyone happy: they will implement rough justice. And, more aggressively, bankruptcy policymakers can impose policy goals upon the process.²⁰⁵ If they want to insulate workers from being fired on the petition date, they can do so. If they want to ensure that healthcare companies do not leave their patients high and dry, they can do that too.

Perhaps a better name for this way of thinking about bankruptcy is "institutionalist," rather than traditionalist. Warren and others value the bankruptcy courts as public institutions with public goals.²⁰⁶ Just like the Securities and Exchange Commission and Commodity Futures Trading

²⁰³ Douglas G. Baird, *Bankruptcy's Uncontested Axioms*, 108 YALE L.J. 573, 573–74 (1998).

²⁰⁴ See Elizabeth Warren, *Bankruptcy Policymaking in an Imperfect World*, 92 MICH. L. REV. 336, 344 (1993); Elizabeth Warren, *Bankruptcy Policy*, 54 U. CHI. L. REV. 775, 777 (1987) [hereinafter Warren, *Bankruptcy Policy*] ("I see bankruptcy as an attempt to reckon with a debtor's multiple defaults and to distribute the consequences among a number of different actors. Bankruptcy encompasses a number of competing—and sometimes conflicting—values in this distribution. As I see it, no one value dominates, so that bankruptcy policy becomes a composite of factors that bear on a better answer to the question, 'How shall the losses be distributed?'" (footnote omitted)).

²⁰⁵ Professor Ronald Mann has argued that any reorganization surplus created by the bankruptcy process can be allocated by the state to whichever stakeholder it chooses. See Ronald J. Mann, *Bankruptcy and the Entitlements of the Government: Whose Money Is It Anyway?*, 70 N.Y.U. L. REV. 993, 1000 (1995).

²⁰⁶ See Warren, *Bankruptcy Policy*, *supra* note 204, at 788.

Commission set out to protect investors,²⁰⁷ and the Consumer Financial Protection Bureau sets out to protect consumers,²⁰⁸ the bankruptcy courts set out to preserve go-forward value in a way that spreads around the pain and ensures that communities across the country are not devastated by financial distress.²⁰⁹ These values are the price of admission.²¹⁰

Viewed in this light, traditionalist bankruptcy scholars tend to view prepacks with suspicion, even alarm. After all, the premise of the prepack is to take advantage of bankruptcy rules while spending almost no time in bankruptcy court. And if bankruptcy courts are meant to keep a watchful eye out for unsecured creditors, the fact that the debtor and secured creditors have conducted most of the process before notifying the court or unsecured creditors seems evasive.

2. *The Proceduralist Take on Prepacks*

By contrast, the proceduralist school sees the primary goal of bankruptcy as providing a level playing field whereupon parties can compete toward a resolution of the company's financial distress. Spearheaded by Professors Thomas H. Jackson and Douglas Baird,²¹¹ the proceduralists argued that bankruptcy is not about adjusting debtors' or creditors' legal rights, but rather about providing "breathing room" and a forum for debate. Their arguments were both descriptive and normative: not only was this theoretical framing the best way to depict bankruptcy law as it exists, but it was also the best way to safeguard and reform it in those areas where it deviated from this vision. Bankruptcy judges, for example, should not put a "thumb on the scale," as Baird recently described it, but should restrain themselves to overseeing a fair and inclusive process, reserving their suspicion and ire for breakdowns in the negotiating process.²¹² Any entitlements provided to the parties by the bankruptcy courts over and above their state law entitlements

²⁰⁷ See Benjamin P. Edwards, *Supreme Risk*, 74 FLA. L. REV. 543, 556–57 (2022).

²⁰⁸ See *id.* at 585; 12 U.S.C. § 5511(a); Alexandra Sickler & Kara Bruce, *Bankruptcy's Adjunct Regulator*, 72 FLA. L. REV. 159, 164 (2020).

²⁰⁹ See Warren, *Bankruptcy Policy*, *supra* note 204, at 788.

²¹⁰ Whether bankruptcy values clash with or resonate with the values of debtor enterprises with an expanded social mission is an open question, and one that one of the Authors has explored at length when it comes to benefit corporations in bankruptcy. See Christopher D. Hampson, *Bankruptcy & the Benefit Corporation*, 96 AM. BANKR. L.J. 93, 118 (2022).

²¹¹ See *e.g.*, THOMAS H. JACKSON, *THE LOGIC AND LIMITS OF BANKRUPTCY LAW* 10 (1986); Douglas G. Baird & Thomas H. Jackson, *Corporate Reorganizations and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy*, 51 U. CHI. L. REV. 97, 101 (1984).

²¹² See BAIRD, *supra* note 39, at 108.

would create a perverse incentive for parties to bring their disputes to bankruptcy court when they should be working it out in the state court system.²¹³

Professor Robert K. Rasmussen took this logic a step further, arguing that firms should be able to design the regime that would govern in the event of insolvency, selecting from a menu of options.²¹⁴

Viewed in this light, proceduralist scholars have largely endorsed prepacks as a way of making bankruptcy negotiations even more efficient. If inclusivity and disclosure are the guiding lights of bankruptcy negotiation postpetition, then so too prepetition. And while the bankruptcy judge may not be able to supervise any prepetition process, so long as the judge is given an opportunity to assess the process and determine whether it provided an appropriate forum, the threat of judicial oversight is still serving its function within the system.

Still, even proceduralist scholars may hold some discomfort with prepack bankruptcy cases. After all, the prepack takes the bankruptcy procedure and moves most of it earlier, away from court supervision. The prepack thus runs roughshod over bankruptcy's default notice provisions, and bankruptcy professionals may well suspect that certain deviations in the process may undermine its inclusivity or fairness.

B. *Small Business Cases Complicate the Picture*

1. *Bankruptcy Values in Miniature*

Small businesses bring unique issues to the bankruptcy debate. They are, as Professor Coordes puts it, “bankruptcy misfits.”²¹⁵ Small businesses tend to be owned by one person—or a small group of people—whose business identity is tied to the company.²¹⁶ The owner may be the founder or entrepreneur who started the business, someone who has been building the company for twenty years. The owner may

²¹³ See Douglas G. Baird, *Loss Distribution, Forum Shopping, and Bankruptcy: A Reply to Warren*, 54 U. CHI. L. REV. 815, 828 (1987) (“Allowing priorities outside of bankruptcy but not inside is an open invitation to forum shopping and would exacerbate all the problems Jackson and I want to minimize.”).

²¹⁴ See Robert K. Rasmussen, *Debtor's Choice: A Menu Approach to Corporate Bankruptcy*, 71 TEX. L. REV. 51, 66–67 (1992). Contractualism provoked another debate among bankruptcy scholars. See, e.g., Elizabeth Warren & Jay Lawrence Westbrook, *Contracting Out of Bankruptcy: An Empirical Intervention*, 118 HARV. L. REV. 1197, 1202 (2005); Susan Block-Lieb, *The Logic and Limits of Contract Bankruptcy*, 2001 U. ILL. L. REV. 503, 518 (2001); Alan Schwartz, *Bankruptcy Contracting Reviewed*, 109 YALE L.J. 343, 346–48 (1999) (proposing a rolling contractualist approach to bankruptcy); Steven L. Schwarcz, *Rethinking Freedom of Contract: A Bankruptcy Paradigm*, 77 TEX. L. REV. 515, 584–85 (1999); Lynn M. LoPucki, *Contract Bankruptcy: A Reply to Alan Schwartz*, 109 YALE L.J. 317, 341–42 (1999).

²¹⁵ Coordes, *supra* note 31, at 377.

