By Richard Drew and Denise J. Penn

Prepacks and Subchapter V: An Uneasy Fit

Since the Small Business Reorganization Act of 2019 (SBRA) took effect on Feb. 19, 2020, subchapter V has provided small businesses a more flexible, efficient and cost-effective path through chapter 11.[1] Nearly 8,200 debtors have elected subchapter V treatment since 2020, and their plans have been confirmed at more than twice the rate and their cases dismissed at about half the rate of other small business cases.[2]

The U.S. Trustee Program (USTP) has played an integral role in the administration of subchapter V cases during the first four years of the SBRA's existence, including selecting and supervising subchapter V trustees,[3] raising objections to eligibility and plan confirmation (when appropriate), and seeking to dismiss or convert cases when warranted. Given its experience with subchapter V cases, the USTP has been interested in recent commentary advocating for the use in subchapter V cases of prepackaged or prearranged plans — a well-known chapter 11 strategy in which a debtor solicits or simply negotiates creditors' approval of a bankruptcy plan before filing.[4]

This article considers the tensions created by attempting to import prepackaged or prearranged plans into the subchapter V context. First, it describes the statutory basis for prepackaged bankruptcies in standard chapter 11 cases, then analyzes the uneasy fit between a prepackaged plan and a subchapter V case. It also explains the heightened due-process concerns that prepackaged subchapter V cases would present.

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Prepackaged Plans in Chapter 11s

Although "prepackaged bankruptcy" appears nowhere in the Bankruptcy Code or Federal Rules of Bankruptcy Procedure,[5] it is an established practice for expediting a chapter 11 case. The debtor in a prepackaged bankruptcy, or "prepack," solicits all impaired creditors for their votes on a plan before filing the case.[6] There are also cases — typically referred to as "partial" prepacks or "prearranged" cases — that involve only partial solicitation or some type of significant prebankruptcy negotiation without any pre-petition solicitation.[7]

Section 1126(b) of the Bankruptcy Code authorizes pre-petition solicitation and acceptance of a plan if the debtor provides disclosures that are compliant with either applicable nonbankruptcy law or § 1125(a).[8] Bankruptcy Rule 3018(b), which establishes the criteria for courts considering whether to allow pre-petition acceptances or rejections of a plan at a confirmation hearing, mandates that votes on a prepackaged plan will not be counted if substantially all members of the voting class are not solicited or if "an unreasonably short time was prescribed ... to accept or reject the plan."[9] The Code also allows requests, supported by cause, to dispense with the meeting of creditors in cases where solicitation occurred before filing and permits the USTP to appoint a committee organized pre-petition as the post-petition committee of unsecured creditors.[10] Debtors use these provisions to seek confirmation of a plan quickly, lower administrative costs and secure other potential benefits, such as less business disruption.

Even with these accommodations in the Code, a debtor seeking to confirm its prepackaged plan must still abide by Bankruptcy Rules 3016, 3017 and 2002, which require at least 28 days of notice (typically by mail) for both approval of the adequacy of pre-petition disclosure and for objections to confirmation (although these hearings are typically combined in prepackaged cases).[11] Those deadlines might be reduced only for cause under Bankrutpcy Rule 9006(c).[12] Similarly, Bankruptcy Rule 6003 prohibits the court from entering orders granting certain kinds of relief during the first 21 days of a case unless the relief is necessary to avoid immediate and irreparable harm.[13]

Despite these notice requirements, courts in a few cases have confirmed prepackaged bankruptcy

1 Pub. L. No. 116-54, 133 Stat. 1079 (2019).
2 *See* "Chapter 11 Subchapter V Statistical Summary Through May 31, 2024," *available at* justice.gov/ust/page/file/1499276/download (unless otherwise specified, all links in this article were last visited on June 24, 2024). Cases that were amended to elect subchapter V treatment after filing are included in the statistics.
3 11 U.S.C. § 1183(a); 28 U.S.C. § 586.
4 *See, e.g.*, Christopher Hampson & Jeffrey A. Katz, "The Small Business Prepack: How Subchapter V Paves the Way for Bankruptcy's Fastest Cases," *Geo. Wash. L. Rev.* (forthcoming), *available at* ssrn.com/abstract=4595995.
5 11 U.S.C. § 101, *et seq.*; Fed. R. Bankr. P. 1001, *et seq.*
6 *The U.S. Trustee Program Policy and Practices Manual at Volume 3*, Chapter 3-13, *available at* justice.gov/ust/file/volume_3_chapter_11_case_administration.pdf/dl.
7 Although these cases may move more quickly than the typical chapter 11, they should typically not include shortened notice periods or waive the meeting of creditors under 11 U.S.C. § 341(e).
8 11 U.S.C. § 1126(b).
9 Fed. R. Bankr. P. 3018(b).
10 *See* 11 U.S.C. §§ 341(e), 1102(b)(1); Fed. R. Bankr. P. 2007.
11 Fed. R. Bankr. P. 2002(b), 3016, 3017; *see also* 11 U.S.C. § 105(d)(2)(B)(vi).
12 Fed. R. Bankr. P. 9006(c).
13 Fed. R. Bankr. P. 6003 (referencing various forms of relief typically found in plans). *See also In re Colad Grp. Inc.*, 324 B.R. 208, 214 (Bankr. W.D.N.Y. 2005) (describing principles that should apply to first-day relief, including that it should avoid "substantive rulings that irrevocably determine the rights of parties").

