

## CHAPTER 11- DOES THE BUSINESS QUALIFY?

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Chapter 11 is not a magical panacea for solving problems facing an entity contemplating the filing of a Petition for this relief. Three major queries must be addressed at the outset of proceeding with this remedy.

The initial determination which must be explored by the Debtor and its professionals is whether the enterprise is viable and has the ability to operate profitably. Can this entity reorganize?

The aforementioned threshold query requires the Debtor to “be forced” by his attorneys, accountants and other advisors to realistically assess the circumstances which caused a deterioration of the debtor’s business and the relationship with its creditors. For the most part, Debtors are “forever optimists” who believe that notwithstanding all of the “rainy days” endured by the business; tomorrow will bring “sunshine” and profitability. Hence it is important, if not mandatory, to review the financial records of last several years to identify the cause of the entity’s illness and the ability of the business to turn itself around. There are times when a Chapter 11 is filed on an emergency basis which does not afford the Debtor the time to make this assessment. In such cases the analysis should be undertaken immediately following the filing of the Petition. Chapter 11 will not make a failing business successful.

Secondly, after reaching the conclusion regarding its viability, the Debtor must investigate its ability to survive during the Chapter 11 case. Can the business operate at break-even while reorganizing? Will the Debtor generate enough revenue to pay its post filing obligations timely with the knowledge that most creditors will require payment on a C.O.D. or cash before delivery basis. Furthermore, in certain industries it must be ascertained whether the Chapter 11 filing will cause such a diminution in business opportunities that the Debtor is, on a practical basis, unable to sustain the effects of the filing on its ongoing revenues. Debtor must also consider the credit or financing needs of the business, i.e. account receivable financing, need for a line of credit or letters of credit - which all require the assessment of the availability of a source of financing during the tendency of the case. Concomitantly one must consider the likelihood of operating if no financing is available.

The third prong of the initial inquiry is the Debtor’s ability to obtain the exit financing necessary to fund its reorganization plan and properly capitalize the business and/or its ability to fund the plan from operations following the approval or confirmation of the plan by the court. This query also requires the Debtor to be cognizant of the costs involved in the Chapter 11 process - fees to professionals, court costs (based on gross disbursements each quarter), potentially increased

cost of “money” from financial institutions caused by the Chapter 11 experience. Furthermore, the Debtor must consider the impact of the Chapter 11 on the community of its vendors and customers.

## **Conclusion**

The foregoing is not intended to be an exhaustive analysis of the due diligence to be performed by the Debtor, its counsel and other professionals prior to filing the Petition. Each case presents unique issues attendant to the three essential questions discussed above. Chapter 11 is not intended for the uninitiated. Thus, it is incumbent upon a Debtor to seek experienced professionals to address the considerations identified above.

Allen B. Dubroff has represented debtors and creditors in more than five hundred reorganization cases and is involved each year in various out of court matters to resolve the claims of creditors/debtors without the need of court supervision. Please feel free to contact Allen B. Dubroff, Esquire at 215-635-7200, facsimile, 215-635-7212, or email, [adubroff@fsalaw.com](mailto:adubroff@fsalaw.com) should you have any questions.

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