University of Miami International and Comparative Law Review

Volume 27
Issue 2 *Spring 2020*

Article 4

7-7-2020

Small Business and Bankruptcy: Recent Changes in Kosovo and the United States Compared

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* Professor of Bankruptcy Law and Practice, Northwestern Pritzker School of Law. Many thanks are due to the many research assistants who helped make this a better paper. In particular, thanks are due to Heidi Hockberger, Brian Valcarce, Khadija Lalani, and Melissa Sanchez. Errors which remain are mine alone.
The author was the principal reporter for the working group to revise Kosovo's bankruptcy law, under the auspices of his work with Checchi and Company Consulting, Inc., a USAID contractor. Thanks are due to James Agee of Checchi for his help and assistance, and to Ardi Shita for his logistical and legal help in Kosovo.

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I. INTRODUCTION

Small and Medium Enterprises (SMEs) are ubiquitous. In the United States, small businesses account for 99.7% of all employers, and about 47.3% of private sector employment.[1] *In the European Union (EU) non-financial business sector, SMEs accounted for 99.8% of all enterprises.*[2] *These enterprises employed almost ninety-eight million people—66.6% of total employment—in the EU.*[3]

SMEs are variously defined. In the United States, until recently the definition of an SME was an enterprise that employed less than 500 individuals.[4] *In the EU, SMEs are defined as businesses which employ less than 250 staff and have an annual turnover of less than €50 million, or whose balance sheet total is less than €43 million.*[5]

This paper focuses on the smaller end of this scale: the micro SMEs. In the EU, a micro SME has ten or fewer employees, and

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1 UNITED STATES SMALL BUSINESS ADMINISTRATION, OFFICE OF ADVOCACY, FREQUENTLY ASKED QUESTIONS (Sept. 2019), https://cdn.advocacy.sba.gov/wp-content/uploads/2019/09/24153946/Frequently-Asked-Questions-Small-Business-2019-1.pdf, at 1 [hereafter "SBA FAQs"].

2 EUROPEAN COMM'N, EXECUTIVE AGENCY FOR SMALL AND MEDIUM-SIZED ENTERPRISES (EASME), ANNUAL REPORT ON EUROPEAN SMES 2018/2019, RESEARCH & DEVELOPMENT AND INNOVATION BY SMES, at 11 (2019).

3 *Id.* at 17.

4 SBA FAQs, *supra* note 1, at 1. Recently, the United States Small Business Administration significantly changed the definition by providing different metrics depending on what industry the business is in. Businesses in the mining trade, for example, may have up to 1,500 employees and still be classified as a small business, while others, such as new car dealers, are capped at 200 employees. *See* 13 C.F.R. § 121.201 (2019).

5 EUROPEAN COMM'N, *supra* note 2, at 16.

either less than €2 million in turnover, or fewer than €2 million in assets on their balance sheet.[6] *Almost all SMEs (93%) in the EU are micro SMEs.*[7] *The number is similar in the US. If sole proprietors (technically not employees) are added in, the percentage of firms with no more than 20 employees rises to 98%.*[8]

The point is that the bulk of all businesses are small. The question this paper asks is whether small businesses are more financially fragile and prone to failure than larger businesses, and if so, if there is any workable legislative response.

II. SHOULD WE EXPECT HIGHER RATES OF FAILURE FOR SMES?

Business failure is a constant. Approximately half of all businesses started die within five years;[9] two thirds don't make it to ten.[10] Within that failure group, SMEs are well represented. Compared with large firms, European SMEs in general are more leveraged and reliant on bank financing and have significantly higher non-performing loan (NPL) ratios.[11] Over the last few years, SME borrowing rates have not declined

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[6] *Id.*

[7] *Id.* at 19.

[8] Small Business and Entrepreneurship Council, Small Business Facts, http://sbecouncil.org/about-us/facts-and-data/ (last visited Jan. 18, 2020).

[9] Bahar Öztürk & Mico Mrkaic, *SMEs' Access to Finance in the Euro Area: What Helps or Hampers?,* at 5 (IMF Working Paper, May 2014), https://www.imf.org/external/pubs/ft/wp/2014/wp1478.pdf; Hartmut Schrör, *Business Demography: Employment and Survival, Eurostat, 70/2009* (2009), http://ec.europa.eu/eurostat/documents/3433488/5284008/KS-SF-09-070-EN.PDF/d43f5156-61fb-4f3a-8bd7-e6902e48c8de; COMMISSION TO STUDY THE REFORM OF CHAPTER 11, AMERICAN BANKRUPTCY INSTITUTE, FINAL REPORT AND RECOMMENDATIONS 277 (2014), https://abiworld.box.com/s/vvircv5xv83aavl4dp4h (reprinting data from the Bureau of Labor Statistics).

