

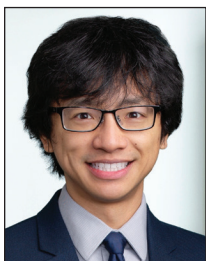
Legislative Update

BY HON. CHRISTOPHER G. BRADLEY AND AN NGUYEN

If It Ain't Broke, Should the Court "Fix" It? Payment Periods in Nonconsensual Sub V Plans



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To confirm a nonconsensual subchapter V plan, a debtor must agree to devote its projected disposable income (or property of equivalent value) to plan payments for a period of at least three years — and up to five years “as the court may fix.”¹ Debtors usually prefer three years, while unsecured creditors prefer the maximum five years. When should the bankruptcy court depart from the debtor’s preference and “fix” a longer plan payment period?

Faced with this question in *In re Trinity Family Practice & Urgent Care PLLC*,² Hon. **Shad M. Robinson** of the U.S. Bankruptcy Court for the Western District of Texas addressed the deference that a bankruptcy court should give to a debtor’s proposed plan payment period and set forth a list of nonexclusive factors to consider in determining whether a plan payment period is “fair and equitable” and whether to “fix” a longer period of up to five years.³ This is one of the numerous areas of subchapter V that remains largely unexplored, and *Trinity Family Practice* breaks new ground.⁴

The factors provide helpful guidance in the exercise of the broad discretion left by Congress to the bankruptcy courts to determine the applicable plan payment period in subchapter V cases.⁵ We provide this article so that courts and practitioners will be able to take advantage of Judge Robinson’s work to guide their consideration of this issue.

Background

In *Trinity Family Practice*, the debtor sought confirmation of a subchapter V plan that provided for payments of projected disposable income over a three-year period.⁶ A creditor holding both an unsecured claim and the sole secured claim voted

to reject the plan and objected to confirmation, arguing that because the debtor could pay more to unsecured creditors if the plan payment period was extended to five years, the plan was (1) not “proposed in good faith,” as required by § 1129(a)(3), and (2) not “fair and equitable” to nonaccepting classes, as required to confirm a nonconsensual plan under § 1191(b).⁷

The court overruled the good-faith objection⁸ but — guided by a novel analysis of various instructive factors formulated by the court — found that the debtor failed to satisfy its burden of demonstrating that the proposed three-year plan payment period was “fair and equitable.” It then found that there was insufficient evidence to determine whether it should exercise its discretion to “fix” a longer plan payment period that would be “fair and equitable,”¹⁰ and instead denied confirmation and granted the debtor leave to file an amended plan.

Determining Whether a Proposed Payment Period Is “Fair and Equitable”

If an impaired class does not accept a subchapter V plan, the resulting “nonconsensual” (or “cramdown”) plan cannot be confirmed unless it satisfies the requirements in § 1191(b), including that the plan is “fair and equitable” with respect to nonaccepting classes.¹¹ Several requirements for satisfying the “fair and equitable” condition are listed in § 1191(c), including that the plan either applies all of the debtor’s projected disposable income during “the three-year period, or such longer period not to exceed five years as the court may fix, beginning on the date that the first payment is due under the plan,”¹² or distributes property with a value not less than the projected disposable income during such period.¹³

In evaluating whether the proposed plan payment period in *Trinity Family Practice* was “fair

1 11 U.S.C. § 1191(c)(2).

2 No. 23-70068, 2024 WL 2704056 (Bankr. W.D. Tex. May 24, 2024).

3 ABI Editor-at-Large **Bill Rochelle** has summarized some of the other topics analyzed in *Trinity Family Practice*. “Three Years Is the ‘Default’ Duration for a Subchapter V Plan, Judge Robinson Says,” *Rochelle’s Daily Wire* (June 7, 2024), available at abi.org/newsroom/daily-wire (unless otherwise specified, all links in this article were last visited on Aug. 21, 2024).

4 As discussed in this article and in Judge Robinson’s opinion, Hon. **Beth E. Hanan** of the U.S. Bankruptcy Court for the Eastern District of Wisconsin also contributed significantly to this area of law. *In re Urgent Care Physicians Ltd.*, No. 21-24000, 2021 WL 6090985 (Bankr. E.D. Wis. Dec. 20, 2021).

5 *Trinity Family Practice*, 2024 WL 2704056, at *15.

6 *Id.* at *1.

7 *Id.*

8 *Id.* at *10-12.

9 *Id.* at *17-22.

10 *Id.* at *18-22.

11 11 U.S.C. § 1191(b).

12 11 U.S.C. § 1191(c)(2)(A).

