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**The Long and Winding Road to the Small Business Reorganization Act: Why Our next Stop Should Be Simplicity and Accessibility**

Daniel O'Hare  
*West Virginia University College of Law*

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THE LONG AND WINDING ROAD TO THE SMALL BUSINESS REORGANIZATION ACT: WHY OUR NEXT STOP SHOULD BE SIMPLICITY AND ACCESSIBILITY

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I. INTRODUCTION

The road through the COVID-19 pandemic has been rough for small and medium-sized businesses, given problems such as limited access to capital, difficulty in meeting customer expectations, and scrambling to adopt different hiring techniques. So far, these problems have resulted in a surge of business bankruptcy filings; such filings in September 2020 were up 78% as compared with those from September 2019. Businesses filed 715 Chapter 11 bankruptcies in the United States during September 2020, compared with 460 during September 2019. While total commercial bankruptcy filings were up 33% over the previous year's data by September 2020, individual bankruptcies actually fell in this period, perhaps due to government aid.

Locally, some medium-sized businesses in West Virginia, including those barely holding on before the COVID-19 pandemic, have faced problems even when already reorganizing through Chapter 11. For example, the parent company of Williamson Memorial Hospital filed for Chapter 11 bankruptcy in October 2019, due in part to the difficulty of delivering healthcare in rural West Virginia. The only hospital in Mingo County, Williamson Memorial, saw its revenues drop by half when COVID-19 forced the cancelation of elective surgeries and reduced emergency room visits from 800 to 300 per month. The hospital had been the main employer in the city, paying $100,000 a year in property taxes and providing a third of the city's occupation and business tax revenue. While Williamson Health & Wellness purchased the hospital for

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5 U.S. Commercial Bankruptcies, supra note 2.


8 Id.

9 Id.
$3,680,000 during its Chapter 11 reorganization, it did not immediately reopen the facility.\textsuperscript{10} For medium-sized businesses such as Williamson Memorial, Chapter 11 is not a magic bullet.

Indeed, the road to reorganization is complex even at the best of times. Issues such as strict deadlines, burdensome reporting requirements, and convoluted definitions have made Chapter 11 increasingly less relevant for small and medium-sized businesses for decades. In response to these longstanding concerns, Congress passed the Small Business Reorganization Act (SBRA) in 2019. The purpose of this act is “to streamline the reorganization process for small business debtors because small businesses have often struggled to reorganize under Chapter 11.”\textsuperscript{11} The new provision for small businesses, Subchapter V, “is intended to be less costly and time-consuming than a traditional case.”\textsuperscript{12} The SBRA made many positive changes, including (1) allowing the owner of a small business to retain a stake in the business as long as its reorganization plan is fair and equitable and the plan does not discriminate unfairly;\textsuperscript{13} (2) allowing only the debtor the right to file a plan;\textsuperscript{14} (3) not requiring a specific timetable for the plan to be confirmed;\textsuperscript{15} (4) creating a new Subchapter V trustee tasked with “facilitat[ing] the development of a consensual plan of reorganization,” among other duties;\textsuperscript{16} (5) requiring an initial status conference within 60 days of the order for relief “to further the expeditious and economical resolution” of the reorganization;\textsuperscript{17} and (6) eliminating the requirement for an


\textsuperscript{11} \textit{In re} Ventura, 615 B.R. 1, 12 (Bankr. E.D.N.Y. 2020).

\textsuperscript{12} \textit{In re} Parking Mgmt., Inc., 620 B.R. 544, 547 (Bankr. D. Md. 2020).

\textsuperscript{13} 11 U.S.C.A. § 1191(b) (West 2021); see generally Hon. Paul W. Bonapfel, \textit{A Guide to Subchapter V of the U.S. Bankruptcy Code} 46–47 (2020). In bankruptcy jargon, this provision describes the elimination of the absolute priority rule. A full discussion of how the SBRA changed Chapter 11 reorganization for small businesses is beyond the scope of this paper. For an extremely helpful overview, see \textit{Bonapfel, supra}.

\textsuperscript{14} 11 U.S.C.A. § 1189(a) (West 2021). If the small business chooses to file under Subchapter V, then it has only 90 days to file a plan, as opposed to the 180 days that small businesses enjoy the exclusive right to file a plan outside of Subchapter V. 11 U.S.C.A. § 1121(e) (West 2021). The time limit to propose a plan can be extended if the failure is not within the debtor’s control. 11 U.S.C.A. § 1189(b). See generally \textit{Bonapfel, supra} note 13, at 34.

\textsuperscript{15} 11 U.S.C.A. § 1181(a) (West 2021). The previous requirement that a plan be confirmed within 300 days of the order for relief, found in 11 U.S.C.A. § 1121(e)(2), no longer applies to Subchapter V small businesses. See generally \textit{Bonapfel, supra} note 13, at 34.


\textsuperscript{17} 11 U.S.C.A. § 1188(a) (West 2021). The court can extend the time for reasons outside the debtor’s control. 11 U.S.C.A. § 1188(b).
unsecured creditors' committee, usually appointed to represent unsecured creditors' interest in a case, unless the court determines one is necessary.\(^\text{18}\)

Despite this progress, the SBRA did not eliminate all the problems small businesses face in Chapter 11. First, the definition of a small business under the new Subchapter V requirements is too complicated. To qualify for a Subchapter V reorganization, the SBRA requires that a small business (1) count only debts\(^\text{19}\) that are noncontingent\(^\text{20}\) and liquidated;\(^\text{21}\) (2) be "engaged in commercial or business activities;\(^\text{22}\) and (3) not count the debt owed to affiliates\(^\text{23}\) and insiders\(^\text{24}\) toward its total debts. These three requirements make qualifying as a small business under the SBRA too convoluted and hinder the statute's attempt to make filing a Chapter 11 reorganization easier. Second, the SBRA's original debt limit of $2,725,625\(^\text{25}\) is too low to include many small and medium-sized businesses. This Note argues that the definition of a small business debtor in Chapter 11

\(^{18}\) 11 U.S.C.A. § 1181(b) makes the requirements of 11 U.S.C.A. § 1102(a) inapplicable to Subchapter V cases. See generally BONAPFEL, supra note 13, at 30.


\(^{20}\) The Bankruptcy Code does not define when debt is contingent, 11 U.S.C.A. § 101, but the term is explained in case law. A "contingent" debt is one that "depend[s] on the occurrence of an extrinsic event." See In re Mazzeo, 131 F.3d 295, 304 (2d Cir. 1997). In bankruptcy, a debt is noncontingent if the events that would trigger it actually occurred before the debtor filed for bankruptcy protection. See, e.g., In re Farber, 355 B.R. 362, 371 (Bankr. S.D. Fla. 2006). An example of a contingent debt would be a parent who co-signs a credit card for a child. In the event a child is unable to pay, the parent becomes liable.

\(^{21}\) Like the term "contingent," the Code does not define "liquidated" debt. 11 U.S.C.A. § 101. "The terms 'liquidated' and 'unliquidated' generally refer to a claim's value (and the size of the corresponding debt) and the ease with which that value can be ascertained." In re Mazzeo, 131 F.3d at 304. In simpler terms, if the value of a claim or debt is uncertain or not easily calculated, it is unliquidated. In re Perez, 400 B.R. 879, 883 (Bankr. S.D. Fla. 2008). The issue is not whether liability exists at the moment of filing bankruptcy (as it is for contingent debt), but instead the amount of the liability. United States v. Verdunn, 89 F.3d 799, 802 (11th Cir. 1996). Disputed debts count toward the total debt, as long as they are liquidated and noncontingent. In re CCT Commc'ns, Inc., 420 B.R. 160, 164 (Bankr. S.D.N.Y. 2009). As a result, this complicated phrase means something like the precise amount of all the debtor's obligations taken together as owed for certain when the petition is filed.

\(^{22}\) As with "noncontingent" and "unliquidated," the Code does not define "engaged in commercial or business activities." In re Ellingsworth Residential Cmty. Ass'n, 619 B.R. 519, 521 (Bankr. M.D. Fla. 2020).


\(^{24}\) The Code provides a complex definition of an "insider," depending on whether the debtor is an individual, corporation, or partnership. See 11 U.S.C.A. § 101(31).

\(^{25}\) The debt limit for small businesses under the CARES Act is $7,500,000, which has been extended until March 27, 2022. After this, the allowed debt limit for small businesses will revert to $2,725,625. See infra notes 109–113 and accompanying text.
Subchapter V reorganizations should be simplified and the debt limit should be raised to $10,000,000.

