CUSTOM CONTENT
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BANKRUPTCY & RESTRUCTURING

A Roundtable Discussion

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>
> DEAN G. RALLIS JR.

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In your view, how significant has the economic damage been to businesses due to the COVID-19 pandemic?

RAANAN & TEDFORD: From our vantage point, the economic disruptions caused by COVID-19 are profound. Most retail businesses have had to shut down or reduce operations significantly. Certain business sectors are impacted more than others. For example, gyms, hair salons, spas, hotels, car rentals, bars, restaurants, and suppliers for these businesses, have largely ceased operations. While some businesses received Federal CARES Act loans/grants, these funds were designed as temporary relief. Most small businesses have either stopped paying rent or negotiated temporary rent reductions/concessions. Small business owners typically carry heavy debt loads, which they generally have not paid during the pandemic. For now, most lenders are either standing down or willing to work with borrowers. However, once the courts reopen and life returns to something akin to normal, many lenders will resume enforcement of their payment rights. That is when we will see many business failures and foreclosure actions.

MOORE: COVID-19 has been catastrophic for many businesses, particularly in retail, travel and hospitality and those with poor cash reserves. Manufacturing has suffered in the short to medium term but should bounce back, although I expect to see more consolidation, outsourcing and homeworking for indirect staff. Independent self-employed workers have also suffered badly and struggled to get financial support. On the other hand, some business services have prospered and some niche enterprises such as micro-breweries have diversified and survived quite well. The logistics industry has, in general, seen an increase in business activity concerning online ordering and home deliveries. Sales of computer games have increased along with online media streaming. It is interesting to see that M&A activity has been maintained throughout the epidemic.

EKVALL: The severity and extent of the financial impact of COVID-19 are not yet known although there is no question that many business sectors have been or will be damaged. What is not necessarily known is the extent of the damage, which depends on when and to what extent people can resume their pre-pandemic routines. Certain sectors and businesses were already struggling before COVID-19, such as brick and mortar retail. Therefore, one can't really attribute all of the damages suffered by that sector to COVID-19. Some of the recent bankruptcy filings such as J.C. Penney and J. Crew were not entirely surprising. Likewise, some sectors have always been more volatile, such as the hospitality industry, so not all of the downturn can be attributed to COVID-19. However, there are a number of businesses that were otherwise financially sustainable that have been significantly impacted by COVID-19, such as travel and event production related businesses. Commercial real estate is a sector that is likely to have been damaged although it is too soon the tell the magnitude of its effect, especially with respect to commercial office space. The severity of the impact will depend on whether and how much workplace habits have changed after the pandemic ends. Overall, however, I believe that the damage is substantial, in part due to the greater number of industries and sectors affected as compared to prior economic downturns.

What are some new trends in financing options during and post- COVID-19?

MOLDO: While not necessarily a new trend, business owners and creditors have explored ideas of how and when obligations incurred during COVID-19 can and will be paid. For instance, landlords have entered into agreements with tenants to defer payment of rental obligations for significant periods of time. These agreements may provide that the accrued rental obligations must be repaid over an agreed period of time beginning in 2021 or later. In other situations, involving a business owner and a vendor or supplier, agreements have been reached to add the amount of the debt incurred during COVID-19 to the amount due at the end of the contract between the parties.

MOORE: There has been increased private equity activity as many businesses are reluctant to take on more debt due to issues of serviceability. This means increased equity release.

Coronavirus aside, when is filing for bankruptcy a good idea typically?

EKVALL: Typically, bankruptcy can be an effective tool if the business is otherwise sound but has substantial legacy debt. Chapter 11 would allow the business to potentially repay just a fraction of the debt and over time. This allows the business to clean up its balance sheet. Bankruptcy can also be useful to a business that has multiple locations, store sites or divisions, where some stores or divisions are profitable but are being dragged down by unprofitable locations or divisions. The Chapter 11 plan can provide for shutting down the unprofitable locations or divisions with the business emerging from bankruptcy with the profitable locations or divisions. Bankruptcy can also be a good idea where the business is selling substantially all assets as a sale blessed by the bankruptcy court provides a high degree of protection for the buyer from successor liability or fraudulent transfer claims. For management of the seller, a bankruptcy sale would also limit its exposure to claims of creditors or other stakeholders.

