

REPRESENTING THE REALLY SMALL BUSINESS DEBTOR

by Thomas J. Raftery

1. **Identifying the client. Who is the client? Identifying conflicts.**

Invariably the person on the other end of the telephone says, “My business is suffering and I need to see you right away. My neighbor (accountant, rabbi, priest, baker, butcher or candlestick maker) told me I need to file chapter 11.”

“Come on down,” you reply.

As the story unfolds you note that the person telling the story often is unable to clearly articulate the structure of the business. Is it a corporation, an LLC or a proprietorship?

“My partner and I,” he starts out leaving you with the impression that the debtor might be a partnership, but then again small business owners who work with other principals often refer to their counterparts as partners even though the business is owned and operated by a corporation.

A good number of small businesses are proprietorships which eases the conflict between principals and the business, but when the business entity is a corporate entity such as an limited liability company the conflict between representing the corporate entity and the principal arises. See *Closely Held Conflicts* by John W. Marshall, Assistant Bar Counsel, Massachusetts Board of Bar Overseers at http://www.mass.gov/obcbbo/closely_held.htm

It is then that you are compelled to explain the intricacies of preferences, fraudulent transfers and fiduciary duties to creditors in a chapter 11 case. You might also explain the swelling, but yet to burst theory of fiduciary obligations of officers and directors of insolvent companies.

2. **Identifying the assets and the guarantors and their assets.**

Who owns what is a huge concern in a small business. Often a principal will buy a substantial piece of machinery in his own name or perhaps that of a relative. When you start to make up a list of the assets, you find out that the machinery is not owned by the debtor, but rather by a related entity who may or may not be friendly.

Small business principals guaranty things more often than they should. Not only do they guaranty things, they tend to pledge their own assets in order to raise

capital especially when the business is suffering. And all too often, by the time they come to see you their personal assets are exhausted by mortgages, pledges and security interests. Nevertheless since a small business principal may have to be his or her own source of new capital, you have to ascertain if they are capable of obtaining capital when and if it is needed.

It is not unusual to find that guarantors do not understand the guaranties that they signed. They fail to realize that the guaranty is often a primary obligation and that the lender can make a claim against the guarantor without resort to the business in the first instance. Moreover, they also tend to ignore the language in the guaranty that prohibits subrogation until the lender is paid in full. They tend to give you that deer in the headlights look when it is explained.

3. **Structural problems.**

It probably goes without saying that some small business principals tend to ignore the corporate structure. They will take money from the till to meet personal obligations and put money in without record as the company needs it. They probably have not had an annual directors or stockholders meeting since the inception of the entity. They easily lend themselves to claims of alter ego and piercing the corporate veil. So among the first questions are whether all corporate formalities have been properly observed and the corporation was not used to promote fraud. See **My Bread Baking Co. v Cumberland Farms, Inc.**, 353 Mass. 614, 620 (1968); **Pepsi-Cola Metropolitan Bottling Co. v. Checkers, Inc.**, 754 F.2d 10, 14-16 (1st Cir. 1985).

Another structural problem is bookkeeping and accounting functions. Who is doing them? Many small businesses will use QuickBooks, but without an understanding of how the software works. Moreover many small business principals will try to do the accounting and bookkeeping functions by themselves in order to save the expense. Sometimes there is a separate bookkeeper, but only working part time. That means that you cannot get financial information quickly at times when you really need it.

4. **Identifying the immediate problems.**

Sometimes the obvious problems are not the real problems. Secured lenders may huff and puff, but unless they have actually moved to take possession of their collateral the relationship is usually manageable. Unpaid withholding and sale taxes usually take several months before the tax authorities realize there are problems. Aggressive unsecured creditors usually can be managed before the litigation stage. As you delve into the business problems, you may discover that the debtor is unable to purchase supplies on credit, may be failing to deliver its

product to its customers. You might also discover that assets in the perceived “partnership” seem to vanish.

War story: the corporate debtor’s principals met with us to discuss the possibility of a chapter 11 case. They related that business was down as a result of the economy at the time and their inventory costs had skyrocketed. They were unable to keep the business going if they had to pay for their sizeable onsite inventory. We filed a chapter 11 petition and our goal was to reduce the existing inventory cost and continue the business going forward. Yet something was wrong. Our monthly operating reports showed little improvement in the business. We and the accountant had anticipated a better performance. We kept harassing the accountant to identify the problem, but he was having difficulty in doing so. At the point when we were fretting about a plan or liquidation, one of the “partners” died.¹ Suddenly the monthly profit improved. We suggested that we might find another accountant whereupon he “discovered” that the recently deceased had a cocaine habit and was selling product off the shipping platform to support his habit. Sometimes the not-so-obvious problem is the one that is killing the business.

5. Determining operating cash requirements and availability.

Projecting the present and the future is not always easy with the small business debtor. Some business people believe that so long as there is cash coming in the door, then there is a profit being made. They often fail to realize that the cash going out is flowing out at a faster rate than it is coming in.

An active accountant or bookkeeper with the ability to create a cash flow projection is essential. Some debtors resist employing additional help, but the number of debtors who have never seen a weekly or monthly cash flow report is alarming. Many debtors never see a monthly report until they have to prepare the monthly operating report for the U.S. trustee.

