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New Bankruptcy Relief Provisions Brought to You by the 2021 Federal Appropriations Act

December 31, 2020

by Irve J. Goldman

The new Consolidated Appropriations Act, 2021 (the “Act”), which was signed into law on December 27, 2020 (H.R. 133), includes within its 5,593 pages a number of new bankruptcy relief provisions for businesses as part of what the legislation calls the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act. Additional bankruptcy relief provisions are found in a miscellaneous section of the Act. A summary of the relief provisions that will affect businesses, predominately small businesses, follows.

PPP LOANS NOW AVAILABLE TO CERTAIN DEBTORS

Under regulations adopted by the SBA in response to the CARES Act, businesses in bankruptcy were disqualified from receiving PPP loans. The SBA regulations spawned an avalanche of litigation which challenged them on grounds that they were unlawfully discriminatory under 11 U.S.C. §525(a), *see e.g. In re Springfield Hospital, Inc.*, 618 B.R. 70, 80-93 (Bankr. D. Vt. June 22, 2020), *appeal pending* Nos. 20-3902, 20-3903 (2d Cir.), or were arbitrary and capricious or exceeded the SBA’s rulemaking authority. *See e.g. In re Gateway Radiology Consultants, P. C.*, 2020 WL 7579338 (11th Cir. Dec. 22, 2020) (reversing bankruptcy court’s ruling striking down the regulations as exceeding SBA authority and as arbitrary and capricious).

In somewhat of a quizzical intermediate approach, the new law provides that only debtors that are proceeding under Subchapter V of Chapter 11, which is the Small Business Reorganization Act of 2019 (“SBRA”), as well as Chapter 12 and Chapter 13 debtors, may apply to the bankruptcy court for a PPP loan. The provisions of SBRA are summarized here, with the caveat that the debt limitations to qualify for SBRA were expanded by the CARES Act to \$7.5 million.

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This new provision is yet another advantage to seeking relief under Subchapter V, but does nothing to resolve the pending litigation over the SBA's prohibition against extending PPP loans to Chapter 11 debtors that are not proceeding under Subchapter V.

Under the new provision, which amends §364 of the Bankruptcy Code, a qualifying debtor may apply for and obtain authority to receive a PPP loan which, if not forgiven, will be treated as a "superpriority" administrative expense in the Chapter 11 proceeding, which means it will come ahead of all administrative expenses in the case. If such an application is made, the bankruptcy court is required to hear it within seven days of the filing and service of the application. In addition, the debtor's plan of reorganization may provide that the PPP loan, if not forgiven, may be paid back under the terms on which it was originally made, which are favorable.

LEASES OF COMMERCIAL REAL ESTATE

Section 365(d)(3) of the Bankruptcy Code requires that Chapter 11 debtors continue to pay rent and comply with all other obligations under a lease of commercial real estate from and after the bankruptcy filing date, but vests authority in the bankruptcy court to extend the time of performance under such a lease for up to 60 days. In yet another plum given to Subchapter V debtors, that section has been amended to allow the bankruptcy court to extend the time for performance under these type of leases for a Subchapter V debtor for an additional 60 days, but only "if the debtor is experiencing or has experienced a material financial hardship due, directly or indirectly," to the COVID-19 pandemic.

The period of time within which a Chapter 11 debtor has to either assume or reject a lease of commercial real estate has also been changed. With the enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), a Chapter 11 debtor became limited to a period of 120 days, or 210 days with the court's permission, to decide whether to assume or reject nonresidential real property leases. Prior to BAPCPA, the initial period of time to make that decision was 60 days, but it could be extended by the bankruptcy court for cause without any outside time limitation.

Under the Act, the period of time to decide whether to assume or reject a lease of commercial real estate has been expanded to 210 days, subject to an additional 90 days with the bankruptcy court's permission.

There is a sunset provision for the foregoing amendments that is two years after the date of enactment of the Act.

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PREFERENCE AMENDMENTS

The Act appears to recognize that many landlords and suppliers have entered into forbearance or deferral agreements with businesses in financial trouble due to the pandemic, and laudably provides preference protection for payments that are made pursuant to these types of agreements. Generally, a payment to a creditor that is made within 90 days of a bankruptcy filing on account of a pre-existing debt can be recovered, or clawed back to the bankruptcy estate, as a preferential transfer (subject to certain defenses).

For landlords of a commercial tenant, any “covered payment of rental arrearages” will be protected from avoidance as a preference if: (i) the payment is made pursuant to an agreement or arrangement to defer or postpone the payment of rent or other charges under the lease, (ii) the agreement or arrangement was made or entered into on or after March 13, 2020, and (iii) the amount deferred or postponed does not, (A) exceed the rent and other charges that were owed under the lease prior to March 13, 2020, and (B) include fees, penalties, or interest in an amount that is greater than what would be owed under the lease, or include any fees, penalties, or interest that would be greater than what would be charged if the debtor had paid all amounts due under the lease timely and in full before March 13, 2020.

For suppliers of goods and services, the protection given is similar to that provided for landlords. Specifically, any “covered payment of supplier arrearages” will be protected from avoidance as a preference if: (i) the payment is made pursuant to an agreement or arrangement to defer or postpone the payment of amounts due under a contract for goods or services, (ii) the agreement or arrangement is made on or after March 13, 2020, (iii) the amount deferred or postponed does not, (A) exceed the amount that was due under the contract prior to March 13, 2020, and (B) include fees, penalties, or interest in an amount that is greater than what would be owed under the contract, or include any fees, penalties, or interest that would be greater than what would be charged if the debtor had paid all amounts due under the contract timely and in full before March 13, 2020.

There is a sunset provision for the foregoing amendments that is two years after the date of enactment of the Act.

CONCLUSION

The ability of a Subchapter V debtor to obtain a PPP loan while in bankruptcy is certainly a welcome addition to the bankruptcy landscape, but left in the lurch are larger companies that do not seem less deserving of the same relief. Subchapter V debtors that are materially affected by the pandemic will also benefit from an additional form of rent relief based on the new authority given to bankruptcy courts to extend the debtor’s time for paying rent and other charges under a lease of commercial real estate for an additional 60 days, on top of the 60-day deferral period that already existed in the law. And all Chapter 11 debtors will now be given

New Bankruptcy Relief Provisions Brought to You by the 2021 Federal Appropriations Act

at least 210 days to decide whether to assume or reject such leases, subject to an additional 90 days with the court's permission.

The new provisions protecting landlords and suppliers from having to disgorge payments that might otherwise be considered preferences if they are made pursuant to a deferral or forbearance agreement reflect a sensible recognition that such arrangements were designed to provide financial assistance to a struggling business and are deserving of protection.

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