RALLIS: Generally, filing for bankruptcy should be seen as a last resort for a financially distressed company after the company has exhausted all other options without success (e.g., an out-of-court workout or restructuring). The initial step of filing the bankruptcy petition is a good idea—and, in fact, becomes a necessary course of action for a company to best preserve its rights—when the company is facing some immediate, adverse act that threatens the company's ability to continue operating its business, such as an impending eviction by a landlord, foreclosure by a secured lender, or attachment of the company's bank accounts by a judgment creditor, as the filing of the petition will give the company some breathing room through the imposition of the automatic stay. However, whether the company being in bankruptcy is ultimately a good idea will depend on how its exit strategy(ies) to successfully reorganize or restructure its affairs.

MOORE: If the directors find that they are unable to pay their creditors when they fall due, they should immediately take insolvency advice and consider whether this is a chapter 7 situation (liquidation) or Chapter 11 (reorganization). The directors should not take on any more debt in order to recover the situation nor should they worsen the position of creditors. Directors should not leave the matter too long.

RAANAN & TEDFORD: A business should consider filing a Chapter 7 liquidation bankruptcy when facing heavy debts with few assets to justify either reorganization or continued payments on the debts. Bankruptcy is designed to give debtors a fresh start, with individuals receiving outright discharge and business owners getting the opportunity to start new businesses unshackled by heavy debt. A Chapter 7 case is ideal for a business owner who did not personally guarantee their business debts and will not lose their personal assets when the business files, or for an owner-guarantor who is also a candidate for personal bankruptcy. Businesses also have the option of filing bankruptcy under Chapter 11. This helps debtors to preserve valuable assets, with an opportunity to suspend collection efforts, pressure creditors to negotiate better contract terms including debt levels, and even reject burdensome contracts. Bankruptcy can also be a tool for holding back aggressive creditors while efforts are made to sell the business or its assets.

MOLDO: I assume this question contemplates the filing of a Chapter 11 bankruptcy. This is a difficult question to answer, and depends on many factors including the type of business, amount of existing debt, and liquidity. Initially, Chapter 11 is expensive, and for a Chapter 11 case to be successful, a business owner will need to have sufficient funds to operate profitably during the Chapter 11. If the business is unable to generate a profit during the Chapter 11 case, a plan of reorganization will probably not be confirmed by the court, and the case may either be converted to Chapter 7 (liquidation) or dismissed. On the other hand, if the business owns valuable assets that can be used to fund a plan of reorganization, or if a business expanded too quickly and needs to resize, filing Chapter 11 may be appropriate. To the extent that the business is burdened with secured debt, initiating discussions with the secured creditor(s) as early as possible is critical. Filing a Chapter 11 with the knowledge, and perhaps, consent of secured creditor(s) is one way to make a successful Chapter 11 case more likely.

Now that we are faced with the COVID crisis, what advice do you have for struggling small businesses faced with the decision to file for bankruptcy?

EKVALL: First, there may be other options besides bankruptcy that may be available, including dissolution under state law, assignments for benefit of creditors, and out-of-court workouts. Second, if the decision is made to proceed with bankruptcy, then the business should find a reputable and experienced business bankruptcy attorney to consult with the company on the pros and cons of the various Chapters that maybe available to the business. The most common two chapters are Chapter 7 for liquidation and Chapter 11 for reorganization or the sale of a going concern. There are distinct advantages and disadvantage under both chapters that need to be carefully explained and considered before a final decision is made. It is also important that the attorney discuss whether the business is eligible to file under the Small Business Reorganization Act of 2019 ("SBRA") and the pros and cons of filing under SBRA. Business owners

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should be mindful that a bankruptcy for the business may not affect any individual liability under guaranties or for certain taxes and employee claims.

MOORE: The first step is to take advice from an insolvency professional or, ideally, a business turnaround practitioner. There may be an alternative to liquidation such as an accelerated sale of the business. It could be that there is a business coming out of an insolvency process if an investor can be found, such as a pre-packaged Chapter 11. So the advice is do not be pushed into liquidation.

RAANAN & TEDFORD: Consider options other than bankruptcy. Communicate with creditors! Explain your situation and ask for reasonable accommodations. If the negotiations fail and you did not personally guarantee the business debt, consider closing the business outside of bankruptcy. If the business can pay off only some debt, explore possibility of first paying off debts that you personally guaranteed. This will simplify future decisions as to whether to put the business into bankruptcy. Consider pursuing an assignment for the benefit of creditors (ABC) under California law. This allows your business to transfer its assets to an assignee/fiduciary who will sell the assets and pay creditors on a pro rata basis. Explore the option of selling your business, preferably for an amount that covers at least the secured debt. Try to sell to a creditworthy buyer who agrees to assume debts you personally guaranteed. Discuss your options with an experienced bankruptcy attorney.