War story: The debtor operated a cash business. The principal was in his early 70's and had never had a problem until the period prior to meeting us. He believed that he was profitable, but even though cash was pouring in the door, the bills kept building up and he was unable to reason why. He fired his accountant when the accountant told him why he was operating at a loss. He fired the next accountant and a financial advisor for the same reason. The fourth person to appear on scene was years ahead of the casual approach to dressing at the office. The new accountant wore plaid shirts, jeans and suspenders and sported a big red beard; he reminded us of a mountain man who would just as soon be trapping beavers as he

¹ Suffice it to say that he died happy.

would rendering accounting services. Yet the debtor's principal loved him and when our mountain man demonstrated to the debtor where the money was being lost, the debtor believed him. It turned out that one line of business that the debtor had recently started was subsidized by the government. As it turned out, the government subsidy was inadequate to meet all the costs associated with the line of business. The mountain man had taken each aspect of the entire business apart and turned each into its own profit and loss center. When the subsidized business was analyzed independent of the other profit and loss centers it was evident that it was the drain on the entire business. When the subsidized line was terminated, the overall business became profitable once again. The moral of the story is that small business sometimes fail to identify the source of their problems.

6. Identifying preferences and fraudulent transfers.

Prevalent amongst small businesses are preferences and fraudulent transfers. It is not uncommon for a debtor to have borrowed money from Mommy Dearest who has mortgaged her residence to lend the money to the debtor for use in the business. The usual situation is that the mother does not take a security interest in the business, but the business is paying her either monthly or in large bites from time to time. We are all aware that those payments are preferential, but the debtor has no clue about the problem until the meeting with you. Many a potential preference claim against mother has kept a debtor out of bankruptcy.

When time are tough, the tough transfer their assets. And they run afoul of the fraudulent transfer laws. Sometimes the transfer is simply a conveyance of the marital home to a spouse. If done within four years while the debtor is insolvent or rendered insolvent, then the transfer is likely fraudulent. The common refrain is "I did it for estate planning purposes." But that usually does not hold water. Many people including attorneys who should know better often recommend transfer to a nominee trust where the debtor as beneficiary retains control as to the disposition of the assets transferred. Although some disagree, most courts have held that transfer to a nominee trust does little to separate the debtor from having all the benefits of ownership of the asset. So even if a transfer to a trust is outside the 4 year statute of limitations for a fraudulent transfer, the use of a nominee trust should be avoided to protect assets.

If the debtor is a proprietor, you must be aware that in the period ten (10) years prior to the filing of the petition any transfers by the debtor may reduce the individual debtor's homestead exemption. See 11 USC § 522(o)².

² (o) For purposes of subsection (b)(3)(A), and notwithstanding subsection (a), the value of an interest in—
(1) real or personal property that the debtor or a dependent of the debtor uses as a residence;
(2) a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence;

7. Identifying secured creditors and their priority.

Who's on first? Yes. Ask a small business debtor which creditors have security interests and in what order, you are likely to get a blank stare. Some have no clue exactly what they signed when obtaining credit from banks or creditors. You have to perform a UCC lien search. In Massachusetts the search is fairly easy because the financing statements are online, but in other states you may have to spend the money to have it done. It is absolutely essential to have a lien search completed. It is not unusual for a secured creditor to use the debtor's trade name rather than the name of the entity itself. For example, a purveyor of sundries that uses the name of the restaurant as the debtor name on the financing statement rather than the name of the actual corporate entity has not perfected its security interest and in the bankruptcy becomes a secured creditor. It is not unusual to find that less sophisticated secured creditors allow their financing statements to lapse. Finally it is still not unusual to find that some secured creditors believe that all they need to become a secured creditor is the filing of a financing statement ignoring completely the requirement of an executed security agreement.

Be aware that the Bankruptcy Code no longer suspends the obligation of a secured creditor to maintain the filing of continuation statements. But what happens if the secured creditor fails to maintain its perfection during the course of the chapter 11 case? One bankruptcy court held that General Electric Capital Corporation retained its priority despite allowing its financing statements to lapse. However, that decision appeared to be based on the provisions of the confirmed plan which established the relative priorities in the case. See **In re Dial Bus. Forms, Inc.**, 273 B.R. 594 (Bankr. W.D. Mo. 2002). The Eighth Circuit Bankruptcy Appellate Panel (the "BAP") affirmed, applying a somewhat different analysis. **In re Dial Bus. Forms, Inc.**, 283 B.R. 537 (B.A.P. 8th Cir. 2002). The Eighth Circuit affirmed the lower courts. **In re Dial Bus. Forms, Inc.**, 341 F.3d 738 (8th Cir. 2003), 2003 U.S. App. LEXIS 18161, 51 U.C.C. Rep. Serv. 2d (Callaghan) 815; Bankr. L. Rep. (CCH) P78,910.

8. Determining liquidation value.

Small business debtors usually fall into two camps: (1) "my stuff is worth nothing" or (2) "my stuff is irreplaceable." One of the best friends you can have is an auctioneer. Get a list of the debtor's equipment and call your friend. He can

(3) a burial plot for the debtor or a dependent of the debtor; or

(4) real or personal property that the debtor or a dependent of the debtor claims as a homestead, shall be reduced to the extent that such value is attributable to any portion of any property that the debtor disposed of in the 10-year period ending on the date of the filing of the petition with the intent to hinder, delay, or defraud a creditor and that the debtor could not exempt, or that portion that the debtor could not exempt, under subsection (b), if on such date the debtor had held the property so disposed of.

give you a rough idea of the value of the debtor's equipment. In one case the debtor told us that his showroom inventory was worth around \$200,000. The auctioneer told us that he just had an auction of similar items where the best he could do was around \$25,000. An orderly sale of the inventory might have brought a better price than the auction, but nowhere near what the debtor thought the inventory is worth.

Intellectual property is far harder to value. The debtor may have plans for a new product which the debtor believes are invaluable, but to date he has not exploited the plans. Where there is no market for the plans or product, it is nearly impossible to determine a value.

