CARES ACT TEMPORARILY INCREASES DEBT LIMITATION FOR SMALL BUSINESS DEBTORS

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) provides much-needed assistance to small businesses affected by the coronavirus pandemic. In addition to providing forgivable loans of up to $10,000,000, the CARES Act more than doubles the debt limitation under the Small Business Reorganization Act of 2019 (SBRA) for a one-year period commencing March 27, 2020. This change will allow more small businesses to reorganize under the newly created Subchapter V of Chapter 11 of the Bankruptcy Code.

Small Business Reorganization Act of 2019

Chapter 11 of the Bankruptcy Code governs business reorganization. In amendments to the Bankruptcy Code in both 1994 and 2005, Congress distinguished small businesses and attempted to provide for a streamlined small business reorganization process. Unfortunately, these efforts have largely proved unworkable for most small businesses as the amendments were tightly confined within the strictures of Chapter 11.

For many small businesses, a Chapter 11 reorganization is not practical because the traditional proceedings are expensive and cumbersome. The SBRA, which took effect on February 19, 2020, created an entirely new subchapter of Chapter 11—Subchapter V—which eliminates some of the procedural barriers and costs of a traditional Chapter 11 proceeding in an attempt to make reorganization more viable for small businesses. Subchapter V includes the following provisions:

- The court must hold a status conference within 60 days of the petition date to discuss the "expeditious and economical resolution of the case," and the debtor must file a report 14 days before the conference detailing how it is attempting to obtain a consensual plan of reorganization;
- The debtor has the exclusive right to propose a plan of reorganization and it must be filed within 90 days of the petition date;
- There is no committee of unsecured creditors unless the court orders otherwise for cause;
- No disclosure statement is required unless the court orders otherwise for cause;
- The debtor is excused from paying quarterly U.S. trustee fees;
- The court may confirm a non-consensual plan of reorganization if the plan does not "discriminate unfairly" and is "fair and equitable" as to each class of impaired creditors that has not accepted the plan; and
- The absolute priority rule is eliminated, which makes it easier for owners to retain their stake in the business.

Cases filed under Subchapter V have similarities to cases under Chapters 12 and 13.

A trustee is appointed to investigate the financial affairs of the debtor, help administer claims, and act as a conduit for the debtor's payments under its confirmed plan. The debtor remains in possession of its property and continues to operate the business. And a plan can be confirmed without the acceptance of a class of creditors if it treats creditors within the class fairly and the debtor commits all of its projected disposable income to making payments under the plan over the course of a three- or five-year period.

To be eligible under the SBRA, a small business must be engaged in commercial or business activities and cannot have more than $2,725,625 of secured and unsecured debt. Additionally, 50% of the pre-petition debt must have been generated from commercial or business activities. A small business is ineligible if its primary activity is owning single-asset real estate. Thus, whether a business qualifies as a small business debtor largely depends on its debt threshold.

Debt Limitation Increase Under the CARES Act

While Subchapter V appears to have created a more workable framework for small business debtors looking to reorganize their financial affairs, it remains inaccessible to many businesses that might otherwise qualify because of the debt threshold proscribed in the SBRA. The CARES Act represents a significant step toward expanding the scope of Subchapter V by increasing the debt limitation under the SBRA from $2,725,625 to $7,500,000. This increase, however, is only temporary and will sunset on March 27, 2021, unless further action is taken by Congress. Some proponents of the SBRA, such as the American Bankruptcy Institute, lobbied Congress for a debt threshold of $10 million before the SBRA was signed into law. While it remains uncertain whether Congress will permanently extend or increase the new debt limitation under the SBRA, it is clear that a much greater number of small businesses will be able to take advantage of Subchapter V over the next year.

For further information regarding the SBRA, the impact of the CARES Act on your business, or insolvency concerns relating to bankruptcy or receivership, please contact attorneys Jessica K. Haskell and Nicholas G. Chmurski.