RALLIS: The best advice for any small business experiencing financial difficulties during this crisis is to be consistently proactive about saving its business. That means preserving cash, communicating with key business partners and creditors (e.g., landlords, secured lenders, and vendors) to keep them apprised of the company's circumstances and to seek relief from them if possible (nobody likes surprises), reevaluating the company's core business to identify and eliminate any unproductive lines or parts of the business, and updating and revising financial projections in light of the company's new reality. When overwhelmed with a barrage of seemingly never-ending issues, some companies tend to bury their heads in the sand, thinking that those issues will work themselves out over time, but that only make matters worse for the company.

What is the first thing a company should do if it plans to file for bankruptcy?

MOLDO: Depending on the size of the company, retaining a bankruptcy attorney and accountant or financial advisor at the earliest time is extremely important. If a business owner waits too long before retaining expert professionals, the success of a bankruptcy case may be directly impacted. There may also be a need to retain other professionals such as valuation experts, tax advisors, financial advisors and brokers (real estate, personal property or other).

MOORE: The first thing to do is to appoint an appropriately qualified insolvency professional who will help the directors or owners decide on which is the best option such as straight liquidation or a reorganization through Chapter 11. This decision will be based on what potential there is for the business longer term.

EKVALL: There are several things a company should do if it is planning on filing for bankruptcy. One of the most important first steps is to find a reputable attorney with expertise in business bankruptcy and reorganizations. Bankruptcy is a specialized field but there are sub-specialties within the practice of bankruptcy. Some bankruptcy attorneys specialize in representing consumer debtors in Chapter 7 and Chapter 13 cases, which is quite different than a Chapter 11 case. Also some attorney specialize in representing creditors, as opposed to debtors. Be prepared to ask your attorney hard questions. Lots of attorneys can file a Chapter 11 case but not many have the expertise to successfully confirm a Chapter 11 plan and get the business reorganized and out of bankruptcy. In addition, be prepared to provide your attorney with several years of financials, including balance sheet and cash flow statements as well as projections. This will allow your preliminary meeting with your prospective attorney to be more productive.

RALLIS: A company anticipating the need to file for bankruptcy must always be thinking and planning ahead, including consulting with restructuring professionals (e.g., bankruptcy attorneys and turnaround specialists) as soon as possible about its options and developing a game plan that outlines the goals it wants to accomplish through a restructuring or reorganization and how it intends to accomplish those goals. Once the bankruptcy case is commenced, the bankruptcy process will be time- and resource-consuming on the company itself (at the time when the company's principals should be focused on improving the business), and a company that enters bankruptcy without already having a clearly defined strategy on how to exit bankruptcy is likely to face greater odds of successfully exiting bankruptcy.

What are the issues and concerns that the owners and management of a business in bankruptcy should be aware of?

MOLDO: Once a bankruptcy case is filed, it is critical that the owners and management must take immediate steps to review and analyze the performance of the company and all financial data. Retaining professionals who specialize in assisting companies in bankruptcy can provide a benefit, but there are associated costs that can be substantial. Also, courts will expect a company in bankruptcy to quickly analyze its assets and liabilities, and determine if any assets should be abandoned, sold or disposed of. If a company has multiple business locations that are leased, an analysis of the leases must be done very quickly. If a lease requires payment of rent that is above market rates, rejecting the lease may be appropriate. This is just one example of how a debtor in bankruptcy needs to analyze its assets, and at the same time, verify financial data, to review business operations. If the business is not profitable while in Chapter 11, confirming a plan of reorganization is not likely. Other issues to investigate are insurance, payments or transfers to insiders, and rights to recover assets pursuant to various theories. Retaining professionals who specialize in bankruptcy is one way to minimize the risk that unknown issues or concerns will arise.

What main advice would you provide to a company looking to start rebuilding its credit after a bankruptcy?

MOORE: Unless the company is acquired by a creditworthy enterprise then it will take time but can be achieved. Slowly taking on small amounts of debt can help providing these are serviced properly as the credit agencies monitor this. Also, timely issues of accounts and the fulfilment of State and Federal obligations can help. It is important to build relations with both suppliers and customers as reference points. In addition, the publication of accounts showing an improved financial position will help in getting credit insurance. But it has to be accepted that these thing stake time. The old adage "time heals" applies.

