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# Is the SBRA Here to Stay? Case Law Developments and Political Will

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**The Small Business Reorganization Act of 2019 – The Subchapter V Trustee**

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**I. Introduction**

Similar to a standard chapter 11 case, Debtor's electing subchapter V status also retain control over their business and serve, at least initially, as a debtor-in-possession. Unlike a standard chapter 11 case, however, the provisions of the Bankruptcy Code *also* provide simultaneously for the appointment of a trustee in every subchapter V case. See 11 U.S.C. § 1183(a). At first glance, the duties and responsibilities of the subchapter V trustee appear analogous to those of a chapter 13 or chapter 12 trustee in that the trustee serves in a supervisory and monitoring role for the case. However, the interplay between certain provisions of the Bankruptcy Code's subchapter V sections and the practical necessities resulting from the, by definition, fast-paced nature of a subchapter V case, lead to interesting dynamics between the trustee, debtor, and creditors and help to create a unique new position in the Bankruptcy Code.

**II. General Duties of the Subchapter V Trustee**

Although not exhaustive of all duties a subchapter V trustee will need to perform in every case, Bankruptcy Code Section 1183 provides the statutory framework of duties expected of a subchapter V trustee. While many duties provided simply reference duties of other types of trustees contained in Sections 704(a) and 11069(a), the statutory listing provided also has a few key trustee duties only found in subchapter V. Specific statutory duties of the subchapter V trustee provided in Section 1183, include:

1. Be accountable for all property received [§ 704(a)(2)].
2. If a purpose would be served, examine proofs of claims and object to the allowance of any claim that is improper [§ 704(a)(5)].
3. If advisable, oppose the discharge of the debtor [§ 704(a)(6)].
4. Unless the court orders otherwise, furnish such information concerning the estate and the estate's administration as is requested by a party in interest [§ 704(a)(7)].
5. Make a final report and file a final account of the administration of the estate with the United States Trustee and the court [§ 704(a)(9)].
6. Perform the duties specified in § 1106(a)(3) and § 1106(a)(4) of this title if the court, for cause and on request of a party in interest, the trustee, or the United States Trustee, so orders. Pursuant to this provision, the trustee is required to:
  - a) investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and

the desirability of the continuance of such business, and any other matter relevant to the case or to the formulation of a plan [§ 1106(a)(3)]; and

- b) once the investigation is completed, file a statement of the investigation [§ 1106(a)(4)(A)].
- 7. After confirmation of a plan, file such reports as are necessary and the court orders [§ 1106(a)(7)].
  - 8. Appear and be heard at the status conference under § 1188 and any hearing that concerns:
    - a) The value of property subject to a lien;
    - b) Confirmation of a plan filed under subchapter V;
    - c) Modification of the plan after confirmation; or
    - d) The sale of property of the estate [§ 1183(b)(3)].
  - 9. Ensure that the debtor commences making timely payments required by a confirmed plan [§ 1183(b)(4)].
  - 10. If the debtor ceases to be a debtor in possession, pursuant to § 1183(b)(5), perform the duties specified in the following sections of the Bankruptcy Code, including operation of the debtor's business and:
    - a) Perform various duties specified in section 704(a), including: (2) be accountable for all property received; (5) examine proofs of claim and object to improper claims; (7) unless the court orders otherwise, provide information regarding the estate as requested to parties in interest; (8) file reports of operations if the debtor is authorized to be operated (9) make a final report and file a final account of the administration of the estate; (10) provide notice of the debtor's domestic support obligation; (11) administer any employee benefit plan; (12) if debtor is a health care business, take reasonable steps to transfer patients. [§ 1106(a)(1)]
    - b) File the list, schedules and statements required under section 521(1) if the debtor has not already done so. [§ 1106(a)(2)]
    - c) For any year for which the debtor has not filed a tax return required by law, furnish, without personal liability, such information as may be required by the governmental unit with which such tax return was to be filed, in light of the condition of the debtor's books and records and the availability of such information. [§ 1106(a)(6)]

11. If there is a claim for domestic support obligation, provide the applicable notice to the holder of the claim and appropriate State child support enforcement agency, as set forth in § 704(c). [§ 1183(b)(6)]
12. Facilitate the development of a consensual plan of reorganization. [§ 1183(b)(7)].