plans as quickly as within one day after a chapter 11 filing, often with the debtor claiming that it had already provided adequate notice pre-petition rather than showing specific cause for such an extreme shortening of the notice periods.[14]

The USTP regularly objects to this practice, which presents serious due-process concerns and could prevent parties-in-interest from meaningfully participating in a case. For example, this practice deprives parties-in-interest of time to review the plan's provisions and object to, or challenge, the debtor's characterization of whether they are impaired and therefore allowed to vote.[15]

Prepackaged Plans in Subchapter V: An Uneasy Fit

Although § 1181 makes certain chapter 11 provisions inapplicable in subchapter V, § 1126 — which governs plan acceptance — still applies in subchapter V cases.[16] As a result, a subchapter V debtor is not prohibited from soliciting acceptances and rejections of a plan before filing if the debtor complies with all related requirements.[17]

However, some features of the SBRA already address many of the expediency concerns that make prepackaged plans attractive in chapter 11 cases. A prepackaged plan offers only marginal speed and cost advantages compared with the usual subchapter V process. These advantages carry the disadvantages of diminishing and distorting the subchapter V trustee's role and complicating the parties' right to examine and object to the debtor's eligibility for subchapter V.

Subchapter V Reduces Deadlines for Confirmation and Case Administration

First, the SBRA significantly reduces the time required to confirm a plan in subchapter V compared with a regular

14 *See, e.g., In re SunGard Availability Servs. Cap. Inc.*, Case No. 19-22915 (Bankr. S.D.N.Y. 2019); *In re Belk Inc.*, Case No. 21-30630 (Bankr. S.D. Tex. 2021).

15 *See, e.g.*, U.S. Trustee Objections in *In re Highpoint Res. Corp.*, Case No. 21-10565, ECF No. 48 (Bankr. D. Del. March 15, 2021); *In re Belk Inc.*, Case No. 21-30630, ECF No. 44 (Bankr. S.D. Tex. Feb. 23, 2021).

16 *See* 11 U.S.C. § 1181.

17 *See, e.g.*, 11 U.S.C. § 1126(b); Fed. R. Bankr. P. 3017.2, 2002.

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Subchapter V Filings

By Ed Flynn

Exhibit 1: Subchapter V Cases Filed by Day

Date	Day of Week	Cases Filed
June 17	Monday	16
June 18	Tuesday	16
June 19	Wednesday	9
June 20	Thursday	91
June 21	Friday	33
June 22	Saturday	0
June 23	Sunday	0

The debt ceiling for subchapter V fell from $7.5 million to just a little over $3 million on June 21 due to the expiration of the temporarily higher limit. This caused a huge spike in filings during the week. On June 20, there were 91 subchapter V cases filed. Surprisingly, another 33 cases were filed on June 21, indicating that there may be differing interpretations on exactly when the debt limit reverted back to the lower level. See Exhibit 1.

There were 165 cases filed during the week — more than double the number filed in any prior week, and about three times the normal weekly rate. See Exhibit 2.

The subchapter V debt ceiling last expired in March 2022. There was also a surge in filings just prior to that deadline, but it was much less severe than this year's surge (81 subchapter V cases were filed during the week of March 21-27, 2022).