²¹⁶ See, e.g., BAIRD, *supra* note 39, at 188 n.13.

also be the business's sole key employee, someone without whom the business simply cannot run. And, correspondingly, the owner's financial future may be tightly connected to the success of the business. Indeed, small business owners sometimes do not take salaries from the business; they are compensated wholly in profits—if there are any.²¹⁷

Additionally, the economies of scale that allow middle-market to large debtors to hire bankruptcy counsel for an expensive chapter 11 case simply are not in play with small business debtors. When they face financial distress, they have no large corporate treasury to draw on.

For those reasons, prepacks fit neatly into the financial profiles and business situations of many small businesses. Owners want to maintain their control over the company and want the certainty that a prepack provides, and constituencies like secured creditors may see a prepack bankruptcy as an efficient and clear-cut approach to an in-court restructuring.

From a theoretical perspective, proceduralist scholars may see some small businesses as the paradigmatic example of cases where prepacks may be helpful. Small businesses—with limited funds and strong reputational concerns from ownership—may find especially appealing a resolution to financial distress that spends as little time in bankruptcy court as possible. Traditionalist scholars, too, may see some small business cases as presenting strong candidates for prepacks. Although large businesses are owned either by the wealthy, diffuse individual investors, or institutional investors with diverse portfolios, small businesses can be the “nest egg” for their owners. Giving ownership a chance to work out a plan with their secured creditors before the bankruptcy gets underway carries the same risks of trampling the rights of the unsecured creditors as it does in a large case, but the benefits are correspondingly higher.

This conclusion is buttressed by the reforms of the SBRA. As discussed above, the SBRA makes the bankruptcy process more streamlined for small businesses and reduces the number of players at the bargaining table—innovations that make prepacks easier to accomplish. The SBRA has thus addressed some of the prepack critics' most compelling arguments against the strategy. For example, LoPucki points out that no official unsecured creditors' committee was appointed in *Belk*, and that the court blessed *Belk*'s prepetition “ad hoc groups.”²¹⁸ In a subchapter V case, of course, the absence of an official unsecured creditors' committee is a nonissue. Similarly, although a standard chapter 11 case generally requires twenty-eight days' notice for the disclosure

²¹⁷ See Gotberg, note 17, at 433.

²¹⁸ See LoPucki, *supra* note 16, at 289. LoPucki does not address whether *Belk*'s prepetition ad hoc groups could have been appropriate under section 1102(b)(1), which specifically authorizes the court to bless creditor-organized, prepetition committees if they were “fairly chosen and [] representative of the different kinds of claims to be represented.” 11 U.S.C. § 1102(b)(1).

statement hearing and, subsequently, for the confirmation hearing, in a small business case, those deadlines can be collapsed.²¹⁹

Vote solicitation may be easier in subchapter V, too. Because plan confirmation does not require an impaired accepting class,²²⁰ some courts have concluded that a subchapter V cramdown plan does not require voting at all so long as the other requirements are met.²²¹

To be clear, ultra-expedited prepacks may not comply with the Bankruptcy Code, whether under subchapter V or chapter 11. As Professor LoPucki and Professor Levitin have pointed out,²²² the Bankruptcy Code's requirement of twenty-eight days' notice of plan confirmation can be shortened for cause,²²³ but it is still subject to other rules that constrain the limits of the strategy. For example, as LoPucki points out, the Rule 2002 notice usually must be given by mail²²⁴ so that even if a bankruptcy judge reduced the notice period to one day, the shortest effective deadline—given the Bankruptcy Code's other rules for mailings—would be four days.²²⁵

Subchapter V does not alleviate those concerns, so for small business debtors hoping to avoid any impropriety, a twenty-eight-day prepack may be the fastest possible case.

²¹⁹ See FED. R. BANKR. P. 2002, 3017, 3017.1.

²²⁰ See 11 U.S.C. § 1191(b) (eliminating the 11 U.S.C. § 1129(10) requirement for confirmation).

²²¹ See, e.g., *In re Arsenal Intermediate Holdings, LLC*, No. 23-10097, 2023 WL 2655592, at *2 (Bankr. D. Del. Mar. 27, 2023).

²²² See LoPucki, *supra* note 16, at 276; Levitin, *supra* note 16, at 1099–1103.

²²³ See FED. R. BANKR. P. 9006(c)(1) (“[W]hen an act is required or allowed to be done at or within a specified time by these rules or by a notice given thereunder or by order of court, the court for cause shown may in its discretion with or without motion or notice order the period reduced.”). Indeed, Rule 9006(c)(1) is subject to exceptions in subsection (c)(2), one of which are the deadlines for filing a plan of reorganization under Rule 3015 in a chapter 12 or chapter 13 case, which cannot be shortened. See FED. R. BANKR. P. 9006(c)(2). The negative implication is, of course, that the bankruptcy court may shorten other deadlines relating to confirmation. Similarly, the plan exclusivity period is subject to strict outer deadlines, deadlines which do not apply in subchapter V. See 11 U.S.C. § 1121(d)(2).

²²⁴ See FED. R. BANKR. P. 2002(b). Excluding adversary proceedings, the court can send electronic notices, instead of mailings, to any recipient who consents in writing or who is a registered user of the court's electronic case file system (“ECF”). See FED. R. BANKR. P. 9036(b).

²²⁵ See LoPucki, *supra* note 16, at 278 (providing that “when a notice is given by mail, three days are added to the prescribed period after the prescribed period would otherwise expire” under Rule 9006(a) (citing FED. R. BANKR. P. 9006(f))). LoPucki registers “doubt that a court could reduce the 28-day periods to one day without abusing its discretion.” *Id.* at 278. Of course, abuse of discretion is an appellate standard of review, so the real question is whether a party asking for such a reduction can show cause under Rule 9006(f)—a standard that should require, at a minimum, an evidentiary hearing. The only possible workaround would be if the entire universe of creditors had consented to electronic notice or were registered ECF users. See *supra* note 224.

2. *Small Is Not Always Simple*

Even so, not all small businesses are appropriate candidates for prepack bankruptcies. Small does not always mean simple. A small business that readily clears the debt ceiling for subchapter V might have a messy balance sheet with disputed, contingent, or unliquidated debt—or a universe of creditors that are unknown or unknowable.²²⁶ And since a prepack typically requires the cooperation of secured creditors,²²⁷ small businesses whose secured creditors are unaccustomed to prepack practice (landlords, trade creditors, or regional banks, say) may have a harder time prompting an effective out-of-court negotiation. Small business debtors who cannot bring the required parties to the table outside of bankruptcy, or who cannot pay for the transaction costs of doing so, may face debt collection action and need the automatic stay and bankruptcy's forum to work out a deal.

Conversely, not all simple cases are small. Imagine a holding company (“HoldCo”) or a mezzanine company (“MezzCo”) whose only business is holding stock in an operating company (“OpCo”). Absent rare legal remedies like piercing the corporate veil, counsel for HoldCo or MezzCo may know—with as close to certainty as one can get—the identities of the entire creditor body. If HoldCo or MezzCo cannot negotiate an out-of-court workout, they may need bankruptcy to cram a plan down on holdouts. But that plan might be close to consensual, and even if it is not, the attorneys for HoldCo and MezzCo can solicit a prepetition vote and provide any nonconsenting debtors with notice of their bankruptcy filing. Now, appreciate that the simplicity of this situation does not turn on the dollar amounts in the capital structure. HoldCo and MezzCo could be small business debtors eligible for subchapter V—or they could have billions of dollars in debt on their books.