*See Exec. Office of the U.S. Trustee, Handbook for Small Business Chapter 11 Subchapter V Trustees, Statutory and General Duties of a Subchapter V Trustee, p.1-5 to 1-7.*

### **III. Facilitating a Consensual Plan: The Subchapter V Trustee's "Principal" Duty Under § 1183(b)(7)**

As seen in the list of duties of the subchapter V trustee shown above, the majority are not dissimilar from those duties required of traditional trustees under other sections of the Code. However, § 1183(b)(7) tasks the subchapter V trustee with the unique duty to "facilitate the development of a consensual plan of reorganization." 11 U.S.C. 1183(b)(7). In fact, the U.S. Trustee's *Handbook for Small Business Chapter 11 Subchapter V Trustee's* provides that this "facilitation of a consensual plan is a *principal* duty of the trustee." *Subchapter V Trustee Handbook* at 3-9. Importantly, one of the duties *not* enumerated in § 1183 in any scenario is the *filing* of a plan. Regardless of whether the debtor becomes dispossessed and the trustee assumes control of the debtor business, if the case remains in subchapter V, the debtor remains the only party able to file a plan of reorganization, which it must do not later than 90 days after the order of relief. 11 U.S.C. 1189(a), (b). This interplay positions the subchapter V trustee in a markedly different role in the case than of other bankruptcy trustees. Other trustees may be viewed in somewhat of an antagonistic position towards the debtor, instead set up in service of the estate with the goal of maximizing return to the estate's creditors. However, by tasking the subchapter V trustee with seeking a consensual plan, but focusing the filing of a plan solely in the debtor, the subchapter V provisions of the Bankruptcy Code force the trustee into a partnership with the debtor and position the trustee in a mediator role between the debtor and its creditors.

As seen in the recent case *In re 218 Jackson LLC*, subchapter V trustees that maintain an adversarial stance against the debtor and lose focus of the subchapter V trustee's role as mediator do not do so without consequence. *In re 218 Jackson LLC*, 2021 Bankr. LEXIS 2232 (M.D. Fla. Aug. 17, 2021). In *218 Jackson*, the subchapter V trustee appointed in the case also served as counsel to a creditor in a separate case under a different judge with similar ownership to the *218 Jackson* debtor. In his role as subchapter V trustee, instead of working with the debtor to develop a plan and address potential concerns, the trustee instead generally served in an antagonistic role, seeking twice to dismiss the case, and further opposed plan confirmation while again arguing that the debtor's case should be dismissed as a bad faith filing. In fact, in submitting his final fee application for \$11,870, time records of the trustee indicated that he spent no time making an attempt at working with the debtor and facilitating communication between the parties to negotiate a potential consensual plan. The debtor subsequently objected to the Trustee's final fee application based on the trustee's actions and argued that his representation in the related case meant that he was not "disinterested" as defined by Section 101(C), and required for appointment pursuant to Section 1183(a). The court did not look favorably on the trustee's actions both based on his

perceived conflict and failure to work with the debtor to make an attempt at developing a consensual plan. In ruling on the Debtor's objection to the trustee's final fee application, the court not only denied the application, but also removed him from the case and further ordered that all previously awarded fees be disgorged.

While the Bankruptcy Code requires subchapter V trustees to work to facilitate a consensual plan, it does not offer much in the way of exactly *how* to go about doing that. In that respect, certain tactics the trustee may take are left to the individual trustee based on the facts at hand, similar to the trustee's exercise of business judgment. At the very least, however, making attempts to bring the parties together and communicate and take active steps towards working towards compromise is the starting point. As further described in the *Subchapter V Trustee's Handbook*:

Section 1183(b)(7) of the Bankruptcy Code provides that a principal duty of the trustee is to facilitate the development of a consensual plan of reorganization. As soon as possible, the trustee should begin discussions with the debtor and principal creditors about the plan the debtor will propose, and the trustee should encourage communication between all parties in interest as the plan is developed. The trustee should be proactive in communicating with the debtor and debtor's counsel and with creditors, and in promoting and facilitating plan negotiations. Depending upon the circumstances, the trustee also may participate in the plan negotiations between the debtor and creditors and should carefully review the plan and any plan amendments that are filed.

*Subchapter V Trustee's Handbook* at 3-9.

