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# 2023 Alexander L. Paskay Memorial Bankruptcy Seminar

## **Subchapter V: The New Frontier for Small Businesses and Individuals**

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# Subchapter V

THE NEW FRONTIER FOR SMALL BUSINESSES AND INDIVIDUALS

## Key differences as to regular 11:

- No impaired accepting class needed
- Shortened deadlines – E.g., 90 days for plan. Also, IDI occurs sooner.
- No absolute priority rule
  - i. But still must be “fair and equitable” if not consensual
  - ii. Projected Disposable Income to Unsecured Creditors (3 years? 5 years?)
- Sub V trustee as “facilitator”
- Only debtor may propose a plan
  - i. 90-day deadline (difficult to extend)
- No creditors committee (unless for cause)
- No Disclosure Statement

## Lesser-Known Sub V Attributes:

- ▶ Claim modification of primary residence (§1190(3))
  - ▶ Only when mortgage funds used for business
- ▶ Admins can be paid over life of plan (§1191(e))
- ▶ No UST fees (Subchapter V Trustee Admin Claim Replacement)
- ▶ Property of the estate includes postpetition assets/earnings (only if non-consensual)
- ▶ Discharge entered:
  - i. Upon confirmation if consensual (§1191(a))
  - ii. Upon completion of payments if non-consensual (§1192)
    - 1. Plan Injunction and Automatic Stay remain in place until discharge.
    - 2. Issue: Can a discharge (non-consensual) be granted if payments are completed before the 3-yr or 5-yr period?

## Subchapter V General Statistics:

- As of December 2023: 4,800 Sub V cases filed nationwide
- 406 of these Sub V cases were filed in the MDFL – we continue to be #1 in the country!
- Prior to Enactment of SBRA, small business chapter 11 cases resulted in confirmation only 25% of the time and mean time to confirmation was 16 months.
- Since SBRA, confirmation of Sub V is roughly 47.5%. Of the confirmed plans, 59% were consensual and 41% were non-consensual. (Taking bets on how many of those were the SBA not showing up). Confirmation time is 6 months.

## Who can be a Sub V debtor?

- ❖ \$7.5M (until at least June 21, 2024) - noncontingent and liquidated
- ❖ “Currently engaged in commercial or business activities”
  - i. Issue: Can a Sub V be used for liquidating a company, as you can in a regular 11? The “currently engaged in commercial activities” seems to refer to whether the debtor has operations on the petition date. There are a few cases which discuss whether “current operations” can mean just winding down and settling debts.
    - 1. Judge Vaughan’s case: *In re Vertical Mac Construction LLC*, 2021 WL 3668037 (Bankr. M.D. Fla. July 23, 2021)
      - a. Corporate debtor can sell assets and liquidate even if operations terminated prepetition

## How Far Does This Go?

- ❖ *In re Ellingsworth Residential Community Association, Inc.*, 619 B.R. 519, (Bankr. M.D. Fla. 2020) – J. Jennemann ruled HOA was eligible even with limited “activities”
  - i. No profit motive required
  - ii. Activities were bank accounts, contracts for lawn and management services
- ❖ *In re Ikalowych*, 20-17547 (Bankr. D. Colo. April 15, 2021)
  - a. Debt must arise from business, but the debtor isn’t required to be engaged in that business on petition date. The debtor isn’t even required to be an owner of the business in which she or he is employed on the filing date.
- ❖ *In re RS Air, LLC* (9<sup>th</sup> Cir. BAP 2022) – a non-operating, non-profit business can be eligible
- ❖ *In re Rickerson*, 636 B.R. 416 (Bankr. W.D. Pa. 2021) – medical practice that had closed years before was not eligible. “Engaged in” is present tense. No operations and no activities despite having an open bank account.
- ❖ *In re Johnson* (N. D. Texas March 1, 2021) – Owner of defunct business is not eligible. Individual debtor owned and operated several small businesses, all of which had become defunct, but investors subsequently sued him. Court said not engaged in business activities as of the petition date.

## Small Business Debtor vs. Small Business Case

- a. “Small business case” – Small business debtor but Sub V not elected
- b. “Debtor” under Subchapter V- “subject to subparagraph (B), means a person engaged in commercial or business activities.... That has aggregate noncontingent liquidated secured and unsecured debts as of the date of the filing of the petition or the date of the order for relief in the amount not more than \$7,500,000.00...not less than 50% of which arose from the commercial or business activities or the debtor...” (exclusions also apply)
  - i. “Case” vs. “Debtor” Distinction important because of 362(n): Stay inapplicable when debtor was in a previous small business case but not in a Sub V