To explain why the definition should be simplified and the debt limit raised, the background section will first explore why the SBRA was necessary and how it built on earlier statutes. Some of the challenges small and medium-sized businesses commonly face in bankruptcy stem in part from earlier laws that were designed to combat fraud and weed out non-viable small businesses. As a result of the challenges introduced in this way, interested professionals, especially the National Bankruptcy Conference and the American Bankruptcy Institute, recommended changes to Chapter 11 to make it less expensive and burdensome for small businesses. Discussion of the SBRA, as well as the CARES Act that temporarily raised the debt limit for small businesses, will illustrate that the SBRA addressed some but not all of the issues small and medium-sized businesses face in Chapter 11 reorganizations. Next, the argument section proposes that to simplify the process of reorganization for small businesses, three components of the SBRA’s definition of a small business in 11 U.S.C.A. § 101(51D)(A) should be eliminated: specifically, the requirements that (1) its debt be contingent and nonliquidated; (2) the small business “be engaged in commercial activities”; and (3) the debt to affiliates and insiders not count toward the debt limit. Raising the debt limit from its current level of $2,725,625 to $10,000,000 would also help small and medium-businesses reorganize under Chapter 11 more cost-effectively and quickly.

II. BACKGROUND

The SBRA only makes sense as part of a larger story: the changing attitude Congress showed toward small businesses from the 1990s until today. To orient the background section, the story will begin with the problems that small and medium-sized businesses have historically faced, and often continue to face, in Chapter 11 reorganizations. Second, a survey of relevant legislation, especially the Bankruptcy Abuse Prevention and Consumer Protection Act, will identify where some of these challenges and stringent requirements originated. Third, a discussion of the proposals from the National Bankruptcy Conference and the American Bankruptcy Institute, two nationally-known advisory groups, will help reinforce the need for a simplified definition of a small-business debtor with a higher debt limit.

A. Challenges to Small Business Reorganization in Chapter 11 and Its Alternatives

The purpose of a Chapter 11 bankruptcy is to establish “a framework for reorganizing a bankrupt business.”26 The debtor enjoys “a financial breathing

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spell” from most creditors’ collection attempts at the same time as the court attempts to ensure that unsecured creditors receive the largest possible return.\textsuperscript{27} The heart of a Chapter 11 bankruptcy is the plan for reorganization.\textsuperscript{28} For conventional Chapter 11 cases, the Code identifies 16 standards that reorganization plans must meet, including the requirements that a qualified plan is proposed in good faith,\textsuperscript{29} that each creditor either accept the plan or receive a minimum return on its debt,\textsuperscript{30} and that the plan is feasible over the long term.\textsuperscript{31} Taken together, the Bankruptcy Code requirements, all of which small businesses had to meet before the passage of SBRA, constituted a formidable obstacle to small businesses seeking to reorganize under Chapter 11.

Congress seems to have intended Chapter 11’s complicated requirements to apply to large companies “with extensive operations and complex capital structures.”\textsuperscript{32} As a result, though many Chapter 11 cases are filed by small business debtors, these debtors are frequently unlikely to exit Chapter 11 with a successful reorganization.\textsuperscript{33} Anne Lawton, a professor at Michigan State College of Law, has been especially vocal about the expensive, cumbersome and lengthy process that awaits small businesses in Chapter 11.\textsuperscript{34}
Lawton determined that only 25.56% of small businesses from a random sample of filers in 2004 were able to confirm a plan, as compared with 48.46% of other Chapter 11 filers.\textsuperscript{35} Similarly, 21.27% of small businesses successfully completed the Chapter 11 process, compared with 43.34% of other Chapter 11 filers.\textsuperscript{36}

Later data confirm the difficulty small businesses face. From 2008 to 2015, more than 18,000 small businesses filed a Chapter 11 petition, only 27% of which successfully filed a plan for reorganization.\textsuperscript{37} This figure does not include the number of small businesses that decided not to file a Chapter 11 bankruptcy because it was seen as unworkable.\textsuperscript{38}

The reasons for these failures are well-known. The deadlines imposed by the Code before the SBRA was implemented proved especially inflexible for small and medium-sized businesses.\textsuperscript{39} Anecdotal evidence suggests that even mid-level companies find Chapter 11 too expensive and clumsy to do much more than liquidate assets.\textsuperscript{40} Small businesses often lack the resources to hire experienced professionals that might enable them to detect or avoid financial problems that might lead to insolvency or to effectively manage a bankruptcy proceeding when financial crises become acute.\textsuperscript{41} As a result, small and medium-sized businesses often file Chapter 11 without much hope of successful reorganization.\textsuperscript{42}


\textsuperscript{35} Lawton, \textit{supra} note 34, at 92. In other words, in 2004, small businesses successfully confirmed a plan at about half the rate of other businesses in Chapter 11. In Lawton’s study, small businesses constituted 37.5% of the total volume of Chapter 11 petitioners. \textit{Id.}

\textsuperscript{36} \textit{Id.}


\textsuperscript{38} \textit{Id.}

\textsuperscript{39} \textit{See infra} notes 60–62 and accompanying text.

\textsuperscript{40} GERALD P. BUCCINO, \textit{STATEMENT TO THE AMERICAN BANKRUPTCY INSTITUTE COMMISSION TO STUDY THE REFORM OF CHAPTER 11} (2012), http://commission.abi.org/sites/default/files/statements/03nov2012/Buccino.pdf.


\textsuperscript{42} Statement of Robert J. Keach, \textit{supra} note 37, at 4.
firms can be seen in the fact that the number of small business Chapter 11 filings decreased every year from 2010 to 2018.\textsuperscript{43} Alternatives to Chapter 11 reorganization have also contributed to its decline in relevance, especially in cases where Chapter 11 offers little hope of success.\textsuperscript{44} Such alternatives include state\textsuperscript{45} and federal receiverships\textsuperscript{46} and assignments for the benefit of creditors.\textsuperscript{47} Because many small and medium-sized businesses see Chapter 11 as ineffective, they turn to these alternatives instead. For example, 26% of the members of the American Bankruptcy Institute’s Business Reorganization Committee who responded to a survey in 2014 had been involved in a receivership in the past five years.\textsuperscript{48} Sixty percent of those who had been involved in a receivership or an assignment for the benefit of creditors had recommended this to their clients as an alternative to bankruptcy.\textsuperscript{49} primarily for the reduced costs.\textsuperscript{50} These findings echo earlier data.\textsuperscript{51}

To reiterate: these problems are not new. They originate in part from earlier statutes that were more concerned with whether small businesses were viable than whether they could efficiently and quickly reorganize under Chapter 11.

\textsuperscript{43} Id.


\textsuperscript{45} State receiverships occur when a court exercises its equitable authority to appoint a neutral party who acts in the best interests of all parties concerned. See Keri L. Wintle, State Receivership: An Alternative to Bankruptcy, ABF J. (Apr. 17, 2018), https://www.abfjournal.com/%3Fpost_type%3Darticles%26p%3D72054.

\textsuperscript{46} Receiverships instituted under federal law also have a long history, dating back from before the advent of modern bankruptcy law. See generally 1 Collier ¶ 21.04 (16th ed. 2021).

\textsuperscript{47} An assignment for the benefit of creditors can serve as an alternative to bankruptcy when no reorganization can salvage the business. In assignments for the benefit of creditors, a failing business contracts with a receiving party that will receive all its assets and interests, which the receiving party liquidates in the best interests of creditors. David S. Kupetz, Assignment for the Benefit of Creditors: Effective Tool for Acquiring and Winding Up Distressed Businesses, A.B.A. (Nov. 15, 2015), https://www.americanbar.org/groups/business_law/publications/blt/2015/11/05_kupetz/. Such assignments for the benefit of creditors are also governed by state law. Id.


\textsuperscript{49} Id.

\textsuperscript{50} Id.

B. The Road to the SBRA

This section begins by considering the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), which focused on maximizing returns for creditors and minimizing abuse and fraud. These concerns led to strict mandatory deadlines and required disclosures, which caused significant challenges for small and medium-sized businesses seeking to reorganize. By emphasizing feasibility over providing a fresh start for debtors and the maximum return for creditors, Congress created problems that made Chapter 11 less relevant for small business debtors. Next, this section explores the response by industry organizations such as the National Bankruptcy Conference and the American Bankruptcy Institute (ABI) to these problems. Both of these organizations recommended changes to make Chapter 11 more efficient and less costly for small business debtors. Building on these suggestions in part, Congress passed the SBRA, which alleviated many, but not all, of these longstanding problems. In the CARES Act, Congress temporarily raised the debt limit for small businesses to $7,500,000, perhaps in response to a belated realization that the SBRA set the limit too low to be helpful.

