Steps To Take if This Pandemic Is Hurting Your Business

Many companies are currently experiencing dramatic reductions in revenues due to the COVID-19 pandemic. Such companies (along with their investors and creditors) are justifiably concerned that they may need to restructure and even potentially seek bankruptcy protection. Below is a list of items that any potentially distressed company should attend to as soon as possible to increase the likelihood of obtaining the most favorable outcome under the circumstances.

I. Focus on Cash

The immediate focus needs to be understanding the company's cash position, with an eye toward maximizing runway – i.e., how long the business can operate before running out of liquidity. Cutting costs is an obvious first step, so the company should carefully review expenses to eliminate any unnecessary items. The more serious the situation, the more aggressive the company needs to be in identifying what is "necessary". In addition, the company can search for additional sources of investment, and if the company has any availability on already-committed financings, it should consider drawing down such amounts.

The company should make sure that it has a cash-flow forecast model that is on a cash basis, rather than only on an accrual basis, preferably for at least a 13-week rolling period. Such a model will facilitate cash tracking and planning and will be useful in any negotiations with creditors that may become necessary.

II. Analyze Key Agreements

Understanding the company's credit agreements, bond indentures, and other financing documents is critical to understanding the company's capital structure and determining viable restructuring possibilities. In particular, it is essential to know the relative priority of various creditor constituencies and the voting thresholds with respect to each for any amendments, waivers, or forbearance agreements.

For secured debt, not only do all collateral-related and intercreditor agreements need to be reviewed from a legal perspective, but the borrower should also investigate whether any material assets are unencumbered and whether lenders have properly perfected any intended liens. Any unencumbered assets can be pledged as part of an out-of-court solution or financing in any bankruptcy.

The company should also review significant vendor, supplier, and customer contracts. The company needs to understand any restrictions on assignment, and similar change-in-control provisions that are often found in contracts. These restrictions may affect the analysis of alternatives because they are often not enforceable in bankruptcy but could potentially cause obstacles in an out-of-court restructuring. In any event, the company needs to manage any concerns of critical contract counterparties during any restructuring. Investigating these relationships will also be helpful for the company's professionals in understanding the business and anticipating potential issues.

III. Formulate a Restructuring Strategy

There is a range of restructuring options available for distressed companies. Out-of-court options include refinancings, tender and exchange offers, equitization of debt, and sales of particular assets or businesses as going-concerns. Bankruptcy potentially expands these options, provides for an automatic stay of collection efforts, lowers consent thresholds, and provides the ability to bind dissenting creditors.

As mentioned above, one of the most important factors in any restructuring is the company's cash needs. The company may or may not be able to borrow under its current capital structure or it may need accommodations that creditors are or are not willing to provide. Sometimes it is only possible to access new money in bankruptcy.

It is important that the company is able to ascertain its view on its enterprise value as early as possible. Different parties in the capital structure are likely to have different views about such value that need to be reconciled or ultimately litigated. Reaching a consensus on value, and determining the feasibility of potential restructuring options given such value, increases the likelihood of avoiding bankruptcy and any related disruption and costs.

In the event bankruptcy becomes inevitable or is needed to facilitate borrowing or other aspects of a restructuring transaction, negotiating a deal before filing for bankruptcy is preferable. When a pre-bankruptcy deal leads to a restructuring support agreement and a pre-packaged reorganization plan, the time spent in bankruptcy will be limited, and any disruption can be better managed.

IV. Prepare a Communication Strategy

A company cannot function without its employees, and it likely cannot survive without its key vendors and customers. The company will need to develop messaging and preservation strategies for each of these groups to allay any concerns and preserve the business.

Employees could be significantly affected by any restructuring or bankruptcy. They may be fearful that they could lose their jobs, so it is important to communicate with them early and clearly. The company should make sure that all employee compensation (including withholdings) and benefits are protected, and developing key employee retention and/or incentive programs should also be considered.

The company may also have to justify its continued viability to both vendors and customers. Again, formulating appropriate messaging to each of these groups can be critical to survival.

V. Engage Professionals

Whether the company is focused primarily on smaller steps, like conserving cash, or whether it is planning to or needs to effectuate a major restructuring transaction, it should consider hiring appropriate professionals to assist it with navigating the process. These could include restructuring counsel, a financial advisor, and an investment banker, depending on the situation.

There are many advisory firms that specialize in distressed situations, and their professionals are able to develop and analyze forecasts and alternative courses of action and provide expertise and credibility that should help in negotiations with creditors. Often, hiring financial professionals will be a condition to any restructuring deal (sometimes even for relatively short-term forbearance agreements), and it is always better for the company to make independent choices on its own terms, rather than under pressure.

Conclusion

In addition to the immediate need to address operational issues related to COVID-19, a company may need to address restructuring alternatives and strategies. A distressed company should start implementing the steps suggested above immediately to best prepare for all possible outcomes and, even if just precautionary, making significant progress on these steps should maximize the likelihood of a successful and smooth restructuring, in the event one becomes necessary.

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If you have any questions about the issues addressed in this memorandum, please do not hesitate to call or email authors Joel H. Levitin at 212.701.3770 or jlevitin@cahill.com; or Richard A. Stieglitz Jr. at 212.701.3393 or rstieglitz@cahill.com; or email publications@cahill.com.