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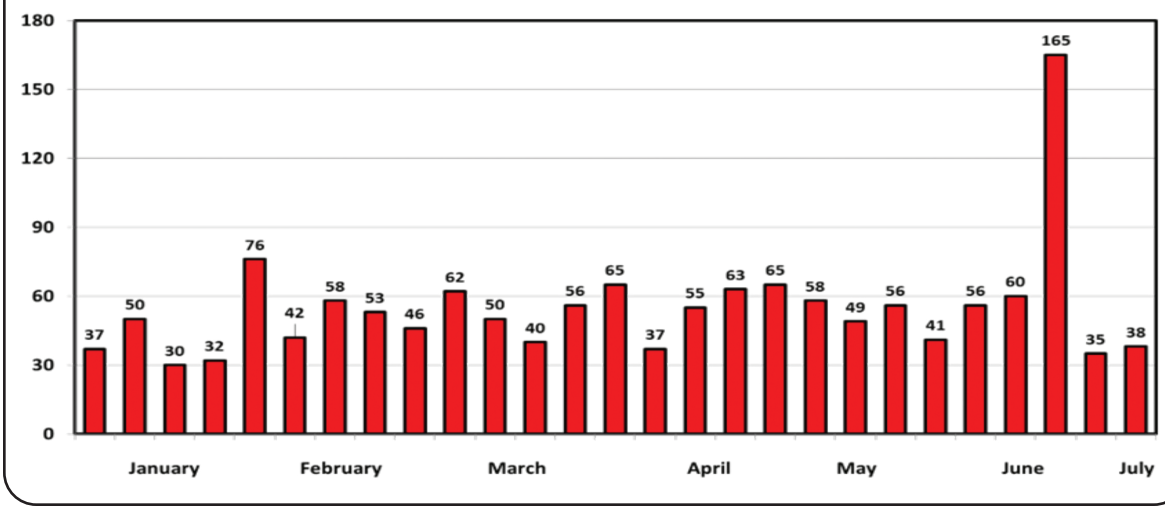
Exhibit 2: Subchapter V Cases Filed by Week (January to July 2024)



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chapter 11. Most notably, unless ordered otherwise, a subchapter V debtor need not file and receive approval for a disclosure statement before it solicits plan acceptances.[18] Instead, immediately after a plan is filed, Bankruptcy Rule 3017.2 allows the court to set confirmation deadlines, subject to Bankruptcy Rule 2002's requirement that parties-in-interest be given at least 28 days of notice of the time fixed for filing plan objections and for the hearing on confirmation.[19]

Furthermore, although § 1189 requires that a subchapter V debtor file a plan within 90 days, there is no bar against the debtor doing so earlier.[20] Similarly, although § 1188 requires a status conference within 60 days after the petition date except in limited circumstances,[21] courts have regularly held them early in the case. Since committees of unsecured creditors are not typically appointed in subchapter V cases — unless a court orders otherwise, for cause[22] — there is typically no delay associated with committee formation.

Accordingly, a subchapter V debtor filing a prepackaged plan that complies with the notice and objection timelines in the Code and Rules would be unlikely to confirm a plan substantially quicker than a debtor filing and soliciting a plan shortly after the petition date. Although a debtor might reach confirmation marginally faster by seeking court approval for shortened timelines, those requests raise significant due process concerns.

Conflict with Eligibility Determinations

Second, a prepackaged subchapter V would impair the ability of parties-in-interest to examine and contest the debtor's eligibility for subchapter V.[23] Since the benefits to subchapter V debtors are so significant, Congress prescribed clear limits governing what debtors may elect subchapter V,[24] which prevents debtors outside those limits from taking advantage of the new subchapter.[25]

Bankruptcy Rule 1020 allows all parties-in-interest 30 days after the conclusion of the meeting of creditors (or the amendment of a debtor's designation statement, whichever is later) to object to a debtor's subchapter V designation.[26] Neither the Code nor the Rules provide a court any ability to waive a party's right to object to a subchapter V designation, but scheduling a subchapter V debtor's confirmation hearing before the 30-day deadline would functionally eliminate parties' rights to object to the designation within the time prescribed, thereby frustrating the statute's careful limitations on eligibility.

Diminishing and Distorting the Subchapter V Trustee's Role

Finally, a prepackaged process in subchapter V diminishes and potentially distorts the appropriate role of the subchapter V trustee. To take advantage of a subchapter V trustee's services in a prepackaged case, some have suggested that the USTP could "designate" a future subchapter V trustee in advance of a case filing.[27] The future trustee could then participate in the pre-petition plan-development process and presumably help garner pre-petition support from creditors. This is a nonstarter.