13 11 U.S.C. § 1191(c)(2)(B).

and equitable” under § 1191(c),¹⁴ the court concluded that “the bankruptcy court should give appropriate deference to the debtor’s business judgment and proposed period of payments.” Section 1189 provides that only the debtor may file a subchapter V plan.¹⁵

In addition, Judge Robinson extensively analyzed the bankruptcy court’s opinion in *In re Urgent Care Physicians Ltd.*¹⁶ and ultimately agreed with that court that a three-year plan term is the “baseline” or “default” under subchapter V.¹⁷ He noted that because a three-year baseline plan payment period “is consistent with the intent of Congress to create a quick, efficient reorganization process that would allow the debtor to obtain a discharge as soon as possible ... while properly balancing the competing interests of debtors and creditors,” if “there is no objection to the proposed period of plan payments, it would likely be uncommon for the bankruptcy court to *sua sponte* raise the issue of the proposed period of plan payments.”¹⁸

If an objection to a proposed plan payment period is filed, “the debtor’s proposed period of plan payments is no longer given the same deference and the bankruptcy court is tasked with fixing the applicable period of plan payments in a subchapter V case.”¹⁹ Departing from the *Urgent Care Physicians* opinion, Judge Robinson held that “unusual circumstances” are not required to shift the three-year default and impose a longer plan term.²⁰ The debtor must carry the burden of establishing that the term is fair and equitable, and the bankruptcy court has the sole authority — and the broad discretion — to “fix” a subchapter V plan payment period longer than the baseline three-year period set by § 1191(c)(2).²¹

Having entrusted bankruptcy courts with this discretion, Congress did not ordain any particular factors for how to exercise it.²² Provisions governing plan length under other Bankruptcy Code chapters are not sufficiently analogous to subchapter V to be instructive.²³ Courts must engage in a fact-sensitive, case-by-case analysis of the totality of the circumstances to “fix” the plan term.

Judge Robinson stepped into the breach to give some shape to this potentially frustrating and amorphous analysis. He formulated a list of nonexclusive factors to instruct his determination of whether the debtor has satisfied its burden of demonstrating that its proposed plan payment period is “fair and

equitable” and, if necessary, where in the three-to-five-year range would be “fair and equitable” to nonaccepting classes.

We are still learning about subchapter V — what its provisions mean, how they can and should work together, and how it differs from other chapters.

The Trinity Family Practice Factors **Capital Reserves or Capital Expenditures During** **the Plan Payment Period**

Where a debtor’s plan projections include reservations for capital expenditures during the plan payment period to support potential future growth of the debtor’s business, creditors “may reasonably argue that the disposable income they must receive should not be depleted when the debtor will gain the benefit of the investment of income in the business.”²⁴ The “competing interests of debtors and creditors” should be weighed by considering evidence of (1) the basis for such reserve and how it was calculated; (2) whether the debtor historically had a capital reserve; (3) any planned future purchases; (4) any cyclical nature of the debtor’s revenue; (5) future debt financing; or (6) specific costs and expenses in the debtor’s business operations that are not accounted for in the plan projections but may arise during the plan payment period.²⁵ Extra scrutiny might be warranted where the amount of projected capital reserves is close to the total projected distribution to unsecured creditors.²⁶

Reasonableness of Income and Expenses Set Forth **in the Plan Projections During the Plan Payment Period**

The court should evaluate the reasonableness of projected income and expenses during the plan payment period, especially as compared to the debtor’s historical operations.²⁷ Any differences between the projections and the debtor’s actual historical financials — including as set forth in a debtor’s schedules and monthly operating reports — should be supported with additional evidence or testimony, including regarding the basis and methodology for calculating the projections and how increased expenses benefit the debtor and its creditors.²⁸

Salary and/or Other Payments to Insiders During **the Plan Payment Period**

Increases in payments and distributions to insiders during the plan payment period could warrant the court “fixing” a longer period unless supported by either historical evidence of such payments or evidence to establish why such payments are necessary, reasonable and appropri-

14 Although *Trinity Family Practice* addresses only subchapter V plans where payments of projected disposable income are made under § 1191(c)(2)(A), the same analyses are applicable to plans that instead distribute property under § 1191(c)(2)(B), as the two approaches differ only in the timing of plan distributions. See generally *In re Packet Constr. LLC*, No. 23-10860, 2024 WL 1926345, at *4 (Bankr. W.D. Tex. April 30, 2024) (observing that primary difference between two alternative approaches in § 1191(c)(2)(A) and (B) is that “approach contained in section 1191(c)(2)(B) ... essentially gives flexibility on the timing of payment”); see also *Legal Serv. Bureau Inc. v. Orange Cty. Bail Bonds Inc.* (*In re Orange County Bail Bonds Inc.*), 638 B.R. 137, 146-47 (B.A.P. 9th Cir. 2022) (holding that plan using liquidated-asset proceeds to make payments in excess of present value of projected disposable income over applicable plan period satisfies § 1191(c)(2)(B)).