3. *Ideal Debtors for Small Business Prepacks*

At least two types of debtors may fit the small business prepack strategy. First, consider a holding company or a mezzanine company that can identify its universe of creditors because it is not an operating company. In situations where the debt burden starts to become overwhelming, the secured creditor might decide to deleverage the balance sheet by filing a quick chapter 11 case to sweep away the unsecured

²²⁶ See, e.g., Shaw, *supra* note 127, at 3 (“[T]he misguided Chapter 11 Lite moniker has resulted in a less expected issue that is raised by sophisticated parties that are surprised when they occasionally find themselves in a Subchapter V. That issue is the erroneous belief that Subchapter V is only for the cheap and easy cases—and that anything that is complicated or deemed sophisticated should not be able to take advantage of Subchapter V despite fitting within its debt cap defined parameters—which belief is wrong.”).

²²⁷ See Swan & Phan, *supra* note 14, at 28.

bond or bank debt—or to negotiate a composition or extension against the backdrop of the threat of a discharge. Such a plan could be fully consensual; if it were, the advantages of subchapter V would be in reduced trustee fees and greater certainty of a smooth path to confirmation.²²⁸ If such a plan were not fully consensual, the secured creditor might well decide that the regular chapter 11 cramdown provisions—which emphasize absolute priority and pro rata treatment—are easier to meet at a contested confirmation hearing than subchapter V’s cramdown provisions. If the secured creditor is undersecured, which is the case for many small businesses, the unsecured creditors stand to gain nothing in a cramdown chapter 11 plan. But their cooperation could be obtained in exchange for some of the value provided by the relatively more streamlined subchapter V consensual plan. The negotiation over whether to do a prepack bankruptcy at all would thus encompass whether the prepack was filed under subchapter V or not.

Second, imagine a small operating business who owes significant debt to a bank that holds liens on all or substantially all the assets of the debtor. The collateral is currently worth more than the amount of the secured debt, so the bank is oversecured. In addition to the bank, the debtor owes numerous unsecured creditors, like trade vendors and employees, who are therefore partially in the money and partially out of the money. The business is limping along, making enough money to service its secured debt, but not much else. The problem for the creditors is that the cooperation of the founder is required: the business will plummet in value without the founder’s labor and expertise. The secured creditor wants to wipe the slate clean of unsecured debt, but it cannot cram a plan down in chapter 11 without washing away the founder’s equity. Instead, the secured creditor proposes a cramdown subchapter V plan that pays off the secured debt, pays nominal or no disposable income over the life of the plan, and then allows the founder to emerge from bankruptcy with a cleaner balance sheet.

Taking all this into account, subchapter V smooths the path for small business prepacks, but that does not mean that prepack cases and small business cases will be coextensive. The next Part explores several initiatives that bankruptcy professionals could undertake to help achieve prepack speed in a subchapter V case.

IV. ACHIEVING PREPACK SPEED IN A SUBCHAPTER V CASE

As explained above, subchapter V’s new rules incentivize debtors and creditors to reach a consensual plan²²⁹ and thus increase the

²²⁸ See Bradley, *supra* note 17, at 278.

²²⁹ See *In re Louis*, No. 20-71283, 2022 WL 2055290, at *17 (Bankr. C.D. Ill. June 7, 2022) (“[A]lthough the provisions of Subchapter V do not affirmatively require a debtor to try to attain

chance of a successful prepack.²³⁰ The debtor will want to avoid the costs associated with up to five years of a subchapter V trustee's supervision and receive its discharge sooner.²³¹ Unsecured creditors have a greater incentive to reach a consensual plan, too, because subchapter V makes cramdowns easier for a debtor.²³² This result is also consistent with the legislative intent to promote a consensual plan, shown by the subchapter V trustee's statutory obligation to "facilitate the development of a consensual plan of reorganization."²³³

This Part first walks through what a subchapter V prepack would look like, imagining the case of GatorCo. It then turns to the closest example of a subchapter V prepack to date, *In re BPI Sports*, and highlights some of the challenges the debtor faced along the way. This Part then advocates for several changes that, although representing only minor adjustments to the SBRA's framework, would further smooth the path toward a small business prepack.

A. *The Small Business Prepack: A Walk-Through*

This Section illustrates how our fictitious retail store from earlier, GatorCo,²³⁴ would file its subchapter V case.

a consensual confirmation . . . the Debtor's decision in this case to forego that effort from the start was certainly contrary to the spirit of the law. And, as it pertains to the Trustee's role, it was contrary to both the spirit and letter of the law.").

²³⁰ A prepack is more likely to result in a successful reorganization when the debtor obtains a consensual plan. *See generally* Practical Law Bankruptcy & Restructuring and Practical Law Finance, *The Prepackaged Bankruptcy Strategy*, THOMSON REUTERS PRAC. L. (2023), <https://us.practicallaw.thomsonreuters.com/9-503-4934> [<https://perma.cc/58W2-3L8S>] ("Execution risk is reduced if the deal is highly consensual, with most key creditors supporting the plan.").

²³¹ Courts, too, may put pressure on debtors to propose shorter plans. *See, e.g., In re Urgent Care Physicians, Ltd.*, No. 21-24000, 2021 WL 6090985, at *10 (Bankr. E.D. Wis. Dec. 20, 2021) ("Congress's recognition that small businesses typically have shorter life-spans than large businesses suggests that a plan term of three years is more reasonable, generally speaking (or as a default), than a five-year term, absent unusual circumstances. And Congress's concern for not only small business owners, but small business employees, customers, and others who rely on such businesses, reflects an intent to balance the shorter life-span planning of small businesses and timely cost-effective benefits to debtors, against the benefits to creditors.").

²³² *See Barcelona Cap., LLC v. Neno Cab Corp.*, 648 B.R. 578, 589 (E.D.N.Y. 2023) ("Subchapter V modifies the rules under which particular classes of claims can be crammed down, which means that a bankruptcy court has greater authority to adopt a debtor's plan even if creditors object to the plan." (quoting *In re Chip's Southington, LLC*, No. 20-21458, 2021 WL 5313546, at *4-5 (Bankr. D. Conn. Nov. 13, 2021))).

²³³ *See* 11 U.S.C. § 1183(b)(7); *see also* Harner et al., *supra* note 128 (finding preliminary data shows that over half of subchapter V cases were able to reach a consensual plan, with most cases being confirmed within 168 days). When a consensual reorganization plan is developed, the trustee's role is terminated, and administrative costs are diminished. This saving aligns with subchapter V's and prepacks' goals of reducing costs. *See* Small Testimony, *supra* note 1, at 4.

²³⁴ *See supra* Section I.B.1 for an analysis of GatorCo's eligibility under Subchapter V.

By this point, GatorCo has concluded bankruptcy makes the most sense after considering out-of-court remedies. After consultation with counsel, GatorCo has concluded it would like to continue operating after bankruptcy, and therefore a chapter 7 liquidation does not make sense. Moreover, GatorCo would like to maintain a positive public image and has emphasized it would like to exit bankruptcy court as quickly as possible.

GatorCo has two options: it can proceed as a small business case under chapter 11 or elect subchapter V. After a review of the costs and benefits of each approach, GatorCo determined subchapter V makes the most sense.²³⁵

GatorCo's first step will be to review its financials. GatorCo begins preparing its twelve-week cash flow models and long-term feasibility model spreadsheets. GatorCo should also investigate whether it anticipates realizing any recovery from a fraudulent, preferential, or other avoidable transfer. GatorCo asks its secured creditor if it wants to advance new funds to pay for the bankruptcy case. With the newly established local rules and guidance regarding subchapter V prepacks,²³⁶ GatorCo can go to its secured creditor with confidence that it can promise a quick reorganization.