What is small business bankruptcy likely to look under the CARES Act?

EKVALL: Under the CARES Act, the debt limit for a business to be eligible to file under the Small Business Reorganization Act of 2019 ("SBRA") has been temporarily increased from $2,725,625 to $7.5 million for cases filed prior to March 27, 2021. A Chapter 11 filed under SBRA is meant to be more streamlined and more affordable for a small business. Thus, the increase of the debt limit will make SBRA available to many more struggling small businesses. The benefits of filing a Chapter 11 case under SBRA are discussed in more detail in my response to the next question in this discussion. In summary, however, SBRA would allow a business to reorganize its financial affairs and clean up its balance sheet by allowing the business to propose a plan that could reduce the total percentage payout to unsecured creditors (i.e., 10% of the total debt) and stretch out the payments over a 3 to 5 year period. This has the potential of eliminating a great deal of debt and provide some relief in terms of alleviating some cash flow difficulties.

MOORE: The CARES Act is a loan which will be forgiven if it is mainly for payroll. Then this loan will go into the balance sheet and should be treated as another creditor. However, the business is unlikely to obtain the loan if insolvency is imminent.

What, in layperson's terms, is the Small Business Reorganization Act of 2019 that went into effect on Feb. 19? Is this new law something that may help businesses now?

RALLIS: The SBRA created subchapter V within chapter 11 (the bankruptcy chapter dealing with reorganization), and this new subchapter is aimed at small businesses seeking to reorganize. The new law provides a more streamlined and expedited (and thus less expensive) process for a small business to reorganize and repay its debts compared to a traditional chapter 11 case. Arguably, the most critical part of the new law is the elimination of the "absolute priority rule," which means that the owners of the small business can now retain their equity without having to pay creditors in full. To be eligible to file under subchapter V, the debtor must have total debts of no more than approximately $2.7 million. However, the CARES Act temporarily increased that debt threshold to $7.5 million through March 2021, making subchapter V available to a larger pool of small businesses who may be impacted by the COVID-19 crisis.

EKVALL: When the Small Business Reorganization Act

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(“SBRA”) first went into effect in February of 2020, it was only available to businesses with debts of no more than $2,725,625. Pursuant to the CARES Act, that debt limit has been temporarily lifted to $7.5 million through March 27, 2021. SBRA is meant to somewhat streamline the Chapter 11 process used to restructure larger businesses so that it can be more affordable and feasible. The law is very new and still largely untested. However, one benefit of SBRA is the likelihood that there will not be a creditors committee appointed. A creditors committee is provided by the Bankruptcy Code to act as a check on the powers of a debtor in Chapter 11. The committee is authorized to retain its own attorneys, financial advisors and other professionals but the costs of the committee’s professional are borne by the debtor, which can severely impair the debtor’s chances of a successful reorganization, especially when margins are already thin. There are also changes that would make it easier for a small business to confirm a plan over the objections of creditors. The main requirements of the plan are that it provides a total percentage payout to unsecured creditors of at least as much as what such creditors can expect to receive in a hypothetical Chapter 7 liquidation and that the debtor is devoting all of its disposable income to its plan to repay such creditors for a duration of 3 – 5 years. There are deadlines in the case that are designed to move the case toward confirmation quicker. Also, there are some cost savings regarding fees that would normally have to be paid to the U.S. Trustee’s Office. Overall, SBRA is meant to improve the debtor’s chances of successfully confirming a plan at a potentially lower cost.

MOORE: The law is a means of streamlining the refinancing the debt of troubled small business through bankruptcy as many small companies suffered from the prolonged processes in place to obtain new finance. In response to the economic distress caused by the COVID-19 coronavirus pandemic, under the CARE Act the eligibility limit for small businesses looking to file under SBRA’s subchapter V has temporarily increased from $2,725,625 of debt to $7,500,000. The threshold will return to $2,725,625 after 1 year. In effect it means it is now more affordable for small businesses to file for bankruptcy and the process time is significantly less.

What are some bankruptcy pitfalls that businesses should avoid?

EKVALL: One way to avoid bankruptcy pitfalls is finding a competent and experienced reorganization counsel that can help with the following potential issues:
1. Are there alternatives to bankruptcy for a financially distressed business and what are the relative pros and cons of the various alternatives?
2. Some businesses are transacting with financially distressed businesses (e.g., key suppliers, customers, or vendors). What are some of the warning signs of financial distress that a business should be looking for in its business partners? What are some of the precautionary steps that a business can take to minimize the risks of non-payment, to prevent a disruption in business relations, and to minimize the potential for lawsuits to recoup payments received as a preferential transfer? What are some of the other issues and concerns that a business may face if its business partner files bankruptcy?
3. What are the issues and concerns that the owners and management of a business in bankruptcy should be aware of?