15 *Trinity Family Practice*, 2024 WL 2704056, at *17.

16 2021 WL 6090985.

17 *Trinity Family Practice*, 2024 WL 2704056, at *17.

18 *Id.*

19 *Id.* (citing *Orange Cnty. Bail Bonds Inc.*, 638 B.R. at 146).

20 *Id.* at *14.

21 *Id.* at *15-16.

22 *Id.* at *16.

23 *Id.* (discussing §§ 1222(c) (imposing “for cause” standard for plan payment periods longer than three years in chapter 12 plans); and 1325(b)(4) (giving court no discretion in establishing “applicable commitment period”); and traditional chapter 11 cases, where plan terms (rather than bankruptcy court) determine plan payment period).

24 Hon. Paul W. Bonapfel, *A Guide to the Small Business Reorganization Act of 2019 and Subchapter V Update* at 146 (June 2022), available at www.ganb.uscourts.gov/sites/default/files/sbra_guide_pwb.pdf.

25 *Trinity Family Practice*, 2024 WL 2704056, at *18.

26 *Id.*

27 *Id.* at *19.

28 *Id.*

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ate.²⁹ Conversely, evidence of “belt-tightening” behavior by the debtor — such as the below-market salaries and other salary reductions for insiders during the plan payment period in *Urgent Care Physicians*³⁰ — could support a finding that a proposed plan payment period is “fair and equitable.”

Risks and Consequences of a Longer Plan Payment Period

Recognizing that “extending a plan will almost always result in a potentially larger distribution to unsecured creditors,” the court should evaluate how a longer plan payment period will affect the debtor and its employees, customers and creditors.³¹ Foremost in this consideration is Congress’s intent that subchapter V make reorganization easier for small businesses.³²

An objection that a proposed plan payment period is not “fair and equitable” should include consideration of the potential risks and consequences to the debtor. For example, in *Urgent Care Physicians*, where the debtor’s insiders were voluntarily taking pay cuts during the proposed three-year plan payment period, the court found that based on the evidence presented, “fixing” a longer pay period was too risky and would disproportionately favor creditors at the debtor’s expense.³³

Any Other Unique or Extraordinary Facts Specific to the Case

The final factor is “a catch-all factor to address any unique or extraordinary facts or circumstances specific to a particular case that are not considered under one of the other factors.”³⁴ It allows the court to weigh any evidence offered in support of the proposed plan period or some longer period “as the court may fix.”

Conclusion

Judge Robinson was at pains to emphasize that the discussed *Trinity Family Practice* factors are not exclusive, nor did he intend any one of them to be dispositive. However, these factors provide much-needed guidance for navigating the payment period in a nonconsensual subchapter V plan.

A debtor seeking confirmation of a nonconsensual plan should be prepared with evidence and testimony to support its proposed payment period, especially if the plan projections provide for any increases in payments or expenses that would otherwise be applied to distributions to unsecured creditors. Similarly, while the burden is always on the debtor, a creditor requesting that the court “fix” a longer plan payment period should nevertheless present evidence to demonstrate why the burden on the debtor of a longer period is outweighed by the benefit to creditors. Finally, the bankruptcy court should weigh any evidence presented in consideration of the factors in determining whether a proposed plan payment period is “fair and equitable” or, if necessary, whether to “fix” a different period.

We are still learning about subchapter V — what its provisions mean, how they can and should work together, and how it differs from other chapters. The indispensable treatise by Hon. **Paul W. Bonapfel** of the U.S. Bankruptcy Court for the Northern District of Georgia,³⁵ the work of ABI’s Subchapter V Task Force,³⁶ numerous excellent opinions and other sources provide much illumination, but there are still many areas in which work remains to be done. In elaborating how to approach the important and novel provisions on plan length in subchapter V cases, Judge Robinson in *Trinity Family Practice* — and Judge Hanan in *Urgent Care Physicians* before him — have done great service to the bankruptcy community. **abi**

²⁹ *Id.*

³⁰ *Urgent Care Physicians*, 2021 WL 6090985, at *4-5.

³¹ *Trinity Family Practice*, 2024 WL 2704056, at *20.

³² *Id.* (citing *In re Lost Cajun Enters. LLC*, 634 B.R. 1063, 1066 (Bankr. D. Colo. 2021)).

³³ *Urgent Care Physicians*, 2021 WL 6090985, at *11.

³⁴ *Id.* at *22.

³⁵ See Hon. Paul W. Bonapfel, *SBRA: A Guide to Subchapter V of the U.S. Bankruptcy Code* (ABI 2024), available at store.abi.org.

³⁶ Read the task force’s Final Report and recommendations at subvtaskforce.abi.org.

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