To Draw or Not To Draw: Using Your Company's Line of Credit Prudently During the Pandemic

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As the coronavirus pandemic continues to strain world commerce and cause historic volatility in the financial markets, many companies are rightly concerned about liquidity in their businesses and within their banks. Until recently the economy was strong and banks were very accommodating to their customers' credit needs. If your business is debating whether or not now is the time to draw down on your existing revolving line of credit, be mindful of some important points to consider for and against the strategy.

No Time Like The Present to Take A Draw: Cash Is King and it may be best in your bank account now even if it means your business will need to make a few months of interest payments as you determine if your finances remain stable throughout the health crisis as opposed to not being available to you when you figure out that you need it. For the foreseeable future, some operating expenses will remain constant, and others will be in total flux as a result of your workforce moving to remote job functionality, customer cash being reprioritized, invoice payments slowing, and supply chains being impacted. The uncertainty will surely have an impact on your company's bottom line and will influence your employment decisions and possibly your ability to remain solvent and ride out the crisis. If your cash begins to dwindle to the point where it is insufficient to cover your operating expenses then your business could be considered insolvent. Once that scenario appears it may be too late to draw on your line of credit as your business may be in default under your existing loan covenants due to a material adverse change; a.k.a "MAC Default". If your lender triggers a MAC Default, it will likely become impossible for you to access your line of credit which means your cash needs will not be met through borrowing. Without available cash, the inevitable can occur; shutdowns, layoffs, credit defaults, and a general inability to perform on your contracts with customers and suppliers. Within a few short months your business could go from thriving to bankrupt.

On the other hand, if your business remains stable and you later determine that you do not need the borrowed cash, then your business can easily repay the line of credit having only incurred a few interest payments.

Don't Incur Debt You Won't Be Able To Repay: As logical as it might seem to keep your cash position strong, employing a borrowing strategy to bolster your company's current cash needs might not be in your long term best interests. There is going to be a proportionate interest expense associated with your draw and your company must be able to cash flow this additional expense. If your company draws down on some or all of its credit and the crisis continues to batter your business despite your best efforts at stabilization, the new indebtedness coupled with the existing cash strain could topple your organization and leave you little or no choice to shutter operations or seek bankruptcy relief. Depending on the structure of your loans, these new borrowings could become the responsibility of the owners of the business and the ripple effect could be far reaching.

In times of crisis where businesses cannot always reasonably predict the consequences of the decisions they make day to day, companies must be prudent and knowledgeable about the risks of using available credit.

Our attorneys are ready, willing, and able to consult with your business regarding any of your financial decisions and strategies and are here for you *even if the worst case scenario has arrived*. Be safe, be smart, be well and always ask questions.

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