UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

In re:	Michael Bonert and Vivien Bonert, Debtors.	Case No.: 2:19-bk-20836-ER Chapter: 11 **MEMORANDUM OF DECISION AUTHORIZING DEBTORS TO PROCEED UNDER SUBCHAPTER V OF CHAPTER 11** **[RELATES TO DOC. NOS. 186 AND 246]** [No hearing required pursuant to Federal Rule of Civil Procedure 78(b) and Local Bankruptcy Rule 9013-1(j)(3)]

At issue is whether the Debtors should be permitted to amend their Chapter 11 petition to elect treatment under the newly-enacted Subchapter V of Chapter 11. The Official Committee of Unsecured Creditors (the "Committee") opposes the Debtors' Subchapter V election. No other opposition to the Subchapter V election is on file.[1]

[1] The Court considered the following papers in adjudicating this matter:

1) [Amended] Voluntary Petition for Individuals Filing for Bankruptcy [Doc. No. 136];
2) Official Committee of Creditors Objection to Debtors' Election of Small Business Designation Chapter 11, Subchapter V [Doc. No. 242];

For the reasons set forth below, the Committee's opposition is **OVERRULED**, and the Debtors are authorized to proceed under Subchapter V.

I. Procedural Background

Michael Bonert ("Michael") and Vivien Bonert ("Vivien," and together with Michael, the "Debtors")[2] filed a voluntary Chapter 11 petition on September 12, 2019 (the "Petition Date"). Doc. No. 1 (the "Petition"). The Debtors stated that they were not "small business debtors" within the meaning of § 101(51D). Petition at ¶ 13.

On March 3, 2020, the Debtors filed an Amended Voluntary Petition [Doc. No. 136] (the "Amended Petition"), which made two changes to the Petition. First, the Debtors stated that they were "small business debtors" as defined in § 101(51D). Amended Petition at ¶ 13. Second, the Debtors elected treatment under the newly-enacted Subchapter V of Chapter 11. *Id.*

On March 12, 2020, the Court entered an *Order Establishing Procedures Governing the Determination of Whether this Case Will Proceed Under Subchapter V of Chapter 11 of the Bankruptcy Code* [Doc. No. 186] (the "Subchapter V Procedures Order"). The Subchapter V Procedures Order fixed March 26, 2020 as the deadline for interested parties to object to the Debtors' election to proceed under Subchapter V, and stated that if an objection was filed, the Court would determine whether a hearing was required and would notify the parties accordingly.

On February 20, 2020, the United States Trustee (the "UST") appointed the Committee, which is comprised of five creditors. Doc. Nos. 128 and 131. On February 28, 2020, the Committee filed an application requesting authorization to employ Blakely LLP ("Blakely") as the its counsel. Doc. No. 133 (the "Employment Application"). On March 12, 2020, the UST objected to the Employment Application, arguing among other things that Blakeley had failed to make the disclosures required under Bankruptcy Rule 2014. Doc. No. 187. On March 13, 2020, the Debtors objected to the Employment Application, arguing among other things that the Employment Application would be moot if the Court authorized the Debtors to proceed under Subchapter V, since under Subchapter V a creditor's committee may not be appointed "[u]nless the court for cause orders otherwise," § 1102(a)(3). Doc. No. 189. A hearing on the Employment Application was initially set for April 22, 2020 at 10:00 a.m. Doc. No. 241.

On March 16, 2020, the UST appointed Gregory K. Jones to serve as the Subchapter V Trustee, pursuant to § 1183(a). Doc. No. 206. On March 24, 2020, the Debtors, the UST, and the Subchapter V Trustee executed a *Stipulation to Continue Deadline to Object to Case Proceeding Under Subchapter V* [Doc. Nos. 234 and 238] (the "Stipulation"). The Stipulation noted that under Bankruptcy Rule 1020(b), parties in interest have thirty days from the conclusion of the § 341(a) meeting of creditors to object to a debtor's statement that it is a "small business debtor" as defined by § 101(51D). Based upon the fact that a debtor cannot elect treatment under

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3) Debtors' Response to the Creditors' Committee's Objection to Debtors' Election of Small Business Designation Under Subchapter V of Chapter 11 [Doc. No. 264];
   a) Request for Judicial Notice in Support of Debtors' Response to the Creditors' Committee's Objection to Debtors' Election of Small Business Designation Under Subchapter V of Chapter 11 [Doc. No. 265]; and
4) Supplemental Brief in Support of the Official Committee of Creditors' Objection to Debtors' Election of Small Business Designation Under Chapter 11, Subchapter V [Doc. No. 267].