GatorCo then reaches out to its unsecured creditors. Unsecured creditors have much less leverage under subchapter V. In some respects, the debtor's outreach to the creditors is out of courtesy, since even if all classes reject the plan—or as is often the case, do not vote at all—it can still be crammed down if it does not discriminate unfairly and is “fair and equitable” concerning each class of claims.²³⁷ Consequently, GatorCo tells the creditors it would like to reach an amicable resolution and, if the creditors agree and sign an RSA, they may receive a better distribution plus the bankruptcy case will be cheaper than if the plan had to be crammed down.²³⁸

In form, GatorCo's restructuring plan is much more condensed than a typical chapter 11 plan. GatorCo has decided to take advantage of the easy-to-use Official Form 425A—essentially a “fill-in-the-blank” reorganization plan.²³⁹ None of the information required to complete

²³⁵ In particular, GatorCo's founder, Allie, is willing to keep working her backbreaking schedule to keep the business in operation, but only if she stands to recover some of the equity value once GatorCo emerges from the plan. Without Allie, the business cannot survive, so debtor's counsel determines that subchapter V is the best option for a path through bankruptcy.

²³⁶ See *infra* Section IV.B.

²³⁷ See 11 U.S.C. § 1191(c).

²³⁸ This additional money results from the subchapter V trustee's role and payments being terminated earlier than if the plan was a cramdown.

²³⁹ See *Official Form 425A: Plan of Reorganization for Small Business Under Chapter 11*, USCOURTS.GOV, https://www.uscourts.gov/sites/default/files/b_425a_0.pdf [<https://perma.cc/PU2X-W8XZ>].

the form is contingent on postpetition activity and can be completed before the bankruptcy filing.

Once GatorCo prepares its first-day filings, it reaches out to the U.S. Trustee's office a few days before it files to ask the U.S. Trustee and the subchapter V trustee likely to be assigned to its case²⁴⁰ to pass along any comments that they may have. GatorCo has followed all requirements of solicitation and disclosure for subchapter V and the U.S. Trustee and subchapter V trustee had only minor changes. In particular, the office asks GatorCo to draft a clearer backup plan in case it cannot make payments.²⁴¹ GatorCo's submittal of the supplemental filings required by the local rules also puts most of its creditors at ease.

When GatorCo submits all its filings, the court agrees at the First Day Hearing that no disclosure statement is required and sets a plan confirmation hearing for twenty-eight days out. One especially testy creditor objects to plan confirmation on the grounds that the plan is infeasible. But with support from the secured creditor, the U.S. Trustee, and the subchapter V trustee, the bankruptcy judge has her concerns assuaged, decides that GatorCo's plan complies with the law, and confirms the plan. One month after filing its petition, GatorCo emerges from bankruptcy and begins making payments.

Ultimately, by using subchapter V as an avenue to restructure its debt, GatorCo was successfully able to exit bankruptcy within a month. The ball was in GatorCo's court during the case, allowing it to bypass many of the risks it would have faced had subchapter V not existed.

B. *Real-Life Limitations*

GatorCo epitomizes the theoretical model of an ideal small business prepack, yet such an archetype remains to be seen. The closest approximation to date is *In re BPI Sports*. Although *BPI Sports* did not fulfill every criterion to be classified strictly as a prepackaged bankruptcy—most notably, the absence of all votes being cast before the filing—it still represents a significant milestone as the first case where the debtor filed a subchapter V plan and a motion to set a confirmation hearing alongside the petition. By looking at *BPI Sports*, we can preview some limitations and challenges for future small business prepacks.

BPI Sports is a company specializing in manufacturing branded supplements for the health industry. In 2023, it faced financial troubles after a failed sales process did not secure the approval of a minority investor. Its circumstances were further worsened by a cash flow shortage that made debt servicing unfeasible. BPI Sports's only way forward, it seemed, was bankruptcy.

²⁴⁰ See *infra* Section IV.B.

²⁴¹ See 11 U.S.C. § 1191(c)(3).

BPI Sports's debts qualified it as a small business debtor under subchapter V. But like many small businesses that would benefit from all of subchapter V's improvements, BPI Sports lacked the funds needed to organize its case. Fortunately, BPI Sports found a lifeline through negotiations with High-Tech Pharmaceuticals ("HTP"), its principal creditor that was owed a supermajority of the debt. HTP committed to finance the administrative expenses associated with bankruptcy, guarantee funding of plan payments to other unsecured creditors, and forgive nearly \$900,000 in prepetition debt. In return, HTP's debt would convert to equity. The sole stipulation was that BPI Sports promptly seek plan confirmation as it entered court. The only way to do this would be through a small business prepack.

BPI Sports did just that.²⁴² It filed for subchapter V bankruptcy, submitted its plan, and moved for a confirmation hearing on September 18, 2023.²⁴³ The plan, which forgave \$900,000 in debt, converted over \$5 million of debt into equity, and funded \$1.8 million for the payment to holders of BPI Sports's remaining debts, received votes of approval from twenty-six creditors shortly thereafter. On October 20, 2023, the court confirmed BPI Sports's plan.²⁴⁴

BPI Sports is the herald of a small business prepack. But it also had some limitations and previews some potential hurdles in the prepack strategy.

First, the Department of Justice and subchapter V trustee seemed reticent throughout the process. For example, the subchapter V trustee asked the court for more time to object to the plan.²⁴⁵ For *BPI Sports*, these concerns did not amount to any true hurdles. The plan was confirmed with no objections. But the warning shot by the subchapter V trustee does signify a potential resistance to a growing practice of prepacks, a concern addressed below by urging increased communication with the subchapter V trustee.²⁴⁶

Second, BPI Sports did not solicit all votes prepetition. Although HTP—the critical vendor—had a supermajority claim, BPI Sports's

²⁴² BPI Sports's proposed order cited a prepublication version of this Article and stated that the strategy outlined in the Article "is precisely what has occurred here." See Notice of Filing Proposed Confirmation Order, *In re* BPI Sports, LLC, No. 23-17463 (Bankr. S.D. Fla. Oct. 19, 2023), ECF No. 114.

²⁴³ *BPI Sports* filed an emergency motion to set confirmation hearing, citing the pre negotiated RSAs that required an immediate request for confirmation. See Debtor's Emergency Motion to Set Confirmation Hearing and for Related Relief at 1, *In re* BPI Sports, LLC, No. 23-17463 (Bankr. S.D. Fla. Sept. 18, 2023), ECF No. 17 ("[T]he petition and plan of reorganization in this case hinges upon an expedient administration of the case that minimizes administrative costs to preserve the going concern, enterprise value of the business.").

²⁴⁴ Order Confirming the Debtor's Subchapter V Plan of Reorganization, *supra* note 137.

²⁴⁵ See Subchapter V Trustee's *Ex Parte* Motion for Extension of Time to File Objection to Confirmation, *In re* BPI Sports, LLC, No. 23-17463 (Bankr. S.D. Fla. Oct. 6, 2023), ECF No. 88.

²⁴⁶ See *infra* Section IV.C.4.

trade creditors were still entitled to vote.²⁴⁷ In other words, not all the creditors were solicited and accepted the plan prepetition.²⁴⁸ If BPI Sports had not met the numerosity requirement, the plan would have to be a cramdown.²⁴⁹ A few trade creditors voting “no” would have made the plan nonconsensual. That concern did not materialize in *BPI Sports*, but it could in other cases.