[10] SBA FAQs, *supra* note 1, at 2; COMMISSION TO STUDY THE REFORM OF CHAPTER 11, AMERICAN BANKRUPTCY INSTITUTE, FINAL REPORT AND RECOMMENDATIONS 277 (2014), https://abiworld.box.com/s/vvircv5xv83aavl4dp4h (reprinting data from the Bureau of Labor Statistics).

[11] WOLFGANG BERGTHALER, KENNETH KANG, YAN LIU, AND DERMOT MONAGHAN, TACKLING SMALL AND MEDIUM SIZED ENTERPRISE PROBLEM LOANS IN EUROPE 6 (IMF Staff Discussion Note, March 2015), https://www.imf.org/external/pubs/ft/sdn/2015/sdn1504.pdf

as much as yields on sovereign bonds, and remain high compared with those for large firms.[12]

These failures don't often result in court-supervised bankruptcies. Indeed, as Professor Edward Morrison has noted, the vast majority of SME failures are handled privately, without the need for a collective action involving all creditors.[13]

But some SMEs might be good candidates for rescue. Given the sheer number of such businesses, it is not a stretch to say that insolvency law should at least attempt to respond to viable small, or even micro, SMEs.

III. RECENT EFFORTS TO DOCUMENT AND ADDRESS TREATMENT OF SMEs IN INSOLVENCY

There have been many government efforts at addressing SME failure over the last thirty years, usually at the administrative and non-bankruptcy level. These efforts have included government-sponsored guaranties, as well as some tax incentives. They have also included government direction to asset management companies on how to deal with SME defaults if SME loans wind up being held by an asset management company.

a. Efforts Outside the United States

Recent scholarship by the World Bank has described these efforts in The Netherlands, Spain, Germany, Sweden, Argentina, India, Greece, the OHADA countries, and the Republic of Korea.[14] The International

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[12] *Id.*

[13] Edward R. Morrison, *Bargaining Around Bankruptcy: Small Business Workouts and State Law*, 38 J. LEGAL STUD. 255, 256 (2009) (stating that in 2003, about 540,000 small businesses closed their doors but only 34,000 filed for bankruptcy and that the "vast majority of small businesses resolve distress under state law"); Edward R. Morrison, *Bankruptcy's Rarity: Small Business Workouts in the United States*, 5 EURO. CO. & FIN. L. REV. 172, 175 (2008) (asserting that federal bankruptcy filings account for only three to four percent of all business closures).

[14] *See generally* WORLD BANK GROUP, INSOLVENCY AND CREDITOR/DEBTOR REGIMES TASK FORCE, WORKING GROUP ON THE TREATMENT OF MSME INSOLVENCY, SAVING ENTREPRENEURS, SAVING ENTERPRISES: PROPOSALS ON THE TREATMENT OF MSME INSOLVENCY (2018), http://documents.worldbank.org/curated/en/989581537265261393/Saving-Entrepreneurs-Saving-Enterprises-Proposals-on-the-Treatment-of-MSME-Insolvency.

Monetary Fund has chronicled similar efforts in Indonesia, Japan, the Republic of Korea, Malaysia, Thailand, and Turkey.[15]

b. United States Reforms — 2019

In the midst of these varied examinations, the United States recently revised its insolvency treatment of SMEs. On August 23, 2019, the President signed the Small Business Reorganization Act of 2019.[16] This Act, effective February 19, 2020,[17] added Subchapter V to Chapter 11, thereby significantly changing the reorganization process for many small debtors. Early estimates calculate that the Act will affect more than 40% of all Chapter 11 filings in the United States.[18]

The Act begins this change by redefining the term "small business debtor" contained in Section 101(51D).[19] Under this change,[20] a small business debtor will be any business entity, including a sole proprietorship:

- That has no more than $2,725,625[21] in aggregate noncontingent liquidated secured and unsecured debts (not counting debts owed to affiliates);
- That is not a member of a group of affiliated debtors (e.g., a corporate group) whose aggregate debts exceed the $2,725,625 debt limit; and
- Whose aggregate debts are derived at least 50% from the debtor's "commercial or business activities."[22]

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[15] *See generally* BERGTHALER ET AL., *supra* note 11, at 28-30.
[16] Small Business Reorganization Act § 5, Pub. L. 116-54, 133 Stat. 1079 (2019).
[17] *Id.* at 1087.
[18] Robert Lawless, *How Many New Small Business Chapter 11s?*, CREDIT SLIPS BLOG (Sept. 14, 2019, 4:28 PM), https://www.creditslips.org/creditslips/2019/09/how-many-new-small-business-chapter-11s.html.
[19] 11 U.S.C. § 101(51D) (2012).
[20] Small Business Reorganization Act, § 4, Pub. L. 116-54, 133 Stat. 1079, 1085 (2019).
[21] This amount will continue to be inflation-indexed under 11 U.S.C. § 104.
[22] 11 U.S.C. § 101(51D) (2012) (the debtor cannot be a person whose primary activity is the business of owning single asset real estate).