[2] Given names are used to distinguish Michael from Vivien. No disrespect is intended.

Subchapter V unless the debtor is also a "small business debtor," the Stipulation requested that the deadline for interested parties to object to the Debtors' Subchapter V election be extended to thirty days after the conclusion of the meeting of creditors.

On April 6, 2020, the Court entered an order (1) approving the Stipulation, (2) extending the deadline for interested parties to object to the Debtors' Subchapter V election to and including May 20, 2020, and (3) adjourning the hearing on the Employment Application pending further order of the Court. Doc. No. 246. The Court explained that the Employment Application could not be adjudicated until after determination of whether the case would proceed under Subchapter V, given that Subchapter V does not contemplate the appointment of a Committee "[u]nless the court for cause orders otherwise," § 1102(a)(3). *Id.*

The Committee is the only party that has objected to the Debtors' Subchapter V election. In opposition to such election, the Committee argues that it would be prejudiced if the case were to proceed under Subchapter V; that the Debtors should be judicially estopped from re-designating as "small business debtors" in order to become eligible for treatment under Subchapter V; and that the Debtors may exceed the small business debt limit under § 101(51D). The Debtors dispute each of these contentions.

II. Findings and Conclusions

The Small Business Reorganization Act of 2019 (the "SBRA") became effective on February 19, 2020. The purpose of SBRA is "to streamline the reorganization process for small business debtors because small businesses have often struggled to reorganize under chapter 11." *In re Ventura*, --- B.R. ---, No. 8-18-77193-REG, 2020 WL 1867898, at *6 (Bankr. E.D.N.Y. Apr. 10, 2020) (publication forthcoming). Nothing in SBRA addresses whether the act applies to pending cases or only to cases commenced after the effective date of the legislation.

The majority of courts that have addressed the issue have found that a debtor who filed a Chapter 11 petition prior to the effective date of SBRA may amend the petition to elect treatment under Subchapter V. In *In re Ventura*, the court allowed the debtor to proceed under Subchapter V, even though the debtor's petition had been filed fifteen months prior to the effective date of SBRA and both the debtor and a creditor had filed competing plans of reorganization. *Id.* at *2–4. The *Ventura* court held that "any practicality and scheduling issues arising from a SBRA designation in a case commenced prior to the effective date of the SBRA" could be resolved by an extension of any SBRA-specific deadlines. *Id.* at *8. The court authorized re-designation to Subchapter V over the objection of the creditor who had filed a competing plan, reasoning that "in general, the new subchapter V provisions do not impair the vested property interests of creditors and, therefore, the concerns supporting application of the canon of statutory construction disfavoring the retroactive application of new law are absent." *Id.* at *9.

Re-designation to Subchapter V in cases filed prior to the effective date of SBRA was also permitted in *In re Body Transit, Inc.*, 613 B.R. 400 (Bankr. E.D. Pa. 2020), *In re Bello*, --- B.R. ---, No. 19-46824, 2020 WL 1503460 (Bankr. E.D. Mich. Mar. 27, 2020) (publication forthcoming), and *In re Moore Properties of Pers. Cty., LLC,* No. 20-80081, 2020 WL 995544 (Bankr. M.D.N.C. Feb. 28, 2020). In *In re Progressive Sols., Inc.*, --- B.R. ---, No. 8:18-BK-14277-SC, 2020 WL 975464 (Bankr. C.D. Cal. Feb. 21, 2020) (publication forthcoming), the court found as a matter of law that there was no reason why re-designation could not be approved, but found that the request for re-designation before it was procedurally improper. The only case of which the Court is aware in which re-designation was not authorized is *In Re*

Double H Trans. LLC, --- B.R. ---, 2020 WL 2549850 (Bankr. W.D. Tex. Mar. 5, 2020) (publication forthcoming).

The Court finds re-designation to Subchapter V to be appropriate on the specific facts of this case. However, it is important for the Court to emphasize that re-designation will not necessarily be proper in all Chapter 11 petitions commenced prior to the effective date of SBRA.

Applying the standard set forth in *Body Transit*, the Court finds that re-designation is warranted if not sought in bad faith and provided that no party will be unduly prejudiced. *Body Transit*, 613 B.R. at 408. The Debtors have satisfied this standard.