RAANAN & TEDFORD: Business bankruptcies have many pitfalls, including:
• Filing inaccurate schedules or statements, which can lead to complications and even dismissal of the case.
• Failing to comply with deadlines, including for filing reports, assuming or rejecting executory contracts, among other.
• Improperly using funds that are subject to creditor liens, without prior court approvals.
• Needless litigation of prepetition lawsuits or claim objections in cases where anticipated creditor distributions do not justify high litigation expenses.
• Failing to realize that a Court can appoint a trustee who takes control of company assets and operations in a Chapter 11 case.
• Failing to understand that a court can bring into bankruptcy businesses that are related to the bankrupt debtor, thereby depriving owners of assets initially left out of bankruptcy court.

MOORE: The most critical pitfall is that of going into it totally unprepared. This means not waiting until the last minute before plans are compiled. When the first signs of potential financial distress and looming bankruptcy occur, the owners and managers need to build a lifeboat. This will contain all the necessary items for the business to recover post-bankruptcy and survive.

MOLDO: Here are some key pitfalls to avoid:
• Not retaining professionals that have substantial experience in bankruptcy.
• Waiting too long before seeking the advice of professionals.
• After a bankruptcy case is filed, not quickly analyzing the overall financial condition of the business, and determining what adjustments should be made.
• Failing to timely comply with all reporting requirements of the United States Trustee and the court.

How has COVID-19 affected the M&A landscape?

MOORE: PEs and VCs are increasingly busy and very selective about the sort of deals they want to handle. So high-risk, troubled businesses may find it difficult to get new finance. There is also a significant amount of consolidation and merger activity where companies are joining forces to survive.

What are some cautionary tales, red flags and lessons you would like to share as an M&A expert?

MOORE: It is said that the deal is not done until the ink is dry. It’s true. Deals usually take longer than planned or expected despite the best intentions of all parties. You can also expect surprises along the way: an unexpected offer from an unknown party at the last minute; a sudden change of heart by a preferred buyer; due diligence that drags on; etc. You will be expected to spend a lot of time on the deal and there is a risk of the business suffering because of this, so it is best to organize around that. Price erosion is the biggest issue especially where you have given exclusivity to one part. They may chip away at the price during dur diligence so you may not get what you expected.

What are the most critical factors in managing a turnaround or restructuring deal during and Post- COVID-19?

MOORE: A successful turnaround of a business requires three things: management, money and time. It needs an injection of experienced turnaround management, new money and the time to implement the necessary changes. Many company directors leave it too late before they ask for help. Asking for help in a distressed situation is good management. Trying to deal with these things in glorious isolation is bad management and doomed to fail. There are five key elements to a business turnaround or transformation. Stage one is a diagnosis of the key issues impacting business performance. Stage two is to create a window of time of short-term measures to stabilize the situation such as speaking with creditors, customers and the bank. The next step is the planning of the turnaround project, including the roles of those involved, timescales and outputs. The fourth stage is the implementation and the fifth is the aftercare to make sure that there is not a reversal in performance.

Can credit counseling be as damaging as bankruptcy?

MOORE: No. Credit counseling is meant to be supportive and a means to find a solution other than bankruptcy.

If the business is privately held, will a business bankruptcy hurt the owner’s credit score?

RALLIS: A business owner’s credit score should not be directly impacted by the bankruptcy of his or her business. However, with any such bankruptcy, the owner must consider the extent that he or she is a guarantor of any of the business’s debts. The filing of bankruptcy by the business may constitute a default under the owner’s personal guaranty, which could spring the owner’s obligation to pay the debt originally owed by the business. In such scenarios, the owner’s failure to pay may adversely affect his or her own credit score.

MOORE: If the company has sole proprietorship status (the affairs of the business are managed by an individual and the business is not incorporated), then it is highly likely that the owner’s credit rating will be affected.

Are there alternatives to bankruptcy for a financially distressed business and what are the relative pros and cons of the various alternatives?

