

# Thinking about starting over? Here's a guide to liquidation

By John M. Collard



**L**iquidation can either be a method to withdraw from a company, or a catalyst to start over again. Small business owners have alternatives.

When a company is in trouble the owner loses all credibility, and bankers and creditors no longer believe what you have to say. Chances are, it is much harder to be creative with new stories to get cooperation. Don't allow asset value to deteriorate further while you wait too long.

When all attempts to save the business have failed, strongly consider the option to liquidate the company. Sell assets, pay debts and minimize personal liability.

Personal guarantees are always a killer to saving your assets. After all, you pledged these assets as collateral to secure credit. Clearly, if there are minimal or no guarantees, this process is much more successful. Negotiating when guarantees are in place is difficult, but possible.

**Regain credibility.** To make a workout work there must be trust, and a working knowledge about this complicated process. Bring in a respected third party, like a turnaround specialist or outside director to guide you, and to regain a positive working relationship with the bank and creditors. These professionals have gone

## ONE OPTION ALLOWS YOU TO START OVER: THE OUT-OF-COURT WORKOUT

through this process before. The very fact that you hire an expert can reestablish that credibility. Often, a bank or creditor will work with a third party when they won't work with you alone. When creditors

realize and believe that there are not sufficient assets to cover debt obligations, they will settle for less on the dollar. Keep negotiations non-legal because lawyers tend to bring the discussion to a different level, but do get legal advice.

Generally speaking, the only beneficiaries of liquidation proceeds are the bank and secured creditors, particularly in a bankruptcy proceeding. Depending on your circumstances there are ways for you to see benefit as well.

**Liquidation alternatives.** There are four alternatives to liquidation, each having advantages and limitations. One allows you to start over. The Workout can provide the best option based upon your situation and desired course of action after liquidation. Most business owners with a large debt burden choose bankruptcy rather than performing a workout because it is easier. Let's look at these alternatives.

## COLUMN:

**File business bankruptcy:** The ultimate goal of Bankruptcy Code is to maximize value for creditors. This option is normally for corporations, partnerships, or LLC, is costly and time consuming. The federal Bankruptcy Court appoints a trustee to sell assets and pay creditors. Not all debt is dischargeable in bankruptcy, examples you are still liable for: trust fund taxes, back taxes, recent purchases, loan to pension plan, bad checks.

The trustee will look back at transactions during statutory periods (90 days for creditors and 365 days for owners) before filing to avoid those of a preferential or fraudulent nature. The company's credit rating will be damaged, but your personal rating will not be.

**Assignment For The Benefit of Creditors (ABC):** Your insolvent business assigns (transfers) all of its assets and debts to a new assignment estate, a third party firm, to be liquidated in accordance with state statutes and Court oversight. The assignee firm sells assets and pays your creditors a fraction of full debt (for a fee), while you proceed on with your life. The assignee is a fiduciary to the creditors.

The assignee controls the ABC process. This process is usually faster and more private than bankruptcy, and it often yields better value for assets sold than in bankruptcy auction. The buyer receives a "bill of sale" that assets are transferred free and clear of claims of creditors. Personally guaranteed debt is still prevalent, but negotiable.

**File personal bankruptcy:** This option is normally for sole proprietorship or for owners with a large amount of personal debt or guarantees. The federal Bankruptcy Court appoints a Trustee to sell personal assets and pay creditors. Your credit will be destroyed and stay part of the record for 10 years.

If you pledge your house as collateral for a loan and the loan is in default, then the lender can foreclose. Bankruptcy can delay the process, but you may lose your home. Most states have a "homestead exemption" that allows you to keep your principal residence if your equity doesn't exceed a certain limit, and you keep payments current.

**Liquidate Out of Bankruptcy (Workout):** The Out-of-Court Workout idea is simple: It attempts to achieve consensual agreement with creditors outside of a court proceeding. You or your representative contacts creditors to arrange for a release of debt in exchange for paying less than the full value. Why will they agree? Often it is a better choice than suing you and attempting to collect against dwindling or no assets, all before you may file for bankruptcy, where they get nothing. For this to work you must: 1) have creditors believe that you are going out of business or into bankruptcy and have no means of paying full value, 2) have some assets or cash flow to pay reduced negotiated debt, and 3) obtain releases from personal liability. The disadvantage to a Workout is that you don't have the ability to involuntarily bind an unwilling creditor who won't

cooperate, which is why credibility is key. Don't kid yourself this is a lot of work.

Many more strategies exist to generate cash, resolve disputes, renegotiate agreements, and start over again. You can use "bankruptcy" and "no assets" as leverage to settle matters. Communication is a strength – use it to direct the process. When you are quiet, creditors assume the worst.

The options in a Workout are only limited by your creativity because you are in control. Credibility is key – get help to regain trust. When executed properly you keep personal wealth and can start over again.

*American City Business Journals syndicated coverage.*

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