How Businesses Can Overcome the Stigma of Bankruptcy

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No matter what industry you're in, the goals of all businesses are inherently the same: turn a profit, maintain significant cash flow and strategically align your business toward flourishing growth. Still, countless businesses each year land themselves in a debacle of uncontrollable and unmanageable debt. For some businesses, bankruptcy is the only route out of the debt spiral.

Businesses turn to bankruptcy for many reasons. It could be anything from a struggling economy to poor business decisions. Whatever it may be, countless businesses find themselves in a place where their bills have become unmanageable, and legal debt relief seems like their only option.

Many business owners will try to avoid bankruptcy in fear of the impact it will have on their reputation among clients, associates, even friends and family. Other concerns are:

- Bankruptcies are listed on public record and can stay on business credit reports for up to 25 years.
- Due to the unregulated nature of business credit, a bankruptcy will impact all three business credit profiles in a variety of ways.
- The negative impact a bankruptcy will have on your business credit profiles will likely increase your risk potential of ceasing operations without paying back creditors.

However, if you focus on the stigma and ramifications, you'll likely never experience the benefits of declaring bankruptcy. **If done properly, both businesses and consumers can end up having their debt negotiated down or even waived entirely**. Many companies learn valuable lessons from bankruptcy, such as managing their finances and staying out of debt.

Despite being a highly stressful decision, filing for bankruptcy can have surprisingly positive effects on a business. It just needs to be done correctly and for the right reasons.

- Filing can give owners a chance to come up from under the weight of their debt, set up a payment plan with creditors, and renegotiate debt/contracts.
- Some businesses end up getting some of their debts dismissed.
- *Limit personal liability:* Business owners can decrease their personal risk by filing for bankruptcy. Depending on your business structure, if an owner was to only close the business without declaring bankruptcy, they would still be liable for debts. Closing a business with Chapter 7 will stop bills from building up.

Filing for Bankruptcy Shouldn't Be Done in Haste

Before doing anything, ask yourself these questions:

- Can my business's financial issues be resolved outside of court?
- Do I need a lawyer? (it is recommended that you procure legal assistance.)
- Will my business remain operational after filing?
- How do I plan on being profitable after bankruptcy?
- Will I reorganize my business structure and management after bankruptcy?
- Do I have a plan for repaying any debts that are not forgiven?
- Am I prepared to comply with the courts and cooperate with creditors? (this can involve exposing the business to criticism inside and outside of court.)

If you have prepared yourself for all that comes with filing for bankruptcy, then you should seek the advice of a legal professional and secure his or her services. While it is your right to file without legal representation, it can be a costly mistake if you do it improperly. You will need to consult with your lawyer about what filing chapter will best fit your situation going forward.

Four Common Types of Bankruptcy

When business owners turn to bankruptcy, they have multiple options. The Chapter they go with will depend on their industry, business structure, and whether they want to remain in business after the bankruptcy has been filed.

1. ***Chapter 7*** – To qualify, the debtor may be an individual, a partnership, a corporation, or other business entity. Under this chapter, the bankruptcy trustee liquidates all of the debtor's nonexempt assets to repay creditors. A business cannot stay operational after filing under chapter 7. This may be a good option for someone with little to no income and a lot of outstanding unsecured debt.
2. ***Chapter 11*** is frequently used by corporations, sole proprietors, or partnerships. It gives them a chance to reorganize their business, stay in control of assets, and negotiate a payment plan

with creditors for less than the original debt owed. All parties must agree upon the repayment plan. This may be the best option for a business that wishes to continue operating.

3. ***Chapter 12*** is a relatively new bankruptcy law and is designed for family farmers or fishermen who have a consistent annual income. It allows them a chance to repay all or part of their debts over time. Chapter 12 was created due to the economic realities faced by many family farmers/fisherman, and is less complicated and less expensive than Chapter 11 or 13.
4. ***Chapter 13*** is an option for individuals or sole proprietors who have a source of regular income, are in need of time to catch up on debts and who do not want to liquidate their assets. Debtors and creditors will negotiate a repayment plan over the course of three to five years. Under this chapter, individuals can save their homes from foreclosure as well as consolidate debts to be paid to the trustee, who then distributes to creditors.

In short, the impact that bankruptcy can have on your business credit will vary depending on what type of bankruptcy you choose, as well as the structure of your business.

How to Overcome Bankruptcy & What Damage Will Be Done

As described above, Chapter 11 is the most common option for businesses with a large number of assets, since it gives your business a chance to maintain control of assets and still operate while reorganizing and restructuring.

- If your business was able to reorganize and prioritize debt during bankruptcy, you should now be able to handle your bills. All bills should be paid on time (or better yet, ***early)***. If that happens, you are now in a place where rebuilding business credit profiles should be a top priority.
- In order to rebuild business credit profiles, you will need some lines of credit and verified vendors, ***who report to the business credit bureaus***.
- After you file, you should be diligent about monitoring all three business credit profiles (as well as the principal's personal credit profiles, depending on your business structure).
- ***Documentation:*** It's crucial to maintain your records after filing for bankruptcy. You must hold onto both your petition for bankruptcy as well as the discharge order. These records can be offered as proof that you no longer owe the discharged debts. If you have a bankruptcy on file, it's possible that you will be asked to provide this proof when seeking other business loans or even personal loans.

How Will a Bankruptcy Impact My Credit?

A bankruptcy on your business credit report is extremely tricky to remove. It can stay on reports for up to 25 years depending on the bureau. Since it is listed on public records, you can expect the filing to impact all three reports.

Depending on your industry and the other factors that impact business credit scores, a bankruptcy will cause the delinquency predictor to decrease. This puts your business in a high risk category.

- The delinquency predictor is listed on your Dun & Bradstreet report – it predicts whether or not your business will continue to pay bills in a "severely" delinquent manner.
- This score ranges from 101 to 670 (with 101 being the highest risk of paying late).

You can also expect that your credit scores will be severely affected by both the late pays and the debt that caused you to file for bankruptcy.

If you have a bankruptcy on file, you should be consulting with a credit expert. Reason being, a bankruptcy can impact businesses in such a wide variety of ways, and the only way to know where it is hitting your business credit is by analyzing each report. Once you sit down to talk with a credit expert about your reports, you need to ask questions about their strategy, how they plan to achieve success, and if they will be able to remove negative information.

From my vast experience in the credit reporting industry, I can tell you that it is possible to revitalize and rebuild business credit after bankruptcy. However, it takes an expert to analyze your reports and tell you exactly how much work is involved, as well as how long it will take to rebuild.

Bankruptcy Takeaways

Arguably, the most important things to take away from bankruptcy are the lessons you learn about debt and managing your company finances. Make sure that you never get your business into a situation again where bankruptcy seems like your only option.

This is especially true for those filing under Chapter 11. In this case, you've been forgiven of some debts, have received the option to reorganize or restructure your business, and have been given the chance to continue operations. The worst thing you can do is put yourself at risk again by not learning from past mistakes.

If your personal credit suffered from your business bankruptcy, do know this: it's important to separate your business and personal accounts, credit– everything. It's hard enough dealing with the emotional turmoil of this financial situation; you have the power to limit or even eliminate personal liability.