#### **IV. Subchapter V Trustee Compensation – Two Paths and Incentives for Forming a Consensual Plan**

By removing the need to satisfy §§ 1129(a)(8), (10), and (15)<sup>1</sup>, confirming a non-consensual "cramdown" plan is much easier in subchapter V. A question then arises – what incentives exist for a trustee to seek confirmation of a consensual plan instead of simply confirming a plan under the easier cramdown provisions of § 1191(b)? In addition to § 1183(b)(7)'s statutory mandate, the Code also builds in other considerations that incentivize the trustee to help build consensus for confirmation under § 1191(a)'s consensual plan requirements. Not surprisingly, these provisions focus on two well established areas for incentivizing action: time and money.

The Code specifically exempts subchapter V trustee's from the § 326 compensation formula based on disbursements. Instead, compensation to the subchapter V trustee is awarded pursuant to § 330(a)(1)(A), which allows for "reasonable compensation for actual, necessary services rendered by the trustee ... and by any paraprofessional person employed by any such person." 11 U.S.C. 330(a)(1)(A). *See In re: Tri-State Roofing*, Case No. 20-40188–JMM, Doc. No. 86 (Bankr. D. Idaho; Dec. 7, 2020). Typically, the trustee will thus be compensated on an

<sup>1</sup> Subsection (a)(8) requires that all impaired classes accept the plan. Subsection (a)(10) requires, as a prerequisite to cramdown under 11 U.S.C. § 1129(b), that at least one impaired class of claims has accepted the plan. And subsection (a)(15) requires that if an unsecured creditor objected to the plan in a case filed by an individual debtor, the debtor pays the greater of the amount of the claim or the debtor's projected disposable income for five years.

hourly basis, with the reasonableness of fees charged evaluated on "the nature, the extent, and the value of such services, taking into account all relevant factors, including:

- a. the time spent on such services;
- b. the rates charged for such services;
- c. whether the services were necessary to the administration of the case, or beneficial at the time at which the services were rendered; and
- d. whether the services were performed within a reasonable amount of time commensurate with the complexity, importance, and nature of the problem, issue, or task addressed."

*Subchapter V Trustee's Handbook* at 3-21, 22.

The *Subchapter V Trustee's Handbook* further cautions that "Trustees are encouraged to keep in mind Congress' stated intent that subchapter V cases not be burdened with excessive administrative expenses when planning their work and submitting their fee applications for review and approval by the court. *Subchapter V Trustee's Handbook* at 3-22.

While fees are approved under § 330, consideration over when they are *paid* depends on whether the debtor's plan is approved under the consensual provisions of § 1191(a) or the cramdown provisions of § 1191(b).

Under a consensual plan, the trustee's services are terminated upon the substantial consummation of such plan, with the debtor itself handling payments under the plan thereafter. 11 U.S.C. § 1183(c)(1). Payment of the Trustee's approved fees and expenses in full, therefor will occur on or before the time of consummation.

Under a non-consensual plan, however, the trustee will typically remain in the case and will himself make payments under the plan over the course of the three to five year period in which the debtor must contribute his disposable income. Additionally, § 1191(e) provides a "Special Rule" allowing for payment of the trustee's fees and expenses as an administrative claim over the course of the three to five year plan period. 11 U.S.C. § 1191(e). This thus provides strong incentives for the trustee to work with all parties to try to reach consensus. If a consensual plan is reached, the trustee can end his role in the case and get paid immediately. If not, the trustee will likely have to remain in the case and take on the administrative burden of administering payment for up to five years, with payments to the trustee for fees stretched out over that same time period.

## V. Subchapter V Trustee Employment of Professionals

Trustees in other sections will typically seek employ counsel in the ordinary course of their involvement in the case. As noted in the *Subchapter V Trustee Handbook*, however, subchapter V is intended to be a "quick and low-cost process to enable to enable debtors to confirm consensual plans in a short period with less expense while returning appropriate dividends to creditors," and, therefore "the services required of outside professionals, if any, will be limited in many cases." *Subchapter V Trustee's Handbook* at 3-17. "Bearing in mind the goal of subchapter V to contain

expenses, the trustee should carefully consider whether a professional is needed in any given case." *Id.*

These matters came to light in the case of *In re Penland Heating and Air Conditioning, Inc.*, 2020 WL 3124585 (E.D.N.C. 2020). In *Penland*, the subchapter V trustee sought to employ counsel in the typical course of action as he was accustomed to do for a chapter 7 case. The court did not fault the trustee for applying for employment of counsel, but denied the application. In doing so, the court cited to the provisions contained in the *Subchapter V Trustee's Handbook* concerning employment of professionals and the need to control administrative expenses of the case. The court went on to provide that his ruling did not mean that employment of subchapter V trustee's counsel was not allowed in every case. Rather, in order to be successfully employed, it would be necessary for the trustee to articulate a specific need as to why counsel was needed based on the specific facts at hand and how the employment would help to serve the goals for subchapter V to reach a consensual plan quickly and at low cost.

