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Creditors can Fight Back even in Sub-Chapter V Bankruptcy Cases.

Greetings Credit and Collection Practitioners! In this edition of "The Credit Times," we feature an article written by Wanda Borges, principal member of the collection law firm, Borges & Associates, LLC.

Wanda is also a board member for the International Association of Commercial Collectors (IACC) and a frequent speaker, contributor and panelist throughout the credit and collection community.

In this article, Wanda speaks about how creditors can protect themselves in Subchapter V bankruptcy cases. For those who are not familiar , Subchapter V took effect in February of 2020 and this section of the US Bankruptcy Code is specifically designed to allow small businesses to reorganize efficiently and in a cost-effective manner.

We hope you find Wanda's insight at how a creditor might protect themselves in this scenario useful for you organization.

~Chad Haynie, EVP Global Revenue, CCC of NY

Creditors can Fight Back even in Sub-Chapter V Bankruptcy Cases.

By: Wanda Borges, Esq.
Borges & Associates LLC

What do you do when you think you've done everything right and you still get stuck with a seemingly uncollectible claim?
You are a diligent Credit Manager! You have a credit application. Your documents are in good order. And you have a personal guarantee. You are confident that Commercial Collection Corporation of NY, Inc. (CCC of NY), together with a good attorney, can recover your debt. Then you receive notice that the corporate debtor has filed a sub-Chapter V bankruptcy petition. You are aware that you have to file a proof of claim. Fortunately, the law firm that was recommended by CCC of NY handles both collection and bankruptcy matters. You are glad that you have the personal guarantee and anticipate collecting from that guarantor. Well, here is a recent experience where the Sub-Chapter V debtor tried to insulate the personal guarantor AND LOST!

In its Plan of Reorganization, the debtor proposed to pay general unsecured creditors from a pool of funds over a period of five (5) years. The pro rata share for each creditor would yield about an eight (8%) distribution. In the Plan, the Debtor included exculpation provisions, discharge provisions and an Injunction for the five-year payment period. We were compelled to file an Objection to Confirmation on various grounds. First and foremost, the recent decision in the Purdue Pharma case by the Supreme Court of the United States said that third-parties (i.e. the personal guarantor) cannot be released in a chapter 11 plan unless the creditor absolutely agrees to it. Although debtor's counsel insisted that he was not attempting to release the guarantor, we asserted that the exculpation provision was merely a thinly-disguised release. The Debtor fixed the exculpation provision so that it only protected fiduciaries of the corporate debtor with respect to anything they did within the chapter 11 proceeding. We also objected that the broadly worded discharge provision would enable a state court to find that the debt owed was completely wiped out by the chapter 11 provision thereby making the personal guarantee meaningless. The Debtor changed that to make it clear that only the corporate debtor was discharged and no guarantor.

This left the injunction. The Debtor claimed that the President of the Company, who happened to be the personal guarantor, needed the entire five (5) years of the plan to concentrate on rebuilding the company and should not be burdened with having to defend against a personal guarantee lawsuit in a state court. In February 2025, a decision came out of the U.S. Bankruptcy Court for the Southern District of New York that granted such an injunction in a small business case. So, Debtor's counsel thought he had a slam-dunk. Upon first reading the decision, my reaction was "Oh Shoot, I may lose!" Nevertheless, we briefed the issue and participated in a full day trial on the issue of an injunction and the court reserved decision. We acknowledged that the principal should be entitled to some short period of time to turn the company around but argued that five (5) years was much too long The Court agreed with us. The Court allowed the Debtor to confirm a Plan that provides for a four (4) month injunction. In addition, the Court directed the personal guarantor to submit to us all of its personal financial records; and issued an order that during the four (4) month period of time, the guarantor is prohibited from transferring any of its assets to any person or entity whatsoever.

In this instance, if the creditor had simply given up, it would have ended up with an eight (8%) return in the Bankruptcy Case and possibly an uncollectible debt from an assetless guarantor five (5) years from now.

We don't yet know the outcome. However, this story is a classic lesson for creditors not to give up. When you receive a bankruptcy notice, immediately let CCC of NY know so that they can contact the appropriate bankruptcy counsel who will investigate every possible scenario to protect your interests. This is only one of several examples of how a creditor working with a reputable agency like CCC of NY as well as bankruptcy counsel, can obtain a favorable and positive result for the creditor.

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