

**A Bankruptcy
Overview- Including
Changes from the
BAPCPA of 2005**

Charles P. Mortimer

Levy – von Beck & Associates, P.S.

Attorneys at Law

600 University Street

Suite 3300

Seattle, WA 98101

Tel: (206) 626-5444

cpmortimer@levy-law.com

Summary

- Basics- a brief review
- Changes to filing/documentation requirements
- Increased reclamation opportunities
- New limitations on preference claims
- Restrictions on assumption of contracts, filing of plans
- Expanded creditor committees
- Stiffer penalties for fraud, filing abuses

Bankruptcy basics- a brief review

- The relevant permutations of bankruptcy-
 - Chapter 7- liquidation
 - Chapter 13- reorganization for individuals with income
 - Chapter 11- general reorganization

The Automatic Stay-

- Effective upon filing
- Stays all proceedings and efforts to collect
- Violations may result in award of actual damages
- Effective through discharge or dismissal

Relief from stay. . .

- Motions for relief from stay may be brought in bankruptcy court
- Does not preclude adversary proceeding in bankruptcy court (ie: for enforcement of reclamation).

Following the Case

- Get the petition- verify your claim is accurately presented
- Track the docket (available online or at clerk's office)
- Meeting of the creditors- the §341 meeting. Chance to question debtor regarding assets.
- Review the plan if Chap. 11 or 13
- Get proofs of claim in on time- date set by motion for Chaps. 11 and 13, only necessary if requested by Trustee for Chap. 7

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005

- Requirement for consumer credit counseling, strategies for fraud reduction
- Over 500 pages of changes
- Including many important to businesses/creditors
- October 17, 2005 implementation

I. New Filing and Documentation Requirements:

- Awareness of requirements by creditors important.
- If debtor doesn't comply with documentation requirements, creditors may challenge or seek to have petition dismissed.
Creates potential leverage for creditors.

Means Testing

- Means test qualification for Chap. 7 liquidation.
 - Based on income qualifications.
 - If there is “abuse,” Trustee or creditor(s) may force dismissal, or with debtor’s permission, conversion to 11 or 13.
- “Abuse” if:
 - Debtor’s income exceeds state median; and either
 - ‘disposable’ net income over 10 years is \$10k or more;
 - ‘disposable’ income between \$6k and \$10k and more than 25% of unsecured claims.

New requirements for debtor documentation . . .

- Sec. 315-Requires filing of Federal tax returns, monthly net income projections, employer payments, anticipated income or expense increases; from commencement to termination.
- Sec. 316- Requires dismissal of a Chap. 7 or 13 case if debtor fails to file all required information, schedules within 45 days of filing.

Auditing and Challenging

- Sections 315 and 316 allow creditors to request copies of required documentation in Chap. 7 and 13 cases.
- Creditor may force mandatory dismissal of case for failure to provide required documentation.

II. Expanded Reclamation Rights-

The **OLD** system . . .

- Reclamation authorized by bankruptcy law (11 USC § 546) as well as the UCC (RCW 62A.2-702)
- Provides right to reclaim the actual goods when in possession of an insolvent debtor
- If petition filed, bankruptcy code controls

Requirements:

- Goods must be sold in ordinary course
- Must have been received by debtor (but reclamation rights subject to buyers in good faith)
- Demand for reclamation must be made within ten days of receipt of goods
- Debtor must be insolvent (petition filed or otherwise unable to pay debts)

Exceptions:

- Under UCC, ten day limitation not required if there is a written misrepresentation of solvency by the debtor within three months before delivery
- Under bankruptcy code, notice may be given within 20 days if 10 day period expires after filing of the case

Reclamation Notice

- Must be in writing
- Must be timely
- Must describe the goods in question
- Should claim “reclamation” and a citation to statute.

What does reclamation claim get you?

- Adversary proceeding or lawsuit to compel
- If you can't secure return of the goods, you can request cash or a lien on the goods if in another's possession.
- May have an administrative claim for amount owed.