1. BAPCPA (2005)

Chapter 11 promises a fresh start for debtors and the maximum return for creditors. Despite this promise, Congress has at times emphasized the need to quickly weed out failed enterprises and combat fraud. In 1994, Congress passed legislation that defined a “small business” case as one with a debtor whose total noncontingent, unliquidated debt did not exceed $2,000,000. Legislative history does not suggest a clear reason why Congress chose this limit. It also does not explain why Congress chose to distinguish so sharply between consumer and business debt in the 1994 Act.

Concerned about the escalating number of bankruptcy filings and the potential for debtors to abuse the system by discharging debts they were able to

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52 Congress listed four reasons underlying the Act: (1) the growth in bankruptcy filings; (2) the significant losses creditors experience in bankruptcy; (3) the potential for debtors to abuse the system; and (4) the perception that many who filed bankruptcy petitions were able to pay a significant portion of their debts. H.R. Rep. No. 109-31, at 3–5 (2005).


pay, Congress passed BAPCPA in 2005.\textsuperscript{56} BAPCPA required every debtor that met the definition of small business in 11 U.S.C.A. § 101(51C) to file as a small business.\textsuperscript{57} Congress worried that creditors were not paying enough attention to small business cases because the sums involved were not significant enough to interest them, and so it mandated additional administrative and judicial oversight for these cases.\textsuperscript{58} Congress recognized that small business debtors “often are the least likely to reorganize successfully.”\textsuperscript{59} As a result, legislators hoped increased attention from judges and trustees would help to “weed out small business debtors who [were] not likely to reorganize.”\textsuperscript{60} To accomplish this, small business debtors had to meet strict mandatory deadlines and make significant disclosures. For example, BAPCPA required the U.S. Trustee to meet with small business debtors even before the meeting of creditors “to begin to investigate the debtor’s viability,” examine its business plan, scrutinize its books and records, and verify that it had filed appropriate tax returns.\textsuperscript{61} Unfortunately, BAPCPA’s changes, especially its deadlines, turned out to be a headache for small businesses.\textsuperscript{62}

Moreover, BAPCPA’s definition of “small business debtor” proved especially convoluted and confusing.\textsuperscript{63} The statute defined a “small business debtor as:

a person engaged in commercial or business activities (including any affiliate of such person that is also a debtor under this title and excluding a person whose primary activity is the business of owning or operating real property or activities incidental thereto) that has aggregate noncontingent liquidated secured and unsecured debts as of the date of the petition or the date of the order for relief in an amount not more than $2,000,000 (excluding debts owed to 1 or more affiliates or insiders) for a case in which the United States trustee has not appointed under section 1102(a)(1) a committee of unsecured creditors or where the court has determined that the committee of unsecured creditors...

\textsuperscript{57} 11 U.S.C.A. § 101(51C).
\textsuperscript{59} Id. at 3.
\textsuperscript{60} Id. at 19.
\textsuperscript{62} AM. BANKR. INST., supra note 44, at 281, n.1006.
\textsuperscript{63} Lawton, supra note 34, at 65–66.
creditors is not sufficiently active and representative to provide effective oversight of the debtor.\textsuperscript{64}

This definition preserved the Bankruptcy Reform Act of 1994's requirement that small business debt includes "noncontingent liquidated secured and unsecured" debt.\textsuperscript{65} It also continued the 1994 Act's hard and fast distinction between consumer and commercial debt.\textsuperscript{66} Anne Lawton observed: "The absence of any explanation in the legislative history for Congress' definitional choices strongly suggests that Congress acted haphazardly rather than methodically when it adopted the current definition of a small business debtor."\textsuperscript{67}

In addition to the concern about this definition, others argued that "the value of BAPCPA's reforms is outweighed by the procedural burdens the statute imposes on small business debtors."\textsuperscript{68} For example, even as they argued that Chapter 11 was more successful than generally believed, Senator Elizabeth Warren and Professor Jay Westbrook noted that despite a six-month time limit for small business debtors to confirm their plans, 82% of the successful small business cases after BAPCPA took longer than this to confirm a plan, and that "the cost of the six-month statutory time limit is potentially quite high."\textsuperscript{69} They noted that the bankruptcy courts were already dealing with the failed small business debtors BAPCPA intended to identify through these time limits.\textsuperscript{70} Moreover, despite the requirement for those who met the statutory requirements to file as small business debtors, most debtors that met the requirements did not do so. Of 2,299 identified cases in 2007, most of which met the criteria identified to file as small business debtors, only 36.8% filed as small businesses.\textsuperscript{71} As a result of these and other criticisms, scholars and interested organizations continued to recommend changes to Congress based on their own research.

\textsuperscript{64} 11 U.S.C.A. § 101(51D) (West 2006).
\textsuperscript{67} Lawton, supra note 34, at 58.
\textsuperscript{70} Id.
Since at least the 1940s, the National Bankruptcy Conference has been an organization of about 60 lawyers, professors, and judges whose purpose is “to advise Congress on the operation of bankruptcy and related laws and any proposed changes to those laws.”\textsuperscript{72} In 2010, the National Bankruptcy Conference published a report in which it identified four major flaws in how Chapter 11 dealt with small businesses: (1) the disproportionate influence of secured creditors;\textsuperscript{73} (2) a lack of enough evidence to determine whether the small business was likely to be successful in the long term; (3) excessive administrative costs; and (4) procedural obstacles, stemming in part from BAPCPA.\textsuperscript{74}

To remedy these problems, the report proposed developing a procedure for small businesses based on the process available to family farmers under Chapter 12.\textsuperscript{75} Besides this, the report also proposed a new definition for a small


\textsuperscript{73} In large Chapter 11 cases, usually the largest unsecured creditors form a committee whose role is to investigate the debtor’s affairs and make sure unsecured creditors get the best possible deal. See generally 1 Collier ¶6.21[2] (16th ed. 2021). In cases involving small businesses, often the U.S. Trustee cannot generate enough interest to form a committee because the potential recovery is too low to make the process of rigorously analyzing the debtor profitable enough. Without an active committee of unsecured creditors, secured creditors, who are going to get paid anyway, often have unusual influence over whether the plan is approved.

\textsuperscript{74} Nat’l Bankr. Conf., supra note 32, at 3.

\textsuperscript{75} Id. at 9–18. First, the report recommended appointing a standing trustee in every small business case in order to provide reliable information to the court to help it assess a small business’s viability. Id. at 11; see 11 U.S.C.A. § 1202 (West 2021) for the appointment of a trustee in Chapter 12 cases. Second, it also suggested that the tight deadlines faced by Chapter 12 filers—requiring the production of a plan within 90 days (id. § 1221) and a hearing on the plan within 45 days (id. § 1224)—would discourage the use of a small business filing merely to delay paying creditors. Nat’l Bankr. Conf., supra note 32, at 11. Third, the report proposed that as long as the small business owner could pay all secured claims, and unsecured creditors receive all the disposable income available for the length of the plan—up to five years—the debtor could remain in charge of the business. Id. For the requirement that Chapter 12 filers pay secured claims in full, see id. § 1225(a)(5). See id. §§ 1222(c), 1225(b) for the court’s ability to confirm a plan for which unsecured debtors are paid all the debtor’s disposable income for a period of up to five years. Unsecured creditors would also have to receive at least as much as they would in a Chapter 7 filing. Nat’l Bankr. Conf., supra note 32, at 11. See 11 U.S.C.A. § 1225(a)(4) for the rule that a Chapter 12 plan provide at least as much return for unsecured creditors as they would receive in a Chapter 7 filing. Chapter 12 permits a court to approve a plan over a creditor’s objection as long as the creditor would receive the full amount of its claim or all the debtor’s disposable income goes to make plan payments. Id. § 1225(b)(1). Such requirements would eliminate the temptation to make wasteful efforts to avoid bankruptcy to retain control of the business. Finally, the report suggested that small businesses, like family farmers under Chapter 12, be permitted to pay certain administrative expenses over the life of the plan, instead of requiring payment immediately when the plan is confirmed. Nat’l Bankr. Conf., supra note 32, at 11–12. The Bankruptcy Code permits payment of section 507 priority administrative expenses over the life of the plan. 11 U.S.C.A. § 1222(a)(2). A Chapter 11 debtor must pay all administrative claims as defined in
business debtor, which it designated a “small business enterprise” (SBE).\textsuperscript{76} The report defined an SBE as “a corporate or non-corporate person—other than a family farmer or a family fisherman—who is engaged in a business or commercial activity and has total debts not exceeding $10 million, provided at least fifty percent of the debt arises from the person’s business or commercial activities.”\textsuperscript{77} This new definition would operate under Chapter 12 as an alternative to the “small business debtor” under Chapter 11, reintroducing the choice of plans that BAPCPA had eliminated.\textsuperscript{78} The report apparently derived the requirement that at least half the debtor’s debt originate from commercial or business activity from the definition of family farmers, at least half of whose debt must come from farming operations.\textsuperscript{79} Although it did not explain why it recommended a higher debt limit for small and medium-sized businesses, it seems likely the higher limit was intended to allow small and medium-sized businesses to reorganize more efficiently. The report also suggested that the reporting requirements in Chapter 11 should be maintained in the case of SBEs filed in Chapter 12.\textsuperscript{80}