War story: In one case where we represented a trustee in bankruptcy despite a worldwide notice to solicit offers we were unable to find any buyers for certain patents held by the debtor. Certain parties claimed that the patents had significant value, but they were unwilling to bid for them. Since this was pre-eBay, we sent out notice to the world (actually over 2,000 notices to companies in the same or similar industries to the debtor) that we would conduct an auction in the bankruptcy court. We received five offers accepting the highest of course. As the sale was being hammered down by the bankruptcy judge, one of the parties claimed the price was too low, but he could offer no evidence of why and the sale was consummated.

eBay and other auction sites make it easier to ascertain values today and the bankruptcy courts routinely authorize use of internet auction sites to sell assets of the bankruptcy estate. It is a good indicator of value today.

9. Determining the proper path: Chapter 7, Chapter 11, Assignment for the Benefit of Creditors, Trust Mortgage, Plan of Composition or simply closing the doors.

Chapter 11 is not the only answer. When liquidation is the likely course, then an assignment for the benefit of creditors may be the answer. It offers a usually quicker and less expensive method for liquidating the assets of a debtor and distributing the proceeds to creditors.

Plans of composition are rarely used today primarily because a creditor's participation is voluntary and a few recalcitrant creditors can upset the apple cart, but from time to time they do work.

Some debtors will simply walk away from the business. They might hand the keys to the bank or the landlord, but they stop doing business and await the onslaught of the creditors.

10. Identifying the professionals: turnaround consultants, needed or affordable?

Clearly the legal and accounting functions have to be had in any business insolvency situation, but are turnaround consultants needed? Most small businesses cannot afford a financial advisor or a turnaround consultant, but sometimes they can be valuable in providing a vetting process for the debtor's assumptions and business plans. In addition to the vetting process, turnaround consultants can also repair credibility problems that the small business principal has with creditors and suppliers.

In addition to adding a veneer of credibility, a financial advisor must be able to quickly assess the internal and external issues facing the company, the debtor's plans to address the issues with available resources and the ability to stabilize the company until a restructuring strategy can be developed and implemented.

A financial advisor advising a company in a distressed financial situation needs to be aware of the available options from a simple trust mortgage in favor of creditors to the fully formal process of a bankruptcy proceeding. Moreover the financial advisor should be generally aware of the advantages and disadvantages of each option. While you can fill in the legal details of each, the financial advisor can be the person who draws the roadmap to financial success in the rehabilitation of the business. Sometimes the only road may be a dead end and lead to liquidation, but the financial advisor has to explore all the options in the hope of avoiding such a drastic conclusion. The financial advisor is akin to the team coach: the small business principal is going to look to the financial advisor to guide it to success.

11. Restarting the business: identifying capital needs and sources.

If fresh capital is recommended it can come from a variety of sources. Debtors who did not tap their home equity, can attempt to borrow against it (although this has to be a thoroughly analyzed and reasoned decision). Family members might be another source. There are a number of sources of capital in the marketplace who will lend to distressed businesses, but their interest rates tend to border on the exorbitant. Among the sources of capital are:

Personal funding. Personal assets are one of the first sources that a small business person may consider using when they decide to raise capital for their business, e.g., retirement accounts, real estate, vehicles and other personal assets.

Friends and family. Family members and friends can provide a means to raise capital. But borrowing money from friends and family may work both for and against the small business owner. Family members and friends may desire a large

stake in the business since they had lent money to it which can lead to resentment and relationship strains.

Venture capitalists. Small business owners might try to raise capital from angel investors and venture capitalists through equity financing. They tend not to look at very small businesses, but it is certainly an avenue to explore, especially if all traditional routes to raise capital have been exhausted.

Debt refinancing. Small business owners might also raise capital through debt refinancing. An advantage of debt refinancing as a way to raise capital is that the owner is able to retain maximum control over the business.

12. Communicating with the client: email, fax, telephone, mail.

Sometimes one of the most difficult tasks in a small business matter is contacting the principal. The cell phone has become ubiquitous and everyone should have an email account, but some debtors manage to find ways to disappear. In certain situations the debtor may simply have too much on his or her mind to focus on tasks that you may think are important, but which are outside the debtor's business realm, e.g., monthly operating reports. One debtor we represented had ADD; whenever we asked for something we had to make the request by fax, email and telephone or else he would simply forget it.

Another aspect of communicating with the client is to let the client know why you do not consider an alternative approach to a problem. If you believe that a chapter 11 case will not work, tell the client why. Small business people may do what we consider to be dumb things from time to time, but on the whole they are not stupid. If you recommend against a course of action, tell them why.

13. Educating the small business client.

Education is the key to success. Sound familiar? If you determine that a chapter 11 case is the appropriate course and your client understands why, then you have an obligation to explain to the client the players and the process. Tell them about the U.S. trustee, the role of the court and the bankruptcy judge and other players in the case. We have seen small business debtors believe that the analyst from the U.S. trustee's office was their appointed trustee in the case and that the examiner at the first meeting of creditors was the judge. It is your job to disabuse the small business debtor of those notions. Provide a list of the players in the case. Following this outline is a list of common terms and players that a debtor may encounter in a chapter 11 case.

14. Obtaining accurate information from the small business client.

You need a basic understanding of accounting and you should know how to prepare a spreadsheet. When a client prepares any financial report you cannot accept it on face value; you have to delve into it to see how it works. It is not unusual to find a spreadsheet that at first blush shows a projection of profit only to discover on examination that a value was added rather than deducted rendering a profitable projection one of loss projection.

It is not unusual to have a small business debtors provide financial data that is based upon history and not reflect current conditions. It may well be that the debtor simply does not account for current conditions. In one case we had the debtor based its income on the number accounts it had and what it believed to be average billings. It was only when it was forced to reconcile its cash account with each customer payment did it realize that its incoming cash flow was far less than the average billing number stated.

Vetting the small business debtor's financial data is crucial. The better you understand the numbers, the better you will be about obtaining accurate data.

