

COVID-19 and Personal Bankruptcy for Small Business Owners

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Most small business owners unavoidably have to either incur business debt in their own name (think of an American Express Card) or personally guarantee business debt. The Coronavirus has had a devastating effect on small business. Many small businesses will simply not be able to weather the storm and survive. In this scenario, an inability of non-operating companies to pay its debts will leave small business owners with personal liability on business debt. Now is the time to educate oneself on personal bankruptcy because if an individual has more business than consumer debt, they may be exempt from chapter 7 bankruptcy's rigorous Means Test and, instead, subject only to a more flexible and forgiving budget test.

If consumer debt exceeds business debt, filing for personal bankruptcy mandates an analysis of whether one is subject to and/or passes the Means Test. The Means Test is nothing more than an eligibility test. In essence the test takes a person's average income over the past 6 months and applies against that, stringent IRS National and Local permitted expenses (expenses the IRS allows for those who have not paid their taxes) to arrive at a disposable income amount. If disposable income is above a certain nominal amount, one will be ineligible to be a chapter 7 debtor and obtain a discharge. That leaves filing a lengthier and complicated chapter 13 reorganization, where all "disposable income" has to be paid to creditors over three or, more likely, 5 years. Alternatively, if a debtor does not qualify for a chapter 13 due to exceeding debt caps, a debtor is looking at an even more expensive chapter 11 or, unfortunately, not filing bankruptcy at all. Not filing results in fending off creditors, lawsuits, wage garnishment and seizure of personal assets.

However, if business debt exceeds consumer debt, the Means Test does not apply. Courts will look to actual income and expenses at the time of filing and not be bound by fixed IRS expense standards. Many small businesses are shut down. The value and sale marketability of a business may be down or non-existent. Owners may have no or diminished income. Now is the best time to consider whether filing personal bankruptcy is a strategic and appropriate form of relief as this option may not be available in the future as circumstances change.

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