These limitations are for insolvency purposes only. They make no reference to, and are independent from, the definition of small business used by the Small Business Administration.[23]

If the debtor qualifies as a "small business debtor," it may elect to have Subchapter V apply to it,[24] with the election to be made on the bankruptcy petition itself.[25] Once an election is made, there are many significant changes and differences from regular chapter 11. They include:

- No creditors' committee;[26]
- Relaxed disinterested rules for professionals hired by the debtor;[27]
- An exclusive right by the debtor to file a plan;[28] and
- The appointment of, and an increased role for, a trustee.[29] Initially, a trustee will be appointed in all Subchapter V cases to facilitate reorganization.[30] Thereafter, a trustee will remain with the debtor at least until consensual confirmation.[31]

In addition, Congress designed cases under Subchapter V to move quickly. Among the provisions expediting the case are provisions that require:

- The court to hold a status conference on the case within 60 days of the case's filing;[32]

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[23] *See* SBA FAQs, *supra* note 1.
[24] 11 U.S.C § 103(i) (2012).
[25] UNITED STATES COURTS, VOLUNTARY PETITION FOR INDIVIDUALS FILING FOR BANKRUPTCY (2020), https://www.uscourts.gov/forms/individual-debtors/voluntary-petition-individuals-filing-bankruptcy.
[26] 11 U.S.C. § 1102(a)(3) (2018) (there is an exception if the court finds cause to appoint a committee).
[27] 11 U.S.C. § 1195 (2018) (this section permits retained professionals to have up to $10,000 in prepetition claims against the debtor and still qualify as disinterested).
[28] 11 U.S.C. § 1189(a) (2018).
[29] 11 U.S.C. § 1183 (2018).
[30] 11 U.S.C. § 1183(b)(7) (2018).
[31] 11 U.S.C. § 1183(c)(1) (2018).
[32] 11 U.S.C. § 1188(a) (2018).

- The debtor, within 14 days before the status conference, to file a report on its plans and progress of the plan;[33] and
- The debtor to file a plan within 90 days of the commencement of the case.[34]

A plan under Subchapter V is subject to most of the rules applicable to regular chapter 11 plans. Differences exist, however with respect to the manner in which a Subchapter V debtor's plan is confirmed.

Under Subchapter V, confirmation comes in two forms: consensual or nonconsensual. The consequences of each are quite different.

Confirmation of a consensual plan (a plan accepted by all classes of creditors) results in the normal consequences of a chapter 11 plan. These include:

- the debtor's immediate discharge, even if an individual;[35]
- the simultaneous revesting of all estate property in the debtor;[36] and
- the discharge of the Subchapter V trustee.[37]

Nonconsensual confirmation, however, has significantly different consequences. Initially, unlike regular Chapter 11, a debtor need not obtain the acceptance of all classes; Subchapter V does not incorporate Section 1129(a)(10)'s requirement of one consenting class.[38] Individual debtors are not subjected to the five-year disposable income test of Section 1129(a)(15).[39]

More significantly, while Subchapter V imposes the same limitations on the fair and equitable treatment of secured creditors as are imposed by regular Chapter 11,[40] Subchapter V permits the debtor to alter the rules generally applicable to unsecured creditors. In particular, it allows

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33 11 U.S.C. § 1188(c) (2018).
34 11 U.S.C. § 1189(b) (2019).
35 11 U.S.C. § 1141(d)(2) (2010). *See* Section 1183 that specifically excludes the delayed discharge for individuals found in 11 U.S.C. § 1141(d)(5).
36 11 U.S.C. § 1141(b)(2) (2010).
37 11 U.S.C. § 1183(c)(1) (2019).
38 11 U.S.C. § 1191(b) (2019).
39 11 U.S.C. § 1191(a) (2019).
40 11 U.S.C. § 1191(c)(1) (2019).

abrogation of the absolute priority rule. Subchapter V provides that a debtor may satisfy the fair and equitable requirement as to unsecured creditors—the source of the absolute priority rule—by providing them payments equal to three to five years of the debtor's future disposable income; it can make these payments as a lump sum, in periodic payments, or through a combination of both.[41] Put another way, the debtor's equity owners (or the debtor, if he or she is an individual) may keep their ownership interests despite not paying all of their unsecured debts in full so long as the plan provides for payments to unsecured creditors equal to three to five years' worth of their disposable income.