Reclamation Summary- the pros and cons

- Must be extremely timely
- Claims are subject to good faith buyers
- Claims are subject to preference powers of bankruptcy trustee
- Goods cannot be co-mingled by manufacturing
- Can cure failure to perfect a UCC security interest

Revised reclamation rules

- Bankruptcy only- UCC reclamation unaffected.
- Expanded Notice period-
 - reclamation notice to be sent within 45 days of debtors receipt of goods.
 - If 45 day period expires after filing of case, no later than 20 days after filing.
- Limitations on avoidance power on reclaimed goods.
 - If reclamation notice is timely, trustee cannot avoid transfer of goods back to seller.

509(b) Claim for Goods Delivered

- Sec. 509(b)- upon motion by a seller-creditor, an administrative claim for goods received by debtor within period 20 days prior to filing. Regardless of notice.

III. Limitations on Preference claims

- Preference claims generally-
 - Based on general power of Trustee or DIP to avoid “preferential transfers” to “insiders” or preferred creditors.
 - Generally, all payments made within 90-day period prior to filing are presumed preferential.
 - Subject to limited defenses.
 - Payments in ordinary course.
 - Contemporaneous exchange for new value.

The new rules-

- Simplified “ordinary course of business” defense.
 - Old rule- payments according to regular business terms between parties (subjective) and according to industry standard business terms (objective).
 - New rule- made in ordinary course of business or financial affairs of creditor or debtor, or, according to ordinary business terms.
- For smaller claims (< \$10k), venue in creditor’s state.
- Expansion of “perfection date” for security interests on transfers from 10 days to 30.

Additional new limitations

- Dollar limits on “de minimus” preference claims.
 - Pref. claims on transactions of less than \$5,000 are barred.
- Recognition of PMSI transfers.
 - So long as security interest is perfected within 30 days, PMSI transfer cannot be avoided.

IV. Limitations on deference to Debtor Estate

- Limitations on extensions for filing of plans
- Limitations on delays in assumption/rejection of contracts.
- New limits on deadline for plans and plan approval.
 - Plan must be filed within 18 months of commencement, no extensions past 20.
 - For “small businesses” (less than \$2M in aggregate debt).
 - Plan must be filed within 180 days of order of relief (stay)- cannot be extended past 300 days absent extraordinary circumstances.
 - Confirmation must be within 45 days of filing, no extensions absent discrete set of circumstances.
- Executory contracts and leases automatically rejected if not assumed (within 120 days).
- Terms of contract must be met for assignment.

V. The Creditor's Committee

- Any party in interest may move to form a creditors' committee; not just US Trustee.

Advantages/disadvantages:

- Power in numbers- united front.
- No reimbursement for costs (administrative claims no longer available).
- Only suitable for large scale cases.

IV. Consequences for Fraud or Procedural Problems

- **Expanded Grounds for Dismissal of Case**
 - Gross mismanagement of the estate
 - Unauthorized use of cash collateral that results in harm to creditors
 - Failure to comply with order of court
 - Unexcused failure to meet case or filing deadline
 - Material default by debtor under plan
- Can result in conversion (to Chap. 7), dismissal, or appointment of Trustee in lieu of DIP.

Other consequences . . .

- Reduction of homestead exemption for fraud.
- Automatic appointment of Trustee in Chap. 11 cases where US Trustee finds evidence of fraud.
- Extension of one year reach back for fraud to two years.
- Avoidance powers extended to reach certain insider payment made up to 10 years prior to commencement.

Summary

- We learned:
 - Stiffer filing/documentation requirements
 - Increased reclamation opportunities (expansion of notice, creation of admin. Claim).
 - New limitations on preference claims (recognition of PMSI, de minimus and venue requirements).
 - Restrictions on assumption of contracts, filing of plans.
 - Expanded availability of creditor committees for complex cases.
 - Stiffer penalties for fraud, filing abuses.
 - Importance of following cases, staying on top of debtor's requirements.