C. *How to Smooth the Path Forward*

This Article has emphasized the legislative intent of subchapter V to promote speed. However, as Bankruptcy Judge Benjamin Kahn framed it, a better iteration of its purpose is “to provide small businesses with the presumption of a faster, more efficient, and feasible path to reorganization.”²⁵⁰ A debtor entering subchapter V is not guaranteed to exit quickly. And although not all small businesses are suited to have their cases disposed of quickly, or filed as a prepack,²⁵¹ there are multiple ways to streamline the process for those debtors who are suited for the small business prepack. Those improvements are discussed below.

1. *Promote Precrisis Preparation*

First, small businesses should insulate their businesses from the chaos of financial distress by maintaining good records beforehand. Financial distress can feel like a maze for small businesses, leaving them puzzling “how did we get here?” and “what is the best escape route?” Answering these questions is not usually a simple task, and one that is best undertaken before a bankruptcy filing.

To be sure, subchapter V makes bankruptcy cases simpler.²⁵² Even still, it is difficult to file a subchapter V without preparing beforehand: “the roadmap for [the] fast path to success must be ready early on in the case. So, without the necessary advance preparation, the subchapter V

²⁴⁷ BPI’s counsel remarked that soliciting all trade creditors before the petition date was not feasible. *September 22, 2023, Virtual Public Hearing*, at 56:17–56:52, AM. BANKR. INST., <https://subtaskforce.abi.org/hearings/september-22-2023-virtual-public-hearing> [<https://perma.cc/EEL9-KHBF>].

²⁴⁸ *See id.*

²⁴⁹ 11 U.S.C. § 1191(b).

²⁵⁰ Benjamin A. Kahn, *Written Statement of the Hon. Benjamin A. Kahn*, AM. BANKR. INST. 3 (June 23, 2023) (emphasis omitted), https://abi-org.s3.amazonaws.com/SubV/wstatements/Benjamin_Kahn_Statement.pdf [<https://perma.cc/3RMU-LMAH>].

²⁵¹ Some debtors enter bankruptcy ill-prepared or needing the protection of the bankruptcy court while it works out its issues. *See supra* Part III.

²⁵² The easy-to-use form plan B 425A and the contracted disclosure under the SBRA—which can be set out in the plan and need not be a separate form—all point toward subchapter V’s inherent efficiency.

cannot possibly work”²⁵³ Some courts have even revoked the subchapter V designation when the debtor has not moved with the speed envisioned by Congress.²⁵⁴

Because the cramdown and feasibility rules in subchapter V are more demanding than under chapter 11, small business debtors may need to do an even better job at keeping records than their chapter 11 counterparts. If GatorCo has no documentation of its revenues or operating expenses, how will it formulate a reorganization plan? Similarly, how will it prove projected disposable income or feasibility of its plan—if it can create one?

For small businesses to navigate bankruptcy swiftly, they must maintain accurate records. For that reason, small business debtors should engage in precrisis preparation. The costs of professional help feel high to cash-strapped businesses, and many small businesses cannot afford not to hire professionals.²⁵⁵ Those outside of the bankruptcy bar—corporate counsel, accountants, and tax preparers—should urge their small business clients to invest in professional help or, at a minimum, use financial management software like QuickBooks. Even with subchapter V, this preemptive approach is a prerequisite to escaping the protracted financial nightmares that bankruptcy was for small businesses not too long ago.

2. Clarify Standards for Cramdown Plans

Second, the standards for cramdown plans must be sketched out with greater clarity, whether by adjudication, local rule, or congressional action.²⁵⁶ In the context of subchapter V, the “fair and equitable” standard and the “feasibility” standard are both ambiguous. This ambiguity makes plan confirmation ripe for contestation—especially since feasibility “is the most important element of [plan confirmation].”²⁵⁷

²⁵³ Cathy Peek McEwen, *Don't Put the Brakes on a Subchapter V*, TAMPA BAY BANKR. BAR ASS'N (Aug. 26, 2021), <https://www.tbba.com/dont-put-the-brakes-on-a-subchapter-v> [<https://perma.cc/GXF9-JQWA>]; see also *In re Seven Stars on the Hudson Corp.*, 618 B.R. 333, 347 (Bankr. S.D. Fla. 2020) (“Subchapter V is intended to be an expedited process. The debtor has the opportunity to use new, powerful tools to reorganize and save its business; but it must do so quickly.”).

²⁵⁴ See, e.g., *In re Nat'l Small Bus. All., Inc.*, 642 B.R. 345, 349 (Bankr. D.D.C. 2022) (revoking the debtor's subchapter V designation after finding “the Debtor's case has not progressed with the expediency Subchapter V case[s] are expected to achieve”).

²⁵⁵ Many thanks to subchapter V trustee Amy Denton Mayer for this point. Mayer was also HTP's counsel in *BPI Sports*.

²⁵⁶ See Michael C. Dorf, *Legal Indeterminacy and Institutional Design*, 78 N.Y.U. L. REV. 875, 915 (2003) (“[A]mbiguity is the enemy of law.”).

²⁵⁷ *In re Bashas' Inc.*, 437 B.R. 874, 915 (Bankr. D. Ariz. 2010). Feasibility functions to distinguish aspirational plans from realistic plans—a distinction that can alter the outcome of any case. *In re Curiel*, 651 B.R. 548, 561 (B.A.P. 9th Cir. 2023) (“[T]he purpose of the feasibility requirement ‘is to prevent confirmation of visionary schemes which promise creditors and equity security

Recall that subchapter V plans must be “fair and equitable concerning each class of claims or interests.”²⁵⁸ The Code introduces two requirements for a cramdown plan to be “fair and equitable”: the plan must (1) pay secured creditors in full (whether through cash, deferred payments, or retained liens), the same as in a normal chapter 11, and (2) pay projected disposable income toward unsecured debt. In addition, the plan must be “feasible”: the debtor must prove it will be able to make all payments under the plan, or it has a reasonable likelihood of making all plan payments and has an appropriate contingency plan if that fails.²⁵⁹ Notably, the provisions of subchapter V allow a debtor to obtain “micro exit financing”: use the new line of credit to pay the present value of its projected disposable income, exit bankruptcy entirely, and make its ongoing payments to the new lender, rather than the old creditors.²⁶⁰

The definition of “disposable income” in subchapter V, however, is so flexible that, as Bradley points out, debtors may exploit it to their advantage.²⁶¹ For business debtors in subchapter V, “disposable income” means income “not reasonably necessary to be expended . . . for the payment of expenditures necessary for the continuation, preservation, or operation of the business of the debtor.”²⁶² Even though “disposable income” is more sharply defined in chapters 12²⁶³ and 13,²⁶⁴ income requirements are hard to write and susceptible to gaming.²⁶⁵ Debtors have every incentive to allocate generous amounts to the “continuation, preservation, or operation” of the business, lowballing payments to creditors. Creditors, conversely, will focus on the word “necessary.” Any uncertainty may lead to a contested confirmation hearing, especially when debtors propose to pay creditors with actual disposable income rather than fixed payments. Courts will have to address how disposable income fits into decisions to grow or shrink the business, as well as

holders more under a proposed plan than the debtor can possibly attain after confirmation.” (quoting *Pizza of Haw, Inc. v. Shawkey’s Inc.* (*In re Pizza of Haw, Inc.*), 761 F.2d 1374, 1382 (9th Cir. 1985))).

²⁵⁸ 11 U.S.C. § 1191(c); *see also id.* § 1129(b)(2)(A).