3. The Small Business Jobs Preservation Act of 2010

Not long afterward, the National Bankruptcy Conference sponsored a proposed bill that revised the small business debtor provisions of the Bankruptcy Code.\textsuperscript{81} The bill, titled the Small Business Jobs Preservation Act of 2010, like its earlier report, sought to simplify the existing definition of a small business debtor by characterizing it as:

a debtor— (A) that is engaged in commercial or business activities; and (B) that has aggregate noncontingent, liquidated, § 507(a)(2) and (3) in full on the date the plan is confirmed unless the claimant agrees otherwise. \textit{Id.} § 1129(a)(9). This would remove one more potential obstacle to bankruptcy relief for small businesses with little or no cash reserves. Congress adopted a similar proposal in the SBRA. The SBRA allows an attorney with a claim of less than $10,000 from before the bankruptcy petition was filed to continue to represent the debtor afterwards. \textit{Id.} § 1195. Thus, the debtor does not have to wait to file bankruptcy until it can pay its attorney. However, this also gives the attorney less leverage to demand payment before filing under 11 U.S.C.A. § 327(a). William K. Norton III & James B. Bailey, \textit{The Pros and Cons of the Small Business Reorganization Act of 2019}, \textit{36 Emory Bankr. Devs.} J. 383, 384 (2020).

\textsuperscript{76} NAT’L BANKR. CONF., \textit{supra} note 32, at 15.
\textsuperscript{77} \textit{Id.}
\textsuperscript{78} \textit{Id.} at 15–16. For BAPCPA eliminating small debtors’ freedom to choose to file as a small business debtor, see \textit{supra} note 57 and accompanying text.
\textsuperscript{80} NAT’L BANKR. CONF., \textit{supra} note 32, at 16.
secured, and unsecured debts as of the date of the order for relief—(i) in an amount equal to not more than $7,500,000 (excluding debts owed to 1 or more affiliates or insiders); and (ii) not less than 50 percent of which arose from the commercial or business activities of the debtor.82

Noteworthy differences from its earlier proposed definition include (1) the lower debt threshold of $7,500,000, compared with the earlier limit of $10,000,000; (2) the specification that debt must be “aggregate noncontingent, liquidated, secured, and unsecured,” exactly like the language of existing law;83 and (3) the provision that the debt limit exclude “debts owed to 1 or more affiliates or insiders,” again in conformity with existing law.84 Whether the intent of making its earlier-proposed definition conform more closely to existing law was to increase the probability of the bill’s passage, the bill did not receive a vote.85 In any event, the bill was far from the last word on Chapter 11 reform.

4. ABI: Commission to Study the Reform of Chapter 11 (2012–14)

The ABI is an organization comprising about 12,000 bankruptcy professionals, founded in 1982.86 Its purpose is to furnish “congressional leaders and the general public with non-partisan reporting and analysis of bankruptcy regulations, laws and trends.”87 In response to longstanding concerns, ABI undertook a three-year, comprehensive investigation focused on “resolution of financially distressed businesses under Chapter 11 of the Bankruptcy Code.”88 Unlike the National Bankruptcy Conference report, the ABI commissioners recommended keeping small and medium enterprise (SME) cases within Chapter 11 instead of relocating them to Chapter 12.89 Despite this difference, the National Bankruptcy Conference report and the ABI commissioners were motivated by similar concerns. The ABI intended its reforms to (1) uncomplicate the process of bankruptcy for SMEs; (2) lessen expenses and “barriers”; and (3) “provid[e] tools to facilitate effective reorganizations for viable companies.”90

In its report, the ABI defined SMEs as business debtors with:

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82 Id. § 1183.
83 See supra note 64 and accompanying text.
84 Id.
87 Id.
88 AM. BANKR. INST., supra note 44, at 3.
89 Id. at 289.
90 Id. at 290.
(i) No publicly traded securities in its capital structure or in the capital structure of any affiliated debtors whose cases are jointly administered with the debtor’s case; and (ii) Less than $10 million in assets or liabilities on a consolidated basis with any debtor or nondebtor affiliates as of the petition date.91

To settle on the $10,000,000 cutoff, the ABI used data compiled by Anne Lawton in her research that suggested “a natural breaking point in the data at the $10 million threshold” for both assets and liabilities.92 The ABI considered companies based on types of industry and geographical region and concluded that the $10,000,000 limit “corresponded with the characteristics identified above of SMEs that are not being well served by current law.”93 Somewhere between 85–90% of Chapter 11 filings would meet this cutoff, excluding individuals and small public companies not covered by the definition.94 The commissioners also rejected many of the qualifiers in BAPCPA’s definition of a “small business debtor,” such as the requirement that the debt be “noncontingent” or “liquidated,” in order to simplify the definition.95

5. Summary

Commonalities among BAPCPA, the National Bankruptcy Conference Report and the ABI Chapter 11 study include (1) identification of a maximum debt or asset limit, which both the National Bankruptcy Conference report and the ABI place at $10,000,000; and (2) the requirement that the debt in question must be substantially derived from commercial activities. As shown above, the statute and the two reports differ significantly in other attempts to grapple with perceived problems facing small businesses in reorganizing under Chapter 11.

C. Small Business Debtors in the SBRA

Noting that small businesses “form the backbone of the American economy,” Congress passed the SBRA with bipartisan support.96 The Act was intended to “streamline the bankruptcy process by which small [business]
debtors reorganize and re rehabilitate their financial affairs. Legislative history acknowledged that the legislation "largely derived from the recommendations" of the National Bankruptcy Conference and ABI. With regard to small businesses, the statute had three "principal features": (1) it required appointment of a trustee for a small business debtor in Chapter 11, who would perform similar duties to a chapter 12 trustee; (2) it required the trustee to monitor the small business debtor's steps toward confirming a plan of reorganization; and (3) it provided that if a plan does not discriminate unfairly and is fair and equitable toward each impaired class of creditors that has not accepted the plan, a court may confirm the plan.

The SBRA updated the definition for a "small business debtor" in the Bankruptcy Code, drawing on suggestions from both the ABI and National Bankruptcy Conference reports while maintaining several key features from BAPCPA. The new definition characterized a small business debtor as a person engaged in commercial or business activities (including any affiliate of such person that is also a debtor under this title and excluding a person whose primary activity is the business of owning single asset real estate) that has aggregate noncontingent liquidated secured and unsecured debts as of the date of the filing of the petition or the date of the order for relief in an amount not more than $2,725,625 (excluding debts owed to 1 or more affiliates or insiders) not less than 50 percent of which arised from the commercial or business activities of the debtor.

