

Problems in the Code

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Removal of the Subchapter V DIP: A Road to Nowhere?

Section 1183 of the Bankruptcy Code, enacted through the Small Business Reorganization Act of 2019 (SBRA), sets forth the duties of a subchapter V trustee, in part by referencing §§ 704(a) and 1106(a). In every subchapter V case, the trustee shall perform the following duties: (1) be accountable for all property received;¹ (2) examine proofs of claim and object, if appropriate;² (3) oppose the discharge, if appropriate;³ (4) furnish information as requested;⁴ (5) make a final report;⁵ (6) appear and be heard in the case;⁶ (7) ensure that the debtor commences plan payments;⁷ and (8) facilitate the development of a consensual plan.⁸

In certain cases, if ordered by the court “for cause,” the trustee shall also (1) investigate the debtor’s acts, conduct, assets, liabilities and financial condition;⁹ (2) file a statement of any investigation;¹⁰ and (3) file post-confirmation reports.¹¹ If the subchapter V trustee’s powers are expanded to include an investigation of the debtor, such investigation includes “any other matter relevant to the case or to the formulation of a plan.”¹²

The Subchapter V Trustee Cannot File a Plan

Notwithstanding this provision expressly relating to the formulation of a plan, as set forth herein, the Code does not permit the subchapter V trustee to file a plan. If the debtor ceases to be a debtor in possession (DIP) as a result of an order under § 1185 of the Bankruptcy Code, the subchapter V trustee is granted the following additional duties: (1) if operating a business, file certain periodic reports;¹³ (2) provide notice relating to a claim for a domestic-support obligation;¹⁴ (3) serve as administrator under an Employee Retirement Income Security Act plan;¹⁵ (4) transfer patients of a health care busi-

ness;¹⁶ (5) file schedules;¹⁷ (6) file tax returns;¹⁸ and (7) operate the debtor’s business.¹⁹

Significantly, the Code never grants the subchapter V trustee the duty (or authority) to collect and reduce to money property of the estate under § 704(a)(1), or to file a plan under § 1106(a)(5).²⁰ In addition, § 1189(a) clearly states that “only the debtor may file a plan under this subchapter.”²¹ As currently drafted, the Code is clear: The subchapter V trustee may never file a plan.

Accordingly, even if the debtor is removed as a DIP “for cause” pursuant to § 1185, and the subchapter V trustee is authorized to investigate matters relevant to plan formulation and operate the debtor’s business under § 1183(b)(5)(B), the subchapter V trustee cannot file, or confirm, a plan — the preferred resolution of a subchapter V case.²² This invites the following question: Who better to file a plan in a chapter 11 case than the person who is operating the business?

Instead, the subchapter V trustee and bankruptcy court are left with a proverbial “road to nowhere,” with the only remaining choices being dismissal or conversion of the case to chapter 7.²³ In a case where the DIP’s removal is warranted, conversion to chapter 7 is ultimately the only viable option, as dismissal would essentially place the debtor back into possession. While a chapter 7 liquidation can solve some problems, the expeditious liquidation of a small business will not preserve jobs and goodwill.

This is a problem in subchapter V, as many of those cases need a confirmed plan to be truly successful. As a subchapter V trustee, there have been cases where I wished that I had the right to file a plan, or at least request the court for the authority



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1 11 U.S.C. § 704(a)(2).

2 11 U.S.C. § 704(a)(5).

3 11 U.S.C. § 704(a)(6).

4 11 U.S.C. § 704(a)(7).

5 11 U.S.C. § 704(a)(9).

6 11 U.S.C. § 1183(b)(3).

7 11 U.S.C. § 1183(b)(4).

8 11 U.S.C. § 1183(b)(7).

9 11 U.S.C. § 1106(a)(3).

10 11 U.S.C. § 1106(a)(4).

11 11 U.S.C. § 1106(a)(7).

12 11 U.S.C. § 1106(a)(3).

13 11 U.S.C. § 704(a)(8).

14 11 U.S.C. § 704(a)(10) via 11 U.S.C. § 1106(a)(1).

15 11 U.S.C. § 704(a)(11) via 11 U.S.C. § 1106(a)(1).

16 11 U.S.C. § 704(a)(12) via 11 U.S.C. § 1106(a)(1).

17 11 U.S.C. § 1106(a)(2).

18 11 U.S.C. § 1106(a)(6).

19 11 U.S.C. § 1183(b)(5)(B).

20 See *In re Body Transit Inc.*, 613 B.R. 400 (Bankr. E.D. Pa. 2020) (noting that § 1106(a)(5) does not apply to subchapter V trustees).

