



The Business Taboo - Bankruptcy

The federal government has enacted a set of laws that can be used by individuals and businesses to help protect them from their creditors. These are the bankruptcy protection laws. Depending on the need, type of business or level of assets, individuals or businesses may take advantage of a specific type of bankruptcy protection as defined in various chapters of the law. The most common bankruptcy chapter used by farmers is Chapter 12 - The Family Farmers Bankruptcy Act of 1986. It is a law specifically designed for family farms with less than \$1.5 million in assets trying to reorganize and stay in business. It provides much leeway in allowing the farmer to hold creditors at bay while making necessary changes to the farm business so that the business can survive. Taboo or not, bankruptcy is a tool that can help save family farms.

Obstacles

The first and biggest hurdle for most people to overcome are the feelings of shame and failure that are inescapable when the certainty of bankruptcy looms. Only after the crying is over, the shock has subsided and the reality of the situation has set in is one able to gather the strength and determination to move forward.

Pride is an obstacle that keeps some farmers from filing for bankruptcy protection or selling-out altogether. Overwhelmed by debt, these farmers struggle for years, making payments on old debt (to the appreciation of their creditors) while the farm business slowly strangles because it is unable to replace capital or make new investments in the business. Some farmers must make the decision to cut losses and start anew with more wisdom and a stronger foothold to ensure a profitable, brighter future for their family at the cost of wounded pride.

Many farmer find themselves at the brink of bankruptcy partly due to the over-generosity and faith their creditors and suppliers have in them. These creditors usually include a fair number of unsecured suppliers that "have been so good to us." Unsecured creditors rarely recover the full amount owed to them by their bankrupt customer. Creditors that are hurt the most are often the ones that have "helped" the most, making the decision to file even more difficult.

Expect your unsecured creditors to advise you against bankruptcy. They have the most to lose. Secured creditors can be supportive, neutral, or altogether unsympathetic, depending on how much they are likely to gain or lose. Debt owed to Federal and State governments for employee payroll taxes are almost never forgiven, but repayment terms can be negotiated.

Bankruptcies are expensive, averaging from \$10,000 to \$30,000 and higher. Most attorneys will require up-front retainers ranging between \$5,000 and \$20,000. Hourly rates between \$150 and \$400 provide the incentive for clients to provide them with the information they need quickly and efficiently. Surprisingly, money itself is not a big obstacle to filing. This is because attorney and court fees are usually paid from funds that were earmarked for banks and other creditors. During the initial stages of bankruptcy, normal payments to creditors can be suspended for at least three months.

Finally, a bankruptcy will affect your credit record for a long long time. That does not mean that you will never get credit again. However, it will always take more explaining.

Who should file

Bankruptcy reorganization under Chapter 12 for farms with less than \$1.5 million in assets or Chapter 11 for businesses with more than \$1.5 million in assets should be done only after analysis shows that your potential to operate a profitable business is very good after reorganization. Business owners need to take a long, hard look at the reason why their business is in dire straits to begin with. If it is due to years of below average profitability, poor management decisions or poor farming resources, then getting-out may be the best option. Farms with high net worth are not usually good bankruptcy candidates.

If the business stumbled during an expansion, a lender pulled out during the middle of a project, management has changed or became significantly better or the farm experienced natural disasters beyond all reasonable probabilities, then re-organization under bankruptcy protection may be an option. Farms with low net worth make for better reorganization protection candidates.

What to expect

Under Chapter 12, farmers have 90 days from the time of filing a petition to submit a

reorganization plan for approval in a Federal bankruptcy court. This is a critical period for the farm business. Creditors sometimes try to have the Judge dismiss the bankruptcy petition so that they can move to seize and liquidate assets to pay off their loan balances. Grounds for dismissal could include risk of the creditor losing the value of their collateral such as livestock, inventory, or equipment. Creditor also may fight to retain control over cash from the sale of farm products. Since most creditors routinely hire attorneys experienced in legal maneuvers to protect their interests, you should also be prepared to put your own team of professionals together to protect your interests.

At the beginning of the bankruptcy, suppliers will expect to be paid c.o.d. Within months if everything goes smoothly, you may be back to a net 30 day billing cycle. Some suppliers may stop doing business with you, but the smart ones realize that the only way to recoup their losses is to keep you as a paying customer. Operating lines of credit are usually not available making it more important to manage cash flow for crop inputs or high labor cost periods. Given the right circumstances, creditors have been known to extend more credit or capital investment and leasing companies may risk additional financing during bankruptcies.

In a bankruptcy plan, farmers can specify a 3-5 year budget for paying creditors, including setting fair amortization schedules and interest rates. Judges have the authority to approve, disapprove, or terminate the bankruptcy protection altogether. Unsecured creditors may be paid from 0-100 percent of their claims depending on the plan and normally, all similar creditors are treated alike. Secured creditors may be forced to write-off debt to an amount equal to the value of their security. Don't expect any creditor to give up money without a fight. This is where an experienced and skilled attorney can really help. Search for a good bankruptcy attorney that is familiar with farming and business planning as well as law before venturing into any bankruptcy plan.

Get tough, be tough.

Filing for bankruptcy protection for re-organization purposes is not an easy way out of a difficult situation. It is a difficult way out of a difficult situation. It cannot save farms that are unable to compete in an increasingly competitive industry. It can provide the needed boost to help smart, competitive farm businesses out of certain perilous situations caused by extraordinary circumstances. In bankruptcy, farm managers must become above average

businessmen and be willing to learn about and live in the world of the legalese. It is not for the faint hearted, but neither is farming.

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