

## Can I Go Bankrupt On Just My Business Debts?

By John Skiba, Arizona Bankruptcy Attorney

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I routinely meet with small business owners that are going through financial difficulties and often get the question if just the business can file bankruptcy and eliminate the company debts. Before I can answer the question it is important for me to understand what the goals and plans are for the business. Are you going to continue operating the business or are you looking to shut it down? Either way sometimes bankruptcy is not the best option.

### **Should the Business File for Bankruptcy?**

If the business you are running makes money and you want to continue to operate the business, you need to deal with your debts through non-bankruptcy settlements or payment plans or look to a chapter 11 bankruptcy. A chapter 11 bankruptcy will allow you to restructure your debts, hopefully allowing you to emerge from bankruptcy in better shape than when you went in. I don't do chapter 11 bankruptcy work, but if you need a referral I can help you out.

If you are looking to shut the business down, a chapter 7 bankruptcy is available but not always necessary. An attorney I know put it this way, if a business is dying, you can let it die a natural death, or you can throw it a great big party for the funeral. Most businesses that are closing can die a natural death and just close up shop. A bankruptcy is not necessary.

However, there are situations where a chapter 7 bankruptcy for your business makes sense. Two situations I have dealt with involved a company that had a significant amount of inventory that they didn't know what to do with and a company that was being sued by numerous creditors.

In the first example the company sold patio furniture. Under their business model the store actually owned all of the patio furniture that it had in stock. So when the company closed down, the owner had a large amount of patio furniture (we are talking a warehouse full of patio furniture) and no real place to store it. By filing a chapter 7 bankruptcy, a trustee was assigned by the bankruptcy court, and the trustee came in and took possession of the furniture, sold it at auction, and then paid creditors of the company. All of this was done at no charge to business owner (other than the attorney fee to file), he no longer had a storage problem, and his creditors received some money on the debts that were owed.

In the second example the company was in the process of shutting down but was getting hammered by law suits. Literally a new law suit each week arrived on the company's door step. Instead of just letting all of the suits linger, the decision was made to file a chapter 7 bankruptcy. Immediately upon filing of the bankruptcy case the court issued a stay that stopped all further litigation on these court matters and allowed the business owners to shut the company down without having to deal with the numerous lawsuits.

## **Businesses Do Not Receive a Discharge in Chapter 7 Bankruptcy**

One important thing to note, companies do not receive a discharge. The discharge order is why individuals file for bankruptcy. This is the order that comes from the bankruptcy court that eliminates your debts. Only people, not companies, can receive a discharge in a chapter 7 bankruptcy. This means that the company debts are not eliminated through a chapter 7 filing, but all of the company's assets are liquidated and the creditors are paid what is available. The company's creditors are then left to pursue personal guarantees that they may have or write off any remaining balance.

## **Dealing with the Personal Guarantee**

In most case where a small business is closing, I will recommend a personal bankruptcy filing and letting the business die a natural death. The reason being is few small businesses have debts that aren't personally guaranteed. The personal guarantee is the hammer that the creditor can use to get you to personally pay the business debt. A bankruptcy filing will generally totally eliminate any personal guarantee liability on your part.

I recently wrote an article describing how in Arizona both spouses must sign a personal guarantee in order for the creditor to be able to collect against any community property. Arizona is one of 9 community property states. The law in Arizona states that in order for the "marital community" to be liable on a personal guarantee, both husband and wife must sign it. This rarely happens.

What does this really mean? It means that the creditor can still sue whichever spouse signed the personal guarantee, but the creditor will only be able to collect from that spouse's separate property. Most married couples in Arizona don't have separate property. Separate property is typically property that you brought into the marriage or an inheritance that you received after marriage.

It is important to understand that the creditor can still sue you and can still annoy you with collection calls even if your spouse did not sign the personal guarantee. A bankruptcy filing will eliminate any liability on a personal guarantee.

So, in answer to the question, can you go bankrupt on just your business debts? You can, but usually I end up recommending a personal bankruptcy filing and just winding down the business.

If your business is going through hard times give me a call and we can discuss your options. My consultations are always free. I can be reached at (480) 420-4028 or via email at [john@skibalaw.com](mailto:john@skibalaw.com) .