²⁵⁹ *See id.* § 1191(c)(2)–(3).

²⁶⁰ *See id.* § 1191(c)(2)(B). This “micro exit financing” concept was discussed by attorney Robert Keach at the 2024 Southeastern Bankruptcy Law Institute’s 50th Annual Seminar.

²⁶¹ *See* Bradley, *supra* note 17, at 274 (“Debtors will have every incentive to lowball their projected revenues and to maximize their projected expenses, leaving a fig leaf of a plan payment to unsecured creditors beyond what is required to pay priority and secured claims.”).

²⁶² 11 U.S.C. § 1191(d).

²⁶³ *Id.* § 1225(b)(2).

²⁶⁴ *Id.* § 1325(b)(2).

²⁶⁵ *See* Bradley, *supra* note 17, at 273 n.101; *see also, e.g.*, Trustee’s Objections to Debtors’ First Amended Chapter 11 Plan at 3, *In re Sizzler USA Restaurants, Inc.*, No. 20-30748 (Bankr. N.D. Cal. Dec. 29, 2020), ECF No. 108 (the subchapter V trustee objected to the plan because the debtor’s projections were a “moving target”).

clarify whether the owner may take a salary over the life of the plan. If the contours of the rule are not successfully sketched out by case law, Congress may need to provide further clarity.

The third requirement, subchapter V's "feasibility" test, requires a more in-depth look than a standard chapter 11 analysis. Although chapter 11 requires a court to find that the plan is not likely to lead to another liquidation or reorganization,²⁶⁶ subchapter V also requires the court to conclude that the debtor can make all the payments—and if the court is not convinced, that the debtor has an appropriate backup plan.²⁶⁷ But courts struggle to effectively oversee debt adjustment plans extending far into the future.²⁶⁸ Although each determination must be made on a case-by-case basis, courts can provide guidance on what types of financial documents and evidentiary support are most helpful to supporting a plan at confirmation. Providing additional legislative or judicial clarity on the feasibility determination will ensure that courts are confirming only the plans that actually meet the requirements and will assist parties in negotiating their way to a confirmable plan prior to the bankruptcy case being filed.²⁶⁹

3. Clarify the Subchapter V Trustee's Role as "Facilitator" and "Watchdog"

Third, the role of the subchapter V trustee should be clarified. A subchapter V trustee plays an imperative role in the case. Perhaps most notably, the subchapter V trustee's presence helps judges who benefit from the subchapter V's unbiased opinions.²⁷⁰ As emphasized by Bankruptcy Judge Deborah L. Thorne, "The negotiations which happen during phone calls or in conference rooms are what lead to success, and the subchapter V trustee—who is present for these discussions but has no emotional or financial ties to the debtor—can provide sage

²⁶⁶ See 11 U.S.C. § 1129(a)(11) ("Confirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan, unless such liquidation or reorganization is proposed in the plan.").

²⁶⁷ *In re Samurai Martial Sports, Inc.*, 644 B.R. 667, 698 (Bankr. S.D. Tex. 2022) ("[Section 1191(c)(3)] fortifies the more relaxed feasibility test that § 1129(a)(11) contains.").

²⁶⁸ For a helpful overview of the theoretical and practical problems plaguing the bankruptcy courts' supervision of estates, see generally Jonathan M. Seymour, *The Limited Lifespan of the Bankruptcy Estate: Managing Consumer and Small Business Reorganizations*, 37 EMORY BANKR. DEV. J. 1 (2020).

²⁶⁹ See, e.g., LoPucki, *supra* note 16, at 252–53 (underscoring the importance of the feasibility determination in prepack cases).

²⁷⁰ See Deborah L. Thorne, *Remarks of Deborah L. Thorne*, AM. BANKR. INST. (July 14, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/Deborah_Thorne_Written_Statement.pdf [<https://perma.cc/W4PF-H6UY>] ("Having a third party who can evaluate without emotion or financial interest has greatly assisted judges and has increased the success rate in subchapter V cases.").

and independent insight to the court.”²⁷¹ According to proceduralists, the bench should endorse these out-of-court workouts with open arms. Some judges, however, value an impartial endorsement from someone who was “in the room” during negotiations. But even if the subchapter V trustee is “in the room,” are they obligated to vet for and report misconduct, such as an insider transaction? The law is not clear.

Bankruptcy Judge Craig Goldblatt frames this question as whether the subchapter V trustee, as an “honest broker,” has a duty to be a “watchdog.”²⁷² The watchdog role is traditionally undertaken by the U.S. Trustee’s office and the creditors’ committee—the latter of which subchapter V removed.²⁷³

Subchapter V trustees should be obligated to take on this role, but only to an extent. The trustee’s explicit duty to “facilitate the development of a consensual plan of reorganization” implicitly requires the trustee to help develop a *lawful* plan.²⁷⁴ In this sense, Judge Goldblatt’s belief that the watchdog role of the trustee should be delineated through case law, not necessarily congressional clarification, may be correct.²⁷⁵ The Department of Justice’s Subchapter V Trustee Handbook already requires the trustee to report any bankruptcy crime under sections 152 and 157.²⁷⁶ The Handbook, however, should be revised to require that the subchapter V trustee report any suspected insider dealings to the U.S. Trustee.²⁷⁷ The “watchdog” role is necessary to streamline subchapter V cases. When a plan is filed with the court immediately, the subchapter V trustee’s scrutiny may alleviate some of the concerns associated with the lack of court oversight in regular prepack cases.²⁷⁸

4. *Facilitate Coordination with the Subchapter V Trustee*

Fourth, court districts should facilitate prefiling coordination with the subchapter V trustee likely to be assigned to the case. Not only do trustees provide value to judges when attesting to what happened “in the room,” but they can also provide guidance to debtors during

²⁷¹ *Id.*; see also Goldblatt, *supra* note 68, at 2 (“[J]udges should be careful not to jump to conclusions about what they think is happening in rooms that they are not in.”).

²⁷² See Goldblatt, *supra* note 68, at 6.

²⁷³ Should the court be made aware of a potential improper dealing, it retains the authority to appoint a creditors’ committee. See 11 U.S.C. § 1181(b). Case law seems like the best choice to establish when the court should appoint a creditors’ committee.

²⁷⁴ See 11 U.S.C. § 1183(b)(7).

²⁷⁵ See Goldblatt, *supra* note 68, at 7.

²⁷⁶ See SBRA Handbook, *supra* note 101, at 5-4.

²⁷⁷ See, e.g., *In re Corinthian Commc’ns, Inc.*, 642 B.R. 224, 233 (Bankr. S.D.N.Y. 2022).

²⁷⁸ However, additional time may be required because the subchapter V Trustee must communicate any concerns with the plan to the U.S. Trustee before filing an objection with the court. See SBRA Handbook, *supra* note 101, at 3-10.

negotiations.²⁷⁹ Subchapter V trustees possess unique skill sets,²⁸⁰ Some are litigators, and others are accountants or turnaround specialists. This knowledge, however, is valueless if the debtor does not communicate with the trustee.

