

## Small Business Bankruptcy Options

When circumstances are dire, bankruptcy can be used to reorganize or liquidate a business. There are several different types of bankruptcy available to entrepreneurs and small businesses. The purpose, eligibility, cost, and impact (benefit) vary depending on the bankruptcy code chapter used. Below is a brief explanation of each major type; for more information particular to your situation, please contact us by filling out our [intake form](#).

### Chapter 11

Purpose	Impacts
<ul style="list-style-type: none"> <li>Intended to be used by large businesses that need to reorganize their debt to a more manageable level.</li> <li>Companies that have recently filed under this Chapter are J. Crew and Hertz.</li> <li>Usually takes 1-2 years to complete</li> <li>Can be prohibitively expensive due to legal and administrative fees and costs</li> </ul>	<ul style="list-style-type: none"> <li>Creditors are temporarily prohibited from taking any action</li> <li>Court may appoint a U.S. Trustee to operate the business</li> <li>Creating a payment plan often involves downsizing the business</li> <li>Potentially “cram down” creditors’ claims and reduce debt, but owners may lose their equity</li> </ul>

Eligible Small Businesses may prefer to take advantage of one of the other Chapters or the new Subchapter V.

### Subchapter V (of Chapter 11)

Purpose	Impacts
<ul style="list-style-type: none"> <li>Subchapter V is a new addition under Chapter 11 that streamlines the process and makes it cheaper to file.</li> <li>Available to business entities and individuals engaged in commercial or business activities</li> <li>At least 50% of debt must be commercial or business debt.</li> <li>Total noncontingent, liquidated secured and unsecured debts of not more than \$2,725,625 (raised to \$7,500,000 until March 2021 under the CARES ACT)</li> </ul>	<ul style="list-style-type: none"> <li>Creditors are temporarily prohibited from taking any action</li> <li>Owner maintains full operational control throughout the process</li> <li>The business does not have to pay for a U.S. Trustee to run the business</li> <li>Can “cram down” unsecured debt and may be able to retain owner equity without the consent of any class of creditors</li> <li>3-5-year payment plan with administrative expenses payed over the life of the plan</li> </ul>

### Chapter 7

Purpose	Impacts
<ul style="list-style-type: none"> <li>Applies to individuals and businesses, but the rules are somewhat different for each.</li> <li>When a company files a Chapter 7 bankruptcy, the company is shut down permanently.</li> <li>The goal is an orderly liquidation of the business.</li> <li>For a business, any debt not paid, remains and is not discharged (as in a personal bankruptcy).</li> <li>Creditors can no longer collect from the company (which will be dissolved), but if owners are personally liable for any of the business debt, they could be left with more liability than with a private negotiation and sale.</li> </ul>	<ul style="list-style-type: none"> <li>Owners give up control of the business to a bankruptcy trustee, who will publicly sell the business (or its assets), and distribute the proceeds among creditors, according to the bankruptcy priority rules.</li> <li>Owners get to step away from the closure and leave the hard work of selling off assets and paying creditors to the bankruptcy trustee.</li> <li>Trustee may take a percentage of the sale proceeds as a fee, leaving more debt behind.</li> <li>Prices paid for the business (or its assets) may be lower due to the fire sale aspect of the sale.</li> </ul>

**Chapter 13**

Purpose	Impacts
<ul style="list-style-type: none"> <li>• Debtors have sufficient monthly income to repay most debts in full, along with other required payments.</li> <li>• Debt must be less than \$419,275 in unsecured debt and \$1,257,850 in secured debt.</li> <li>• Sole proprietors may file under their own names, and reorganize both their personal and business debts, and keep their businesses open.</li> <li>• Allows filers to keep many of their assets while reorganizing and catching up past due payments through a payment plan.</li> <li>• Payment plan usually lasts 3-5 years (CARES Act extended this to 7-years for the next year).</li> <li>• Payment amounts are based on income levels.</li> <li>• Debtor makes monthly payments to the Bankruptcy Trustee and the Trustee pays the creditors according to the plan.</li> </ul>	<ul style="list-style-type: none"> <li>• The amount that must be repaid depends on income, expenses and the types of debt.</li> <li>• Although certain priority debts must be repaid fully, such as certain taxes and domestic support obligations, it is possible to reduce the balance of some secured debts (such as car or equipment loans) to the value of the property.</li> <li>• Filers can keep certain items needed to maintain a home and job, which allows sole proprietors to keep business assets, through “tools of the trade” exemptions up to a certain dollar value.</li> <li>• Filers can also keep nonexempt assets, so long as they pay for them through the plan.</li> <li>• Filers may be able to get out from under personal guarantees under certain circumstances.</li> </ul>

Choosing among the various options for small business bankruptcy can be complicated. However, if you are a small business that is organized as anything other than a sole proprietorship, your main options are Subchapter V or Chapter 7 depending on your specific scenario. If your business is organized as a sole proprietorship you may be eligible for Chapter 13, in addition to Subchapter V and Chapter 7. Consult a bankruptcy attorney to determine the correct option for your business. For additional information, or a referral to a bankruptcy attorney, please fill out our [intake form](#) or contact your County’s Bar Association Attorney Referral Service or the [Pennsylvania Bar Association](#).