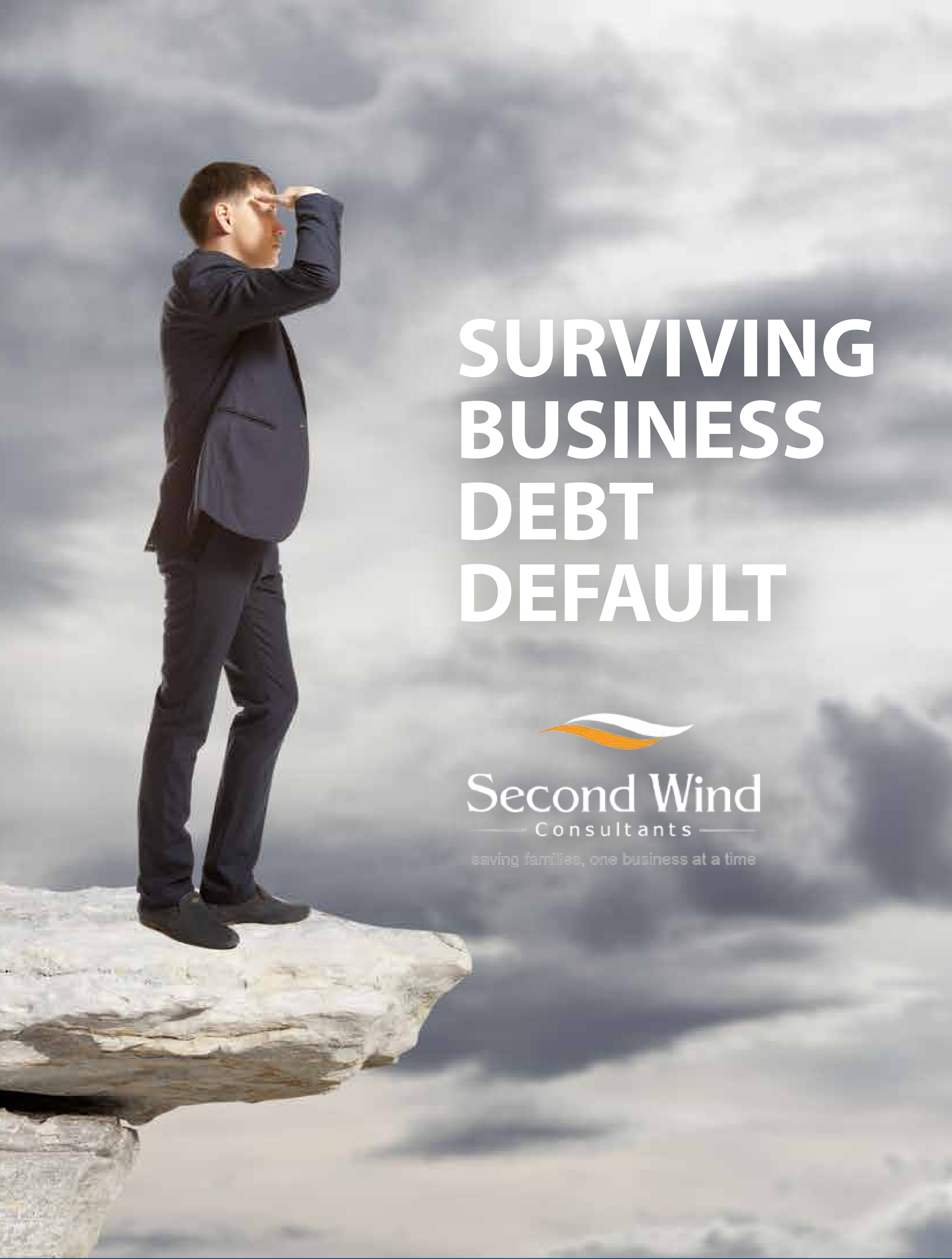


# SURVIVING BUSINESS DEBT DEFAULT

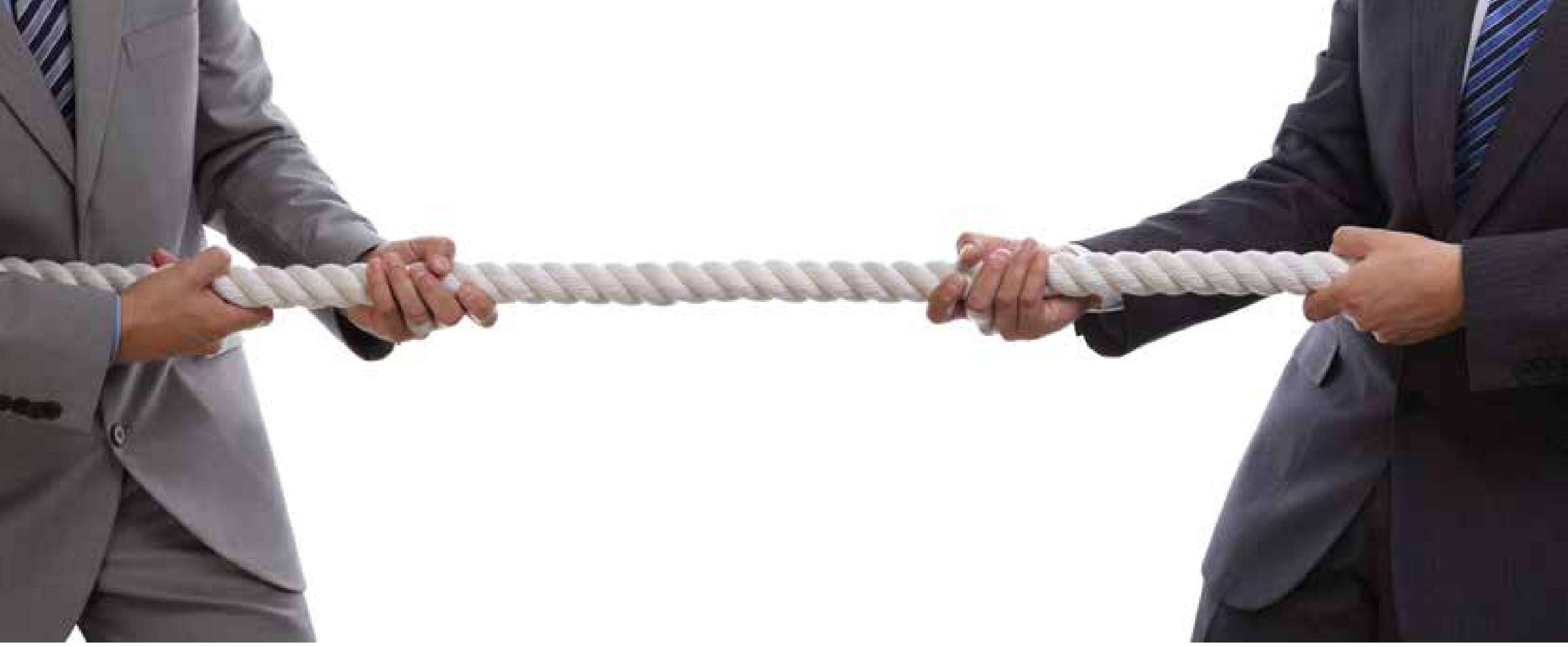
Second Wind
Consultants
saving families, one business at a time

# Regain Control over your Business

If you are reading this guide, you are undoubtedly struggling to pay your business debts and you are looking for some type of remedy to help you sleep at night. I'm glad you found us, as this might be the first step in getting you and your business back on an upward trajectory. You asked for free help, so hopefully you find the content in this guide valuable, and it helps you to start thinking differently about how you run your business.

We speak with struggling business owners every day, from small family owned restaurants to managers of publicly traded companies. There is no business debt situation we are unfamiliar with, so the lessons presented here can be applied to a company of any size, industry or financial composition. Over many years in the trenches fighting for the survival of businesses, we have discovered some basic "best practices" debt reduction strategies that can be applied to your company today in order to help you manage and reduce your debt. I encourage you to thoroughly read this guide to the end and implement the suggestions we have made in your own business. This is certainly not the furthest extent of our knowledge and ability, so if you have any questions along the way, you can always reach out and schedule a free no-obligation consultation with a debt expert or business turnaround professional so we can talk about your specific situation in great detail.

Let's start by looking at a typical debt situation and narrowing down what options are available to you. Perhaps you acquired your company for an inflated value using debt, or you purchased a franchise model that failed to reach promised sales levels and you never really had a chance to get off the ground. Maybe you are a business veteran who is struggling for the first time in 30+ years because of the Great Recession of 2008. No matter what your situation is, you really only have three options for handling your unmanageable debt and one of them is clearly superior to the rest.