The USTP cannot lawfully authorize a person to engage in trustee duties before their appointment in an actual case.[28] Even if the USTP had that authority, subchapter V trustees are currently appointed case by case on the condition that they are disinterested.[29] There would be significant practical difficulties in determining disinterestedness before a debtor files disclosures made under penalty of perjury with a court. Furthermore, only an appointed subchapter V trustee, not a trustee-designate, is entitled to compensation for their services under § 330.[30]

Since a subchapter V trustee cannot take part in plan development pre-petition, a prepackaged plan effectively renders moot the trustee's most important statutory duty: the responsibility to "facilitate the development of a consensual plan of reorganization."[31] Practical experience shows that as intended by the SBRA, the subchapter V trustee regularly plays a critical role in assisting debtors with financial and business analysis and helping parties with entrenched disagreements come to consensus on a reorganization plan.[32]

Even worse than stripping subchapter V trustees of their central duty, a prepackaged plan process would threaten to distort the limited role left for trustees, bending it to improper purposes. The mere presence of a subchapter V trustee in a prepackaged case might be taken as a guarantee of neutral oversight, when in fact the trustee had no influence at all on the plan process. Even more significant is that trustees may find themselves drawn into cajoling and herding reluctant creditors into supporting the prearranged plan presented to them as a *fait accompli* — a role at odds with their duty to foster truly consensual plans.

Subchapter V Prepackaged Cases Present Heightened Due-Process Concerns

In addition to clashing with a prepackaged case strategy, subchapter V magnifies the due-process concerns inherent in any attempt to shorten the 28-day period to object to confir-

18 Although the court may for cause order a subchapter V debtor to file a disclosure statement under § 1181(b), this has rarely occurred in practice.
19 Fed. R. Bankr. P. 3017.2, 2002(b).
20 *See* 11 U.S.C. § 1189. Section 1121(a), which specifically authorizes a debtor to file a plan with a petition commencing a voluntary case, is not applicable in subchapter V (*see* 11 U.S.C. § 1181(a)), but there is no prohibition against the debtor doing so.
21 11 U.S.C. § 1188.
22 11 U.S.C. § 1181(b).
23 11 U.S.C. § 1182; Fed. R. Bankr. P. 1020.
24 11 U.S.C. §§ 1182(1), 101(51D).
25 *See* H.R. Rep. No. 116-171 at 1, 4 (2019).
26 Fed. R. Bankr. P. 1020(b).
27 *See* Hampson & Katz, *supra* n.4 at 45, 53.
28 The existence of a "case" is the precondition for the USTP's appointment authority. *See* 11 U.S.C. § 1183(a).
29 *Handbook for Small Business Chapter 11 Subchapter V Trustees*, Dep't of Justice Exec. Office for U.S. Trustees, *available at* justice.gov/ust/file/subchapterv_trustee_handbook.pdf/dl; *see also* 11 U.S.C. § 1183(a).
30 *See* 11 U.S.C. § 330(a).
31 *See* 11 U.S.C. § 1183(b)(7).
32 *See* Final Report of ABI's Subchapter V Task Force at 22-24 (2024), *available at* subvtaskforce.abi.org.

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mation. Because a subchapter V debtor can secure plan confirmation under § 1191(b) without a single creditor voting in favor of the plan,[33] a creditor's ability to object to confirmation might be its only practical means to protect its interests in a subchapter V case.

Moreover, creditors in a subchapter V case might be more unsophisticated and unfamiliar with bankruptcy than those in a traditional chapter 11 prepackaged case. Thus, any limitations on a creditor's time to object to and participate fully in subchapter V case confirmation must be subject to rigorous scrutiny.

Similarly, requests to waive the meeting of creditors deserve particular attention in subchapter V. Section 341(e) enables a court to order — for cause — that the USTP not convene a meeting of creditors if the debtor solicited acceptances for a plan pre-petition.[34] Since subchapter V cases involve small businesses whose circumstances are often relatively unknown, the meeting of creditors is a crucial opportunity for creditors to learn about a debtor's operations and finances, its plan to emerge from bankruptcy, and the facts concerning its eligibility for subchapter V.

33 11 U.S.C. § 1191(b).
34 11 U.S.C. § 341(e).

Conclusion

Subchapter V provides a streamlined bankruptcy process for certain small business debtors. In almost all cases, the expedited time frames already built into the process eliminate the need for the extremely shortened deadlines often featured in prepackaged cases. As a result, the USTP will generally advocate for an exceptionally strong showing of cause for any attempt to shorten the 28-day period to object to plan confirmation or to impair a creditor's ability to object to a debtor's subchapter V eligibility.

Similarly, the USTP will generally oppose attempts to waive the meeting of creditors in a subchapter V case absent extraordinary circumstances. The USTP will continue to monitor all subchapter V cases to ensure that subchapter V continues to work for all stakeholders in the bankruptcy system. abi