RAANAN & TEDFORD: Financially distressed businesses have multiple options aside from bankruptcy, including:
• Debt renegotiation: Getting creditors to reduce their claims is the least expensive option. Reaching out to creditors, though, may signal financial difficulties which could hurt the business’ ability to borrow money.
• Dissolution: A business can liquidate its assets, pay creditors based on lien priorities, and cease operating. If owners

personally guaranteed the debts, creditors would sue the guarantors. Owners may have to file personal in addition to corporate bankruptcy.

• Assignment for the benefit of creditors (ABC): This allows an owner to transfer business assets to an assignee/fiduciary who assumes responsibility for liquidating the assets and paying creditors. A business owner can arrange to purchase the business assets from the assignee.

• Asset sale: By selling corporate assets, an owner can pay critical business debt, avoid personal liability, and at times preserve a limited part of the business.

• Sale of the business: An owner can sell the business entity to a competitor or a better-funded entrepreneur. Often, the new owner will assume corporate debts and relieve the prior owner of personal liability.

MOORE: Yes, there are certainly other options which should be considered. At NMS we focus on turning the business around to avoid bankruptcy wherever possible. This will involve appointing a turnaround specialist and will usually involve making arrangements with creditors and bringing new finance into the business. Many good companies go down unnecessarily because they have been pushed into bankruptcy as the only option.

Under what circumstances would a business entity with financial difficulties not be a good candidate for bankruptcy?

RALLIS: Any company with unrealistic expectations about its business and finances would not be a good candidate for bankruptcy. When a company is at the point of considering bankruptcy, the company must recognize that tough decisions need to be made to better ensure its survival in the future. That might mean trimming unnecessary costs, eliminating unproductive parts of the business, laying off employees, and holding off on any plans to expand into new areas of business. Simply because business had been booming in the past for a company does not mean that business will quickly rebound to that level in the near future. Particularly for a company that has not faced financial difficulties before, the company must take a hard look at its new reality and adjust its plan for returning to financial strength accordingly.

MOLDO: Here are some circumstances where businesses would not be a good candidate:

• The value of the business assets was so much less than the amount owed to secured creditor(s).

• Financial projections failed to indicate that the business would operate profitably in the future.

• The entity lacks funds to retain experienced professionals.

• The purpose of filing bankruptcy was primarily to delay an event such as a foreclosure.

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What options other than bankruptcy do businesses have when facing financial difficulties?

MOLDO: Other possible remedies to consider are a receivership or assignment for the benefit of creditors. There are benefits to these alternatives, but there are also possible downsides to consider. For instance, a receivership may provide more flexibility and options regarding business operations, but if a sale of the business is considered, possible buyers of assets may be more comfortable with a bankruptcy sale. However, recent authority exists which authorizes a court overseeing a receivership to approve a sale free and clear of liens. Until recently, many state courts were very reluctant to issue orders approving sales of assets free and clear of liens. Another factor to consider is that even if a receivership is commenced, creditors have the right to commence an involuntary bankruptcy. Therefore, if a receivership is chosen as the remedy, expediting the process of a sale or restricting it is very important. Assignments for the benefit of creditors is another option to consider. While assignments can be very effective, as there is no court oversight, a sale of assets may not provide a buyer with the desired level of protection. Specifically, unlike a bankruptcy or receivership, in an assignment, there is no court to issue an order approving a sale. However, successful assignments usually occur when most of the work to achieve a sale or disposition of assets takes place before the assignment is effective. This process requires the company (assignor), secured creditor, and proposed assignee to work together to have all of the

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pieces arranged in advance such that on the effective date of the assignment, very little remains to be done.

If business owners elect to place their company in either bankruptcy or through an assignment for the benefit of creditors, can they purchase their company's assets back in those proceedings?

RALLIS: If a company is in bankruptcy or subject to an assignment for the benefit of creditors, the owners of the company do have the opportunity to purchase back the company's assets (including possibly the purchase of the business as a going concern) in those proceedings. However, the owners must consider that any asset sale will likely require that they pay close to fair market value for the assets sought to be acquired and will likely be sold as part of an auction, where other parties will be entitled to submit overbids. Additionally, to the extent that the assets are subject to a secured lender's lien and the lien exceeds the value of those assets, any sale would also require obtaining the cooperation of its secured lender(s).

What are some of the advantages and disadvantages of filing a business bankruptcy?