## 1. Debt management and repayment plan

You are essentially paying your debts off in full with this strategy. Your company is in debt, you're struggling to pay and you also have limited assets and negative cash flow. Your plan is to pay the minimum amount monthly to your creditors plus some extra when you can to pay down the principal. You may perhaps ask your creditors to stretch out payment terms or reduce interest, penalties and fees, but at the end of the day, you will try and repay in full because you think it is the most honorable thing to do and you feel optimistic about the future.

What many business owners don't understand is when you have dug yourself deep in debt, climbing out of it is twice as hard. Let's say your company has accrued $200,000 in old debt on its balance sheet and you have been losing money. Reversing the trend is hard, but you also now need to generate $200,000 in cash to climb out of the hole. In a typical debt management plan, you cannot simply pay minimums plus a bit extra, you really need to allocate more to the debt if you want it paid in any reasonable amount of time. Another thing many don't realize is, if you need $200,000 in cash to pay off your debt, often you will be taxed on any new profits first before you can pay old debt! You really need to earn close to $275,000 before you have all the funds you need to repay the $200,000 of old debt! The "debt overhang" and the IRS are working against you and very few businesses can reverse this trend once they fall into a downward spiral. You had great intentions wanting to pay the debt in full, everyone wants to pay their bills. But, it is simply unrealistic for most small businesses to climb out of a big hole, so you need to explore more drastic measures.

## 2. Bankruptcy

If you are a small business owner contemplating a bankruptcy, please do yourself a favor and read this entire guide to the end and implement the recommendations we outline before you even consider bankruptcy as an option. Bankruptcy serves a purpose for individuals carrying huge debts who need a fresh start, but for small businesses, this is the beginning of the end of their company.

There are several types of bankruptcy, Chapter 7, 11 and 13, each with its own set of disadvantages.

## Chapter 7

This is in essence a complete business liquidation. The business is no longer in your control but instead a court appointed trustee takes control of the assets and sells them off to satisfy creditors. You lose your company, you lose control and worse yet, all your personal guarantees remain in place for you to deal with and your company is now gone. Often the trustee will spend much time scrutinizing your personal expenditures, any high salaries or disbursements in order to get the failing business owner to pay even more to the bankruptcy estate. After all, bankruptcy has huge costs and the trustee gets paid a percentage of what they collect for creditors. So it is in their best interest often to try and "pierce the corporate veil" and come after everything you have. If you are trying to SAVE YOUR COMPANY, you definitely DO NOT want to file a chapter 7 bankruptcy.

## Chapter 11

There is a reason that 70% of chapter 11 filings end up failing. You better have at least $25,000 to hire a good attorney, but then there are other fees, cash collateral restrictions, lots of administration and loss of privacy and control. In a chapter 11, you are going into court in the hopes that your creditors will be fair and take less than they are owed and allow your business to survive. However, you likely have multiple creditors in various "classes" and it is hard to get everyone to agree to a plan that results in them taking less than what they are owed. Especially if your business has limited assets, the creditors will vote to simply liquidate you if you don't have enough collateral. What ends up happening 70%+ of the time is the business cannot support the costs nor does it have the assets; customers and vendors become afraid because the company is in bankruptcy and the court converts you into a chapter 7 case and the business gets liquidated. Do you like those odds for your company's survival?

## Chapter 13

Why a company would file a chapter 13 is beyond my level of comprehension. The business basically goes into court and gets forgiven of penalties, fees and interest that it owes on various debts. Principal is not reduced and the company now has a bankruptcy on their record. The business owner could usually achieve the same level of success as simply working out arrangements with all the individual creditors and avoiding the bankruptcy, the high costs and the credit blemish.

## 3. Debt Restructuring and Settlement

In a debt restructuring plan, you can save your business from being liquidated, achieve debt forgiveness with creditors and maintain full control of your company throughout the process. There is no public record and all settlements that are reached will be kept confidential. This process happens outside of court, without the high cost and administrative oversight that a bankruptcy would entail, and it can achieve a similar result. Essentially you are going through a process of restructuring your business so its assets are protected from creditor liquidation, then you are settling the outstanding obligations for only a portion of the balance owed.

