Can Small Businesses Survive Chapter 11?

Abstract

A majority of small U.S. businesses attempting to reorganize in bankruptcy fail to successfully do so. Subchapter V of Chapter 11 was introduced in 2020 for firms with less than $7.5 million in total liabilities to streamline the process by reducing bankruptcy costs and negotiation frictions and enabling entrepreneurs to retain their ownership. Employing regression-discontinuity and difference-in-differences designs, we show that many small businesses reorganize under the new procedures that otherwise would have been liquidated. Further, expected creditor recoveries are at least as high in Subchapter V as in similar small business reorganizations, and post-bankruptcy survival rates are no lower. Our results show that the increased ability to preserve small businesses is not associated with a bias toward continuing unviable firms, and that creditors are not harmed by a shift in bargaining power toward small business owners.

This paper is joint work with Edith Hotchkiss (Boston College), Benjamin Iverson (Brigham Young University) and Xiang Zheng (University of Connecticut)

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