

Statement of

The Honorable Sheldon Whitehouse

United States Senator
Rhode Island
March 17, 2010

Committee on the Judiciary
Subcommittee on Administrative Oversight and the Courts
Hearing on "Could Bankruptcy Reform Help Preserve Small Business Jobs?" March 17, 2010
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The hearing will come to order.

While some economists may have declared the recession over, its painful aftermath - in the form of a prolonged period of unemployment - continues nationwide. The national unemployment rate stands at almost 10% and the situation is even worse in some areas: Senator Session's state of Alabama has an 11.1% unemployment rate and my state of Rhode Island ranks third nationwide at 12.7%. Job retention and preservation should be, and is, at the top of our legislative agenda.

Today we are going to explore changes to the Bankruptcy Code that would help small companies to reorganize and stay in business. The ideas we will discuss today are worthwhile to consider for two reasons: (1) small businesses account for over half of all jobs nationwide; and (2) unlike other job-preserving measures like tax cuts and government investment, bankruptcy reform can be accomplished with zero cost to the federal budget.

While small business bankruptcy reforms may prove a powerful tool in cutting job losses, the need for a new bankruptcy reorganization option has been clear for some time. Chapter 11 was designed for large, publicly-traded companies and doesn't work well for smaller companies for a number of reasons. First, Chapter 11 extinguishes equity so the debtor-owners exit the bankruptcy not owning their company anymore. A change in shareholders may not discourage big corporations from reorganizing, but for small businesses the corporate entity and its owner cannot be so easily disaggregated.

Second, small businesses often have a number of trade creditors and other unsecured creditors that do not participate in a Chapter 11 because their claims are too small. This failure to participate leaves the secured creditors steering the bankruptcy, often toward liquidation.

And finally, the Chapter 11 process is time-consuming and expensive and attorneys fees and other administrative costs often eat up so much of the firm's value that there is not enough left for the firm to emerge from bankruptcy as a going entity.

The National Bankruptcy Conference has proposed addressing these three issues by opening up Chapter 12 - a process currently available only to family farms and fishermen - to a wider group of small businesses. I expect that Judge Small will discuss this proposal in his testimony today. I

have reviewed the NBC's report and believe that they make a strong case for the Chapter 12 approach.

I want to stress however that I look forward to hearing the thoughts of all of the witnesses on possible small business bankruptcy reforms. It appears from the written testimony that each of you acknowledges that certain changes to bankruptcy law might help to preserve small business value and to save jobs.

As we discuss the NBC proposal, there are a number of variables about which I am interested in getting the witnesses' feedback. Is the proposed definition of "small business entity" appropriate? Should the reforms be made permanent or be enacted on a trial basis as Chapter 12 for family farms initially was?

Through it all, one thing is clear: Small businesses are the lifeblood of our economy, and they're hurting in today's economic climate. We should be considering all options, including reforms to our Bankruptcy Code, to help small business keep their doors open and keep their employees on the payroll.

I look forward to a lively discussion with our distinguished panel of witnesses:

Ed Mendenhall owned a fitness center in Warren, RI from 1996 to 2009. In his testimony, Mr. Mendenhall will describe his efforts to save his business. Mr. Mendenhall is a graduate of the University of Rhode Island and has an extensive background in personal training and fitness.

Chuck Bullock practices bankruptcy law in Detroit, Michigan, an area with no shortage of bankruptcies in recent years. He has represented small business debtors, and secured and unsecured creditors. A graduate of the University of Michigan and the University of Memphis School of Law, Mr. Bullock teaches bankruptcy at Cooley Law School.

Tom Small served as U.S. Bankruptcy Judge for the Eastern District of North Carolina from 1982 to 2009. He also served as President of the National Conference of Bankruptcy Judges and as a Board Member of the American Bankruptcy Institute. He holds degrees from Duke University and Wake Forrest University School of Law. Judge Small continues to be an active member of the National Bankruptcy Conference and serves as Co-Chair of its small business working group. Judge Small helped Senator Grassley to draft the original Chapter 12 back in the 1980s.

Joseph Mason is the Hermann Moyse/Louisiana Bankers Association Chair of Banking at the Louisiana State University and Senior Fellow at the Wharton School. Dr. Mason's academic research focuses primarily on investigating liquidity in thinly-traded assets and illiquid market conditions. A graduate of Arizona State University, he has an M.S. and Ph.D. from the University of Illinois.

Thomas B. Bennett has been a United States Bankruptcy Judge for the Northern District of Alabama in Birmingham since 1995. For over fifteen years, he was a partner with the law firm of Bowles Rice McDavid Graff & Love PLLC and served as head of the firm's bankruptcy, creditors' rights and commercial litigation practice groups. Judge Bennett graduated from Girard

College in Philadelphia, Pennsylvania in 1966 and received his undergraduate and graduate degrees in economics as well as his law degree from West Virginia University.