The concept of disposable income is based upon similar concepts in Chapters 12 and 13. In Subchapter V, the term "disposable income" is defined, for non-individual debtors, as the debtor's income less "the payment of expenditures necessary for the continuation, preservation, or operation of the business of the debtor."[42] For individual debtors, "disposable income" is income less amounts "reasonably necessary to be expended . . . [f]or . . . the maintenance or support of the debtor or a dependent of the debtor; or . . . a domestic support obligation that first becomes payable after the date of the filing of the petition"[43]

Additionally, to confirm its plan, the debtor must also show it can make the payments scheduled in the plan and, in some cases, provide for alternate consequences (such as the sale of non-exempt property) if it can't.[44]

In addition, if the debtor confirms a plan non-consensually:

- The trustee is kept in place to monitor the debtor until the end of the payment plan;
- The trustee coordinates and disburses plan payments;[45] and
- The debtor's discharge is delayed until all scheduled payments have been made.[46]

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[41] 11 U.S.C. § 1191(c)(2) (2019).
[42] 11 U.S.C. § 1191(d)(2) (2019).
[43] 11 U.S.C. § 1191(d)(1) (2019).
[44] 11 U.S.C. § 1191(c)(3) (2019).
[45] 11 U.S.C. § 1194(b) (2019).
[46] 11 U.S.C. § 1192.

Small business debtors who do not elect treatment under Subchapter V will receive the treatment given to qualifying SMEs from 1994 to 2020: increased reporting burdens and an accelerated the confirmation process.[47]

An alternate treatment exists for sole proprietors who qualify for Chapter 13. Chapter 13 allows for modification of business debts and adjustment of business secured debts. It has debt limits,[48] however, and these limits hamper its usefulness as a business reorganization device. This is evidenced by the fact that only 1,769 individual chapter 13 business cases were filed in the twelve months ending September 30, 2019.[49]

IV. SIGNIFICANT CONSIDERATIONS IN DRAFTING SME BANKRUPTCY PROVISIONS

There have been many studies and articles regarding SME bankruptcy.[50] In addition, the problem of SME insolvency has inspired seven eminent scholars to suggest a "modular" approach to SME

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[47] *See, e.g.,* 11 U.S.C. §§ 1116 (reporting requirements), 112(e) (exclusivity requirements) & 1129(e) (confirmation requirements). *See also* "United States Approach," *infra* at page 9.

[48] A chapter 13 debtor may not have more than $419,275 in uncontested and mature unsecured debt, and no more than $1,257,850 in uncontested and mature secured debt.

[49] Table F-2, U.S. Bankruptcy Courts—Business and Nonbusiness Cases Commenced, by Chapter of the Bankruptcy Code, During the 12-Month Period Ending September 30, 2019, *available at* https://www.uscourts.gov/file/26761/download. This can be compared to the 284,258 consumer cases filed under chapter 13 during the same period. *Id*.

[50] In addition to the articles already cited, see Michelle M. Harner, *Are Small- And Medium-Sized Companies Worth Saving?*, 34 AM. BANKR. INST. J. 7 (July 2015); Edward R. Morrison, *Bargaining Around Bankruptcy: Small Business Workouts and State Law*, 38 J. LEG. STUD. 255 (2009); Donald R. Korobkin, *Vulnerability, Survival, and the Problem of Small Business Bankruptcy*, 23 CAP. U. L. REV. 413, 426–27 (1994) ("Larger businesses also tend to have more operational flexibility, and sometimes may weather economic slow-downs by shifting from one product line to another, or from one geographical area to another. In contrast, small businesses are less likely to have cash reserves, and they are generally undiversified in their products and customer base. Furthermore, small businesses are often in industries characterized by intense price competition. During inflationary times, they may not have the luxury of raising prices in order to compensate for rising operating expenses. Meanwhile, regulatory burdens and tax increases hit small business the hardest, depleting severely limited working capital.") (citations omitted); EUROPEAN COMM'N, ENTERPRISE AND INDUSTRY DIRECTORATE-GENERAL, FINAL REPORT OF THE EXPERT GROUP, A SECOND CHANCE FOR ENTREPRENEURS: PREVENTION OF BANKRUPTCY, SIMPLIFICATION OF BANKRUPTCY PROCEDURES AND SUPPORT FOR A FRESH START (2011), http://ec.europa.eu/DocsRoom/documents/10451/attachments/1/translations/en/renditions/native.

insolvency.[51] These reform efforts have not, with the possible exception of Japan, led to many efforts to craft lasting legislative solutions through better in-court procedures. And those that have tried, have had mixed success. A number of countries have introduced simplified procedures for SMEs in their general insolvency regimes (Germany, Greece, Slovenia, Spain) or special processes (Italy).[52] The Italian over-indebtedness agreement (*concordato preventivo*) is "specifically designed for micro and small SMEs and is part of the in-court toolkit. It involves a stay and a majority voting process (60 percent of creditors in value)." [53]

In designing statutes for insolvent SMEs, it is relevant to note the differences between SMEs and larger and more mature businesses. SMEs tend to have more bank debt and be more highly leveraged.[54] Although they sometimes have assets that can be used as collateral, the quantity and perceived quality of the collateral may be of lesser desirability.[55] They tend to use guaranties more, and the guaranties tend to be from friends and relatives.

