

## Swift action vital to flatten the “Insolvency Curve”

A leading voluntary insolvency firm has warned that an insolvency avalanche is inevitable if distressed SMEs don't take urgent action now.

National firm, Jirsch Sutherland, says while the financial support announced by the federal government will certainly help some, many business owners may put off making important decisions while their various debt obligations continue to accrue in the background, ultimately leading to a financial cliff many will fail to scale.

“A debt deferment strategy may be understandable, but business owners need to realise they may just be postponing the inevitable. It's crucial to make changes now to help flatten the “Insolvency Curve” that's looming. This is especially important for those that were already experiencing financial distress prior to the COVID-19 crisis,” says Sule Arnautovic, Jirsch Sutherland Partner.

“The federal government's debt deferral strategy means that in, say, six months' time there will be a proliferation of SME businesses getting into dire financial straits. Imagine having to pay six months of rent, utilities and financing costs, as a lump sum, before you can open your doors. That's what some businesses will be facing when we move from the crisis to a recovery environment.

“There are not many businesses that will be able to take that type of capital hit. With the challenge of re-establishing market position, renewing trading relationships with suppliers and adapting to a changed environment, a lot of businesses will be forced into a financial restructure through an insolvency procedure.

“Debt deferment with no exit or recovery strategy is fatal,” Arnautovic says

He warns that similarly to medical professionals being pushed to their limits to assist those who are critically ill, insolvency and restructuring professionals are likely to be pushed to their limits when stimulus packages expire. “That's when the Insolvency Curve is likely to increase dramatically,” he says. “If viable businesses are being inundated with mass terminal insolvencies of their clients at that time, it may cause some contagion to other businesses that might otherwise be saved/restructured, as creditors scramble to deal with the fallout to their own businesses.”

Arnautovic says there's a range of measures that can help position businesses to ride out the crisis or restart once it's all over. These could include:

- **Restructure a business early**, utilising the framework established under the [Safe Harbour](#) legislation.
- **Create a Creditors' Trust** for participating creditors. This is a legal arrangement used to accelerate a company's exit from external administration.
- **Merger and consolidation.**

- **Implement “Holding”, “Hibernation” or other Deeds of Company Arrangements (DoCAs)** to extend the period of debt moratoriums. This will buy time to investigate potential restructuring opportunities.
- **Liquidate now and minimise losses** in order to allow a business to restart further down the track

For business owners that were struggling to make ends meet prior to the COVID-19 crisis and had accrued losses and unpaid liabilities, the time to act is now. “The regulatory and ethical obligations upon directors have never been so great – and neither have the consequences for the individuals who get it wrong,” Arnautovic says. “Good intentions can still result in directors becoming personally liable for making the wrong call. Deliberately avoiding the debt issue can land directors in even hotter water. The recent government moratorium on insolvent trading is somewhat of a red herring, given the raft of director obligations stipulated in Australia’s corporate legislation.”

And for those who believe their businesses may have prospects on the other side of the crisis, Arnautovic has this advice: “All businesses will be impacted in some way by this crisis and I urge directors to seek professional advice immediately to understand all of their options, which should include the formal insolvency/restructuring options that are available.

“And it’s not just the financial ramifications that are at play here, the mental health implications are also massive. Dealing with a business problem early can offer clarity for all involved and help reduce ongoing stress and anxiety.”

### **Reasons why company directors and accountants/lawyers should not delay insolvency/restructuring appointments:**

- **Market value of many business assets** have been adversely impacted, which essentially translates to a lower restructure cost for various restructure supporters who are trying to offer creditors more than they would get in a liquidation scenario.
- **Creditor support for restructure:** creditors are more likely to understand why businesses have collapsed at this time and to support restructure efforts to ensure continuity of business post crisis.
- **Unpaid liabilities:** if the business had accrued unpaid liabilities before the crisis, it is unlikely to survive even with government support.
- **Accessing the Fair Entitlements Guarantee Scheme (FEG) for employee entitlements.** This takes time to come through, so acting now offers staff a quicker solution in difficult times.
- **Personal guarantees don’t fall away:** business owners should be aware of ‘sleeping personal guarantees’ that will raise their heads later – e.g. leases, make-goods, trade credit applications, finance, credit card debts etc. Any debt deferral decision may exacerbate liabilities, which could put personal assets at greater risk.
- **Deferment of liabilities will be added to existing liabilities:** e.g. not paying rent for six months is not necessarily a pardon for that period, and extra interest could well be capitalised into the outstanding liability amount. Always check the full terms and conditions of any finance agreement for any deferment.



- **Supplier support and doing the right thing:** many businesses have close, long-term relationships with their suppliers. By acting early, you protect and/or limit their exposure to your ongoing debts.
- **Preparing for the “new dawn”:** by exiting a business experiencing financial stress, when the upturn does come, you can assess if and when you get back into business, either with a new model, strategy or market etc.

**-ENDS-**

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## About Jirsch Sutherland

Established in 1984, Jirsch Sutherland is one of Australia’s leading national independent insolvency specialists. The Jirsch Sutherland team works closely with small and mid-size accounting, finance and legal firms – and their clients – to provide a wide range of expert corporate and personal insolvency services including liquidations, voluntary administrations, receiverships and bankruptcy.

With head offices in Sydney, Melbourne, Brisbane, Newcastle and Perth, supported by a network of regional offices, Jirsch Sutherland’s national reach combined with a local presence underpins the company’s ongoing success. For over three decades, Jirsch Sutherland has earned a well-deserved reputation for protecting and guiding clients through the insolvency process in a fair and ethical way.

In Western Australia, Jirsch Sutherland trades as WA Insolvency Solutions.

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