15. Directing client focus to priority items, e.g., the MOR, the Plan.

This is also an education issue. The debtor must know the importance of the monthly operating reports and the eventual need for a plan of reorganization. With respect to the MOR's, you have to insist that they be timely even if it means that you call the debtor on the hour each hour. Good cases have been lost for want of the filing of the MOR's and the court is not going to tolerate a debtor that cannot complete the simple reports applicable to small business debtors. Every time you speak to a debtor you should make a reference to progress toward a plan and the completion of the MOR's.

16. Principal relationships with family and third party lovers.

You have to understand what is going on in the small business principal's environment that might affect his or her ability to cope with the matters at hand. Is a divorce imminent? Are there health issues? Like it or not you are likely to wind up as your client's new friend and confidant. You have to understand the problems and must focus the client's energies on the salvation of the business. The rest can come later.

All too often you will discover that spouses and relatives are on the payroll of the small business and may be receiving perquisites such as a company vehicle, but without really working at the business. While the U.S. trustee will ask questions

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in that area, you have to anticipate them and be prepared to inform the small business debtor that the spouse who does no work at the business, but drives the company Escalade and receives a salary is in for a shock. There is nothing wrong with family members working for a business, but they have to contribute at least equal to their compensation.

Clients with substance abuse problems present a particular problem. Communications with a client who is under the influence of drugs or alcohol may seriously impair the client's ability to understand a recommendation or a request. It is a dilemma for counsel, but there are options. For a discussion of the issue see *The Lawyer as Counselor Representing the Impaired Client* By Timothy David Edwards, GPSolo Magazine - October/November 2004 or <http://tinyurl.com/qkz8ow>.

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The following are short descriptions of terms that the debtor may run into in a bankruptcy case:

Abandonment	A disclaimer of any interest by the trustee or debtor in burdensome or inconsequential property. Once property has been “abandoned,” it is no longer property of the estate, and parties with a security interest in the property may proceed against it.
Abstention	A Bankruptcy Court may abstain from hearing a particular civil proceeding on the finding that it is in the interest of justice or in the interest of comity with state courts or state law. A Bankruptcy Court must abstain from a hearing involving a non-core proceeding based on a cause created by state law, where such cause is actually pending and can be timely adjudicated in a forum of appropriate jurisdiction. The Bankruptcy Court may abstain from hearing an entire bankruptcy case on the finding that the interest of both creditors and the debtor will be served by dismissal of the petition.
Administrative Expense Claim	A priority claim including the cost and expenses of preserving the estate or operating the business after the petition, and all professional fees and charges that are allowed.
Adversary Proceeding	A lawsuit within a bankruptcy case. It is usually started with the filing of a complaint and the Bankruptcy Court Clerk will assign it a separate docket number.
Automatic Stay	The filing under any chapter of the Bankruptcy Code automatically operates as a stay against the commencement or continuation of most judicial, administrative or other proceedings against the debtor or the debtor’s estate. The purpose of the stay is to give the debtor “breathing time” for rehabilitation. The law provides a number of exceptions to this general rule. A party seeking relief from the automatic stay must file a motion to lift stay. This is also the most contested portion of a Chapter 11 case. See the discussion below.
Avoidance Power	The Bankruptcy Code grants the trustee the power to avoid certain transactions or transfers occurring before the commencement of the case, including preferences and fraudulent conveyances.
Bankrupt	A term formerly used under the Bankruptcy Act to describe a debtor who had been adjudicated a bankrupt under the Bankruptcy Act. This term is not used in the Bankruptcy Code.

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Bankruptcy Code (“The Code”)	Legislation found at 11 U.S.C. §101 et. seq. (“Title 11”) containing both substantive and procedural law for bankruptcy liquidation and rehabilitation cases. The Code has been amended several times since its passage in 1978.
Bankruptcy Court Clerk	The Clerk at the Bankruptcy Court receives all documents that are placed in the court record in a bankruptcy case. In addition, the Clerk’s office schedules hearings for the bankruptcy judges, usually upon written request by an attorney.
Bankruptcy Judge	The role of the Bankruptcy Judge is to preside over the administration of a bankruptcy case, and to decide contested aspects of that case, which involve either the liquidation or reorganization of a debtor. A Bankruptcy Judge does not become actively involved in the daily administration of the bankruptcy case, as that task has been delegated to the debtor, U.S. Trustee, appointed trustees, examiners and creditors’ committees.
Cash Collateral	Cash, negotiable instruments, documents of title, securities, deposit accounts or other cash equivalents in which the debtor’s estate and an entity other than the estate have an interest. Cash collateral may not be used, sold or leased in the ordinary course of business unless the creditor with an interest in the collateral consents or the court, after notice and a hearing, authorizes the transaction.
Civil Proceeding	Any action that occurs within a bankruptcy case and includes contested matters, adversary proceedings and plenary actions, as well as disputes related to administrative matters in a bankruptcy case.
Claim	Any right to payment, as well as any right to an equitable remedy for breach of performance if that breach also gives right to payment.
Confirmation	The process by which the Bankruptcy Judge approves a plan of reorganization of a debtor.
Core Matters	Proceedings arising under Title 11 or arising in a case under Title 11 in which the Bankruptcy Judge may conduct the entire proceeding and may enter the final and dispositive order or judgment.

