

6 Options for Escaping Distress

By Dan Rexford

Because we have worked with distressed business for 22 years, we know that each situation is unique and canned solutions simply do not yield strong results. However, it is useful to categorize potential solutions, examine them thoroughly and apply them to your situation. There are six ways of escaping distress: 1) Improve financial performance; 2) Restructure the loan(s); 3) Secure new financing; 4) Bring in new equity; 5) Capitalize on a sales and marketing process; and 6) Liquidate.

We created a simple tool for our clients, providing a framework for taking a hard look at the business as it currently stands and determining which solutions are truly options. Although we deleted the names to protect our client, an actual example appears below.

6 Options for Escaping Distress*	Status at Xxx XXXXXXXXX	Advantages to XXXXXX XXXXXX	Equity Partners' Contribution
1) Improve financial performance.	Exhausted -- great recession prohibited success.	N/A	N/A
2) Restructure the loan.	Most Likely Exhausted – XXXXX XXXXX fatigued and uncooperative	Bringing in new money or having an impartial 3 rd party fully test the market could lead to XXXXX reconsidering	Will turn over every stone.
3) Secure new financing.	Highly unlikely without very strong balance sheet. Linked to 4) below.	If it is possible, probably best possible outcome.	Will turn over every stone.
4) Bring in new equity.	Unlikely without clear path to financing. See 3) above.	If it is possible, pretty fair outcome.	Will turn over every stone.
5) Capitalize on the sale process afforded by bankruptcy.	Highly likely because of advantages associated with process.	Best chance to participate in upside as part of NEWCO and obtain release from deficiency claims.	Will attract multiple suitors.
6) Liquidate.	XXXXXX XXXXXX's "solution."	Disaster.	N/A

* See article from well-known bankruptcy counsel, Bobby Guy, <http://www.turnaround.org/Publications/Articles.aspx?objectID=9108>

IMPORTANT NOTE: Nothing prevents you from joining forces with the investors you have already talked with and participating in a sale process. In fact, because you will bring such strong value, I expect every prospective Buyer will want you on their team.

In this particular instance, the owner concluded that everything possible had been done to improve the business. While this is generally the case, as we conduct our analysis we often provide recommendations business owners find effective. While our partners have significant management expertise, management consulting is not our core business so generally these types of recommendations are provided without charge. We see it as a natural outgrowth of our process and simply the right thing to do for our clients.

This particular client had also determined that further attempts to restructure the loan with the existing creditor would be fruitless and, in this case, we agreed. In other cases, we have found that creditors may well consider restructuring if a 3rd party has given them a true, real-world assessment of their situation. In these challenging economic times, creditors are often simply too busy to fully assess their situation and appreciate accessing other professionals' expertise.

In this instance, we had to tell this client that refinancing was highly unlikely. We knew the market and the players and did not believe anyone would refinance the loan with favorable terms. This was harsh medicine, but it is critical to face challenges head on. There appeared to be a possibility of restructuring the existing lender's debt via a plan of reorganization, but it needed to be bullet proof. The creditor was fatigued, aggressive and prepared for battle.

Securing an equity infusion would be highly unlikely in this example as well because additional financing would be needed to further develop the business and make it profitable. No one could be expected to put in additional equity without a clear path to additional financing, which simply was not available for this business.

This particular client would benefit most from a comprehensive sales and marketing process. Like most owners, they had had discussions with potential investors and they knew their business concept and plan would be successful if they could escape distress.

A planned, structured, scheduled, exhaustive sales and marketing process has four primary benefits: 1) The process may yield a price that satisfies creditors and offers an attractive return for equity holders; 2) If the owner has access to capital, he may be able to buy the company back at an attractive price, debt free; 3) Crystallizing the process brings potential investors who had previously talked about contributing capital to the table; and 4) The owner is introduced to a wide array of potential buyers/investors and is free to join forces with them.

Liquidating is almost always an option of last resort. If there really aren't any prospects for the business, agreeing to liquidate and maximize the value of what is left for creditors is often helpful with obtaining relief from personal guarantees. While we can maximize the value of assets in liquidations and have had good success obtaining relief from personal guarantees, our interest lies in keeping businesses open, saving jobs, and providing opportunity for recapitalized, strengthened companies to realize their potential.

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