21 See *In re Online King LLC*, 629 B.R. 340 (Bankr. E.D.N.Y. 2021) (subchapter V trustee is not permitted to file plan); *In re Coepris Equity Fund LLC*, 2024 WL 1155450 (9th Cir. 2024) (only debtor may file subchapter V plan); *In re Young*, 2021 WL 1191621 (Bankr. D.N.M. 2021) (same).

22 The stated SBRA’s legislative purpose was to provide a fast track for small businesses to confirm a consensual plan with the assistance of a subchapter V trustee. See *Handbook for Small Business Chapter 11 Subchapter V Trustees*, Chapter 1 (February 2020).

23 However, at least one court has solved the problem by revoking the debtor’s designation under subchapter V and appointing a chapter 11 trustee. See *In re Nat’l Small Bus. Alliance Inc.*, 642 B.R. 345 (Bankr. D.D.C. 2022). But see *In re Free Speech Sys. LLC*, 649 B.R. 729 (Bankr. S.D. Tex. 2023) (questioning bankruptcy court’s authority to revoke designation).

to do so. In regular chapter 11 cases, the debtor's exclusive right to file a plan can be terminated in appropriate circumstances,²⁴ and the threat of that happening increases the likelihood of a confirmed, consensual plan.

Curiously and in comparison, although the subchapter V trustee is never expressly granted the power to collect and reduce to money property of the estate under § 704(a)(1), subchapter V trustees with expanded powers often collect and reduce property of the estate to money through the sale or liquidation of assets. At least one reported decision has held that the subchapter V trustee may move for relief under § 363(b) of the Bankruptcy Code, which governs the sale or use of property of the estate outside the ordinary course of business.²⁵ As subchapter V trustee, I have sold property under § 363 in some cases.²⁶

A Possible Solution

How can this “road to nowhere” in the Code be solved so that the subchapter V trustee can file a plan? The most direct solution would be to amend § 1183(b)(5)(A) to expressly include the right to file a plan under “paragraph 5 of section 1106(a) of this title.” In addition, § 1189(a) — limiting the authority to file a plan to only the debtor — would need to be amended to state “except when the debtor ceases to be a [DIP].” With these legislative amendments, a subchapter V trustee who is substituted for the DIP could file a plan in appropriate cases.

Alternatively, § 1183(b) could be amended to expressly include the subchapter V trustee's right to file a plan under

§ 1106(a)(5) of the Bankruptcy Code “if the court, for cause and on request of a party-in-interest, the trustee,” or the U.S. Trustee expands the subchapter V trustee's powers, or in essence terminates exclusivity in the trustee's favor. This alternative solution would permit the subchapter V trustee to file a plan, perhaps a competing plan, while the debtor was still in possession. It seems that a competing plan dynamic would create leverage that could help lead to a global consensual plan that would also include the debtor's consent.

Conclusion

It is a fact that the subchapter V trustee has a statutory responsibility to participate in the plan process. If the subchapter V trustee's participation cannot result in the formulation of a consensual plan, then the bankruptcy court should have the power to authorize the subchapter V trustee to file a plan. If the bankruptcy court had such discretionary power, the likelihood of a confirmed plan would be increased.

This is directly consistent with subchapter V's primary goal. There is no clear policy reason why the subchapter V trustee should be prohibited from filing a plan. The subchapter V trustee is there to assist the parties in reaching consensus, but if the trustee cannot do that, the next-best result is plan confirmation.

As a subchapter V trustee, I certainly understand that the trustee is not generally adversarial with the debtor, but under appropriate circumstances, the subchapter V trustee is permitted, and perhaps encouraged, to become adversarial, (e.g., to file a motion to remove the DIP). A request for authority to file a plan is a less-adversarial move than a motion for removal of the DIP, and it would improve the process. **abi**

Editor's Note: *ABI's Subchapter V Task Force released its Final Report and recommendations to Congress in April 2024, which is accessible at subvtaskforce.abi.org.*

²⁴ 11 U.S.C. § 1121(c).

²⁵ *In re Roe*, 2024 WL 206678 at *1 (Bankr. D. Ore. 2024) (“The Subchapter V Trustee is a trustee under the Bankruptcy Code and may move for relief under section 363(b).”). In *Roe*, the bankruptcy court held that the power to use or sell property was not “exclusive” to the debtor suggesting that a subchapter V trustee could sell property of the estate even without having expanded powers. *But see In re Turkey Leg Hut & Co. LLC*, 2024 WL 2797455 (Bank. S.D. Tex. 2024) (holding as matter of first impression that subchapter V trustee lacks standing to seek injunctive relief in debtor's favor).

²⁶ *See In re H2O Inv. Props. LLC*, Case No. 2:23-bk-00373-FMD, Doc. No. 176 (Bankr. M.D. Fla. April 30, 2024).