Cramdown	One of two methods by which a debtor can confirm its Chapter 11 plan. Creditors may consent to the debtor’s plan, or the debtor may “cram down” a plan over the objections of creditors where at least one class of impaired claims or interests have voted in the requisite number and amount to accept the plan, and certain other requirements are met with respect to all non-consenting impaired classes or claims or interests.
Debtor-in- Possession	A Chapter 11 or Chapter 12 debtor that operates its own business and remains in possession of its assets and property. For purposes of the Code, a debtor-in-possession has substantially all the rights and powers of a trustee. The Bankruptcy Judge may order that the debtor-in-possession be replaced by a trustee appointed by the U.S. Trustee.
Discharge	An order that bars the debtor’s in personam liability on claims within its scope, and acts as a permanent injunction against judicial proceedings or non-judicial collection efforts with respect to such claims.
Dischargeability	Refers to a process or finding on whether each individual debt is eligible for discharge.
Disclosure Statement	A pleading filed with the Bankruptcy Court Clerk and sent to creditors which contains information about the debtor and the Plan of Reorganization.
Estate	Created by the filing of a voluntary, joint or involuntary petition and consisting of all of the debtor’s legal and equitable interest in property as of the commencement of the case. An individual debtor is able to exempt certain property from the estate. Property of the estate also does not include (1) any power that a debtor can exercise for someone else’s benefit; and (2) traditional spendthrift trust interests required by state law. The estate is administered by a debtor, a debtor-in-possession or a trustee.
Examiner	An individual who may be appointed by the Bankruptcy Court with duties limited to conducting an investigation of specified acts and business affairs of the debtor-in-possession. The appointment of an examiner does not change the status of a debtor as a debtor-in-possession who remains in control of the property of the estate during the Chapter 11 bankruptcy case.

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Executory Contract	A contract under which the obligations of both the debtor and the other party are so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other. The Code grants the trustee the ability to assume, assign or reject executory contracts and unexpired leases for the benefit of the estate, subject to Bankruptcy Court approval.
Federal Rules of Bankruptcy Procedure	Provides the procedural law of bankruptcy. Besides the Federal Rules of Bankruptcy Procedure, each district as well as each individual Bankruptcy Judge may have its own local rules.
Fraudulent Conveyance	A transfer that can be avoided by the trustee if the transfer was made with (1) actual fraud evidenced by an intent to defraud, hinder or delay creditors; or (2) constructive fraud, evidenced by the debtor's receipt of less than reasonably equivalent value in exchange for the transfer.
Objection to Claim	The filing of an objection to a claim initiates a process that ultimately will result in the allowance or disallowance of that claim by the Bankruptcy Court.
Voluntary Petition	When a debtor voluntarily seeks relief under one of the chapters of the Bankruptcy Code. The filing of the petition operates automatically to invoke the stay.
Involuntary Petition	When creditors file a petition seeking to place the debtor in either Chapter 7 or 11. If the debtor contests and prevails, the court shall dismiss the involuntary petition. If the debtor does not contest, or contests and loses, the Bankruptcy Court shall enter an Order for Relief.
Plan of Reorganization	The document the debtor submits for confirmation to restructure and perhaps forgive certain pre-petition debt. The debtor proposes plans in Chapter 11, Chapter 12 and Chapter 13.

<p>Preference</p>	<p>A transfer of the debtor’s property to or for the benefit of a creditor, for or on account of an antecedent debt, made while the debtor was insolvent, within 90 days before bankruptcy (or within one year before the petition was filed in an “insider” situation), and the effect of which was to give the creditor more than he would have otherwise received in a Chapter 7 distribution. The trustee’s power to avoid preferences is designed to achieve the policy of fostering equality of distribution among the creditors of an insolvent debtor.</p>
<p>Priority Claim</p>	<p>Unsecured claims entitled to priority and distribution over other unsecured claims, including administrative expenses, claims arising in the ordinary course of the debtor’s business after the filing of an involuntary petition and before the entry of the Order for Relief; certain wage, salary or commission claims up to \$10,950 per claimant; certain contributions to employee benefit plan; certain claims of farmers and fishermen; certain consumer claims of up to \$5,400; and certain unsecured tax claims.</p>
<p>Property of the Estate</p>	<p>Includes real and personal property, tangible and intangible property, and property in which the debtor has an interest held by others. Property acquired after the petition generally is not property of the estate.</p>
<p>Proof of Claim</p>	<p>Document a creditor files, together with all supporting evidence of such claim, including documentation reflecting perfection of a security interest, if any. There is usually a deadline in which to file a Proof of Claim.</p>
<p>Reference</p>	<p>Device by which District Courts delegate bankruptcy jurisdiction to the Bankruptcy Court, and Bankruptcy Judges act as trial courts-in-fact in nearly all bankruptcy matters.</p>
<p>Related Matter</p>	<p>Proceeding related to cases under Title 11 in which, unless the parties consent otherwise, the Bankruptcy Judge submits proposed findings and conclusions and the District Court makes the dispositive Orders.</p>
<p>Removal</p>	<p>Process by which either the defendant or plaintiff may transfer a civil action in a non-bankruptcy forum involving the debtor to the District Court (and by the standing order of reference to the Bankruptcy Court).</p>

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Schedules	Pleadings filed with the Bankruptcy Court Clerk containing the assets and liabilities of a debtor.
Secured Claim	Claim by a creditor that has collateral of equal or greater value than the amount of the claim.
Statement of Affairs	Pleadings filed with the Bankruptcy Court Clerk containing information about the financial transactions and affairs of a debtor.
Trustee	The court-appointed representative of the estate who actually administers the estate. A Chapter 7 Trustee is in charge of liquidating the estate. In some Chapter 11 cases, the debtor-in-possession is replaced by a Chapter 11 Trustee who administers the estate. In Chapter 13, there ordinarily is at least one standing trustee in each district to whom all cases under Chapter 13 are assigned.
United States Trustee	Responsible for matters of administration of a bankruptcy case. Employed by the U.S. Department of Justice, the U.S. Trustee's responsibilities include (1) appointing from the private sector the members of a panel of trustees who administer bankruptcy cases; and (2) supervising the actions of the private trustees and the administration of all bankruptcy cases.
Unsecured Claim	Claim by a creditor that has no collateral to secure its claim or that has collateral of lesser value than the amount of the claim.
Withdrawal of Reference	District Court's power to withdraw in whole or in part matters that have been referred to the Bankruptcy Court, including both core and non-core proceedings as well as cases.