Added to this is a central puzzle—to the extent that the business is entrepreneurial, there is a fuzzy line between the entrepreneur and the business. This has legal and business consequences. The owner is often the heart of the business' assets yet cannot (we hope) be collateralized and liquidated in the same way that a pure corporation's assets can be realized. Legal recourse is often clouded by whether the entrepreneur/owner has selected a limited liability vehicle for the business, or whether he or she has remained a sole proprietor (or has given guaranties of the debtor of a wholly-owned entity that essentially expose the owner's assets to a particular creditor the same as if he or she has remained a sole proprietor). Added to this mix is the relative fragility of an SME's finances, which are

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[51] RONALD DAVIS, STEPHAN MADAUS, ALBERTO MAZZONI, IRIS MEVORACH, RIZWAAN J. MOKAL, BARBARA ROMAINE, JANIS SARRA & IGNACIO TIRADO, MICRO, SMALL, AND MEDIUM ENTERPRISE INSOLVENCY (Oxford Univ. Press 2018).

[52] BERGENTHALER, *supra* note 11, at 11.

[53] *Id*.

[54] HIGH LEVEL EXPERT GROUP ON SME AND INFRASTRUCTURE FINANCING, FINANCE FOR GROWTH 5 (2013) ("In general, young and small companies face larger obstacles to accessing finance and, once they do, they rely heavily on bank debt and pay higher financing costs."), http://www.d20-ltic.org/images/hleg_report_2013.pdf [hereinafter *HLEG Report*].

[55] ORGANIZATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, FINANCING SMEs AND ENTREPRENEURS 2014: AN OECD SCOREBOARD 37-38 (2014), http://www.keepeek.com/Digital-Asset-Management/oecd/industry-and-services/financing-smes-and-entrepreneurs-2014_fin_sme_ent-2014-en.

often unable to handle the added costs that restructuring professionals require.

From this, there are some standard tropes that need to be considered when drafting legislation. Costs should be reduced, and the most common way to keep costs low is to simplify and speed up the process. So too is the taint of bankruptcy. In the small world in which SMEs operate, failure reverberates. One SME's failure to pay is often another SME's lost revenue, and nonpayment often results in a grudge.

But perhaps the most perplexing, and potentially emotional, issue is an economic one: many SMEs are simply not viable. Despite its owners' wishes, it should not receive assistance to survive; doing so only diverts resources and time away from otherwise viable businesses.[56]

V. ELEMENTS OF A SUCCESSFUL SME APPROACH

This background suggests certain elements of a legislative response to SME insolvency. First, the process must acknowledge that many SMEs simply do not merit rescue, and thus procedures should be in place to conduct "triage" on entities who file to test whether they deserve the court's scarce time. Second, creditors' expectations of a recovery must be addressed, and clear indications of entitlements on insolvency should be set. Finally, given the overlapping identity between the entrepreneur and his or her business, there should be relief available not only for the legal form of the business, but also for the owners of the business.

On the first point, sorting the meritorious from the detritus is a daunting task. Feasibility analysis is rarely simple, and generally requires more than superficial knowledge of a debtor's finances. The cost of an independent review of these finances is thus typically equally as daunting. There does, however, exist a rough proxy that can be used. As noted above, SMEs use bank financing to a higher degree than most other businesses.[57] Before extending this credit, the bank generally examines the debtor's finances in much the same way a screening mechanism would for an insolvency procedure. As an SME encounters business problems, a bank is generally monitoring the effect of these challenges on its existing analysis of the SME's viability. Finally, if new financing is required to meet the challenge, the bank is typically the only source of such funds.

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[56] *See* Michelle M. Harner, *Are Small- And Medium-Sized Companies Worth Saving?*, 34 AM. BANKR. INST. J. 8 (July 2015); Morrison, *supra* note 13.

[57] *HLEG Report*, *supra* note 54.

These generalizations suggest that the feasibility of the rescue of an SME is often assessed by the involved financial institution; indeed, as it is likely the only source of exit financing, that financial institution will control whether the SME reorganizes, or liquidates. As a consequence, the willingness of an SME's bank to go forward is an available, and likely necessary, proxy for the feasibility and viability of an SME reorganization.

The second point—the plight of other creditors—must also be taken into account. These creditors also have a role in recovery. Their willingness to continue to extend credit may be a factor in whether the business can survive. But what can these other, non-bank creditors, expect? They likely understand that the support of a bank or other financial institution will be necessary for the survival of a debtor. They also know that banks will put their own interests first. But they do not typically expect that a bank will run a debtor's business solely for the bank's own benefit; that is, legitimate self-interest ends with debt repayment. This roughly translates into an expectation that adjustment of non-bank creditors' debts will not be so radical as to deprive them of what they would have received if the debtor had simply closed up shop and liquidated. In short, non-bank creditors have a legitimate interest in tolerating a reorganization only if it returns to them at least what they would have received in a liquidation. This so-called "best interest" test is often a touchstone of any reorganization. In SME reorganization, however, it may have lesser significance, as the result of an SME liquidation is usually zero return to non-bank creditors – thus making the "best interest" test somewhat easily met.