The SBRA made further exclusions as well, which are not strictly relevant to this paper. The operation of the new provision, Subchapter V, is not automatic: the debtor must choose to be treated as a small business debtor under the SBRA. Thus, if a qualified debtor does not elect to be treated as a small business debtor, most of the current provisions of Chapter 11 remain in effect. However, there is one difference: where a small business proceeds

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99 Id. at 4.
98 Id. at 4.
97 Id. This allows the owners of small businesses to retain ownership of their businesses in certain situations. See supra note 13 and accompanying text.
101 First, the SBRA excluded any debtor within financially related entities with "aggregate noncontingent liquidated secured and unsecured debts in an amount greater than $2,725,625 (excluding debt owed to 1 or more affiliates or insiders)." Id. § 101(51D)(B)(i). Second, it excluded any debtor subject to the reporting requirements of § 13 or § 15(d) of the Securities Exchange Act of 1934. Id. § 101(51D)(B)(ii). Third, it excluded "any debtor that is an affiliate of an issuer" as described in § 3 of the same Act. Id. § 101(51D)(B)(iii).
103 BONAPFEL, supra note 13, at 8.
under the usual requirements of Chapter 11, SBRA amended 11 U.S.C. § 1102(a)(3) so that it does not require an unsecured creditors’ committee unless the court orders one.\textsuperscript{104} Whether a debtor chooses to file as a “small business debtor” (i.e. under Subchapter V) or as a “small business case” (i.e. a small business under a conventional Chapter 11), it must meet all of the requirements of the revised definition of a small business debtor in 11 U.S.C. § 101(51D)(A).\textsuperscript{105}

\textbf{D. The CARES Act}

Congress provided financial assistance to individuals and businesses struggling because of the COVID-19 pandemic in the CARES Act of 2020.\textsuperscript{106} Locally, of the $1.25 billion Congress allocated to West Virginia, approximately $40 million was reserved for small business grants.\textsuperscript{107} As of July 8, 2020, West Virginia had made about 2,291 Paycheck Protection Loans over $150,000 to businesses and municipalities within the state and 10,815 such loans under $150,000.\textsuperscript{108}

In addition to providing such relief, the CARES Act temporarily raised debt limits for small businesses filing under Subchapter V of SBRA to $7,500,000.\textsuperscript{109} The new debt limit under the CARES Act was set to expire on March 27, 2021.\textsuperscript{110} However, the COVID-19 Bankruptcy Relief Extension Act of 2021 extended these limits until March 27, 2022, after which the previous

\textsuperscript{104} Id. at 2.

\textsuperscript{105} This is because the SBRA’s definition of a “small business case” itself appeals to the definition of a “small business debtor.” The SBRA defines a “small business case” as “a case filed under chapter 11 of this title in which the debtor is a small business debtor and has not elected that subchapter V of chapter 11 of this title shall apply.” 11 U.S.C.A. § 101(51)(C).


\textsuperscript{109} 11 U.S.C.A. § 1182(1) (West 2021). One example of a substantial change wrought by the CARES Act in the Bankruptcy Code not relevant for the purposes of this paper is 11 U.S.C.A. § 1329(d), which allows for the modification of a Chapter 13 plan for a period of up to seven years from the date of the plan’s first payment if a debtor is experiencing hardship due “directly or indirectly” to COVID-19. At least one court has ruled that debtors who are not current with their Chapter 13 payments can still modify a Chapter 13 plan under the CARES Act. See \textit{In re} Gilbert, 622 B.R. 859, 861 (Bankr. E.D. La. 2020).

\textsuperscript{110} CARES Act, § 1113(a)(5).
limit of $2,725,625 will apply once again.\textsuperscript{111} Besides the desire to include more potential “small business debtors” in the definition provided by the SBRA, it is unclear what exactly motivated Congress to set the debt limit at this point.\textsuperscript{112} During this period, small businesses that choose not to proceed as a “small business debtor” would not have access to the new, higher limit of $7,500,000 and will be limited to a total debt or asset limit of $2,725,625.\textsuperscript{113}

The history leading to the SBRA reveals how some parts of its definition of a “small business debtor” derive from earlier laws such as BAPCPA. While Congress intended BAPCPA in part to make small businesses prove their viability, the SBRA is intended to provide small businesses with a comparatively quick and inexpensive reorganization under Chapter 11. Thus, retaining the elements of BAPCPA’s definition intended to make small businesses prove they are viable in the SBRA makes no sense. As a result, although the SBRA provides small businesses with many of the tools necessary to shed debt and reorganize while maintaining control, the unclear and burdensome definition of a “small business debtor,” coupled with its stingy debt limit, places unnecessary burdens on such businesses.

III. STREAMLINING THE DEFINITION OF SMALL BUSINESS DEBTOR

The SBRA was intended to “streamline the bankruptcy process by which small businesses debtors reorganize and rehabilitate their financial affairs.”\textsuperscript{114} However, the clunky definition of a “small business debtor” included in the SBRA complicates this goal by maintaining unnecessary qualifications from earlier legislation and setting the debt threshold for such debtors far too low. Since earlier laws focused on winnowing viable small businesses from non-viable ones, and not streamlining the process, keeping such qualifications in the SBRA’s definition is counterproductive. Specifically, Congress should eliminate the requirements that (1) specify the debt should be noncontingent and liquidated; (2) prescribe that the debtor be “engaged in commercial or business activities”; and (3) exclude debts owed to affiliates and insiders. In addition, the SBRA’s debt limit for such potential small business filers is too low, and it should be raised to $10,000,000 to include as many small and medium-sized businesses as possible. By doing so, Congress could better implement the policy choices it made in the SBRA and reinforce the important role small and medium-sized businesses play in U.S. economic prosperity.


\textsuperscript{112} The author was not able to find any legislative history that explained why the legislature chose $7,500,000 as the limit for small business debtors.

\textsuperscript{113} BONAPFEL, supra note 13, at 9.

\textsuperscript{114} H.R. REP No. 116–171, at 1 (2019).
A. The SBRA’s Definition of a Small Business Debtor Should Be Simplified

As explained above, legislators intended BAPCPA to “weed out small business debtors who are not likely to reorganize.”\(^{15}\) It imposed strict deadlines and mandatory disclosures for this reason.\(^{16}\) Unfortunately, this weeding-out process is complicated by BAPCPA’s uneven editing, as courts have noted. For example, one district court recognized that “BAPCPA was imprecisely drafted,” and thus concluded that the usual canons of statutory construction were necessarily limited as a result.\(^{17}\) Another court noted more bluntly: “while a debate rages over whether William Shakespeare or someone else wrote the plays and sonnets attributed to the Bard of Avon, there will never be a similar debate over the authorship of the BAPCPA because no one wants to be associated with that body of work.”\(^{18}\) When such hastily-drafted language is preserved in legislation intended to simplify the course of Chapter 11, the results are particularly unfortunate. Several elements of BAPCPA’s definition of a “small business debtor” that were preserved in the SBRA provide unnecessary obstacles to a court deciding if a debtor qualifies as a small business without providing much benefit in return.

1. Noncontingent and Liquidated Debts

The first such element mandates that to qualify as a small business debtor, an organization’s debts must be “aggregate noncontingent [and] liquidated.”\(^{19}\) The term “aggregate debt” is sometimes taken to be more inclusive than the simple term “debt.”\(^{20}\) For example, in interpreting 11 U.S.C. § 101(18A) (2010), the Ninth Circuit concluded that debts that had been discharged against a debtor in a previous bankruptcy but were still enforceable against her property should be considered part of the debtor’s “aggregate debt.”\(^{21}\)

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\(^{16}\) See supra notes 56-61 and accompanying text.


\(^{18}\) In re Grydzuk, 353 B.R. 564, 566-67 (Bankr. N.D. Ind. 2006).


\(^{20}\) See, e.g., In re Perkins, 581 B.R. 822 (B.A.P. 6th Cir. 2018) (holding that the term “aggregate debt” included a Chapter 12 debtor’s farm and non-farm debts). For discussion of the term “debt,” see supra note 19.

\(^{21}\) In re Davis, 778 F.3d 809, 813–14 (9th Cir. 2015).
The definition of a “small business debtor” also requires that such debts be “noncontingent” and “liquidated.”\textsuperscript{122} As we saw above, this means the precise amount of all the debtor’s obligations taken together as owed for certain when the petition was filed.\textsuperscript{123} Is such a detailed definition of the nature of debt necessary or beneficial? In a word, no. Neither the National Bankruptcy Conference nor the ABI reports included comparable language defining the nature of the debt necessary to qualify as a small business debtor.\textsuperscript{124} Moreover, in a large study of Chapter 11 cases from 2004, Anne Lawton argued that including noncontingent and liquidated debt in the definition of a small business debtor was unnecessary and counterproductive.\textsuperscript{125} The amount of debt a business owes, whether or not contingent or unliquidated debts were included, predicted whether or not a debtor was likely to complete Chapter 11 successfully.\textsuperscript{126} Moreover, there is no way for a third party who reviews the debtor’s schedules to accurately determine whether debt is genuinely contingent, liquidated, or even belonging to an insider, since the debtor is not required to identify such information.\textsuperscript{127} Such requirements waste time and do not help to weed out nonviable business entities.\textsuperscript{128} They make even less sense in view of the SBRA’s intent to “streamline the bankruptcy process by which small business debtors reorganize and rehabilitate their financial affairs.”\textsuperscript{129}