Small Business Debtors: BAPCPA and Other Relevant Code Provisions¹

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I. Eligibility – a comparison of debt limitations

A “**small business debtor**” is defined in 11 U.S.C. § 101 (51)(D) as a person engaged in commercial or business activities with aggregate noncontingent liquidated secured and unsecured debts of not more than \$2,190,000² (excluding affiliate/insider debts) for a case where unsecured creditors’ committee is not appointed, or if appointed, is not active.

An individual debtor “engaged in doing business” as that term is defined in 11 U.S.C. § 1304 is eligible to take advantage of the streamlined reorganization process offered by chapter 13 if that individual owes noncontingent, liquidated, unsecured debts of less than \$336,900 and noncontingent, liquidated secured debts of less than \$1,010,650³ pursuant to 11 U.S.C. § 109(e).

II. Pre-Filing Considerations

A. Automatic Stay:

11 U.S.C. § 362(n): The automatic stay does not automatically apply to a **small business debtor** who was either a debtor in a **small business case** that either was dismissed or had a plan confirmed in the two years before the petition date, or is a debtor that acquired substantially all of the assets or business of such a debtor. In order for the automatic stay to apply, such **small business debtor** must show, by a preponderance of the evidence, both that the filing of the petition resulted from circumstances beyond the debtor’s control not foreseeable at the time the case then pending was filed, and that it is more likely than not that the court will confirm a feasible plan (not a liquidating plan) within a reasonable amount of time. If the bankruptcy case was involuntary, the debtor can show that the filing did not involve collusion by the debtor with creditors, or if the debtor acquired

¹ This outline is not exhaustive, but rather intended to highlight the BAPCPA amendments impacting small business debtors, and the more relevant Code milestones to confirmation for “really” small business debtors. For practical considerations, see the companion article by Thomas J. Raftery with these panel materials. Also, for a comprehensive timeline for all individual chapter 11 debtors (including small business debtors and single asset real estate cases), see the timeline of Nina Parker with the Consumer Forum written materials, together with her acknowledgment at footnote 2.

² The debt limit is subject to adjustment every three years pursuant to 11 U.S.C. § 104(b).

³ These debt limits are likewise adjusted every three years pursuant to §104(b).

2009 Northeast Bankruptcy Conference

substantially all of the assets or business of a **small business debtor**, the debtor can show that the acquisition was in good faith.

B. Insurance:

11 U.S.C. § 1116(5): A **small business debtor** is required to maintain customary and appropriate insurance. Ensure proper coverage prior to filing.

C. Reclamation:

11 U.S.C. § 546(c): Vendors may reclaim goods received by an insolvent debtor within 45 days pre-petition if the seller makes a written reclamation demand within 45 days after the debtor receives the goods, or within 20 days post-petition if the 45-day period expires.

D. Venue:

28 U.S.C. § 1408: There is 180-day look-back period for venue purposes. Specifically, the debtor must have been domiciled, resided, had its principal place of business or its principal assets in the state it files its petition during this period. Alternatively, the debtor must have been domiciled, resided, had its principal place of business or its principal assets in such state for the longer portion of this 180 days than in any other state.

E. Exemption, Domicile, Discharge, and Misc. Issues for *Individual Doing Business as Small Business Debtor*:

Ten Years Pre-Petition

11 U.S.C. § 522(o): Beginning of look-back period for exemption limitation purposes. Specifically, the value of a debtor's interest in: (i) real or personal property used by the debtor or a dependent as a residence or claimed as a homestead, (ii) a cooperative that the debtor or a dependent uses as a residence, or (iii) a burial plot, is reduced to the extent that such value is attributable to any portion of any property that the debtor disposed of in the 10 year period pre-petition with the intent to hinder, delay or defraud a creditor and that the debtor could not exempt, or that portion that the debtor could not exempt if on such date the debtor had held the property so disposed of.

1,215 Days Pre-Petition

11 U.S.C. § 522(p): Beginning of look-back period for other, more general, homestead exemption purposes. The debtor cannot exempt any interest exceeding \$136,875.00 acquired in (i) real or personal property used as a residence or claimed as a homestead, (ii) a cooperative that owns the debtor's or dependent's residence or (iii) a burial plot or real or personal property claimed as a homestead,

unless the interest was transferred from a debtor's previous principal residence, acquired prior to the beginning of the 1,215 period, into the debtor's current principal residence, if both such residences are located in the same street.

730 Days Pre-Petition

11 U.S.C. § 522(b)(3)(A): Beginning of look-back period for domicile requirements. Specifically, an individual debtor must be domiciled in the state of filing during this period in order to claim exemptions under that state's law. If not, then the exemption laws of the state in which the debtor was domiciled during the 180 days immediately preceding the 730 day period, or for a longer period during those 180 days than anywhere else, applies.

One Year Pre-Petition

11 U.S.C. § 1141(d)(3)(C) and § 727(a)(2): Beginning of look-back period for discharge purposes. Specifically, if the debtor transferred or harmed an interest in property with the intent to hinder, defraud or delay a creditor during this period, then a discharge of the debtor's debt may be denied.

180 Days Preceding Petition Date

11 U.S.C. § 109(h): Period of time during which individual debtor must complete credit counseling.

6 Months Preceding Last Day of Month Prior to Month Petition is Filed

11 U.S.C. § 109(d) and § 707(b): Beginning of look-back period for means testing. Individual debtor's average monthly income during this period will be considered for purposes of determining current monthly, determining an individual's eligibility to file under Chapter 11. Note: Only applies if majority of debts are consumer debts.