Many business owners do not even know that this option exists mainly because there are few companies that offer this service and people think that the only options are to either pay in full or file a bankruptcy. A debt restructuring plan such as the one offered by Second Wind, is almost a hybrid of both strategies. You won't be filing bankruptcy, and you also will not be paying your debts in full, you will maintain control of your company, the process, but you will also end up repaying a portion of your debt. Something we often refer to as "affordable losses."

Clearly one strategy stands out above the rest. This is because we strongly believe that the current bankruptcy code is very flawed and puts small business owners at a huge disadvantage. Chapter 11 might work for many multi-billion dollar companies, but it will not work for a small business owner who cannot even afford the attorney's fees. Our strategy recognizes these flaws and delivers a better result outside of court, a venue where the small business owner actually has a chance of winning.

I hope you have a better understanding of what your options really are and you interested in speaking with us further about a debt restructuring and settlement plan for your company.

But first, please read the following five suggestions that you can implement in your business today to get your debt under control. If this is not enough to alleviate your woes, please don't hesitate to get in touch with us for a more in depth discussion so we can formulate a strategy specific for reducing your business debts.

# Plan of Action

## 1. Prioritize your debts and create a clear debt management plan

We once had a client in the food business that was heavily in debt and on the brink of failure. When we first analyzed his business debt problems, he was in default with his secured creditors and he was spending $12,000 per month repaying old vendor debts. Come to find out, all the vendors had cut him off or put him on cash on delivery terms, but yet he was still paying their old debt. We asked him one simple question, "WHY?"

Come to find out, they were all threatening lawsuits, shaming him, and they worked in his industry, so he felt guilty. Bottom line, he was being emotional and failed to prioritize his debts properly and it was about to kill his company.

Prioritizing your debts serves two critical purposes. It forces you to allocate your cash flow towards the debts and expenses that are most crucial to the operational success of the company. It also allows you to identify which debts you may want to attempt to settle or modify in order to improve cash flow and best yet, it REMOVES THE EMOTION from this process.

The best place to start prioritizing your debts is to create a business debt schedule for your business. A business debt schedule is a financial document that lists all creditors of the business. This is not the same thing as an accounts payable schedule, as that report takes into account only short-term unsecured debt, nor is it a balance sheet, which does not itemize each debt. A template of a debt schedule is displayed below.

**Business Debt Schedule As of: 01/01/2015**

**Company Name**

| Creditor Name | Original Amount | Original Date | Present Balance | Interest Rate | Maturity Date | Monthly Payments | Security/Collateral | Notes |
|---|---|---|---|---|---|---|---|---|
| | | | | | | | | |
| | | | | | | | | |
| | | | | | | | | |
| | | | | | | | | |
| | | | | | | | | |
| | | | | | | | | |
| | | | | | | | | |
| Total $ | $ - | | | | Total Monthly: | $ - | | |

Download the template in Microsoft Excel format by clicking here:
http://secondwindconsultants.com/wp-content/uploads/Business-Debt-Schedule.xlsx

When creating this business debt schedule, a business owner should begin by listing the business' secured creditors first. The rule of thumb here is to list the creditors in order of who can do the most damage to the business should the debt be in default.

Secured creditors are creditors who filed a lien or UCC-1 against the assets of the business and have rights to liquidate that collateral in the event of default. These creditors should be the first priority when it comes to payment. We suggest listing them in order of date of origin because the creditor with the first lien filing has the most secured rights against your business collateral.

From there you should analyze your list of supplier debts by putting them into the following categories:

### Critical Vendors

These are vendors or suppliers that play a key role in the operations of your business. They could supply a key raw material or not be easily replaced by a competitor on the open market. Let's pretend you are an electronics manufacturer and one of your key components that sets your product apart can only be obtained from one vendor in the entire country. This supplier would be highly critical and you should make their payable a priority.

### Somewhat Critical Vendors

These are creditors, vendors or supplier for which you would like to maintain an ongoing working relationship with but also could be replaced with other suppliers if necessary. You can attempt to settle with these vendors, or slow pay because they have little recourse against the business should you not pay them on time or at all.

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Once the schedule is complete, you can now take a look at your cash on hand, and pay your creditors in order of priority. You might be surprised to see how much money you were throwing away by paying creditors who are very low on your priority list. You might save thousands of dollars per month just by completing this exercise.

## 2. Create a settlement budget & raise cash

Now that you have prioritized your debts, you should be managing your company's cash flow properly and only paying those obligations that are of the utmost importance. Now it is time to take some of that excess cash you are saving and build a war chest of funds to settle with. It is not always easy, but here are the steps you should take to make it happen.