BEWARE OF MAINTENANCE AND REPAIR RESPONSIBILITIES IN COMMERCIAL LEASES

One of the most important aspects of a commercial lease is apportioning the maintenance and repair responsibilities for the leased premises. Maintenance and repair responsibilities

vary greatly based on the type of lease, design of the leased premises, and negotiating power of the landlord and tenant.

At the outset, it is important to appreciate the structure of each lease. Generally speaking, there are two categories of leases based on how rent is calculated. On one end of the spectrum is the gross lease (sometimes called a “full-service lease”), which provides that a tenant’s rental payment includes all expenses associated with the leased premises. On the other end of the spectrum is the net lease, which provides that a tenant’s rental payment is net of certain expenses in association with the leased premises. In a net lease, the tenant reimburses the landlord for these expenses in the form of additional rent or pays the expenses directly.

Variations of the gross lease and net lease exist. A modified gross lease is more tenant-friendly and allows the landlord and tenant to negotiate which expenses relating to the leased premises should be included and excluded from the tenant’s rental payment. A triple net (NNN) lease is the most common type of net lease, and generally provides that a tenant pays the landlord for its proportionate share of real estate taxes, insurance, and operating expenses (usually specifically defined) in addition to the tenant’s base rental payment. An absolute net lease is the most landlord-friendly type of lease and apportions all risk and expenses associated with the leased premises, including all maintenance and repair responsibilities, to the tenant.

Chapter 704 of the Wisconsin Statutes governs landlord-tenant rights. Section 704.07 provides default rules for maintenance and repair obligations in the absence of contrary language in a commercial lease.

A landlord’s obligations include:

- Keeping common areas in good repair;
- Keeping equipment that furnishes services (e.g., heat, water, elevator, air conditioning) to the tenant in good repair;
- Making all necessary structural repairs; and
- Repairing and replacing plumbing, electrical wiring, machinery, and equipment furnished with the leased premises.

Wis. Stats. § 704.07(2).

A tenant’s obligations include:

- Repair and remediation for damage and infestation caused by action or inaction of the tenant; and
- Ordinary and routine maintenance and repairs for plumbing, electrical wiring, machinery, and equipment furnished with the leased premises.

Wis. Stats. § 704.07(3).

Typically, a landlord is responsible for the repair of structural and major component parts of the leased premises, as well as any replacements that would be considered capital expenditures, such as the roof, parking lot, and foundation. The tenant remains responsible for maintenance and ordinary repairs to items inside of the leased premises over which the tenant has control. In many commercial leases, however, a landlord may attempt to shift repair and replacement responsibilities to a tenant for items that exclusively service the leased premises. One common example is heating, ventilation, and air conditioning (HVAC) systems, which can carry considerable costs.

A good rule of thumb is that the longer the lease term and the fewer number of tenants in a particular building, the more likely it is that a tenant will take on additional maintenance and repair responsibilities. Landlords and tenants should be careful to clearly apportion these responsibilities to avoid ambiguity. For example, “operating expenses” should be clearly defined to avoid any misunderstandings between the parties.

Whether you are a landlord or a tenant, our experienced legal team at O’Neil Cannon can answer your lease questions and protect your interests.

OCHDL IS PLEASED TO ANNOUNCE THAT ATTORNEY NICHOLAS G. CHMURSKI HAS JOINED THE FIRM

Attorney Nicholas G. Chmurski, a graduate of Marquette University, has recently joined the Milwaukee law firm O’Neil Cannon Nick is a member of the Business Law and Real Estate and Construction Groups. His business background and clerkship experience make Nick a valuable resource, as he is able to contribute across practice groups to help solve a wide range of legal issues.

O’Neil Cannon, founded in Milwaukee in 1973, is a full-service legal practice that primarily focuses on providing business law and civil litigation services to closely-held businesses and their owners. The firm represents corporations, institutions, and partnerships at all stages of the business life cycle, helping them start, grow and transition from one generation to the next. We also assist business owners with their personal legal needs including tax and estate planning, family law and litigation—including personal injury litigation.