F. Look-back Periods for Avoidance Actions

Four Years Pre-Petition

Mass. Gen. Laws. Ch. 109A § 10, and other UFTA state fraudulent transfer laws: Beginning of period during which an action to avoid a fraudulent transfer or obligation must be brought under Massachusetts law. Other states have different statutes of limitations regarding pre-petition fraudulent transfer avoidance actions.

Two Years Pre-Petition

11 U.S.C. § 548(a): Beginning of look-back period for fraudulent conveyances. Specifically, this is the period during which transfers of property can be avoided pursuant to subsection (1)(A) of this section if made by the debtor with the actual

2009 Northeast Bankruptcy Conference

intent to defraud, hinder, or delay creditors. Alternatively, transfers of property can be avoided pursuant to subsection (1)(B) if the debtor transferred such property or incurred such obligations in exchange for a less than reasonably equivalent value, if that the debtor (i) was insolvent at the time of the transfer or became insolvent due to the transfer, (ii) was engaged or about to be engaged in business and the transfer resulted in unreasonably small capital, (iii) intended or believed to incur debts beyond debtors' ability to repay or (iv) made such transfer for the benefit of an insider or incurred such obligation for the benefit of an insider under an employment contract outside the regular course of business.

One Year Pre-Petition

11 U.S.C. § 547(b): Beginning of preference period for transfers made by the debtor to insider creditors.

90 Days Pre-Petition

11 U.S.C. § 547(b): Beginning of preference period for transfers made by the debtor to non-insider creditors.

III. Petition Date and First Day Motions

28 U.S.C. § 1930(a)(b), Fed. R. Bankr. P. 1006(b), MLBR 1006-2(a): \$1,000 + \$39 filing fees due.

Fed. R. Bankr. P. 1020(a): Debtor must state whether it is a **small business debtor** in voluntary case.

11 U.S.C. § 1116(1): **Small business debtors** must file petition documents and either (i) a balance sheet, statement of operations, cash-flow statement and federal tax return, or (ii) a statement made under penalty of perjury that no such documents have been prepared and no taxes have been filed.

Fed. R. Bankr. P. 1007(a)(1) and (d): Debtor must file with the petition a list containing the name and address of each entity included or to be included on Schedules D, E, F, G and H, and a list of 20 largest unsecured creditors.

Fed. R. Bankr. P. 1007(b)(5): Debtor must file a statement of current monthly income.

Fed. R. Bankr. P. 1007(b)(7): Debtor must file a statement of completion of course concerning personal financial management in a case in which § 1141(d)(3) applies. (*d/b/a only*)

Fed. R. Bankr. P. 1007(b)(8): Debtor claiming exemption under § 522(b)(3)(A) must file a statement regarding proceedings in which the debtor may be found

guilty of a felony described in § 522(q)(1)(B) or liable of debt described in § 522(q)(1)(B). (*d/b/a only*)

Fed. R. Bankr. P. 1007(f): Debtor must file a statement of social security number. (*d/b/a only*)

11 U.S.C. § 363, § 364, § 366: First day motions regarding payment of prepetition wages, salaries and benefits; interim use of cash collateral; interim DIP financing; adequate assurance to utilities. Note: 11 U.S.C. § 503(c): Limits the court's ability and discretion to grant retention bonuses to so-called "key employee" and severance payments to insiders; section now provides a ceiling for any such bonus or severance and requires that any services must be essential to the survival of the business.

IV. Post-petition, Pre-Confirmation Case Activities and Deadlines

Two Days Following Order for Relief

Fed. R. Bankr. P. 1007(d): Debtor must file a list of 20 largest unsecured creditors in an involuntary case.

Seven Days Following Order for Relief

11 U.S.C. § 1116(l): Debtor in **small business involuntary case** must, by this date, either file (i) a balance sheet, statement of operations, cash flow statement and federal tax return or (ii) a statement made under penalty of perjury that no such documents have been prepared and no taxes have been filed..

15 Days Post-Petition

Fed. R. Bankr. P. 1007(c): Debtor must, by this date, file all schedules and statement of financial affairs.

15 Days Post-Petition/ Post-Order for Relief

Fed. R. Bankr. P. 1007(a)(3): Debtor must, by this date, file a list of equity security holders.

Fed. R. Bankr. P. 1007(f): Debtor in an involuntary case must, by this date, file a statement of social security number. (*d/b/a only*)

Fed. R. Bankr. P. 1020(a): Debtor must by this date file a statement indicating whether it is a **small business debtor** in an involuntary case.

Fed. R. Bankr. P. 2016(b): An attorney wishing to do so must, by this date, file a statement of attorney compensation as required by §329 of the Code.

2009 Northeast Bankruptcy Conference

20 Days Prior to § 105(d) Status Conference (to be held not more than 45 days Post-Petition)

MLBR 1002-1(b): Deadline for noticing of § 105(d) conference. Specifically, court or designated party to serve notice of conference on debtor, creditors' committee or list of creditors, equity security holders' committee, secured creditors, taxing authorities, US Trustee, any party who requested the conference, any party who has made an appearance and any other party as directed by the court. Other states may have similar noticing requirements. Note: 11 U.S.C. § 105(d): Bankruptcy judge shall hold status conference in chapter 11 case 'as are necessary to further the expeditious and economical resolution of the case.'

15 Days Prior to 341 Meeting of Creditors

Fed. R. Bankr. P. 4002(b)(4) and MLBR 4002-1(a): Creditor wishing to do so must, by this date, make written request for copy of debtor's federal tax return.

7 Days Prior to 341 Meeting of Creditors

Fed. R. Bankr. P. 4002(b)(4), MLBR 4002-1(a): Debtor must by this date respond to a creditor request of a copy of tax returns by either denying existence of such tax returns or opposing the request. Other states may have similar deadlines.