A. The Committee Will Not Be Unduly Prejudiced By Re-Designation

The Court finds that the Committee will not be unduly prejudiced by re-designation. The Committee had been in existence for only a short period of time before the Debtors elected treatment under Subchapter V. The Committee was appointed on February 20, 2020; the Debtors filed their Amended Petition electing treatment under Subchapter V on March 3, 2020. The Court has not yet ruled upon the Committee's application to employ Blakely as its counsel.[3]

In addition, the Court will provide the Committee an opportunity to show cause why it should be permitted to continue in existence after the Debtors' Subchapter V election takes effect. *See* § 1102(a)(3)("Unless the Court for cause orders otherwise, a committee of creditors may not be appointed in a small business case or a case under subchapter V of this chapter"). The Committee will not be disbanded if it can demonstrate that its continued existence will improve recoveries to creditors, will assist in the prompt resolution of this case, and is necessary to provide effective oversight of the Debtors.

The Committee asserts that allowing the case to proceed under Subchapter V would be prejudicial because it has already expended significant resources opposing numerous claim objections filed by the Debtors (the "Claim Objections"). This argument suffers from two problems. First, at the time the Committee opposed the Claim Objections, the Court had already entered the Subchapter V Procedures Order, which made clear to all parties the possibility that the Court might permit the Debtors to elect treatment under Subchapter V. The Committee made its decision to oppose the Claim Objections with full awareness that its future role in this case was uncertain. In fact, at the time the Committee opposed the Claim Objections, its application to employ Blakely LLP as its counsel had not been ruled upon.

Second, in opposing the Claim Objections, the Committee defended the interests of particular creditors in their individual capacity, as opposed to representing the interests of the general unsecured creditor body as a whole. The Committee lacks standing to assert rights on behalf of specific creditors in their individual capacity. The responsibilities of a creditor's committee are enumerated in § 1103(c). A creditor's committee may:

1) [C]onsult with the trustee or debtor in possession concerning the administration of the case;
2) [I]nvestigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and the desirability of the continuance of such business, and any other matter relevant to the case or to the formulation of a plan;

[3] As noted above, the Committee's Employment Application is opposed by the Debtors and the UST.

3) [P]articipate in the formulation of a plan, advise those represented by such committee of such committee's determination as to any plan formulated, and collect and file with the court acceptances or rejections of a plan;
4) [R]equest the appointment of a trustee or examiner under section 1104 of this title; and
5) [P]erform such other services as are in the interest of those represented.

§ 1103(c).

In *In re Anderson*, 349 B.R. 448 (E.D. Va. 2006), the court examined the extent to which a creditor's committee was entitled to participate in a claim objection proceeding. The *Anderson* court found that in connection with the claim objection proceeding, it was appropriate to permit the committee to participate in discovery regarding the debtor in possession's alleged fraud, a matter common to every creditor's claim. *Id.* at 464. The court took care to emphasize that through such participation, "the Committee did not seek, or purport, to assert the rights or claims of any particular Committee member." *Id.* The court noted that the rights of the individual committee members had been asserted by the claimants' counsel, not the committee's counsel. *Id.*

In contrast to *Anderson*, the Committee's opposition to the Claim Objections asserted rights on behalf of particular creditors. That is, the Committee asserted that the claims of particular creditors should be allowed based on the Committee's contention that the Debtors are alter egos of Bonerts. The issue of the Debtors' status as alter egos of Bonerts is not common to all creditors who have filed proofs of claim. The following creditors have filed proofs of claim on account of indebtedness incurred directly by the Debtors:

1) Discover Bank (Claim No. 4);
2) Southern California Edison Company (Claim No. 8);
3) KeyPoint Credit Union (Claim No. 15);
4) Arvest Bank (Claim No. 20); and
5) JH Rose Logistics, LLC (Claim No. 33).

The Committee's advocacy on behalf of specific alter ego creditors was not in the interests of the creditor body as a whole, because allowance of the claims of the alter ego creditors would reduce the recovery of creditors asserting claims directly against the Debtors. Therefore, in electing to oppose the Claim Objections, the Committee was not "fulfilling its primary responsibility to represent the interests" of *all* of its members. *Id.* at 465. *See also In re Drexel Burnham Lambert Grp., Inc.*, 138 B.R. 717, 722 (Bankr. S.D.N.Y.), *aff'd*, 140 B.R. 347 (S.D.N.Y. 1992) ("Counsel for the ... committee do not represent any individual creditor's interest in [a] case; they were retained to represent the entire ... class. Therefore, counsel for the creditors' committee do not owe a duty to [one creditor] to maximize its interest at the expense of the remaining creditors in the represented class."). Where the work performed by the Committee in connection with the Claim Objections was not appropriate, the Committee cannot rely upon having performed that work to support its assertion that it would be prejudiced by the Debtors' Subchapter V election.

