# What Is a Subchapter V Bankruptcy and How Does It Differ From a Traditional Chapter 11 Bankruptcy?

Subchapter V is a subchapter of Chapter 11 of the Bankruptcy Code and is intended to be a streamlined, cost-effective path to reorganization for small businesses. However, Subchapter V cases lack some creditor protections that are hallmarks of traditional Chapter 11 cases, thereby putting creditors at a potential disadvantage.

## Key Issues

- **Eligibility.** Only small business debtors can file a Subchapter V case. To qualify, a debtor must have no more than $3,024,725 in aggregate, noncontingent, liquidated secured and unsecured debts, and 50% of such debts must come from commercial or business activities. The debts of affiliates do not count toward this limit, nor do contingent or unliquidated debts (although courts are not always clear on what qualifies as contingent or unliquidated debts for eligibility purposes). The debt threshold was increased in 2020 under the CARES Act to $7.5 million in the aggregate, but the increased debt limit expired in June 2024, drastically decreasing the number of debtors that can qualify for Subchapter V.
- **No Creditors' Committee.** Unless specifically ordered by the court, there is no creditors' committee appointed in a Subchapter V case. On one hand, this significantly reduces the cost of a Subchapter V case versus a traditional Chapter 11 case. No estate funds are used to pay committee professional fees, thereby preserving funds to pay creditors. However, a creditors' committee is an important protection for unsecured creditors who, standing on their own, may not have much leverage to influence the outcome of a case to best serve their interests. A Subchapter V trustee is appointed in every case to ensure the debtor remains on track, overseeing the debtor's progress, monitoring its financial condition, and assisting parties in negotiating in the case. While useful, this is a far cry from a committee solely dedicated to the interests of unsecured creditors.
- **No Disclosure Statement.** Unlike a traditional Chapter 11 case, the debtor is not required to file a disclosure statement. The idea behind this is to save the debtor the time and

expense of having to prepare a disclosure statement. For creditors, however, it means less information about the debtor and its case.

- **Plan Exclusivity.** Unlike a traditional Chapter 11 case where creditors are permitted at the conclusion of the exclusivity period to file a plan, only a debtor may propose a plan in Subchapter V. This eliminates an important creditor rights tool, whereby creditors can propose a plan that is more attractive than the debtor's plan and obtain confirmation of such plan despite the objection of the debtor. Moreover, Subchapter V requires that the debtor file its bankruptcy plan within 90 days of the petition. While this expedited timeline is designed to keep Subchapter V cases brief (and less costly), it also puts time pressure on creditors or other interested parties to negotiate the terms of a proposed plan.

- **No Absolute Priority Rule and No Voting on Plan.** In a traditional Chapter 11 case, all unsecured creditors must be paid in full before equity interests receive anything under a plan. This precept, called the Absolute Priority Rule, does not apply in Subchapter V. A Subchapter V plan can provide for equity holders in the debtor to retain their interest in the business as long as the plan is fair and equitable (see discussion below) without the need to infuse new value into the company, even while unsecured creditors are not fully paid on their claims. Another major difference between a traditional Chapter 11 case and Subchapter V is that there is no voting on the plan. This means that the process for a debtor to confirm its plan is the same whether a creditor consents or objects to the plan. The lack of the Absolute Priority Rule, combined with the ability to confirm a plan without creditor consent, acts to strip creditors of leverage in a Subchapter V case.

- **Nonconsensual Plans.** In a traditional Chapter 11 case, to confirm a plan, at least one impaired class of creditors must vote in favor of the plan. A Subchapter V plan can be confirmed without creditor consent as long as the plan is "fair and equitable." A plan is fair and equitable if it either provides that all of the debtor's projected disposable income for the first three to five years of the plan (as set by the court) is applied to make payments to creditors under the plan *or* the value of property distributed under the plan for the first three to five years is not less than the projected disposable income.

## Takeaway

Subchapter V cases are fast-moving and, while efficient, remove some of the standard creditor protections of a traditional Chapter 11 case. Experienced bankruptcy counsel can help a creditor navigate a Subchapter V case and take the right steps to protect its interests.