



News & Types: Client Advisories

Recent Significant Commercial Bankruptcy Filings

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EXECUTIVE SUMMARY

With the COVID-19 pandemic continuing to exact a tremendously heavy toll on the worldwide economy, you have probably noticed an increasing number of U.S. companies filing for bankruptcy protection. A list of entities filing for bankruptcy in the last few months include companies in a variety of industries, such as J.C. Penney, Hertz, Gold's Gym and, more recently, Chesapeake Energy and Briggs & Stratton. According to some business analysts, a tidal wave of COVID bankruptcies is predicted to wash over the United States in the second half of 2020 and even more so in 2021.

Masuda Funai attorneys routinely represent creditors in bankruptcy proceedings in order to protect their contractual and legal interests and rights to payment. We have extensive experience in handling complex bankruptcies, and we were heavily involved on the creditors' side in some of the more prominent national bankruptcies of the last 10-15 years. Some of the considerations that creditors/suppliers have to navigate in a bankruptcy include the following:

Automatic Stay: Upon the bankruptcy filing, an automatic stay is put in place by the Court. Subject to limited exceptions, the stay stops creditors from initiating or continuing collection efforts against the debtor or its property to obtain payment on pre-petition debt;

Getting Paid for Goods in Transit: If goods are currently in transit, a creditor may be able to stop their delivery in order to obtain critical vendor status (see below) or at least to get paid in advance for those goods. Therefore, upon learning of the bankruptcy being filed, it is important to immediately review shipment receipts, bills of lading, and internal records to determine whether there are any shipments in transit to the debtor and whether any of them may be legally stopped;

Reclamation Notice: Administrative claims, unlike general unsecured claims, are normally paid in full. By promptly issuing a reclamation demand for goods shipped within 45 days before bankruptcy, it may be possible to convert an unsecured claim for those goods to an administration claim. Timing is critical in the issuance of such a notice;

Credit Sales: A supplier selling to the debtor on open account, without a binding executory contract (see below), is not obligated to continue to do business with it and may choose to cease doing business with the

debtor or negotiate new terms under which it chooses to do so. A creditor may be able to obtain improved payment terms, such as cash in advance;

Executory Contracts: If a supplier's contract with the debtor has material obligations that are still left to be performed by both sides at the time of the bankruptcy filing, the debtor may choose to either assume or reject the remainder of the contract with the supplier. A careful review of all the agreements and documents that govern the relationship between the creditor and the debtor is required to determine whether there is, in fact, an executory contract in play. Whichever way the debtor chooses to proceed on the executory contracts carries with it both benefits and burdens to the supplier which must be clearly understood. The assumption/rejection process by the debtor can be purposefully lengthy, but a supplier can file a motion with the bankruptcy court requiring the debtor to speed up a binding decision;

Critical Vendor/Essential Supplier Status: If this status is obtained, in many instances, the debtor's pre-petition receivables will be paid in full or very close to it. This status is obtained by court order and indicates to the court that the supplier's continued work with the debtor is so vital that the supplier must continue to perform work for, and be paid by, the debtor. Critical vendor status is often considered to be a Holy Grail of post-petition efforts to collect on a pre-petition debt and may be difficult to obtain without hard-nosed and determined negotiations;

Repossession of Collateral/Payment on Depreciation of Collateral's Value: If a creditor has sold to the debtor on a secured basis and if the debtor refuses to pay for its continued use of the collateral while in bankruptcy, it may be possible to move the Bankruptcy Court to force the debtor to pay for its on-going use of the collateral or force the debtor to return the collateral to the creditor. That involves lifting the automatic stay and can take considerable time;

Goods Shipped Within 20 Days of the Bankruptcy Filing: Under §503(b)(9) of the Bankruptcy Code, a creditor is entitled to an administrative priority claim for goods received by the debtor within 20 days of its bankruptcy filing. To accomplish that, a specific §503(b)(9) claim must be timely filed in accordance with Court instructions, and failure to do so acts as an absolute bar on this claim;

Proof of Claim: A timely filed proof of claim may be required to preserve a creditor's right to a pro-rata share of any distribution to unsecured creditors from the bankruptcy estate. Same as above, failure to timely file a required proof of claim acts as an absolute bar to any unsecured distribution; and

Preference Claims: Many creditors have preference lawsuits filed against them by the debtor's trustee to return to the debtor any amounts received by the creditor within 90 days prior to bankruptcy filing. There are specific defenses available to the creditor under the Bankruptcy Code to fight the preference claims, and it is important to understand the preference concept as soon as some concerns about the business dealings with the debtor arise, often well before there is an actual bankruptcy filing. Accurate records keeping is also a must.

Please keep in mind that the foregoing list does not necessarily include all the matters, rights and remedies that your company may have in a particular bankruptcy. This is a brief, preliminary advisory for informational purposes only and is not intended to replace legal counseling. If you require further information about a particular bankruptcy filing, have specific questions about your dealings with a company filing for bankruptcy or

would like our assistance to take action to protect any rights or claims you may have, please feel free to contact Gary Vist or Rein F. Krammer who have extensive multi-decade experience in the bankruptcy/creditors' rights area, or any other attorney at Masuda, Funai with whom you have worked in the past.