Before you get started, it is important that you change both business and personal bank accounts in order to protect your available cash. You don't want to start saving, only to see a creditor aggressively sweep your accounts! Your old accounts may be compromised by previously allowing your creditors access to the sensitive account information. By starting over in a new bank account, you decrease the likelihood that any of your creditors successfully garnish or lien your bank accounts since they do not know where they are located. You can read more in detail here:

http://secondwindconsultants.com/can-bank-accounts-garnished-sba-loan-default)

Once your cash is safe, you need to begin to build savings in anticipation of settlements. As part of that savings plan, you should reallocate the savings realized from not paying monthly debt service. In order to settle with most creditors, it requires payment default. During that period, you should redirect any cash flow saved by not paying debt service into an account that will be used for future settlements. For example, the client mentioned above allocated the $12,000 per month that he was paying to unnecessary vendors to a savings account instead of minimum payments. In six months he built up over $70,000, which was used to make settlements on all the old debt. Why pay a vendor that is owed $20,000, $1,000 per month when in four months you could offer them $6,000 to settle in full? You will be surprised what kind of reduction a creditor will take after a few months of receiving nothing, but you need to start building up cash for these lump sum payments now. You will read more about the settlement process below.

Another way to raise settlement funds is to sell underutilized assets. If you have excess equipment that is not being used enough to be considered a profitable asset, liquidating it and turning it into cash can be an effective way of creating settlement funds and reducing debt. Make sure that any assets you sell are not subject to a lien filing. If the collateral is secured, you will need approval of your creditor prior to any sale.

The same logic can be applied to selling excess inventory. Call your biggest customers and offer them a big discount if they purchase some of your old inventory or hold a liquidation sale. One recent client of ours was a Stove Company in Vermont. They had some $250,000 in inventory on their balance sheet that hasn't sold in years. When we suggested they hold an auction and turn that inventory into $50,000 cash, they nearly threw us out of the room. It took them time to realize that the $250,000 value on their balance sheet was a fantasy and it wasn't worth that amount. The $50,000 received in the sale went a long way in settling with their creditors and reducing the overall company's debt.

Once you have produced as many settlement funds as possible from the business, any remaining amount necessary to settle with all your creditors will need to come from the personal net worth of the business owner.  Take a look at your personal assets and income. Determine how much of your monthly household income can be set aside for settlement funds and determine whether any personal assets can be easily liquidated. This might not be easy as you may have reduced pay and already put assets into your company, but make sure you do everything you can to save more and sacrifice for the good of your company.

After creating your savings plan, it is important to put in place automatic systems. Open a separate bank account just for settlement funds and schedule transfers in advance from both your business operating accounts and personal accounts. By doing this you can ensure the cash flow saved from debt service and any excess household income will be saved and available when necessary. When any sale of assets or inventory occurs, deposit the money into this separate account. Do not keep a debit card for this account and do not use the funds for any other purpose. If strict policies are not put in place, the cash will be allocated elsewhere. Businesses struggling to be profitable always have pressing needs and it will be easy to dip into these funds if you don't set rules for yourself.

## 3. Settle your unsecured debts

Once you take step #1 & #2, this should expand on the work you have already completed. Once you have created a debt schedule and prioritized your debts and created a budget and savings plan it is time to get some of the debts eliminated with some good old fashion haggling with your creditors.

Settling your unsecured debts for less than what's owed will improve your businesses cash flow and will clean up your balance sheet. Using the debt schedule previously discussed, you should have a list of your unsecured creditors in order of priority

Critical vendors should be addressed first in order to ensure that the business continues to operate as normal. You can achieve debt forgiveness with these creditors if you adequately explain your financial situation and request a partial write down of the balance owed. However, the goal in this group is more to maintain the relationship and establish repayment plans that satisfy both parties. Often paying the balance owed over the course of 6-12 months will maintain the relationship and allow the business the cash flow relief it needs.

"Somewhat critical relationships" should attempt to be settled for less than what is owed. If successful, you will both retain the relationship and settle the outstanding obligation. If not, the creditor has little recourse against you and your business and the relationship can easily be replaced with another vendor.

