

# Overview of Avoiding Corporate Guarantees

Small business owners who guarantee their corporate obligations, reduce the corporation's usefulness as a liability insulator.

Most major corporate debts – particularly bank loans – require the small business owner's personal guarantee. However, you can usually sidestep guarantees demanded by other creditors (as well as escape liability on existing guarantees) with common sense and a tougher attitude. Avoid suppliers who demand your personal guarantee. Find prospective suppliers who will give your corporation some credit without your personal guarantee. If one supplier demands your guarantee, find a more lenient supplier.

However, understand creditor's concerns. Reduce their risk. Convince a creditor to forego your guarantee. A supplier who refuses to extend your corporation a \$20,000 credit line without your personal guarantee may risk \$10,000. Or will the supplier accept alternative collateral or lien on the businesses assets to forego your personal guarantee? Or will a guarantee from an affiliated corporation be an acceptable substitute?

If you must sign a personal guarantee, negotiate for a partial guarantee. This limits your exposure. Have your creditor cancel your guarantee once your business establishes a good track record for prompt payment.

Never guarantee existing debts. You gain nothing. Once a business falters, creditors plead, promise, threaten and cajole for the owner's personal guarantee. But why risk your personal assets to secure an already shaky corporate obligation? And don't assume that your business will pay its obligations. Companies in deep trouble seldom fully pay their debts.

Have your partners sign whatever guarantees you sign. If your partners are less wealthy than you, the creditor will chase you for payment. Creditors chase the deepest pockets.

If you have already signed personal guarantees, your goal is to extricate yourself from these obligations. Verify which obligations you guaranteed. Businesspeople do not always know which debts they guaranteed. The guarantee may have been in an order form or credit application. Ask every creditor whether you personally guaranteed their debt and request copies.

Then terminate outstanding guarantees. You can revoke guarantees for future credit, and should revoke your guarantee to avoid further liability. And don't forget to cancel your outstanding guarantees for future purchases when you sell your business.

If your business is in financial trouble, float the business for as long as possible to pay the personally guaranteed debts before your company fails. Or secure your guaranteed creditors with a mortgage on the business. Your guaranteed creditors will be paid from the business' liquidation ahead of the non-guaranteed creditors. You reduce the odds that you will be forced to pay these debts from your own pocket.

Your final objective: Negotiate releases on any outstanding guarantees. You need bargaining power. For example, a creditor owed money may accept returned merchandise, partial cash or a mortgage on business assets in exchange for canceling your personal guarantee. Do you owe your bank? Will they cancel your guarantee if you agree to help the bank recover more than they could on their own when they liquidate your business? Secured lenders need the business owner's cooperation to maximize their recovery. Bargain your cooperation for those concessions that reduce or eliminate your personal exposure.

Not all creditors or lenders who hold your guarantee will release your guarantee for your cooperation. This same creditor may respond to less friendly overtures. Chapter 11 may forestall foreclosure and wouldn't be to your creditor's advantage. You have bargaining chips to coax creditors to cancel guarantees.

If you personally guaranteed a corporate debt, do the paperwork to indemnify and reimburse yourself from your corporation. Your corporation can give you an indemnification and a security interest on its assets. You then have a priority claim and will be reimbursed from the corporate assets ahead of its unsecured creditors.