## Hot Topics in Sub V:

- Can corporate debtors discharge 523(a) claims?
  - *Under* 11 U.S.C. § 1192, if confirmation is non-consensual, discharge does not include any debt “of the kind” specified in §523(a). §523(a) provides that a discharge under §1192 does not discharge an “individual debtor” from those listed under (a).
  - *Cantwell-Clearly Co. v. Clearly Packaging, LLC (In re Clearly Packaging LLC)*, 21-1981 (4th Cir. June 7, 2022). Because 11 U.S.C. § 1192 specifies debts “of the kind” specified in §523(a), the limitation to individual debtors does not apply. So, no discharge for corporate debtors.
  - Several bankruptcy courts have disagreed. See *In re Industries, LLC*, 2022 WL 16858009 (*Bankr. W.D. Tex.* 2022)

## More Hot Topics :

- Projected Disposable Income v. Actual

- 11 U.S.C. §1191(a)(2) requires payment of “projected disposable income” for 3 to 5 years or the value thereof in a non-consensual confirmation.
- Is actual income okay?
- Compare with Chapter 13 - §1325(b)(1)
- Two courts have weighed in so far
  - Yes – *In re Staples*, 2023 WL 119431 (Bankr. M.D. Fla 2023)(Actual income is consistent with Code)
  - No – *In re Orange County Bail Bonds, Inc.*, 638 B.R. 137 (B.A.P. 9<sup>th</sup> Cir. 2022) (Actual income is not permitted by Code.)
- Consider that only the Sub V debtor can modify the plan

## What is the Role of a Sub V Trustee?

- ▶ Under 11 U.S.C. §1183 the Sub V Trustee should “facilitate the development of a consensual plan of reorganization”
  - ▶ See *In re Jackson*, 631 B.R. 937 (Bankr. M.D. Fla. 2021) – J. Vaughan decision removing and denying fees to Sub V Trustee that was not disinterested and was not facilitating a consensual plan.
- ▶ Does this mean the Sub V Trustee should never object to confirmation?
  - ▶ See §1183(b)(3)
- ▶ What is the role vis a vis the US Trustee? Where do they overlap?

## Other Issues

- ❑ When is a 5 year plan more appropriate than 3 years?
  - ❑ Capital contributions?
- ❑ Which is better for an individual debtor – Chapter 13 or Subchapter V?
  - ❑ Control
  - ❑ Fees
  - ❑ 3 year default versus 5
  - ❑ Ability to modify homestead
- ❑ Does the non-inclusion of the absolute priority rule mean that “old” equity can be “new” equity if the debtor company is sold during the case?

# Faculty

**Justin M. Luna** is a partner and chairs the Bankruptcy Department of Latham, Luna, Eden & Beaudine, LLP in Orlando, Fla., and advises clients in restructuring matters across Florida and the south-east. He regularly represents public and private companies, significant secured creditors, investors and asset-purchasers in troubled company financings and restructuring transactions, including out-of-court workouts and formal insolvency proceedings. Mr. Luna is also a federal and Florida trial attorney who represents companies and individuals litigate fraudulent transfers, preferences, and complex commercial, banking and financial technology matters. He has advised participants in the financial restructurings of: Caesars Entertainment Operating Co., Aeropostale Inc., Furniture Country Gallery, The Vue at Lake Eola, Gooding's Supermarkets, MGM Resorts LLC and many others. Mr. Luna has experience representing clients in a wide range of industries, including financial services, entertainment, hospitality, health care, retail, manufacturing, aviation, information technology, biomedical, real estate and logistics. He is AV-Rated by Martindale-Hubbell and has been named a Rising Star by *Super Lawyers*, chosen as a Next Generation Participant by the National Conference of Bankruptcy Judges and named as a finalist of the Top 40 Under 40 by the *Orlando Business Journal*. He also is a frequent speaker and author on a variety of topics across the bankruptcy and banking spectrum. Mr. Luna is a current board member for the Orlando City Foundation and the Middle District of Florida Bankruptcy *Pro Se* Clinic. He received his B.S. *magna cum laude* from the University of Florida, Warrington College of Business and his J.D. from the University of Florida, College of Law.

**Aleida Martinez-Molina** is a partner with AXS Law Group PLLC in Miami. After beginning her career in New York in the creditors' rights group of an AmLaw 100 international law firm, she returned to Florida to cast a wider net and further develop her own multifaceted practice. Through the years, Ms. Martinez-Molina has gained highly specialized experience in niche practices and industries, including hospitality, aviation and maritime law, which overlap with her core financial reorganization practice. In addition to her financial reorganization practice, she serves as one of six subchapter V trustees in the Southern District of Florida. She also acts as outside general counsel to various highly successful businesses in the hospitality and cruising sectors. Throughout her career, Ms. Martinez-Molina has represented foreign investors, foreign governments, government-owned entities and multinational corporations in cross-border disputes. She is fully bilingual in Spanish and English and communicates well in Portuguese and French. Ms. Martinez-Molina is a member of the National Association of Bankruptcy Trustees' Membership Committee, a board member of Legal Services of Greater Miami and serves on its Audit and Budget Committee, and a member of Human Rights Watch-Miami, and the Cuban American and American Bar Associations. She received her A.B. from Princeton University and her J.D. from Columbia Law School.