At least one court has already spent significant resources addressing the question of contingent and nonliquidated debt to determine a debtor’s eligibility under the new SBRA provisions. In \textit{In re Parking Management, Inc.}, the court considered whether more than $1,800,000 obtained under the Paycheck Protection Program (PPP) should be included as part of the debt limit needed to qualify as a small business debtor under the new SBRA provisions.\textsuperscript{130} In a question of first impression, the court analogized to the requirements of debt eligibility in Chapter 13, under which the process of determining eligibility should be as efficient and expedient as possible.\textsuperscript{131} When the amount of the debt is the subject of a case or controversy, the court is free to investigate and redefine

\begin{itemize}
\item \textsuperscript{122} 11 U.S.C.A. § 101(51D)(A).
\item \textsuperscript{123} See supra notes 20–21 and accompanying text.
\item \textsuperscript{124} See supra notes 77, 91 and accompanying text. As noted above, however, the National Bankruptcy Conference-sponsored bill, the Small Business Job Preservation Act of 2010, did include this language. See supra note 82.
\item \textsuperscript{125} Lawton, supra note 54, at 1026–28.
\item \textsuperscript{126} Id.
\item \textsuperscript{127} Id.
\item \textsuperscript{128} Id.
\item \textsuperscript{129} H.R. REP. No. 116-171, at 1 (2019).
\item \textsuperscript{130} 620 B.R. 544, 547 (Bankr. D. Md. 2020).
\item \textsuperscript{131} Id. at 550.
\end{itemize}
the nature of that debt; no finding of bad faith is required.\textsuperscript{132} To determine whether the PPP loan was noncontingent and liquidated, the court engaged in a detailed consideration of the process of applying for and receiving these loans, and the extent to which they are forgivable.\textsuperscript{133} A debt is contingent if it depends on a future or external event that may or may not occur.\textsuperscript{134} Since repayment of the funds depended on whether they were used for ineligible purposes and whether the employer met employee retention criteria, the court determined the debts were contingent and thus did not qualify as part of the debt limit.\textsuperscript{135}

Likewise, the court needed to determine whether the PPP loans were liquidated or not. Courts use the term “liquidated” to refer to a debt that is “fixed, certain, or otherwise determined by a specific standard.”\textsuperscript{136} Similar to its analysis of whether the debt was contingent, the court reasoned that since it was uncertain whether the debtor would use the funds for ineligible purposes or meet its employee retention targets, the debts were not liquidated.\textsuperscript{137} Moreover, because the loans could be partially forgiven, the court also could not determine the precise amount owed from the loans.\textsuperscript{138} Thus, the court concluded that the exact amount of its debt when it filed the petition was not liquidated.\textsuperscript{139} Because the debts were both contingent and unliquidated, the court ultimately did not include them in the total debt allowed for the debtor to qualify under the SBRA.\textsuperscript{140}

Not including the requirement that a debt be liquidated and noncontingent would have saved the court a considerable amount of analysis and allowed the reorganization to proceed more smoothly. It would also have avoided the unintended consequence of government loans, intended to help a small business during a pandemic, from impeding the process of efficient reorganization. Moreover, if the debt limit was raised to $10,000,000, as proposed below, it may have been more obvious based on the debtor’s filing that it qualified as a small business for purposes of the SBRA.

2. “[E]ngaged in commercial or business activities”

A second unnecessary element in SBRA’s definition of a “small business debtor” is that the debtor be “engaged in commercial or business activities.”\textsuperscript{141}

\textsuperscript{132} Id. at 551 (citing \textit{In re} Stern, 266 B.R. 322, 326 (Bankr. D. Md. 2001)).
\textsuperscript{133} Id. at 556–58.
\textsuperscript{134} See, \textit{e.g.}, \textit{In re} Green, 574 B.R. 570, 577 (Bankr. E.D.N.C. 2017).
\textsuperscript{135} \textit{In re} Parking Mgmt., Inc., 620 B.R. at 558–59.
\textsuperscript{136} \textit{In re} Barcal, 213 B.R. 1008, 1014 (B.A.P. 8th Cir. 1997).
\textsuperscript{137} \textit{In re} Parking Mgmt., Inc., 620 B.R. at 559–60.
\textsuperscript{138} Id.
\textsuperscript{139} Id. at 560.
\textsuperscript{140} Id.
While the SBRA preserved this language from earlier legislation, the SBRA added the requirement that at least half of the debtor’s liabilities result from business or commercial activities, as recommended by the National Bankruptcy Conference report. It seems unnecessary to include both requirements.

A debtor engaged in commercial activities includes “any affiliate of such person that is also a debtor under this title.” The purpose of this language is apparently to include the personal bankruptcies of small business owners, even if these personal debts do not derive from commercial activity. In such a case, the quoted language requires that the small business owner also have a bankruptcy case currently before the court.

However, it is unclear why the personal debts of small business owners should be considered as part of a comprehensive small business filing, given Chapter 11’s longstanding distinction between consumer and corporate debtors. Thus, Lawton observes:

What basis exists for distinguishing between the individual consumer debtor who owns a small business enterprise that also is in bankruptcy, and the individual consumer debtor who files for chapter 11 because her liabilities exceed the cut off for a chapter 13 case? Moreover, what end is served by increasing the complexity of the sorting mechanism that the “small business debtor” definition serves?

Again, this requirement has spawned unnecessary and even contradictory interpretations. In In re Ventura, the court considered whether a mortgage taken out in connection with the operation of a bed and breakfast constitutes debt arising from “commercial or business activities.” As noted above, the Code does not define this phrase. The Ventura court cited an earlier case to note that business debt, unlike consumer debt, was incurred with the hope of profit. The court concluded that though the transaction seemed like a typical home mortgage, the primary purpose of the loan was to enable the debtor to run

142 See supra note 32, at 15.
144 Lawton, supra note 34, at 69.
145 In re Wright, Ch. 11 No. 20-01035-HB, 2020 WL 2193240, slip op. at *3 (Bankr. D.S.C. Apr. 27, 2020).
146 See supra notes 55 and 64 and accompanying text.
147 Lawton, supra note 34, at 69.
149 See supra note 22 and accompanying text.
150 In re Ventura, 615 B.R. at 19 (quoting In re Martin, No. 12-38024, 2013 WL 5423954, slip op. at *6 (Bankr. S.D. Tex. Sept. 26, 2013)).
Therefore, the debtor was engaged in commercial or business activities.

Other courts have denied that the profit motive helps to distinguish business debt from consumer debt. For example, the court found in *In re Ellingsworth Residential Community Association* that the SBRA was "clear and unambiguous." Based on its reading of the statute, the court held that a non-profit community association was "engaged in commercial or business activities" because it contracted for goods and services, hired professionals, filed tax returns, and was registered with the state as a corporation. Directly contradicting the *Ventura* court, the court concluded that the requirement that a debtor be "engaged in commercial activities" does not mandate that the debtor aim at or make a profit. Other authorities similarly read the SBRA as not requiring that the debtor currently be engaged in economic or commercial activities. For example, one court found that a debtor’s addressing residual business debt satisfied this requirement. Another court agreed, holding that a debtor qualified even though some of its debts originated from businesses that were no longer in operation.

Even this brief survey of the phrase "engaged in commercial or business activities" demonstrates that it has caused unnecessary confusion. Moreover, perhaps the courts that adopt a generous interpretation of "commercial or business activities" are signaling that this requirement does not advance the purpose of the SBRA. Eliminating this unnecessary requirement would help to simplify the process of determining whether a particular debtor qualifies for the provisions of Subchapter V.

3. Debts Owed to Affiliates and Insiders

Following earlier law, the SBRA definition of a "small business debtor" calculates the total liability of $2,725,625 by "excluding debts owed to 1 or more affiliates or insiders." The problem with this provision is the amount of time trustees and creditors must spend trying to verify the information given by the

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151 *Id.* at 20.


153 *Id.*

154 *Id.* at 521–22.

155 See 2 *COLLIER ¶ 101.51D (16th ed. 2021).*


158 11 U.S.C.A. § 101(51D)(A) (West 2021). For BAPCPA’s inclusion of this language, see *supra* note 64 and accompanying text. For discussion of “affiliate” and “insider,” see *supra* notes 23–24.
debtor on its schedules. Even if they spent such time, it might be wasted effort. Lawton calculated that in only 10 of the 782 cases in the random sample she examined, or 1.3%, did subtracting insider or affiliate debt affect whether the debtor could qualify as a small business debtor. Moreover, as of the date Lawton wrote, nothing in bankruptcy forms, schedules, or rules required debtors to disclose their total insider debt. As a result, requiring disclosure of such information does not provide sufficient benefit to justify its cost.