For "unnecessary vendors", the only goal should be settlement, and for as little as possible. There is no relationship to salvage so debt reduction is the sole objective. Often times it is beneficial to wait until these debts are written off and sold to debt collectors for a discount. Those debt collectors are then looking to make a profit, not necessarily collect the entire balance. For example, if you owe a $10,000 debt to a creditor and after many months of non-payment they sell the debt to a collection agency for $1,000, you would likely be able to settle with that creditor for $2,000 (20% of the original balance). The collection agency would make a nice profit and you are able to settle for far less than what's owed. A win for you, as it eliminates the risk of being sued, and takes $8,000 of debt off of your company's balance sheet.

This is particularly true for credit cards and lines of credit. When dealing directly with the original creditor, they look to retrieve as much of the balance as possible. If you do receive a settlement, it is typically for 45% or more of the original balance. Whereas if you wait until the debt is sold to a collection agency, the opportunity to settle for much less will arise.

A settlement proposal to unsecured creditors is typically less formal than one presented to a secured creditor. You should not offer any financial information and provide the absolute minimum of what they request. If a creditor accepts any settlement, it is important to obtain a contingent release letter from the creditor that states that upon receipt of the settlement amount, they agree to release you and your business from any further obligation stemming from the debt in question.

If you can successfully do this for most of your unsecured creditors, in 12-24 months you could significantly clean up your company's debt load and be in a much healthier position to grow your company.

## 4. Loan modification requests

You borrowed money to buy a business or to expand it but since obtaining the loan, revenues are down and you are struggling to make payments. Sound familiar?
A loan modification may provide the additional cash flow relief you and your business require in order to get back on the upswing. A successful loan modification can reduce your payments by re-amortizing your debt and/or lowering your interest rates. This is not always easy to accomplish, as a bank will not always grant relief to a business that is still current, but struggling on payments. If the financials are too strong, you will be declined. If they are too poor, you might be at risk of being liquidated or put into a banks' workouts department. Make sure you are prepared and confident before you attempt this on your own and you can read more on the subject here:

http://secondwindconsultants.com/sba-loan-modification-loan-deferment-qualify

First, contact your lender and advise them of your struggle and be prepared to discuss your hardships and also your plan to remedy your problem. Additionally, have your financial books in order as the typical documentation they will be requesting is as follows:

2 years tax returns

- Personal financial statements
- Current balance sheet
- Year-to-date profit and loss statement
- Accounts payable schedule
- Accounts receivable schedule

The lender heavily relies on the financial information provided, so make sure it is accurate and that you know your numbers well for future discussions. Beyond the numbers themselves, the banker will also examine your character when making a decision. They will ask themselves:

- Has the borrower been truthful and transparent?
- Are they reliable? Do they return phone calls and emails promptly?
- Are their financial records in order or do they run their business like a personal piggy bank?
- Are they a hands-on operator who will be able to succeed in the turnaround plan?

If you are not prepared and you do not give the bank a reason to believe you can turn the company around, why would they work with you? Wouldn't it be better to cut their losses and move on rather than help an inept operator?

Knowing your business well and demonstrating huge commitment to success is the best way to reach a successful loan modification. Therefore we highly suggest that every modification request include the following two pieces, even if they are not requested by the lender:

### Letter of Explanation

This is a formal written letter from the business owner to his banker. It should summarize all conversations had to date with the banker, discuss the current financial standing of the company, and spell out exactly what is being requested of the bank and why the business will be able to honor such a request. Tell them what measures you have implemented to turn the company around and what further efforts you are taking. You should demonstrate personal sacrifice here and show that forces beyond your control are having an effect on your business.

### Cash Flow Pro Forma

Many business owners have no experience when it comes to projecting accurately and may need the assistance of an expert in order to do so. An accurate pro-forma is a critical element in obtaining a modification from your lender, so seek help if you do not know how to put one together or download this guide:

http://secondwindconsultants.com/second-wind-cash-flow-proforma

By providing accurate, month-by-month projections going out at least 12 months, it takes the guesswork out of the equation for the bank. They no longer have to make assumptions based on past performance alone and therefore will not come to inaccurate conclusions. You also need to show them that your request is temporary and that your business will get back on track quickly if they work with you.

These two items tell your story. Many of these decisions are made by committees of bankers and not just the representative you may regularly speak with. Therefore, without these items, your voice is not heard throughout the process and you have no platform in which to affect the outcome.

To be successful in achieving a modification, your entire presentation should prove that the business is incapable of honoring the debt service payments as originally agreed, but is capable of honoring the proposed reduced modified payment terms. If your financial presentation and projections do not show that the company is capable of performing under the new terms, the modification request will be denied and liquidation proceedings could occur.