# Faculty

**Marc E. Albert** is a partner with Stinson LLP in Washington, D.C., and chairs its Bankruptcy and Creditors' Rights Group. He has concentrated over the past 35 years in the areas of financial restructuring, insolvency and creditors' rights. Mr. Albert has represented debtors, creditor committees, lenders and other creditors. He has been appointed by the Office of the U.S. Trustee as operating trustee in chapter 11 and 7 cases, and he has been on the Chapter 7 Trustee Panel in the District of Columbia for over 30 years. He also serves as counsel in a variety of bankruptcy and nonbankruptcy matters, including representing numerous clients who have tax problems with the Internal Revenue Service or state tax authorities. Prior to joining the firm, Mr. Albert was litigation counsel with the Tax Division of the Department of Justice. With three other attorneys, he started a boutique bankruptcy law firm that grew to become one of the leading bankruptcy firms in Northern Virginia. Mr. Albert maintains an AV rating from Martindale-Hubbell and is admitted to practice in Pennsylvania, the District of Columbia, Maryland and Virginia, and before the U.S. Supreme Court. He is a member of the District of Columbia, American and Virginia Bar Associations, and the Walter Chandler Inn of Court, National Association of Bankruptcy Trustees, ABI, World Affairs Council – Washington, D.C., and the George Washington University Law School Mentoring and Recruitment Program. He was recognized in 2015 with the Founders Award from World Affairs Council and is listed in *The Best Lawyers in America* from 2011-17 for Bankruptcy and Creditor/Debtor Rights/ Insolvency and Reorganization Law and Litigation-Bankruptcy, *Washington D.C. Super Lawyers* from 2012-17 for Bankruptcy & Creditor/Debtor Rights, and the 2015 edition of *Chambers USA: America's Leading Lawyers for Business* in Bankruptcy/Restructuring. Mr. Albert received his B.A. in 1970 and his J.D. in 1973 from George Washington University, and his M.L.T. in 1984 from Georgetown University.

**Hon. Michelle M. Harner** is a U.S. Bankruptcy Judge for the District of Maryland in Baltimore, appointed in 2017. Prior to her appointment to the bench, she was the Francis King Carey Professor of Law and the Director of the Business Law Program at the University of Maryland Francis King Carey School of Law, where she taught courses in bankruptcy and creditors' rights, business associations, business planning, corporate finance and the legal profession. Judge Harner lectured frequently during her academic career on various topics involving corporate governance, financially distressed entities, risk management and related legal issues. Her academic scholarship is widely published, with her publications appearing in, among others, the *Vanderbilt Law Review*, *Notre Dame Law Review*, *Washington University Law Review*, *Minnesota Law Review*, *Indiana Law Journal*, *Fordham Law Review* (reprinted in *Corporate Practice Commentator*), *Washington & Lee Law Review*, *William & Mary Law Review*, *University of Illinois Law Review*, *Arizona Law Review* (reprinted in *Corporate Practice Commentator*) and *Florida Law Review*. Judge Harner has served as the Associate Reporter to the Advisory Committee on the Federal Rules of Bankruptcy Procedure, the Reporter to the ABI Commission to Study the Reform of Chapter 11, and most recently chaired the Dodd-Frank Study Working Group for the Administrative Office of the U.S. Courts. She also served as the Robert M. Zinman ABI Resident Scholar for the fall of 2015. Judge Harner is an elected conferee of the National Bankruptcy Conference, an elected Fellow of the American College of Bankruptcy, and an elected member of the American Law Institute. She previously was in private practice in the business restructuring, insolvency, bankruptcy and related transactional fields, most recently as a partner at the Chicago office of the international law firm Jones Day. Judge Harner



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