Like the other two unnecessary requirements in the SBRA’s definition of a small business debtor, the requirement that the debt is calculated as “excluding debts owed to 1 or more affiliates or insiders” has already spawned controversy. In In re Serendipity Labs, the debtor filed a Chapter 11 petition, choosing to proceed under the SBRA’s new Subchapter V provisions. One of the debtor’s creditors objected that, because an affiliate owned more than 27% of the debtor’s voting securities, it was ineligible under the Code’s definition of an “affiliate.” Although courts disagree over precisely when a related company’s control of stock meets the 20% threshold required to count as an “affiliate,” that disagreement is unimportant here. More significant is the simple fact that a court had to engage in a technical analysis to determine that the debtor did not qualify as a small business debtor under the SBRA.

Review of these requirements shows they counteract the SBRA’s intent of making reorganization quicker and less costly for small businesses. Moreover, the disclosures already required by the SBRA provide enough information for creditors and interested parties to evaluate small businesses’ prospects for success. Under 11 U.S.C. § 1190(1), a small business debtor must file a “brief history of business operations,” an analysis of what the creditors would receive if the assets were converted to cash (a liquidation analysis), and an explanation for how the debtor plans to meet payments under the proposed plan. While these requirements are significantly fewer than the 16 enumerated in 11 U.S.C. § 1129(a), they provide enough information for creditors and other interested parties to begin to form judgments about the feasibility of the proposed plan and to begin negotiations. Thus, retaining the elements of a small business debtor

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159 Lawton, supra note 34, at 86–87 (giving a vivid example of how difficult ascertaining such data can be).
160 Id. at 88.
161 Id.
164 Id. at 681. See also 11 U.S.C.A. § 101(2) (West 2021).
165 See In re Serendipity Labs, 620 B.R. at 684–86 for fuller discussion.
166 Id. at 686.
discussed above is not necessary under the SBRA in order to determine whether a business remains viable.

4. Conclusion

These three provisions do not make it easier for a creditor or trustee to verify whether a debtor qualifies as a small business debtor. Instead, recent court cases suggest they have provided new grounds for controversy. In view of how these requirements were carried over from earlier laws, especially BAPCPA, into the SBRA, it bears repeating that under BAPCPA, of 2,299 identified Chapter 11 cases in 2007, most of which met the criteria identified to file as small business debtors, only 36.8% did so. This becomes especially concerning when one remembers that, if a debtor met the definition of a small business debtor under BAPCPA, filing as a small business was supposed to be mandatory. If Congress is serious about streamlining Chapter 11 to allow small business to reorganize, it should simplify the SBRA’s definition of a small business debtor by eliminating these unnecessary qualifications. Moreover, the debt limit should be raised to enable a greater number of small to medium-sized businesses to reorganize with fewer procedural hindrances.

B. Raising the Debt Limit To $10,000,000 Makes Reorganization Easier for Medium-Sized Businesses

Estimates vary for how many debtors qualify for SBRA’s definition of a small business debtor using the current guidelines. In a recent study, one researcher examined data and concluded that from the 11 years between 2008 and 2018, an average of 39.8% of the total 71,463 Chapter 11 business cases would qualify for the new definition of small business debtor. The percentage ranged over this period from 36.5% to 43.5%. However, the author notes that in recent years, the average was closer to 42.2%. Given the increased attractiveness of the provisions of this new form of Chapter 11, proportionately more of those who qualify will choose to take advantage of its provisions. As

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168 See Lawless, supra note 71.
171 Id.
172 Id.
173 Id.
a result, it may be correct to estimate that “up to half of Chapter 11 debtors” would be eligible to file under the SBRA debt limit of $2,725,625.174

As we have seen, however, the SBRA was intended to “streamline the bankruptcy process by which small business debtors reorganize and rehabilitate their financial affairs.”175 As such, the fact that Congress has not proposed a clear rationale for the aggregate liability limit of $2,725,625 is troubling.176 Whatever the reason, there is some support for this limit. In a study examining almost 800 Chapter 11 cases from 2004, Lawton found a statistically significant correlation between liability size and success in reorganization.177 “Congress’ $2 million cutoff for [noncontingent liquidated] liabilities better predicted the point at which plan confirmation and performance rates became significant” than larger debt limits did.178 Consequently, she proposed defining a small business debtor based only on the existence of an official creditor’s committee and the extent of a debtor’s liability.179 However, Lawton was careful to qualify her conclusions. Significantly, she observed that the correlation between the $2,000,000 cutoff and the higher rate of success did not imply causation; it was also possible that debtors with larger liabilities were better able to navigate the Chapter 11 process than small businesses were.180 Secondly, Lawton assumed the validity of BAPCPA’s goals of winnowing viable businesses from non-viable ones,181 which runs counter to the expressed goal of SBRA, as we have seen. However, just because BAPCPA imposed stingy debt limits is no reason to continue them. The ABI report expressed the commission’s conviction that many small business debtors were failing to complete their reorganizations, not because of a fatal flaw in their business models, but because they were not receiving the necessary support during the process, and this conviction was supported by witness testimony and some related literature.182

Raising the total liability limit to $10,000,000, as suggested by the National Bankruptcy Conference and ABI reports, would have the effect of giving approximately 85–90% of all Chapter 11 filers a chance to reorganize.

Robert Drummond, Relief in Federal Covid-19 Response Includes Chapter 11, Chapter 13 Bankruptcy Changes, 45 MONT. LAW. 16, 18 (2020).


Lawton, supra note 54, at 1014.

Id. at 1024–25.

Id. at 1025.

Lawton, supra note 34, at 58.

Lawton, supra note 54, at 1025.

See Lawton, supra note 34, at 57 (assuming, for the sake of argument, that BAPCPA legitimately sought to distinguish those businesses that might successfully reorganize from those which would not through its definition of a small business debtor).

AM. BANKR. INST., supra note 44, at 285.
under the new Subchapter V rules. The ABI Commissioners observed that this debt limit was best suited to counter the problems small and medium-sized businesses face, as discussed above. They observed a “natural breaking point in the data at the $10 million threshold.” Given the research and anecdotal data behind the ABI report, their recommended limit of $10,000,000 seems more appropriate than the one enacted by Congress, for which a clear rationale has proven elusive.

The result of raising the total liability limit in this fashion would be to minimize the costs and strict deadlines associated with filing a Chapter 11 bankruptcy for medium-sized companies. As noted above, some medium-sized businesses are failing to complete the Chapter 11 process not because their business plans are lacking, but simply because they lack the expertise to navigate the process. Allowing medium-sized businesses to meet the definition of a “small business” would provide them access to the simpler rules under the SBRA’s simplified timetable, allowing them to save costs.

In addition, the increased pressures small and medium-sized businesses face due to the COVID-19 pandemic also support raising the debt limit to $10,000,000. In a global survey of 2377 small and medium-sized businesses in March and August 2020, 31% to 32% cited access to capital as the factor that most constrained their operations. Over half (56%) of such businesses are also facing reduced revenue as a result of the COVID-19 pandemic, and 54% report reduced demand for their products. Because the pandemic itself served as a kind of sorting mechanism that ended the less viable small and medium-sized businesses, Chapter 11 does not need to repeat this process through its cumbersome definition of a small business debtor.

