



Bankruptcy News

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Why bankrupt a corporation?

When does it make sense for a corporation to file Chapter 7 ?

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A corporation may either end its business operations and file Chapter 7 or continue in business and file Chapter 11 to reorganize in hopes of becoming profitable again.

When a corporation files Chapter 7 it must stop its business activities and turn over all assets to a bankruptcy trustee to be sold to pay off business debts.

If the corporation files Chapter 11 it will be allowed to continue in business but must file a reorganization plan with the court stating how it will become profitable again. The plan may propose to eliminate some of the corporate debts in order to help the business make a recovery.

Although corporations do not receive bankruptcy discharges, there may be some instances when it is desirable for a corporation to file Chapter 7, such as :

When it appears a creditor may put a lien on property that could otherwise be used to pay debts for which the shareholders or officers are personally liable, such as trust fund taxes or leases or other obligations that are personally guaranteed.

When the services of a trustee are desirable to handle the liquidation of assets and the winding up of the business, freeing the corporation's officers to seek employment, etc.

When filing bankruptcy may discourage creditor suits which have a tendency to name the officers and shareholders personally, irregardless of whether they are legally liable for the debt

Of course, corporations may go out of business without filing bankruptcy by merely liquidating their assets and ceasing operations. Creditors have a right to recover to the extent the corporation has assets. If there are no assets, the corporation is basically *judgment proof* and creditors will not be able to collect from the corporation.

The problem with this approach is that some creditors may incorrectly interpret the business's failure to pay as a sign of wrongdoing and sue the officers or the corporation to try to collect their debt. Even if these claims are invalid, they will still have to be defended otherwise the individuals involved risk having a judgment entered against them.

There is no single answer as to when a failed business should file Chapter 7. Usually it depends on the value of the business assets; the aggressiveness of creditors; and the availability of corporate officers and management to oversee the process of winding up business operations.

<http://www.vermontbankruptcy.net/why.pdf>