Finally, the legislation must address the interests of the SME's ownership. If there is value in the SME left after debts are paid, that value must be preserved. More likely, however, either directly or through guaranties, the owner will be liable for various business-related debts. The owner must have some ability, beyond private order negotiation, to deal with such debt, either through the availability of proceedings offering a debt discharge, or through direct cancellation of the debt.

VI. UNITED STATES APPROACH

For many years, the approach of the United States was constricted. Small business bankruptcies were essentially treated as a nuisance – a breeding ground for sloth and delay.[58] Following these assumptions, the 2005 amendments to the United States' Bankruptcy Code imposed greater reporting requirements,[59] speedier confirmation requirements,[60] and Draconian consequences for those small businesses that found it necessary to file for bankruptcy again within two years of their earlier case.[61]

This approach changed in 2019. While the new Subchapter V remedy still requires some speed,[62] it relaxes the strict time limits previously imposed. It also permits the abrogation of the absolute priority rule[63] – a boon to sole proprietors – and it introduces the ideas of a standing trustee to monitor the debtor activities.[64] Finally, if a plan is consensually confirmed, this monitor is dismissed, allowing the debtor's creditor body to deal consensually and unilaterally with the restructured debtor.[65]

VII. KOSOVO'S APPROACH

Many of these innovations were anticipated four years ago when Kosovo, a country deep in the Balkans, revised its bankruptcy law.[66] Kosovo is a country of about 1.85 million people.[67] About 64% of all businesses have some form of bank financing, with 23% of all firms using bank loans for working capital finance.[68] Most of the credit is on a secured

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[58] *See, e.g.*, Hon. Edith H. Jones, *Chapter 11: A Death Penalty for Debtor and Creditor Interests*, 77 CORNELL L. REV. 1088, 1089 (1992) ("Chapter 11 is more an intensive-care ward (or mortuary) than a healing potion for sick businesses.").

[59] *See, e.g.*, 11 U.S.C. §§ 308, 1116 (2005).

[60] *See, e.g.*, 11 U.S.C. § 1129(e) (2005).

[61] *See, e.g.*, 11 U.S.C. § 362(n) (2005).

[62] § 2(a), 133 Stat. at 1081 (codified at 11 U.S.C. § 1189(b)(The debtor has to file a plan within 90 days of the commencement of the case).

[63] *Id*. at 1082 (codified at 11 U.S.C. § 1191(c)(2).

[64] *Id*. at 1079 (codified at 11 U.S.C. § 1183).

[65] *Id*. at 1079 (codified at 11 U.S.C. § 1183(c)(1).

[66] The new law was passed by the Kosovo legislature on June 9, 2016, and published in the Kosovo Official Gazette on July 7, 2016, with an effective date of July 22, 2016. Law No. 05/L-083 On Bankruptcy, 07.07.2016 XK. The relevant SME provisions of the Kosovo Law are reprinted in the appendix.

[67] The World Bank, *Kosovo*, http://data.worldbank.org/country/kosovo (last visited Jan. 17, 2020).

[68] OECD, EUROPEAN TRADING FOUNDATION, EUROPEAN UNION AND EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT, SME POLICY INDEX: WESTERN BALKANS AND TURKEY 2019: ASSESSING THE IMPLEMENTATION OF THE SMALL BUSINESS ACT FOR EUROPE, at 636 (2019), https://doi.org/10.1787/g2g9fa9a-en; THE WORLD BANK, INTERNATIONAL

basis, or supported by several personal guaranties. It is a relatively poor country, with almost 18% of its population living in poverty.[69] Until 2016, it had no bankruptcy law; well, it had a bankruptcy law, but its drafting left holes to be filled by regulations. Those regulations were never written.

In drafting the law, the working group responsible for shepherding the legislation expressed an interest in an expedited procedure for SMEs. That procedure was drafted as Chapter II of the law, and its text appears as an appendix.

a. *Kosovo's SME Definition and Election to be Treated as a SME*

SMEs were designated as businesses (which in Kosovo can be legal entities or individual sole proprietors) that have 25 or fewer employees and less than €1,000,000 in turnover.[70]

If the debtor qualifies, then it can make an election to be treated under the special SME rules. The election to be treated under the SME rules must be made within ten days of opening the case.[71] Even if it does elect, however, most of the reorganization provisions will still apply unless otherwise stated.[72] For example, one rule that has been kept the same in both types of cases is the best interest of creditors test: a plan proponent must show that the property distributed and to be distributed under the plan must, for every creditor, equal or exceed what that creditor would have received had the case been a liquidation case.[73]

b. *Kosovo's Focus On Reorganization Speed*

If the debtor elects the SME treatment, there are several key differences from the regular reorganization procedure. Initially, the first difference in an SME case is its speed. An SME should file a plan within

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FINANCE CORPORATION, ENTERPRISE SURVEY, KOSOVO, REPUBLIC OF, COUNTRY PROFILE 2013, at 13 (2013), https://www.enterprisesurveys.org/content/dam/enterprisesurveys/documents/country-profiles/Kosovo-2013.pdf.

