

# IS YOUR TENANT CONSIDERING BANKRUPTCY?

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## POTENTIAL DEBT RELIEF FOR DISTRESSED SMALL BUSINESSES IMPACTED BY COVID-19



As the devastating economic effects from COVID-19 continue to take their toll on businesses, waves of new bankruptcy filings are looming on the horizon. The Sacramento Business Journal recently reported that nearly one-third of local small businesses are in jeopardy of closure due to a lack of liquidity. But not all of these small businesses are doomed for failure.

Recent changes to the U.S. Bankruptcy Code and the CARES Act will change the landscape for those businesses that choose to file for bankruptcy protection and could help many of these small businesses survive through reorganization.

Earlier this year, the Small Business Reorganization Act of 2019 ("SBRA") created a new Subchapter V under Chapter 11 of the U.S. Bankruptcy Code, offering small businesses a greater opportunity to successfully and efficiently reorganize, preserve jobs, maximize the value of assets, and ensure the proper allocation of resources. Effective March 2020, the CARES Act expanded the SBRA and raised the debt limits to capture more small businesses within its parameters. As a result, we foresee more businesses taking advantage of the benefits afforded by the SBRA as the effects of COVID-19 prove detrimental to business viability.

Prior to SBRA, small businesses aiming to stay in operation and avoid a total liquidation were unlikely to reorganize under Chapter 11 of the Bankruptcy Code due to the costs and

administrative burdens associated with the process. Yet, filing under Chapter 7 may not have been desirable if the business was ineligible, owned valuable assets or the owners desired to keep the business going during bankruptcy. These administrative and procedural hurdles paved the way for the SBRA to offer a new and specialized bankruptcy category for eligible small businesses.

The SBRA caters to small businesses whose time and resources are more limited. It eliminates or streamlines some of the more costly or burdensome elements of the alternative bankruptcy relief options, permitting small businesses the opportunity to reorganize. Additionally, small businesses receive greater access to the same benefits that larger businesses enjoy under the original Chapter 11. As a result, businesses that do not really fit squarely into any prior bankruptcy option have a new avenue of relief. It does not only benefit small businesses but also their employees, suppliers, landlords and others who rely on the business. In particular, the bankruptcy trustee appointed by the court assists in formulating a consensual plan, reports any misconduct and monitors distributions in accordance with the confirmed plan. All of these items benefit the creditor. To the extent that the business remains viable, creditors such as landlords will benefit from tenant occupancy and timely payment of rent.

Accordingly, the SBRA, as temporarily modified by the CARES Act, provides a potentially valuable instrument for those eligible small businesses facing liquidity issues that are searching for a quicker and more cost-efficient option. We expect to see more bankruptcies as the aftermath of COVID-19 unfolds. With the revised Bankruptcy Code, we hope to see many of these small businesses weather the storm and revive once again, benefitting landlords and lenders.

If you have any questions regarding these changes and how they may affect your business, contact your Trainor Fairbrook attorney.