One obvious alternative to the $10,000,000 limit is to permanently maintain the $7,500,000 debt limit imposed by the CARES Act. Such a limit was proposed by the Small Business Jobs Preservation Act of 2010 and supported by Michael C. Blackmon. Such a limit would include between 78% and 86.7% of all Chapter 11 debtors. Blackmon notes that the National Bankruptcy

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183 Id. at 288; see also supra note 77.
184 AM. BANKR. INST., supra note 44, at 288. For the problems small and medium-sized businesses experience in Chapter 11 bankruptcies, see supra, notes 40–43 and accompanying text.
185 AM. BANKR. INST., supra note 44, at 287.
186 See supra note 41; see also AM. BANKR. INST., supra note 44, at 285 n.1035.
187 In March, 31% of small and medium-sized businesses surveyed reported this result, increasing slightly to 32% in August. SALESFORCE RESEARCH, supra note 1, at 12.
188 Id. at 13.
189 See supra note 81 and accompanying text.
191 Id. at 364 (citing AM. BANKR. INST., supra note 44, at 309–10).
Conference report on small businesses advocated raising the debt ceiling to $10,000,000, provided that at least half the debt originated from business or commercial enterprises.192 Similarly, the Bankruptcy Code's definition of a "family farmer" also requires that at least half of the debts of such debtor arise out of farming operations.193 The Family Farmer Relief Act of 2019 raised the debt limit for family farmers from $4,411,400 to $10,000,000.194 This suggests that Congress followed the National Bankruptcy Conference in patterning the small business debtor classification, at least in part, on the family farmer in Chapter 12. Yet Blackmon argues that it would be more sensible to "echo, rather than mirror" the recent increase to a $10,000,000 limit on farming debt in the definition of a small business debtor in Chapter 11 because farming debt is more easily anticipated than small business debt.195 But he provides no data to support this contention, and even if it were true, it would not follow that a "narrower field" such as family farming necessarily requires a higher debt ceiling than small business debtors.196 If anything, the fact that the National Bankruptcy Conference consciously modeled its proposals for small business debtors on the requirements for family farmers argues that the debt limits should be the same.

More persuasive is Blackmon's conclusion that "[r]egardless of the final figure, the debt limit should be raised so more distressed businesses can take advantage of Subchapter V."197 Given the problems that small and medium-sized businesses will likely face in the coming years, the legislative advances of SBRA should not be limited by an inadequate debt ceiling and cluttered with qualifications that do not help to streamline business reorganizations.

C. A Proposed Solution

If the above suggestions are found to have merit, a revised definition of a small business debtor would read:

The term “small business debtor”—(A) subject to subparagraph (B), means a person (excluding a person whose primary activity is the business of owning single asset real estate) that has aggregate secured and unsecured debts as of the date of the filing of the petition or the date of the order for relief in an amount not more than $10,000,000, not less than 50 percent of which arose from the commercial or business activities of the debtor.

192 Id. at 360. For the National Bankruptcy Conference definition, see Nat'l Bankruptcy Conference, supra note 32, at 15.
194 Blackmon, supra note 190, at 360; but see 11 U.S.C.A. § 101(18A).
195 Blackmon, supra note 190, at 364.
196 Id. at 363.
197 Id. at 365.
(B) does not include—(i) any member of a group of affiliated debtors that has aggregate secured and unsecured debts in an amount greater than $10,000,000.\footnote{Compare this proposed language with existing statutory language. 11 U.S.C.A. § 101(51D).}

Such a definition would preserve the definitions added by the SBRA and revised by the CARES Act in 11 U.S.C. § 101(51D)(B)(ii)-(iii),\footnote{See BONAPFEL, supra note 13, at 11–12.} but it would eliminate the overly-complicated requirements discussed above. Eliminating these requirements helps restore the definition of a small business debtor in the Bankruptcy Code to something closer to its original purpose of a bright-line sorting technique. In large part, such a definition is supported by both the ABI, and the National Bankruptcy Conference.\footnote{For the ABI definition, see supra note 91; for the National Bankruptcy Conference’s definitions, see supra notes 77, 82.}

Businesses will not need to perform a complicated analysis of their finances in order to determine whether they qualify under this definition; such a determination should be relatively straightforward in the majority of cases.

Simplifying the process of reorganization and expanding its reach would help to counterbalance the comparatively larger costs that smaller firms bear, and which have been especially acute during the COVID-19 pandemic. In general, smaller firms carry greater risk than large businesses because they have higher debt levels than larger companies and rely more frequently on bank debts and shareholder loans.\footnote{Robin Greenwood, Benjamin Iverson, & David Thesmar, Sizing Up Corporate Restructuring in the Covid Crisis 8 (Nat’l Bureau of Econ. Rsch., Working Paper No. 28104, 2020), http://www.nber.org/papers/w28104.} Thus, they are more at risk than larger businesses over comparatively small debt obligations. Moreover, as presently construed, Chapter 11 “imposes costs that can be as high as 30% of a small business’s total value,” making it prohibitively expensive.\footnote{Id. at 19.} As a result, 90% of businesses with less than $1,000,000 in liabilities liquidate, while only 5% reorganize.\footnote{Id. at 18.} After the liquidation of a small business, reallocation of the labor and capital is comparatively difficult, especially in a recession.\footnote{Id. at 19–20.} One factor in the wave of liquidations is that smaller firms are less likely to receive funding that allows them to continue operations during bankruptcy when compared to larger firms.\footnote{Id. at 21.}

Nor would a large-wave default on medium and small business loans “meaningfully affect bank balance sheet[s] in aggregate.”\footnote{Id. at 20–21.}
Reducing the cost, complexity, and time required for a Chapter 11 reorganization could also be vital in the courts' ability to deal with an anticipated surge of cases. One analysis estimates that judge caseloads could increase by 158% from 2019 levels, more than caseloads in the Great Recession of 2008–2009. Depending on the amount of increase in bankruptcy filings, between 50 and 246 temporary bankruptcy judges could be necessary to ensure that the average judicial workload does not increase more than it did in 2010, at the height of the Great Recession.

Though certainly not a cure-all for the economic woes caused by COVID-19, simplifying the definition of a small business under the Code and raising the debt limit would allow more small and medium-sized firms to reorganize under the streamlined requirements provided by the SBRA. Moreover, this fits the policy Congress articulated in the SBRA.

**D. A Policy Choice: To Burden Small Businesses or Not?**

Ultimately, the question concerns legislative policy: should the Bankruptcy Code place demands on small and medium-sized businesses that disadvantage them in reorganizing under Chapter 11 when compared with larger companies?

Congress itself seems to have answered in the negative. It intended the SBRA to "streamline the bankruptcy process by which small business debtors reorganize and rehabilitate their financial affairs." Congress seems to have been influenced by the importance of small businesses to the national economy, which also suggests they should not be unfairly burdened. Small businesses create two thirds of new jobs and represent 44% of U.S. economic activity. Even before the COVID-19 outbreak, many small businesses had not completely recovered from the Great Recession. For example, though self-employment had expanded since 2010, it had not yet recovered from the levels...
it enjoyed before the Great Recession.\textsuperscript{213} The COVID-19 pandemic significantly affected small businesses, especially those in accommodations, food services, arts and entertainment, which suffered significant declines in November 2020 relative to their operational capacities the previous November.\textsuperscript{214} Thus, though COVID-19 is not the only reason why Congress should have simplified its definition of small businesses in the Bankruptcy Code, it provides an excellent example of why simplifying this definition could be so urgent: small businesses are central enough to the economy that placing unnecessary burdens on them is economically unwise as well as unfair.

Locally, the situation is just as urgent. Though health care providers such as Williamson Memorial Hospital\textsuperscript{215} may still struggle to provide quality health care in a rural setting, the costs, fees, and cumbersome process of reorganizing in Chapter 11 bankruptcy should not make its situation worse. If the debt limit were raised to $10,000,000 and the problematic provisions of the SBRA’s definition of small businesses were removed, Williamson Memorial would presumably not face as many obstacles in seeking to reorganize relatively efficiently and cheaply as a small business debtor under Subchapter V. For the sake of these businesses, and others that prove vital to the well-being of the communities they serve, these changes should be made quickly.

IV. CONCLUSION

Because Congress intended the SBRA to streamline the Chapter 11 process for small businesses, it should reformulate its definition of small businesses to provide the clarity and efficiency it valued in the SBRA. Specifically, Congress should have deleted the requirements (1) that debts be liquidated and noncontingent; (2) that debtors be "engaged in commercial or business activities"; and (3) that debts not be owed to insiders or affiliates.\textsuperscript{216} Such requirements make the Code’s definition of small businesses unnecessarily complicated and conflict the SBRA’s intent to provide efficient and less costly reorganizations for such debtors. Moreover, Congress should raise the debt limit to $10,000,000 in order to include as many small to medium-sized enterprises as possible. These changes to the Code’s definition of a small business debtor would allow such businesses to circumvent the burdensome disclosure requirements, deadlines, and costs that often make Chapter 11 reorganizations unworkable for

\begin{itemize}
\item \textsuperscript{215} See supra note 6.
\item \textsuperscript{216} 11 U.S.C.A. § 101(51D)(A) (West 2021).
\end{itemize}
small and medium-sized enterprises. Because Congress has found small businesses to be so central to the American economy, it should provide them the tools to quickly and efficiently reorganize under the SBRA.

Daniel O'Hare*