**Bradley S. Shraiberg** is a founding partner of Shraiberg Page P.A. in Boca Raton, Fla., where he focuses on advising companies experiencing financial difficulties, purchasers of and investors in distressed companies, and lenders to and creditors of such companies. He also regularly advises officers and directors of companies involved in debt restructuring on matters relating to corporate governance and fiduciary duty. During his career, Mr. Shraiberg has represented retail, manufacturing, construction, aerospace and other companies requiring financial and operational restructuring. He has experience with complex reorganizations, and some of the companies that he has recently con-

firmed plans of reorganization for, or negotiated a structured, consensual dismissal, include Enclave at Hillsboro, LLC, Atlantic Coast Refining, Inc., Jade Winds Association, Inc., Tuscany Energy, LLC, Auburn Trace, Ltd. and Mile Marker, Inc. Mr. Shraiberg also represents national retailers, landlords and developers in their capacity as creditors within various insolvency proceedings, as well as their litigation associated with complex commercial matters, such as Office Depot, MillerCoors, B/E Aerospace, KLX, Inc., Fiserv Securities, Anscas Homes, BBX Capital, Duffy's Sports Group and Sterling Development Corp. Due to the current economic conditions, a large portion of Mr. Shraiberg's clients are development companies and/or their principals. He has experience restructuring developers' financing and finding alternative financing and/or angel investors. He also has negotiated with all of the major financial institutions, and has amassed a network of investors that are interested in investing in or purchasing distressed assets. Mr. Shraiberg is a member of the Florida Bar and is licensed to practice in the U.S. District Courts for the Southern and Middle Districts of Florida. He is an active member of the Palm Beach County Bar Association, ABI and the Bankruptcy Bar Association for the Southern District of Florida, for which he is a past director and the past chairman of the local rules committee. Mr. Shraiberg has been recognized as a top bankruptcy and restructuring lawyer by *Chambers & Partners USA* since 2011, and as a top bankruptcy lawyer by *Super Lawyers* since 2012 and *Florida Trend's* Legal Elite since 2011. He received his B.A. in 1994 from the University of Miami and his J.D. *cum laude* in 1997 from the University of Miami School of Law.

**Hon. Lori V. Vaughan** is a U.S. Bankruptcy Judge for the Middle District of Florida in Orlando, sworn in on Feb. 25, 2020. She started her career as a law clerk to Hon. Karen S. Jennemann. Judge Vaughan then practiced bankruptcy law for 21 years at two law firms, representing debtors, creditors and trustees in jurisdictions across the country. Most recently, she was a shareholder at Trenam Law in Tampa, Fla., and before that, she practiced at Foley & Lardner, the last year of which she spent practicing out of its New York office. Judge Vaughan previously served as president of the Tampa Bay Bankruptcy Bar Association, chair of the Bankruptcy/UCC Committee of the Florida Bar's Business Law Section, and board member for the International Women's Insolvency & Restructuring Confederation. She has also sat on the boards of the USF Financing Corp. and USF Property Corp. Before taking the bench, Judge Vaughan was recognized by *Florida Super Lawyers* as being among the top 100 Lawyers in Florida, the top 50 Lawyers in Tampa Bay and the top 50 Women Lawyers in Florida. She also has been recognized by *Chambers USA* and *The Best Lawyers in America*. Judge Vaughan received her B.A. with high honors from Eckerd College in 1995 and her J.D. with honors from the University of Florida, College of Law in 1998.

**Aaron A. Wernick** is a sole practitioner with Wernick Law, PLLC in Boca Raton and specializes primarily in chapter 11 debtor representation. He has successfully confirmed more than 95 percent of his chapter 11 reorganizations. Mr. Wernick is Board Certified in Business Bankruptcy Law and Consumer Bankruptcy Law by the American Board of Certification, and serves on its board of directors. He is licensed to practice in all federal courts in Florida, as well as the Eleventh Circuit Court of Appeals and the U.S. Supreme Court. He also is licensed to practice in California and Wisconsin and is admitted to the federal courts in California. Mr. Wernick is experienced in handling complex restructuring, insolvency and bankruptcy cases. He has been quoted in *The Wall Street Journal* as well as in local news sources on bankruptcy matters, and he has served on various moderating panels, most recently at the National Association of Bankruptcy Trustees on the subject of secured transactions and the UCC. Mr. Wernick is listed in *Super Lawyers* and has a 10/10 rating on Avvo. After graduating from college, he was on the faculty at Fudan University in Shanghai, China, for a year,

having previously studied Mandarin for four years. In law school, he was a teaching assistant, conducting classes for law students visiting from various Asian countries. Mr. Wernick then worked for a private-equity group, specializing in the acquisition of distressed assets, where he discovered his passion for the bankruptcy world. After acting as a plaintiff's lawyer in a FINRA arbitration, where the brokerage firm filed chapter 11, he was hooked on the chapter 11 process. Mr. Wernick received his undergraduate degree *cum laude* in 1994 from the University of Pennsylvania and his J.D. in 1999 from the University of Wisconsin Law School.