B. The Debtors Sought Re-Designation in Good Faith

The Court finds that the Debtors sought re-designation in good faith. In making this finding, the Court rejects the Committee's contention that the Debtors' Subchapter V election was motivated primarily by a desire to divest the Committee of its role in this case. In support of its

argument, the Committee emphasizes that the Debtors did not indicate that they were "small business debtors" (a pre-requisite to electing treatment under Subchapter V) until March 3, 2020, approximately six months subsequent to the Petition Date.

The Debtors have offered a plausible explanation for why they did not initially designate themselves as "small business debtors." As of the Petition Date, the Debtors were not operating a business, and therefore did not believe that the "small business" designation applied. However, a case decided subsequent to SBRA's enactment made clear that the "small business" designation is not limited to a debtor currently engaged in business or commercial activities:

> Although the brief legislative history of the SBRA indicates it was intended to improve the ability of small businesses to reorganize and ultimately remain in business,[6] nothing therein, or in the language of the definition of a small business debtor, limits application to debtors *currently* engaged in business or commercial activities…. [The debtor] is "engaged in commercial or business activities" by addressing residual business debt ….

In re Charles Christopher Wright, No. CA 20-01035-HB, 2020 WL 2193240, at *3 (Bankr. D.S.C. Apr. 27, 2020).

The Court finds that the Debtors' initial decision not to seek a "small business" designation was reasonable given that the Debtors were no longer operating a business and received the majority of their income from Vivien's salary, Michael's Social Security, and passive investments. The Debtors' subsequent re-designation, made in reliance upon subsequent authority clarifying that the "small business" designation is not limited to debtors currently engaged in business operations, was likewise reasonable. The re-designation is appropriate since the majority of the Debtors' liabilities are business debts stemming from their prior operation of Bonert's Inc., a bakery. The Debtors' decisions with respect to the "small business" designation were not motivated by gamesmanship, but rather by the Debtors' understanding of the facts and the law as they existed at the time of each designation.

C. The Debtors Are Not Judicially Estopped From Re-Designating As "Small Business Debtors"

The Committee asserts that the Debtors should be judicially estopped from taking the position that they are "small business debtors." The Court disagrees. Under the doctrine of judicial estoppel, "[w]here a party assumes a certain position in a legal proceeding, and succeeds in maintaining that position, he may not thereafter, simply because his interests have changed, assume a contrary position, especially if it be to the prejudice of the party who has acquiesced in the position formerly taken by him." *New Hampshire v. Maine*, 532 U.S. 742, 749, 121 S. Ct. 1808, 1814, 149 L. Ed. 2d 968 (2001). Judicial estoppel "is an equitable doctrine invoked by a court at its discretion." *Id.* at 750. Invocation of the doctrine is appropriate where "the party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped." *Id.* at 751.

Judicial estoppel does not apply because the Debtors have not gained an unfair advantage or imposed an unfair detriment upon the Committee by designating themselves as "small business debtors" on March 3, 2020. As discussed, when the Debtors filed their Amended Petition containing the "small business" designation, the Committee had been in existence for fewer than two weeks and had not obtained employment of counsel. Therefore, the Committee did not

undertake any significant activities in reliance upon the absence of a "small business" designation.

D. The Debtors' "Small Business" Re-Designation is Not Barred by the Pre-SBRA Provisions of the Bankruptcy Code

The Committee argues that the pre-SBRA version of § 101(51D)(A) bars the Debtors from re-designating as "small business debtors." Under the pre-SBRA version of § 101(51D)(A), a debtor in a case in which a creditor's committee had been appointed could not qualify as a "small business debtor," unless the court "determined that the committee of unsecured creditors is not sufficiently active and representative to provide effective oversight of the debtor." SBRA removed this limitation on which debtors could qualify as "small business debtors."