Fed. R. Bankr. P. 1007(b)(1), 4002(b)(2), MLBR 1007-1(c)(1): Debtor must by this date submit all documents required for § 341 meeting.

30 Days Post-Petition

11 U.S.C. § 1116(3): **Small business debtor** must by this date file all schedules and statement of financial affairs upon notice and hearing.

MLBR 1006-2(a): Fee installment payment due for individual debtor. *(d/b/a only)*

11 U.S.C. § 362(c)(3): An individual debtor with a prior case dismissed within one year of the filing must by this date file a motion and conclude hearing to extend the automatic stay. *(d/b/a only)*

11 U.S.C. § 362(c)(4): An individual debtor who has had two prior cases dismissed within one year must by this date request that the automatic stay will take effect. *(d/b/a only)*

Before § 341 Meeting of Creditors and Continuing Throughout Case

28 U.S.C. § 586(a)(7); 11 U.S.C. § 1116(2): A **small business debtor** is required to attend an initial interview with the US Trustee, to be held before § 341 meeting, for an evaluation of the debtor's viability, and inquiry about the debtor's

business plan and responsibility to file various reports. The debtor may also be required to attend other meetings with the U.S. Trustee or scheduled by the court.

11 U.S.C. § 308: A **small business debtor** is required to file periodic financial and other reports containing information including the debtor's profitability, reasonable approximations of the debtor's projected cash receipts and cash disbursements over a reasonable time period, comparisons of actual cash receipts and disbursements with projections in prior reports, and whether the debtor is both in compliance with post-petition requirements by the Code and Rules, and is also timely filing tax returns and other required government filings and paying taxes and other administrative expenses when due.

Approximately 30 Days Post-Petition

11 U.S.C. § 341: Meeting of creditors.

45 Days Post-Petition (or as soon thereafter as practicable)

MLBR 1002-1(a)(1): Deadline for court to hold initial status conference under 11 U.S.C. § 105 (d). Other states may have similar deadlines.

60 Days Post-Petition

MLBR 1006-2(a): Fee installment payment due for individual debtor. Other states may have similar fee deadlines. (*d/b/a only*)

11 U.S.C. § 108(b): Debtor must by this date file a pleading, demand, notice, proof of claim or loss, cure a default or perform any other such act required under nonbankruptcy law if the law fixes a time for such action, and it has expired post-petition.

60 Days Post-Petition/ Post-Order for Relief

11 U.S.C. § 365(d)(5): Debtor must from this date on, perform under an unexpired lease for personal property, other than personal property leased to an individual primarily for personal, family, or household purposes, until lease is assumed or rejected. A court, after notice and a hearing, and based on the equities, can order that the debtor is not required to so perform.

Approximately 60 Days Post-Petition (30 Days after 341 Meeting)

Fed. R. Bankr. P. 1020(b): Deadline for US Trustee or party in interest to object to designation as **small business case**.

2009 Northeast Bankruptcy Conference

Approximately 90 Days Post-Petition (60 Days after 341 Meeting)

MLBR 3002-1: Any party seeking administrative expense status for a claim must by this date to file a request for administrative expenses for goods delivered to debtor within 20 days prior to commencement of case and in the ordinary course of business. Other states may have similar fee deadlines.

90 Days Post-Petition (d/b/a only)

MLBR 1006-2(a): Final fee installment payment due for individual debtor. Other states may have similar fee deadlines.

120 Days Post-Order for Relief

11 U.S.C. § 365(d)(4)(A): Debtor must by this date either assume or reject an unexpired lease of nonresidential real property in which the debtor is the lessee, in the absence of prior confirmation of plan or an order of the court for cause.

11 U.S.C. § 365(d)(4)(B): Debtor must by this date file any necessary motion to extend time to assume or reject an unexpired lease or nonresidential real property.

180 Days Post-Petition

Fed. R. Bankr. P. 1006(b)(2): Deadline to make final installment payment for cause shown. *(d/b/a only)*

V. Plan and Disclosure Statement; Confirmation; Dismissal or Conversion

180 Days Post-Petition

11 U.S.C. § 1121(e)(1): Termination of plan exclusivity period for **small business debtor**.

300 Days Post-Petition/ Post-Order for Relief

11 U.S.C. § 1121(e)(2): Deadline to file plan and disclosure statement in **small business case**.

45 Days Post-Filing of Plan

11 U.S.C. § 1129(e), 11 U.S.C. § 1121(e)(3): A **small business plan** that conforms with the Code must be confirmed by this date, unless (i) the debtor demonstrates by a preponderance of the evidence that it is more likely than not that the court will confirm a plan within a reasonable period of time, (ii) a new deadline is imposed, and (iii) the order to extend is signed prior to the expiration of the existing deadline.

Note: 11 U.S.C. § 363(b): The sale of customer personally identifiable information is limited under circumstances where privacy pledges existed pre-filing. The sale or lease of such information must either be (i) consistent with the policy in effect which prohibited the transfer of such information; or (ii) approved by the court upon the showing of certain standards. Notice prior to selling or leasing such information may be required.

Note: 11 U.S.C. §1112(b): This section now delineates several specific examples of “cause” for conversion or dismissal of a Chapter 11 case; limits a court’s discretion to deny conversion or dismissal and shifts the burden of proof to the debtor once cause is shown; and requires that a court determine a motion to convert or dismiss in an expedited fashion.

VI. Litigation

Two Years Post-Order for Relief

11 U.S.C. § 546(a): Deadline to bring action to avoid a statutory lien, fraudulent transfer or preferential transfer unless a trustee was appointed in the case less than one year prior.

11 U.S.C. § 108(a): Deadline to bring an action under nonbankruptcy law, if such law fixes a time for commencement of such action which is later than the petition date and earlier than two years post-petition.