[69] The World Bank, *supra* note 67.

[70] Law No. 05/L-083 art. 11.

[71] *Id*. art. 14.1.1.

[72] *Id*. art. 12.1.

[73] *Id*. art. 14.1.5 (Articles 79.1.4.1 & .2 deal with feasibility for non-SME cases, and require that "confirmation of the plan of reorganization is not likely to be followed by the need for the filing of a subsequent case under this Law; and [¶] all payments and distributions under the plan of reorganization will be timely made . . . .").

thirty days of the case's opening, and upon request of a party in interest, the court must dismiss the case if no plan is confirmed within sixty days from time of filing.[74]

c. *Kosovo's Adoption of a Monitor*

A second difference is that in each SME case the court appoints a monitor,[75] chosen from regular liquidation case administrators. This monitor consults with the debtor as to business issues and as to the content of any plan to be filed.[76] The monitor is also responsible for assessing the feasibility of the plan.[77]

d. *Kosovo's Radical Alteration of Traditional Creditor Voting*

Voting requirements signify a third difference. Unlike the simple majority rules for regular reorganizations,[78] the court will confirm an SME plan only if 75% of all secured classes voting approve, and at least 33% of all unsecured classes voting approve.[79] This somewhat unusual voting was motivated by the realization that SMEs will not survive in Kosovo without the support of their bank or other secured creditor. Colloquially, cramming down bank debt for SMEs is not realistic. The low amount set for unsecured classes reflects the need for some support, but if three-quarters or more of secured creditors support the plan, and if the best interest of creditors test is met (which is also a requirement),[80] then unsecured creditors have been protected.

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[74] *Id*. arts. 12.2, 12.4.
[75] *Id*. art. 13.
[76] *Id*. art. 13.4.
[77] *Id*. art. 13.5 (The bankruptcy bill as originally drafted had a separate definition of feasibility. Unless displaced by other SME provisions, feasibility was defined "as a condition of confirmation of a plan of reorganization, means that confirmation of the plan is not likely to be followed by the need for further financial reorganization or liquidation (unless the plan calls for liquidation). Unless otherwise specified, the plan proponent has the burden of proving that a plan is feasible, and must meet that burden by a preponderance of the evidence." This provision was omitted when the Kosovo legislature adopted the law).
[78] *Id*. art. 78.1.
[79] *Id*. art. 14.1.3.
[80] *Id*. art. 14.5.

e. *Kosovo's Major Change: A Different Approach to Determining Feasibility*

A fourth difference is how to satisfy the requirement of feasibility. This can be met in four different ways.[81]

First, if there is unanimous support from all secured creditor classes, the plan is deemed feasible.[82] The thinking behind this is that if all banks (or if the only bank) support the plan, then their self-interest can serve as a rough proxy for future feasibility.

Second, once the debtor decides to ballot creditors, the monitor is required to perform his or her own feasibility assessment.[83] As monitors are drawn from the pool of bankruptcy administrators (who will have to comply with various ethical and financial standards),[84] they should have familiarity with such determinations. At this point, however, the effect of the monitor's response is flipped from the traditional role: the monitor reports only if he or she believes that the plan is *not* feasible.[85] Silence in this case is treated as a tacit approval of the plan's feasibility.[86] This option was chosen to conserve costs. If the debtor has its bank's approval, there is little reason for the monitor to say "me too" coupled with an extensive and expensive justification. Silence thus effectively communicates agreement.

Third, if the unsecured creditors approve the plan by a 50% margin, feasibility is again deemed to be present.[87] The basis for this method is that because unsecured creditors have the protection of the best interest test, any vote is really over the allocation of the going-concern surplus. Traditionally, the going-concern surplus has been decided and divided by majority vote. With a majority vote of unsecured creditors, and a super-majority vote of secured creditors, the time and cost of a feasibility proof would be generally wasteful.

Finally, the debtor may choose to prove feasibility as if it were not in a SME case.[88]

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[81] *Id*. art. 14.1.4.
[82] *Id*. art. 14.1.4.4.
[83] *Id*. art. 13.6.
[84] *Id*. art. 13.2.
[85] *Id*. art. 13.7.
[86] *Id*. art. 1.4.1.
[87] *Id*. art. 1.4.2.
[88] *Id*. art. 1.4.3.

f. Kosovo's Abolition of Absolute Priority Rule for SMEs

The fifth and final difference is the abolition of the absolute priority rule — the rule that all debt must be paid in full or consent before equity holders retain any interest.[89] Here, the reasoning is that the blurred lines between entrepreneur's and entity's worth do not justify the necessity of requiring full payment as a condition of confirmation. On a going forward basis, the basic protection is that provided by the best interests test. If the liability of the owner/entrepreneur is desired, the creditor has always had the ability to negotiate for a personal guaranty.

g. Kosovo's Limited Ability for an Individual Entrepreneur to Receive a Discharge

If the plan is confirmed, the discharge is entered upon confirmation.[90] With respect to the individual entrepreneur, the law provides, for the first time, a limited discharge of all business debts of individuals.[91] As a result, if an entrepreneur has incorporated his business, but has still given guaranties, he can cause the business to file and then he or she can also file their own bankruptcy, and have the cases heard together. In this way, the entrepreneur can receive a discharge of his or her debts to the same extent as the discharge received by the business.