MOLDO: Some of the key advantages:
- All litigation is stayed
- Time is available to formulate a plan of reorganization
- The ability to eliminate unprofitable assets
- Use of the Bankruptcy Code to recover preferential or fraudulent transfers

Some of the main disadvantages:
- Cost
- Reporting requirements and the need for complete transparency and disclosure
- The possibility of having to interact with a creditor's committee
- Uncertainty of market conditions and the overall economy

Some businesses are transacting with financially distressed businesses (e.g., key suppliers, customers, or vendors). What are some of the warning signs of financial distress that a business should be looking for in its business partners? What are some of the precautionary steps that a business can take to minimize the risks of non-payment, to prevent a disruption in business relations, and to minimize the potential for lawsuits to recoup payments received as a preferential transfer?

RAANAN & TEDFORD: Signs that a business is financially distressed include multiple, unexplained late payments, constant bank changes, requests that payments be sent to lock boxes, sudden and dramatic turnover of high-level employees, the loss of a key client(s), pending lawsuits involving key business operations, diminished quality of products or services, and requests for special financial accommodations suggesting the business has a hard time raising capital. To minimize risks associated with a financially distressed partner, a business can insist that all payments be made on time or even cash on delivery. A letter of credit from a reputable bank will also ensure payment and protect against bankruptcy avoidance actions. To reduce disruptions, a business can split its orders among multiple vendors or partners, which will ensure uninterrupted supply in the event one partner files for bankruptcy.

RALLIS: Some obvious warning signs of a debtor's financial distress include the debtor's deviation from its normal payment schedule (e.g., making sporadic, unpredictable payments), an increase in the overall amount and aging of the accounts receivable by the debtor, and a breakdown in communications with the debtor. At the earliest signs of the debtor's financial distress, a business should reach out to the debtor (and thereafter persistently stay on top of the debtor) to demand and ensure that it complies with the established terms and conditions of the parties' contractual relationship, including the timely payment of invoices. If the debtor is unable to comply, a business should consider requiring any future delivery of goods or services be conditioned on the debtor's payment in advance of or contemporaneously with (i.e., on a COD basis) any such delivery.

Do guarantors of the debts of a bankruptcy debtor have defenses that can excuse them from liability under the personal guarantees?

RAANAN & TEDFORD: The short answer is (always) maybe. California Civil Code sections 2787 through 2855, as well as common law, provide guarantors multiple defenses. These include exoneration, where terms of the original obligation were altered without the guarantor's permission (Civ. Code 2819), lack of consideration/value received by the guarantor (Civ. Code 2792), guarantor's obligations cannot exceed or be more burdensome than those of the principal borrower (Civ. Code 2809), and a right to demand that the creditor first seek payment from the principal obligor and foreclose on property securing the debts (Civ. Code 2845, 2849), among others. Unfortunately, California guarantors often waive most of their defenses (Civ. Code 2856), with exception of those based on public policy considerations such as crimes committed by a creditor. Business owners who sign personal guarantees need to carefully read loan documents to understand whether they are waiving valuable rights.

If business owners elect to place their company in either bankruptcy or through an assignment for the benefit of creditors (ABC), can they purchase their company's assets back in those proceedings?

RAANAN & TEDFORD: Yes. An owner of a business being liquidated in either bankruptcy or ABC can purchase the company's assets and continue the business under a new entity. In a bankruptcy, the owner's purchase offer will be subject to overbids from other potential buyers, including competitors.

> 'Retaining professionals who specialize in bankruptcy is one way to minimize the risk that unknown issues or concerns will arise.'
>
> BYRON MOLDO

In an ABC, the owner can purchase its company assets from the assignee without allowing others to overbid, if the purchase price is reasonable.

What are some of the other issues and concerns that a business may face if its business partner files bankruptcy?

RALLIS: A business may be the counterparty to an executory contract or unexpired lease with the debtor who has filed bankruptcy. In that situation, the business must be cognizant that it may be required to continuing performing under that contract or lease in the interim (i.e., until the time that the debtor has proposed to assume or reject the contract or lease), notwithstanding the fact that the debtor's prepetition obligations under the contract or lease remain outstanding and unperformed.

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BANKRUPTCY & RESTRUCTURING

Survey Reveals Financial Advisors' Outlook

COVID-19 is wreaking havoc across the country, especially in the financial markets and economy. With trillions of dollars in assets managed by the financial advisory community in the U.S., it's logical to explore how financial advisers are feeling about the pandemic and their outlook for the economy. According to the 2020 Trends in Investing Survey by the Financial Planning Association (FPA), the Journal of Financial Planning, and Janus Henderson Investors, financial advisers are feeling bearish about the market and economic outlook for the next six months.