Once you present the package to the creditor and they accept the terms, a loan modification agreement must be drafted and signed by all parties, recording the new terms and conditions of the modification.

## 5. Reduce your rent

You entered into a lease agreement with your landlord, so you should honor this commitment. However, when your business is struggling and at risk of closing, wouldn't it be prudent for you AND your landlord to make some sacrifices? In many cases, a landlord would rather work out a modification to their agreement with you than look for another tenant when you inevitably go out of business. You may feel guilty at first, but this is just part of doing business and you need to explore all options to keep your company going.

Rent is typically the next largest expense for a business after their labor and cost of goods. Getting a reduction in this expense would certainly help your business through any cash flow struggle, so definitely consider this measure. In order to be successful at a landlord workout you must understand a few key elements listed below before you begin:

### Understanding current market rent rates

In order to be able to approach your landlord and request a reduced rent rate, you should first understand what similar property is renting for in your area. The reason this is important is because if your landlord is able to rent your location to someone else for $10 per square foot and there are many replacement tenants out there, then they should not rent to you for any less than that amount. Alternatively, if you can rent similar space for $10 per square foot or less, then you should not be paying your landlord much more than that. By having researched comparable properties, you can create a compelling case to the landlord for a reduced rate.

### Understanding the amount of square feet you truly need

How many times have you walked into a business and noticed that half their space is empty? I have visited many clients over the years and seen this exact scenario. So I always ask my clients, "Why do you need 10,000 square feet if you are only using 5,000?" They simply didn't know that they could do anything about it.

Once you present the package to the creditor and they accept the terms, a loan modification agreement must be drafted and signed by all parties, recording the new terms and conditions of the modification.

Similarly, it may be possible for your landlord to offer you a similar space within your building for a reduced rate just by moving. By understanding exactly how much space the business needs to operate, you can create an opportunity that benefits both your business and the landlord. You just need to be creative and have a discussion with your landlord. Wouldn't they rather help you and your business than see you go out of business and have a vacancy in their building?

## Request for rent reduction

Once you have done your research on how much space you need and the current market rates for similar space in your area, it is time to present the landlord with a request for a rent reduction. This request should include the following information along with honoring any additional requests of the landlord.

- Letter of Explanation / Request for rent reduction
- Current business financials
- Listing of other properties within the area for comparison

The letter of explanation should focus on the business performance and how the above market rent rate is preventing profitability and solvency. It should also summarize your research into current market rates. The objective is to prove that the business is not able to perform as originally agreed and to prove that current market rent rates are lower than the contracted lease rate and therefore a reduction is appropriate in order to avoid a vacancy and assure long-term tenancy. If successful you will prove that the landlord will do no better by forcing an eviction of your business and leasing to another interested party because doing so would require they rent the space for the current market rate, which you are willing to pay without the cost and risks associated with finding a new tenant.

The current business financials should show the cash flow struggles of the company and detail any other secured creditors the business has to offer. This shows the landlord that the business truly cannot afford the current rent and that the business assets are encumbered by other creditors and are of no value to the lease obligation. Once in agreement for a new lease rate, the current lease needs to be amended.

Hopefully your landlord will be flexible and grant you one of the options above. Many landlords can be stubborn and threaten you with an eviction if you don't comply with the original rent. Depending on the severity of your situation, it might be a good idea to consult with an expert or hire an attorney to help you through this negotiation. In most cases though, you will find that landlords are business people and will act rationally if you present a compelling case.


## Take Action

We truly hope that you have found some useful information in this guide and that you will actually implement some of these recommendations on your own. We would love to hear your feedback on this guide, so please feel free to contact us http://secondwindconsultants.com/contact anytime.

At Second Wind Consultants we provide small business owners with solutions to their business problems every day. We focus on debt restructuring and settlement, performance consulting and capital formation in order to give your business the resources it needs to be successful. This guide is just a small example of the type of guidance we can provide to get your business on track. If the measures you have taken are not enough, we are always here to provide professional guidance and support and can offer you a full debt-restructuring plan. Call us at 866-600-9080 or click here http://secondwindconsultants.com/contact to request a consultation if you would like to speak with us regarding a more aggressive action plan.

Best of luck to you and your business.

Sincerely,

Your Friends at Second Wind