The SBRA anticipated that subchapter V filings would become common enough that jurisdictions might need one or more standing subchapter V trustees.²⁸¹ Districts that want to encourage subchapter V prepacks should consider appointing standing subchapter V trustees, so that debtors' counsel can share the plan with them before filing.²⁸²

For the same reason, jurisdictions should require debtors to communicate regularly with the subchapter V trustee. Take, for example, the initial order for debtors in the Middle District of Florida:

Communication with Subchapter V Trustee. Debtor's counsel or, if Debtor is self-represented, Debtor, shall contact the Subchapter V Trustee (the "Trustee") within five days of the date of this order to discuss the Trustee's facilitation of the development of a consensual plan of reorganization. The Debtor is expected to communicate regularly and share information with the Subchapter V Trustee as is appropriate under the facts of the case.²⁸³

²⁷⁹ See Thorne, *supra* note 270, at 2 ("In several cases, the operational experience of the subchapter V trustee has led to improved pricing, marketing, and other business advice which has saved businesses and led to confirmable plans.").

²⁸⁰ In theory, all subchapter V trustees should hold the requisite skills need to facilitate plans efficiently. However, as some practitioners note, "the skill sets and motivations of the pool of applicants were understandably varied." See Meredith S. Grabill, *Written Statement of The Hon. Meredith S. Grabill*, AM. BANKR. INST. 4 (July 14, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/Meredith_Grabill_Written_Statement.pdf [<https://perma.cc/9TQX-XDTK>]. For this reason, we also urge the U.S. Trustee to offer training to potential trustees to "promote uniformity and consistency in skills sets among [them]." *Id.* at 5. Some jurisdictions are already doing so. See, e.g., Susan K. Seflin, *Written Statement of Susan K. Seflin*, AM. BANKR. INST. (July 14, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/Susan_Seflin_Written_Statement.pdf [<https://perma.cc/6QGP-G98Z>] ("In January of 2021, the subchapter [V] trustees in the Central District of California participated in a weeklong mediation training program to improve our mediation skills and it was incredibly helpful.").

²⁸¹ See 28 U.S.C. § 586(b) ("If the number of cases under chapter 12 or 13 of title 11 commenced in a particular region so warrants, the United States trustee for such region may, subject to the approval of the Attorney General, appoint one or more individuals to serve as standing trustee, or designate one or more assistant United States trustees to serve in cases under such chapter."); see also 11 U.S.C. § 1183(a).

²⁸² Subchapter V trustees are paid out of the plan, so their business model already relies on deferred payments. See 28 U.S.C. § 586(e)(2). Thus, a subchapter trustee might welcome the opportunity to review a small business prepack plan before it was filed, saving time and expense later in the case.

²⁸³ Order Prescribing Procedures in Chapter 11 Subchapter V Case, Setting Deadline for Filing Plan, and Setting Status Conference (M.D.F.L. Bankr.) (on file with authors). Penalties for failing to comply include "imposition of sanctions against the Debtor or Debtor's counsel, including, but not limited to, conversion or dismissal of the case, removal of the Debtor as debtor-in-possession, and monetary sanctions." *Id.*

The rule is a step in the correct direction but should go further in specifying the minimum timing of communication. For example, a debtor must submit a plan within ninety days of the initial petition.²⁸⁴ This means the debtor could submit the plan on the ninetieth day, without the trustee ever seeing the plan. And some debtors do. Unfortunately, many of these plans are mere “placeholders” where the debtor did not provide the trustee with an opportunity to review the plan.²⁸⁵ A rule specifying the requirements of communication, specifically requiring the debtor to submit filings to the trustee, may streamline the case. Consider this addition:

The Debtor shall submit any disclosure statement, proposed plan, and related motions to the Trustee no later than three days before the Debtor files the papers with the court.²⁸⁶

The addition of one sentence would not only allow the subchapter V trustee to advise the debtor of any oversight but would also force regular correspondence with the trustee.

5. Clarify or Develop Local Rules

Finally, and consistent with bankruptcy’s objective to facilitate the efficient resolution of cases, courts can promulgate local rules that delineate what is necessary to streamline a debtor’s time in court.²⁸⁷ Local rules work in tandem with the Bankruptcy Code provisions to achieve “the orderly and expeditious disposition of cases.”²⁸⁸ A significant advantage of local rules is their ability to be implemented and revised quickly by the judiciary. Moreover, local rules can respond to the differing needs of specific jurisdictions. Notably, although numerous jurisdictions have promulgated local rules for chapter 11 prepacks,²⁸⁹

²⁸⁴ 11 U.S.C. § 1189(b).

²⁸⁵ See ABI FINAL REPORT, *supra* note 72, at 53 (explaining that a “placeholder plan” is where a “practitioner[] file[s an] incomplete or bare-bones plan solely to meet the 90-day statutory deadline with the expectation that they can remedy the deficiencies prior to the confirmation hearing”).

²⁸⁶ This order is entered into a case after the debtor files its case, and thus would not require the debtor to submit filings to anyone before entering court. However, we do suggest that jurisdiction enact local rules doing exactly that. See *infra* Section IV.C.5.

²⁸⁷ See FED. R. CIV. P. 83(a); FED. R. BANKR. P. 9029(a).

²⁸⁸ *Federal Rules, Local Rules & General Orders*, U.S. DIST. CT., N.D.N.Y., www.nynd.uscourts.gov/federal-rules-local-rules-general-orders [<https://perma.cc/N3ZR-T7HQ>]; see *Procedural Guidelines for Prepackaged Chapter 11 Cases in the United States Bankruptcy Court for the Southern District of New York*, U.S. BANKR. CT., S.D.N.Y. [hereinafter SDNY Prepack Guidelines], www.nysb.uscourts.gov/sites/default/files/prepack.pdf [<https://perma.cc/YYC4-EZY8>] (“[T]his document . . . attempts to provide bankruptcy practitioners with help in dealing with practical matters which either are not addressed at all by statute or rules or are addressed indirectly in a piecemeal fashion . . .”).

²⁸⁹ The Bankruptcy Court for the Southern District of New York promulgated local rules for prepacks in 2024 without mentioning subchapter V. See *In re Amended Procedural Guidelines for*

the Authors have not identified any local rules explicitly addressing subchapter V prepacks.

Although courts have not specifically addressed subchapter V prepacks, local rules governing chapter 11 prepacks should apply equally to subchapter V.²⁹⁰ These established local rules address a range of matters relevant to the small business prepack, including filing requirements, disclosure obligations, notice procedures, and plan confirmation standards.²⁹¹

First, local rules should require a debtor desiring a small business prepack to submit its plan and all first-day papers to the U.S. Trustee's office at least one week before it intends to enter court.²⁹² With the imperative role that a subchapter V trustee plays in a subchapter V case, submitting filings to the U.S. Trustee's office—and, through that office, to the subchapter V trustee assigned to the case—before the case's start would allow the debtor to resolve any issues the trustee has with the filing, reduce the uncertainty of whether the trustee will delay the case with objections, and reduce the administrative burden on the U.S. Trustee's office. The U.S. Trustee's office already mandates that a prospective subchapter V trustee review initial case filings within two days of the case being filed.²⁹³ And, “[i]mmediately upon appointment, the trustee must determine the status of the case.”²⁹⁴ The subchapter V trustee thus has no time to waste after the initial case filing, and prescribing for early satisfaction of those obligations will alleviate some of the pressure the office is under to ensure a speedy case.

Prepackaged Chapter 11 Cases, U.S. BANKR. CT., S.D.N.Y. (Jan. 22, 2024), <https://www.nysb.uscourts.gov/sites/default/files/m621.pdf> [<https://perma.cc/9N6V-MLHS>]. The Bankruptcy Court for the Southern District of Florida recently abrogated its local rule for chapter 11 prepacks in favor of the “current local rules and procedures set forth on the individual web pages for each judge.” *In re Abrogation of Local Rule 3017-3, Court Guidelines for Prepackaged Chapter 11 Cases, and Clerk’s Instructions for Chapter 11 Cases*, U.S. BANKR. CT., S.D. FLA. (May 27, 2021), https://www.flsb.uscourts.gov/sites/flsb/files/documents/general-orders/AO_2021-04_Abrogation_of_Local_Rule_3017-3%2C_Court_Guidelines_for_Prepackaged_Chapter_11_Cases%2C_and_Clerk’s_Instructions_for_Chapter_11_Cases.pdf [<https://perma.cc/6JNL-5QFP>].