This year's survey, conducted annually since 2006, showed the pandemic is having a direct impact on the optimism advisers have for the economy's short-term prospects. With President Trump declaring a national state of emergency on March 13—in the middle of fielding the survey—it provided an opportunity to see how advisers' six-month economic outlook shifted almost immediately. Results from March 7-13 showed advisers were generally neutral or somewhat bearish, with just 12 percent bearish. After March 13, nearly one-third of advisers were bearish (31%).

Another byproduct of the pandemic is the fact the survey pointed to financial advisers now opting for equities over cash and equivalents. Among the findings, 25 percent of advisers plan to increase their use of individual stocks, compared to 15 percent in 2019. Meanwhile, 14 percent of advisers said they plan to decrease their use/recommendation of cash and equivalents in 2020, compared to 5 percent who indicated so in 2019.

"It's not surprising to see more advisers re-evaluating their asset allocation strategy," said Adam Hetts, Global Head of Portfolio Construction and Strategy at Janus Henderson Investors. "The survey results rhyme with the unusually large volume of client inquires we've received since the COVID-19 sell-off began. An unprecedented market environment seems to have translated into an unprecedented amount of rebalancing and reallocation. What's really different to me about this year is the humbling effect this sell-off has had on investors - portfolio losses once thought unique to the Global Financial Crisis have come back again. When once-in-a-lifetime losses become once-in-a-decade, everything changes."

Each year, the survey looks at where financial advisers are investing today and where they plan to increase or decrease investments over the next 12-months. For the past several years, Exchange-Traded Funds (ETFs) have been the overwhelmingly preferred investment vehicle by financial advisers. This year was no different, with 85 percent currently using or recommending them. While ETFs continue to reign, Environmental, Social, and Governance (ESG) funds are now growing in popularity, with 38 percent of advisers using them.

ESG funds were first included in the survey in 2018 when 26 percent of advisers indicated they were using or recommending ESG funds with clients. That percentage remained steady at 26 percent in 2019 and increased meaningfully to 38 percent of advisers currently using or recommending ESG funds in 2020. Nearly one-third (29%) of advisers indicated in the 2020 survey that they plan to increase their use/recommendation of ESG funds over the next 12 months. Almost 40 percent of advisers reported that clients had asked them about investing in ESG funds in the past six months.

"Part of the magic of financial planning is to align a client's financial decisions with their values. I think the increase in ESG usage reflects an increasing awareness of how important ESG is to some clients and the increasing quantity and quality of ESG vehicles," said Dan Moisand, CFP, practitioner editor of the Journal of Financial Planning and past national president of FPA.

The 2020 survey, which received 242 responses by financial advisers of various backgrounds and business models, also indicated that clients were, not surprisingly, asking about the effects of general volatility (76%) and COVID-19 (70%) in their portfolios. Other key findings from the 2020 Trends in Investing Survey, include:

- In the 2019 survey, 55 percent of advisers indicated that clients were inquiring about investing in cannabis investments, and the number dropped to 34 percent this year. Likewise, cryptocurrencies saw a drop from 25 percent in 2019 to 17 percent in 2020.
- While a majority of financial advisers continue to favor a blend of active and passive investment management (66%), there appears to be a slight decrease in favoritism—29% in 2019 to 24% in 2020—toward a purely passive approach.
- Fifty-seven percent of advisers have reevaluated asset allocations over the previous three months, but it appears the reasons for the reevaluations changed mid-survey due to current events. For example, before March 13 (declaration of a national state of emergency), 26 percent of advisers reevaluated asset allocations because of the economy. After March 13, 64 percent say the economy was a factor.

"Many advisers make reevaluating allocations a consistent part of their process, but it's clear the Coronacrash hastened the timetable for that for many," added Moisand. "Broad diversification is so easy and cheap to attain these days; it makes sense that increasing usage of mutual funds would continue to rise. And the tax efficiency and trading flexibility of ETFs continues to draw interest. I'd be curious to see in next year's survey if advisers moved to more alternative investments or other non-traditional vehicles like options contracts to hedge. With their 'normal' investments down, marketers ramp up their efforts, and consumers often look at less plain vanilla offerings during bear markets."

Of those surveyed, 79 percent are Certified Financial Planner professionals, 54 percent indicated that they work as an independent IAR/RIA, and 35 percent say they have more than 21 years of financial services experience.

Learn more about FPA at FinancialPlanningAssociation.org

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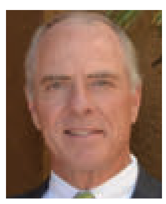

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