Dealing with Insolvency

Insolvency is defined as a state in which a business or organization can no longer meet its financial obligations as they become due. Unfortunately, insolvency has become increasingly common for small businesses since May 2021, due in large part to the effects of the COVID-19 pandemic.

In fact, 1 in 6 Canadian small business owners were considering closing in the past year, according to the Canadian Federation of Independent Business. And, given that economic issues have continued since then, it's possible that even more small businesses are currently grappling with near or total insolvency.

This insight discusses what to do if your business is dealing with insolvency and outlines possible preventive measures.

Options for Insolvent Businesses

For businesses that find themselves insolvent, there are a few courses of action. These options include the following:However, it's important to keep in mind that a property may be assigned several different values, including the following:

- **Restructuring**—A company facing insolvency has the option to gain protection under the Bankruptcy and Insolvency Act, or the Companies' Creditors Arrangement Act (CCAA). Under the CCAA, a company will have the opportunity to come to an agreement with its creditors. Once the agreement is settled, the company will be released from its debts.

- **Bankruptcy**—When a company can no longer pay its debts, the best option may be formally declaring bankruptcy. When bankruptcy is filed, proceedings initiated against creditors are suspended and assets will be liquidated.

- **Receiverships**—In the case of a receivership, the court will appoint a third party to take control of assets, supervise liquidation proceedings and remit the proceeds according to priorities established by the law.

One in 6 (181,000) Canadian small business owners were considering closing in the past year, according to the Canadian Federation of Independent Business.

Preventive Measures

If a business is experiencing a significant financial downturn, it's important for owners to educate themselves on potential solutions. Even profitable businesses run into cash flow problems from time to time. By taking swift and immediate action, it may be possible to avoid insolvency altogether. Consider the following tips a business can use to get back on track:
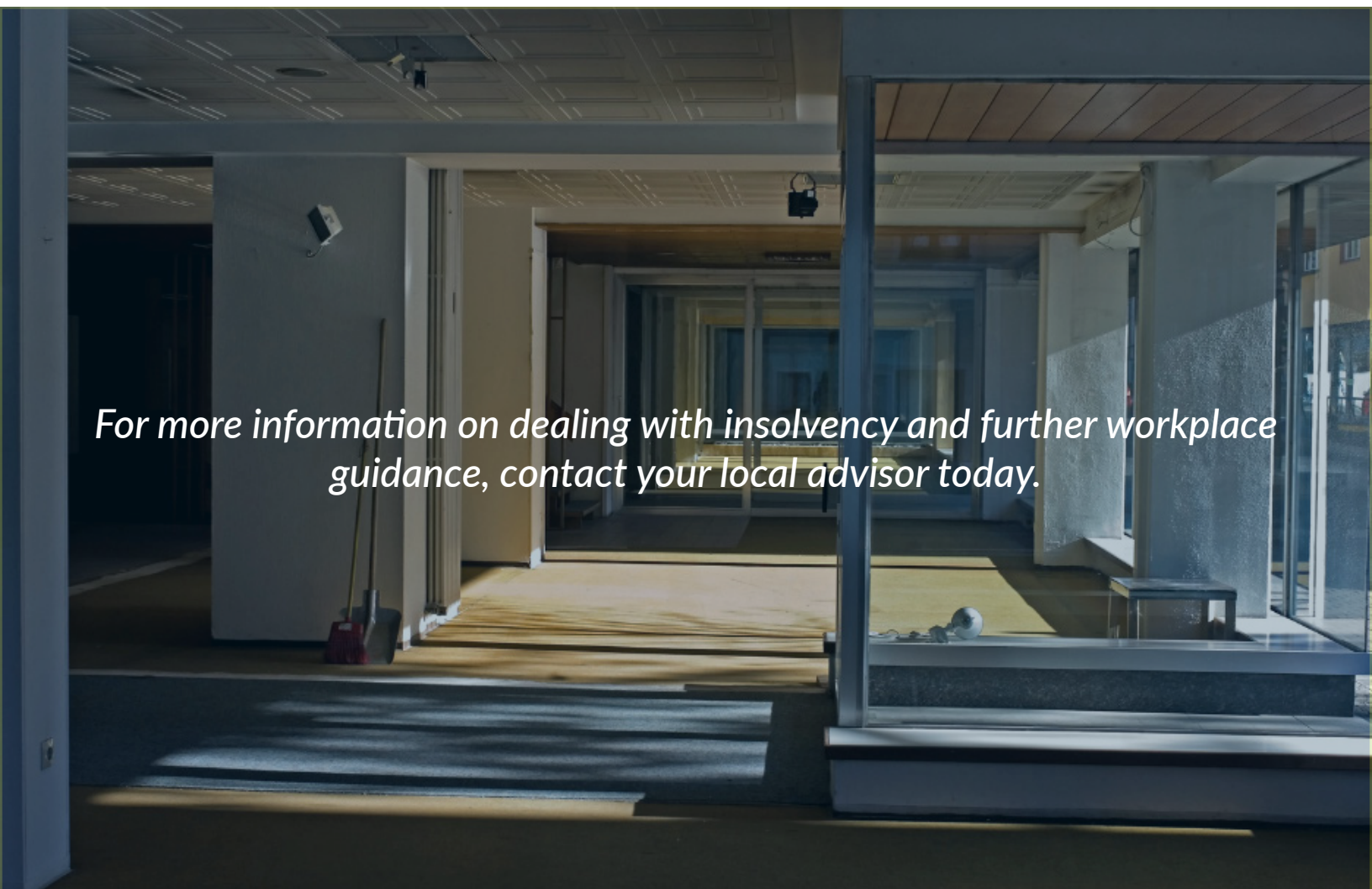
- **Analyze and improve cash flow.** While stocks and assets are nice to have on the books, their value could be depreciating. As such, any unnecessary or underused stocks and assets can be sold off to inject some liquidity into the business. If necessary, invoice financing or asset-based lending can also be considered; some companies will pay a percentage of a business's outstanding invoices to improve interim cash flow.

- **Review incoming payments.** A business should take a look at payment terms with clients to make sure they are being invoiced regularly, accurately and on time to ensure a free flow of cash. Additionally, a business should take swift action to recover any payments or debts owed by customers or suppliers.

- **Reduce overhead costs.** Reduce expenditures by assessing cost-cutting strategies. Consider relocating to a more affordable premises, review staffing requirements and temporarily cut back on any business expenditures that are not immediately bringing in profits.

- **Negotiate with creditors.** If possible, talk to suppliers and other creditors to negotiate manageable payment terms for any debts owed.

Conclusion

It is no surprise that businesses are struggling financially during the current economic climate. Alongside cost-cutting strategies, consider engaging with an insolvency expert to uncover and assess all your available options. The earlier a company is able to take action, the more likely it'll be able to recover.

For further workplace guidance, contact us today.

For more information on dealing with insolvency and further workplace guidance, contact your local advisor today.

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LOCATIONS

Edmonton: 1.800.665.5243

Calgary: 1.866.845.8330

Kelowna: 1.800.665.5243

lloydsadd.com

navacord.com

info@lloydsadd.com

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