

## My Customer Filed Bankruptcy: Now What?

It's the thing creditors most dread: the announcement that a customer has filed for bankruptcy. But there are a few steps credit managers can take to prepare for when that moment happens and to ease the way to a claim during a case.

When a customer files for bankruptcy, think in terms of a checklist. **File preservation** is critical at this juncture. Gather information. You need to preserve information—both paper and electronic, including email—in preparation for your proof of claim. Invoices and bills of lading should be included for goods received by the debtor within 20 days of the bankruptcy filing, in support of the 20-day goods priority claim. In regards to preference exposure and defenses, preserve payments received within 90 days of the filing. Proofs of delivery, pay history and credit group data are all helpful in proving a claim.

When the bankruptcy case is filed, what else should creditors consider doing beyond gathering information? **Tracking down case information and files** can nowadays be done electronically in most cases. Pacer.gov is an excellent resource, from which you can access any documents filed in a bankruptcy case. In Chapter 11 filings, claims agents designated by the debtor will set up informational websites that contain all the files of the case. Creditors can discover what caused the bankruptcy filing, what the debtor intends to do, any details if there is a prenegotiated plan, whether the debtor is planning to sell assets and more.

One of the first documents to look for is an order that approves financing. In Chapter 11 cases, the debtor in possession (DIP) financing order approves new financing through a new or existing lender. A cash collateral order allows a debtor to use the cash proceeds of a lender's collateral. DIP financing and cash collateral orders are usually approved on an interim basis shortly after Chapter 11 filing and on a final basis a few weeks later. These usually include a budget of approved debtor expenditures.

Do not do any business with a debtor before confirming that there is an order in place for the debtor to make payments. Check for an interim order. Check later for a final order and check the budget. The DIP financing order is not a guarantee of payment, however. If the debtor liquidates after secured claimants are paid, you may not get your claim, or payment may take years.

Be aware that there is a hierarchical system of claims, with secured claims at the top, then administrative expense claims, then lower-level priority claims, and general unsecured claims near the bottom. If you are at the bottom of hierarchy of claims, how do you get higher up the ladder? One way is to successfully **seek critical vendor status**. Critical vendor status requires court approval and the agreement of the debtor. It doesn't guarantee that creditors will get paid, it does not protect against preference risk and it is subject to negotiation; but it often does move them higher in the pecking order.

Another benefit may come from the Uniform Commercial Code's (UCC) **right to stop delivery of goods**. If insolvency can be proved, the creditor can withhold delivery of goods in its possession and switch to cash terms going forward. These rights are not impacted by passage of title or risk of loss.

How does a creditor assert a proof of claim? Be sure to **follow directions in filing a proof of claim**, and be sure to file it on time. Missing the deadline may mean loss of distribution or voting rights. Deadlines can be checked on Pacer.gov. Debtors may file objections to proofs of claim, to which creditors must respond in a timely manner or risk reduction or elimination of the claim. Because claims have real value, there is a strong motivation to fight them.

Finally, the **creditors' committee**, can be a valuable resource. It is representative of the unsecured creditor body and is a vehicle through which those with unsecured claims can get a better recovery than without it. The committee has the opportunity to shape the progress and outcome of the case by evaluating the debtor's decisions and direction, object to actions not in the best interests of unsecured creditors and stay current on the debtor's financial condition.

Remember: If you don't assert a right, you risk losing it. Keeping these resources and information in mind may make the process a little easier if that dreaded moment happens when a customer files for bankruptcy.

*Source: "My Customer Filed Bankruptcy: Now What?," a NACM teleconference conducted by Bruce Nathan, Esq., partner at Lowenstein Sandler LLP.*