Unlike the United States reforms, there is no requirement under Kosovo law that the debtor pay any future income to creditors. The best interest test was deemed sufficient to protect their economic expectations and interests.

VIII. CONCLUSION

SMEs have different profiles than the traditional reorganization candidate. They are smaller, rely more on the skills and connections of their entrepreneurs-owners, and use outside financing more. They also fail at higher rates; half of all businesses start fail in five years, two-thirds in ten.

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[89] *See generally Id*. art. 14 (concept missing from confirmation requirements).
[90] *Id*. art. 15.
[91] *Id*. art. 105.1 (with some exceptions); *Id*. art. 107.

Both Kosovo and the United States have recognized these factors and have fashioned their insolvency laws to reflect them albeit in different ways. Kosovo's relies more on simplicity and the preferences of secured creditors; the United States relies more on traditional reorganization techniques and increased incentives to reach consensual plans. Whether Kosovo's more streamlined procedure or the United States' more complicated approach will result in better reorganizations is for time to tell.

IX. APPENDIX: SME PROVISIONS OF KOSOVO LAW

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Chapter II
Expedited Proceedings For Facilities To Small And Medium Enterprises (SME) And For Pre-Agreed Plans

Article 11
SME Definition

For purposes of this Law, Small and Medium Enterprise (hereinafter SME) shall be considered a business organization which has in annual turnover up to one million (1,000,000.00) Euro or has up to twenty-five (25) employees.

Article 12
SME Procedure

1. A case involving an SME debtor shall, unless specified in this Law to the contrary, be treated in all respects as a reorganization case.

2. In each SME case, the SME should file a reorganization plan within thirty (30) days from the day of initiation of bankruptcy proceeding.

3. If the debtor is an individual, then only the debtor may file the reorganization plan. If the debtor in a SME case is a legal person, then only the debtor may file a plan for the first thirty (30) days after the initiation of bankruptcy proceeding.

4. If a SME debtor's case does not produce a confirmed plan within sixty (60) of the opening of the case, the court shall dismiss the case upon the request of a party in interest.

Article 13
Monitor

1. In each case when an SME is a bankruptcy debtors, the court shall appoint a monitor.

2. The court may select the monitors from any eligible panel or listing of Administrators.

3. The court shall consider the monitor a professional person, and the monitor may apply for compensation from the estate as provided in Chapter IV of this Law.

4. After appointment, the monitor shall consult with the debtor regarding the debtor's business, its prospects, and its ability to formulate a plan that creditors will accept.

5. A monitor shall review each plan a SME debtor files to determine whether it proposes an economically feasible plan. The review may occur before or after the debtor files the plan with the court.

6. If the debtor intends to solicit votes on any plan, it shall inform the monitor of that decision, and the monitor shall then have ten (10) days it which it may file with the court a report containing the monitor's opinion on the feasibility of the plan.

7. If a monitor does not file a report according to paragraph 4 of this Article, the court shall consider that the monitor has agreed for the plan.

Article 14
SME Relief

1. An SME debtor may confirm a plan without meeting all the requirements of Chapter VI of this Law if the court finds each of these conditions are satisfied:

1.1. within ten (10) days from the initiation of bankruptcy proceeding, it files at the court a written request for the implementation of Chapter II of this Law;

1.2. the monitor appointed under this Chapter has filed at the court a report on the feasibility of the plan and the report has been delivered to all parties in interest before the commencement of voting procedure;

1.3. it has been delivered to all creditors affected by the plan for voting, and that the plan has been approved by:

1.3.1. seventy-five percent (75%) of all classes of secured creditors; and

1.3.2. at least 33.33% of all unsecured creditors vote in favour of plan;

1.4. The court concludes the plan is feasible when:

1.4.1. if the monitor has not submitted a report, then Article 13 of this Law applies;

1.4.2. at least fifty percent (50%) of all unsecured creditors voting on the plan accept the plan;

1.4.3. in all other cases, the debtor must prove that the plan is feasible;

1.4.4. or when all secured creditors who vote for reorganization approve the plan.

1.5. the debtor proves that the plan will pay all impaired creditors no less than they would have received had the debtor filed a liquidation case.

Article 15
SME Discharge

A SME debtor shall receive a discharge upon confirmation of its plan. A discharge under this Article shall have the same effect on claims against the SME debtor as would a discharge under Chapter VI of this Law