

INSIGHTS + NEWS

Client Alert: The Impact of Recent Amendments to the United States Bankruptcy Code on Lenders

BY MARK W. POWERS • MAY 5, 2021

On March 27, 2021, President Biden signed into law the COVID-19 Bankruptcy Relief Extension Act (the Extension Act). The Extension Act temporarily extends certain bankruptcy relief provisions that were enacted as part of the Coronavirus Aid, Relief, and Economic Security Act (the CARES Act), as further amended and/or extended as part of the Consolidated Appropriations Act (the CAA) which was signed into law on December 27, 2020. This alert highlights the impact of these changes on banks and other lenders.

SUBCHAPTER V DEBT LIMITS

Increase of Debt Limit to \$7.5 million

The Small Business Reorganization Act of 2019 created Subchapter V of chapter 11 of the Bankruptcy Code, and became effective on February 19, 2020, immediately before the onset of the COVID-19 pandemic. Subchapter V was enacted to streamline the reorganization process for smaller companies with debts up to \$2.7 million. The CARES Act increased the debt limit for eligible debtors from \$2.7 million to \$7.5 million. The increase to \$7.5 million was originally set to expire on March 27, 2021; however, the Extension Act further extends the \$7.5 million debt through March 27, 2022.

Impact on Lenders

Subchapter V provides a faster and cheaper bankruptcy option and is working well for both borrowers and lenders. The extension of the \$7.5 million debt limit to March 27, 2022 will make it easier for a smaller company to reorganize, and for a lender to thereby preserve the going-concern value of its collateral. Many practitioners expect Congress to enact a further (and perhaps permanent) extension of the \$7.5 million debt limit increase prior to March 27, 2022.

FILING PROOFS OF CLAIM IN BANKRUPTCY

Ability to File a Supplemental Proof of Claim

The CAA amends sections 501 and 502 of the Bankruptcy Code to create a process that permits certain eligible lenders to file a supplemental proof of claim for amounts that accrued under any forbearance agreement entered into between a debtor and lender under the CARES Act.

Impact on Lenders

This provision is intended to compensate lenders for damages incurred due to the implementation of the CARES Act. The provision sunsets on December 27, 2021.

UNEXPIRED NON-RESIDENTIAL REAL PROPERTY LEASES

Extensions of the Deadline to Make Timely Payment Under a Non-Residential Lease Due to COVID-19 (Section 365(d)(3) of the Bankruptcy Code)

Section 365(d)(3) of the Code requires a debtor to make timely payments under an unexpired non-residential real property lease upon the filing of the bankruptcy case until the lease is assumed or rejected by the landlord, *unless* the debtor obtains a court order extending the deadline for “cause” for a period not to exceed 60 days from the petition date. The CAA now permits a debtor in a small-business Subchapter V case to seek an additional 60-day extension to commence making payments (up to 120 days total) if the debtor can show that it is experiencing a material financial hardship as a result of the COVID-19 pandemic.

Impact on Lenders

If the Lender’s customer is a commercial landlord whose tenant is in a Subchapter V proceeding and obtains a 60-day extension under Section 365(d)(3), then the landlord may experience short-term cash flow issues. The change to 365(d)(3) is set to expire on December 27, 2022. While this change will apply to any case filed before that date, the change is unlikely to be further extended.

Time for Debtor/Lessee to Assume or Reject Non-Residential Leases (Section 365(d)(4)(A) of the Bankruptcy Code)

Prior to the CAA, Section 365(d)(4) provided a debtor that is a lessee under a non-residential real property lease with an automatic 120-day period to assume or reject the lease, with the right to move for an additional 90-day extension for “cause” shown. The CAA extends the automatic 120-day period to 210 days while retaining the debtor/lessee’s right to move to extend the automatic 210-day deadline for an additional 90 days for “cause” shown. This change now gives the debtor/lessee up to 300 days to assume or reject a non-residential real property lease.

The change to Section 365(d)(4)(A) applies (A) to *all debtors* (not just debtors in Subchapter V) and (B) and without the need to demonstrate a material financial hardship. The change to 365(d)(4)(A) is also set to expire on December 27, 2022. While this change will apply to any case filed before that date, the change is unlikely to be further extended.

Impact on Lenders

The change to Section 365(d)(4)(A) will not materially impact lenders. During the period, as extended, the debtor/lessee will be required to continue to make current payments to the landlord.