²⁹⁰ See *In re Double H Transp. LLC*, 603 F. Supp. 3d 468, 473 (W.D. Tex. 2022) (“[S]tatutory sections that apply to standard Chapter 11 bankruptcies apply to Subchapter V. . .”).

²⁹¹ For example, although the Southern District of New York Prepack Guidelines outlines rules such as Creditors’ Committees and voting requirements that are not relevant in subchapter V, other rules such as scheduling motions and notice requirement are applicable to subchapter V cases. See SDNY Prepack Guidelines, *supra* note 288; see also *supra* Section II.B (noting the lack of a statutory committee of unsecured creditors); *In re Arsenal Intermediate Holdings, LLC*, No. 23-10097, 2023 WL 2655592, at *2 (Bankr. D. Del. Mar. 27, 2023) (“[T]here is no requirement that creditor votes be solicited in a case under subchapter V.”).

²⁹² Standard chapter 11 prepack guidelines consistently have provisions requiring a debtor to communicate with the U.S. Trustee before filing bankruptcy. See, e.g., SDNY Prepack Guidelines, *supra* note 288.

²⁹³ SBRA Handbook, *supra* note 101, at 3-10.

²⁹⁴ *Id.* at 3-1.

Second, courts adopting subchapter V guidelines should address presumptively reasonable notice periods²⁹⁵ and provide a model official ballot. Presumptive notice period will give creditors ample opportunity to contest the plan, even though such objections may be overcome with subchapter V's easier path to cramming down a plan. Similarly, the model official ballot provides a preapproved means to collect votes, diminishing the chance that a successful objection can be made as to the ballot's adequacy.²⁹⁶

CONCLUSION

Small businesses need a bankruptcy process that enables them to reorganize effectively—especially given the vital role that small businesses play in the American economy.²⁹⁷ For decades, Congress has tried to speed up chapter 11 bankruptcies without hindering bankruptcy's rehabilitative goals. Those attempts have not worked for small businesses. The Bankruptcy Reform Act of 1994 codified a fast-track option for small businesses but neglected to account for small business debtors' lack of resources. BAPCPA directly addressed prepacks and sped up small business cases, but its provisions were so convoluted that very few debtors could successfully exit bankruptcy.

The SBRA represents Congress's best approach to date. Subchapter V's departure from the absolute priority rule, simplified paperwork, and quicker timelines allow debtors to successfully exit bankruptcy quickly.²⁹⁸ The ability for a small business owner to keep equity in the company after getting through the subchapter V payment plan incentivizes small business owners to take advantage of bankruptcy. For their part, creditors are more likely to work with debtors to facilitate

²⁹⁵ Cf. SDNY Prepack Guidelines, *supra* note 288, at 22 (requiring a twenty-day notice period).

²⁹⁶ Cf. *In re Walat*, 87 B.R. 408, 414 (Bankr. E.D. Va. 1988), *aff'd*, 89 B.R. 11 (E.D. Va. 1988) (finding that a bankruptcy court had the authority to issue a local rule prescribing a form for chapter 13 plans that differed from the Official Forms and that the rule “insure[d] the just, speedy and inexpensive determination of chapter 13 plan confirmations”).

²⁹⁷ See, e.g., Cipriano, *supra* note 17, at 149 (describing how small businesses “drive the American economy”); Mawhinney, *supra* note 6, at 29 (“There is a saying in bankruptcy: Equality is equity. The social good bankruptcy delivers is preserving something for the greatest number of stakeholders. Subchapter V helps small business owners hold onto what they have. It is a bulwark against financialization, preserving individual wealth and keeping it diffuse across society. Ultimately, this increases the number of stakeholders and strengthens the legitimacy of our institutions. A strong liberal society depends on lots of individuals with a vested stake.”).

²⁹⁸ See Robert J. Gonzales, *Written Statement for June 23, 2023 Public Hearing on Eligibility Issues in Subchapter V Cases*, AM. BANKER. INST. (June 22, 2023), https://abi-org.s3.amazonaws.com/SubV/wstatements/Robert_Gonzales_Statement.pdf [<https://perma.cc/7RGD-U7U8>] (“My firm has successfully confirmed every Subchapter V case we have filed, and the timeframe for confirmation has been as little as 49 days (petition date to confirmation order).”).

a consensual plan so that they avoid subchapter V's easier path to a cramdown.

As argued above, these innovations also make subchapter V a particularly viable forum for a small business prepack. Subchapter V implicitly fosters prepacks while avoiding many of the limitations of standard chapter 11 prepacks, including scholars' concerns with prepacks violating notice periods. Because of this revolution in bankruptcy law, practitioners should reassess their standard bankruptcy practices. Debtors who want to exit bankruptcy quickly should reassess their subchapter V eligibility. Similarly, debtors already filing a subchapter V case should consider whether their case might make sense as a prepack. A debtor who fails to be ready early in the case lacks respect for the legislative intent of subchapter V and may "artificially press[] the brakes" on its case.²⁹⁹

Time will tell. Small businesses have been using the Bankruptcy Code to reorganize for a long time, but subchapter V practice is still relatively young. The Authors take no position on how voluminous small business prepacks will become. Subchapter V's prodebtor innovations may alter the equilibrium so that prepacks are less necessary than they were before the SBRA. Debtors may file for subchapter V to obtain the benefits and expertise of a subchapter V trustee. And as discussed above, not every small business debtor fits the profile for a prepack strategy; the approach only works in very particular circumstances—and most crucially require debtors and creditors who can coordinate prebankruptcy.

There is still a lot to be worked out, as discussed above in Part IV. The standards for cramdown plans under subchapter V are murky. Even though courts can attempt to delineate the edges of projected income, Congress may need to provide further clarity. Similarly, coordination with the U.S. Trustee's office, subchapter V trustees, and precrisis preparation may help smooth the path forward to fast-track reorganization. Lastly, courts should provide clear guidance with local rules, as many already do for chapter 11 and chapter 11 prepack cases.

Chapter 11 is not always the end of the story for American businesses. It can represent an opportunity for a fresh start, and the system accordingly sets out to preserve not just the value of the business's assets but the go-forward value of the enterprise as a whole. To be sure, bankruptcy is an area of hard-edged negotiation and—in the big business context—attracts bankruptcy professionals who spend their working days in the gritty world of financial distress.³⁰⁰ But for small business owners, bankruptcy also stands for American pragmatism and

²⁹⁹ McEwen, *supra* note 253.

³⁰⁰ See, e.g., Jared A. Ellias, Ehud Kamar & Kobi Kastiel, *The Rise of Bankruptcy Directors*, 95 S. CAL. L. REV. 1083, 1095–96 (2022) (analyzing the increasing role of bankruptcy directors

American optimism. Creative and problem-solving lawyers who represent small businesses, their creditors, and their stakeholders, should take advantage of the SBRA —prepacks and all—to find strategies that enable small business debtors to turn around and try again.

appointed prepetition); Jared A. Elias & Robert J. Stark, *Bankruptcy Hardball*, 108 CAL. L. REV. 745, 757–62 (2020) (describing the rise in hard-edged tactics in insolvency).