In determining whether re-designation is authorized, the Court applies the law in effect at the time the Debtors sought re-designation. This is consistent with the approach of courts that have held that debtors who sought bankruptcy protection prior to SBRA's enactment could take advantage of Subchapter V. *See, e.g., In re Moore Properties of Pers. Cty., LLC, Debtor.*, No. 20-80081, 2020 WL 995544, at *5 (Bankr. M.D.N.C. Feb. 28, 2020) (court applied "the law in effect at the time it has been asked to render its decision" to determine whether the debtor was a "small business debtor"); *In re Charles Christopher Wright,* No. CA 20-01035-HB, 2020 WL 2193240 (Bankr. D.S.C. Apr. 27, 2020) (same).

The current version of § 101(51D)(A) does not bar debtors in cases in which a creditor's committee has been appointed from designating themselves as "small business debtors." The fact that the pre-SBRA version of § 101(51D)(A) contained such a bar is not relevant.

E. The Debtors Do Not Exceed the Debt Limit Under § 101(51D)

The Committee contends that the Debtors may not qualify as "small business debtors" because it is possible that their non-contingent debts exceed § 101(51D)'s limit of $2,725,625. The Committee points to a claim asserted by Key Point Credit Union ("Key Point") in the amount of $1,836,000 and a claim asserted by Arvest Bank ("Arvest") in the amount of $2,950,000.

In its proof of claim, Key Point states that its claim against the Debtors is based upon the Debtors' personal guaranty of loans to Beefam LLC and Bonerts MV LLC and is "contingent." Arvest's proof of claim is also based upon the Debtors' personal guaranty of loans to Beefam LLC and Bonerts MV LLC. Arvest states in its proof of claim that its loan was not in default as of the Petition Date.

The Committee argues that the Key Point and Arvest claims may not have been contingent as of the Petition Date, and therefore may count toward the § 101(51D) debt limit, because the Debtors stated in their Schedules that the Key Point and Arvest loans were "presently in non-monetary default" as a result of litigation and the Debtors' Chapter 11 filing. *See* Doc. No. 32 at p. 13. The Committee asserts that it is entitled to discovery regarding the loan documents to ascertain whether the Key Point and Arvest claims were contingent as of the Petition Date.

The Committee's argument overlooks the fact that the § 101(51D) debt limit was raised to $7.5 million by the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act"), 134 Stat. 281 (enacted March 27, 2020). Even if the Key Point and Arvest claims were non-contingent, the Debtors would not exceed the debt limit.

In addition, on the record before it, the Court finds that the Key Point and Arvest claims were contingent as of the Petition Date. The creditors themselves indicate on their proofs of claim that

the claims are contingent. Key Point expressly states that its claim is "contingent," Proof of Claim 15-1 at ¶ 8; Arvest states that the loan guaranteed by the Debtors "was current" as of the Petition Date, Proof of Claim 20-1 at ¶ 9. Michael testifies that the loans giving rise to both claims were "not in default prior to the filing of the instant case" and that Beefam LLC and Bonerts MV LLC "remain current" on the loans. Declaration of Michael Bonert [Doc. No. 264] at ¶ 2. The Committee's speculation that the claims might be non-contingent cannot overcome this clear evidence to the contrary.

F. The Passage of Certain Deadlines Does Not Prevent this Case from Proceeding Under Subchapter V

The Committee maintains that this case cannot proceed under Subchapter V because it is not possible for the Debtors to comply with certain deadlines, such as filing a plan within 90 days of the order for relief as required by § 1189(b) or attending a status conference to be held within 60 days of the order for relief as required by § 1188(a).

The passage of these deadlines does not prevent the case from proceeding under Subchapter V. As noted previously, in *In re Ventura*, the court allowed the debtor to proceed under Subchapter V, even though the debtor's petition had been filed fifteen months prior to the effective date of SBRA and both the debtor and a creditor had filed competing plans of reorganization. *Ventura*, 2020 WL 1867898, at *2–4. Relying upon §§ 1188(b) and 1189(b), which provide that the status conference and plan filing deadlines may be extended "if the need for an extension is attributable to circumstances for which the debtor should not justly be held accountable," the *Ventura* court found it appropriate to extend the deadlines that were impossible for the debtor to meet. *Id.* at *8.

For the same reason, the Court finds extension of the status conference and plan filing deadlines to be warranted here. As held in *Ventura*, the Debtors are "not required to comply with deadlines that clearly expired before the Debtor[s] could have elected to proceed" under Subchapter V. *Id.*

III. Conclusion

Based upon the foregoing, the Committee's opposition to the Debtors' Subchapter V election is **OVERRULED**. The Court will enter an order consistent with this Memorandum of Decision.

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Date: June 3, 2020

Ernest M. Robles
United States Bankruptcy Judge