

What to do while waiting for your federal bailout.

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If your company is struggling to stay in business during these tough economic times, filing bankruptcy may seem like the only viable option. Instead of becoming a creditors' worst nightmare, however, it may make sense to think about a structured process outside of the bankruptcy courts. In attorney lingo, this is referred to as a "workout."

A workout can be a beneficial tool for small businesses and it can alleviate some of the burdens which are associated with filing for bankruptcy. A workout starts with approaching creditors as early as possible to open up an honest line of communication regarding your business situation. A business, as well as creditors, can ultimately save thousands of dollars by working out a plan to avoid bankruptcy. Chapter 11 bankruptcy proceedings are expensive and the fees incurred from lawyers, accountants and investment bankers can add up quickly.

Another advantage to a workout is that it can be more efficient and flexible than the structure of a Chapter 11 bankruptcy proceeding. An out-of-court restructuring permits a company and creditors to solve problems in a non-litigious environment. It also helps to avoid negative publicity that would come with a bankruptcy. Although a workout will require determination and resolve, it can be well worth the time and effort. The following are necessary ingredients for a successful workout.

Communicate with creditors as early as possible. To maintain goodwill with creditors, you should approach them as early as possible. If you're represented by a professional, your creditors will know you're serious about solving your problem. Creditors will be glad they were approached early, rather than after you've decided to file for bankruptcy.

Be prepared. Before communicating with creditors, all pertinent information should be prepared. This includes updated financial statements, balance sheets, profit and loss statements, tax returns, security agreements with lenders, lists of all creditors, lease agreements and any and all other pertinent data.

Hire appropriate professionals. Insolvency attorneys, accountants, and, if appropriate, business consultants who are turnaround management experts can give an independent analysis and appropriate advice to the company. Management may be too emotionally involved and unable to make objective decisions.

Identify the company's problems. Are there market conditions, lack of capital, inadequate management or other reasons for the problems? Once identified, a plan should be developed for resolving the problems.

Designate creditor groups. The company should determine which creditor groups with which to communicate or meet. Among the creditor groups are lenders, lessors,

unsecured creditors, landlords, taxing authorities and debt/equity holders such as bondholders and shareholders if appropriate.

Consider method of communication. There are several ways in which to communicate with creditors. There is no substitute for face-to-face meetings. Usually, a company will meet with each of its lenders on an individual basis. Similarly, if restructuring is needed with a landlord or the taxing authorities, an individual meeting should take place.

Unsecured creditors in many instances are usually numerous, consisting of suppliers, vendors and other trade debt. Calling a group meeting of unsecured creditors can be the most efficient method to address the company's unsecured creditors. Creditors can also be invited to an informal meeting, but often communication by teleconference, fax and e-mail will suffice.

In order to ensure the credibility of the process and to formalize the relationship between unsecured creditors and the company, a credit adjustment firm is usually asked to call and conduct the meeting. There are various companies that specialize in organizing and facilitating creditors' meetings. At the creditors' meeting, the company should candidly state its problems and present a realistic plan for resolution. The professionals and/or management should detail the assistance requested from creditors. It is normal for creditors, if they determine that it is in their collective best interest, to negotiate with a company.

Honesty is best. Management and its professionals must disclose all information frankly and honestly. Starting off on the right foot in the workout process goes a long way toward a successful conclusion. The company should not withhold information in order to enhance its negotiating position. The information will surely be discovered later, which will lead to a loss of credibility and most likely a failure in negotiations.

When the communication between a company and its creditors is open, the parties involved are practical enough to know that a workout will be far better than a liquidation of the company, where recovery to creditors may be minimal or non-existent.

Clearly state your proposal. Stating your problems and supplying credible information is the first step. The company then needs to be very specific as to what it is requesting from its creditors, which may include:

- A moratorium on payments.
- A 100 percent repayment plan, which would provide for fixed minimum payment upon regular intervals with supplemental payment based upon profits.
- A settlement of less than 100 percent in one or more cash payments.
- Substitution of debt for some form of debt/equity combination.
- Continued shipment of products on a protected basis.
- Various combinations of the above.

Once an agreement is reached with unsecured creditors, a written document should be distributed and executed to each unsecured creditor. A properly written plan can alleviate future controversy. Insolvency professionals can ensure the proposal conforms to the requirements of a bankruptcy plan of reorganization and that there is adequate disclosure, similar to a bankruptcy proceeding. You should also keep in mind recalcitrant creditors may precipitate an involuntary proceeding. However, once a substantial number of creditors have accepted the written plan, involuntary proceedings may be avoided.

A workout provides a number of advantages over Chapter 11. It holds the promise of a substantially reduced and restructured debt within a much shorter period than bankruptcy. Proceedings are private and away from the public scrutiny of the bankruptcy court, which could ruin customer confidence and ultimate profitability. There is no huge up-front payment, as much of the work can be completed at a fraction of the cost of a bankruptcy proceeding. A mountain of time-consuming and onerous bankruptcy paperwork is avoided and there is no trustee to look over your shoulder, searching for process illegalities.

From your creditors' perspective, the workout holds the prospect of a higher, faster return than in Chapter 11, and certainly more than if your company goes under. A well-executed process ensures there is no preferential treatment and the process incorporates communication and attention to detail, so fewer problems emerge. Creditors come to understand their losses can be minimized and there is nothing to gain by pushing the company into bankruptcy and closing it down.

A workout in itself will not ensure your future success, but it may provide breathing space to analyze what went wrong and establish how to return to solvency. If nothing else, you get the opportunity to stay alive and wait for market conditions to improve.

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