



Why Should a Lawyer Look at your Proof of Claim? Because Not All Claims are Equal

Your customer files for bankruptcy. Your business receives a Proof of Claim form from the bankruptcy court, or a claims agent. You complete the form, fill-in what your business is owed, maybe you attach copies of invoices, and you file the form. It seems like a simple form to complete and file, but you may be waiving a number of rights, including the right to be paid in full a lot sooner and dollar for dollar negotiations against a potential avoidance action in the future. Certain types of claims are entitled to administrative or priority status in a bankruptcy, which may mean payment in full (as opposed to pennies on the dollar) and a lot sooner.

Here is a brief example of how a real client looking to save maybe \$1,500 in legal fees lost \$75,000.

Example: Manufacturer provides goods to Customer over a number of years. Manufacturer is always paid by Customer's sister company, Affiliate, but figures it is fine because they are related companies. Business is not going well for Customer, and Customer and Affiliate each file a chapter 11 bankruptcy case. Manufacturer files a Proof of Claim for \$100,000 in Customer's bankruptcy case for unpaid goods. Customer does not have a lawyer look at its Proof of Claim.

Two years later, Customer's and Affiliate's Plan is confirmed, a Liquidating Trust is formed to pursue litigation claims, and Manufacturer receives a demand letter and then is served with a Complaint by the Liquidating Trustee. Manufacturer calls its lawyer.

Lawyer reviews the Complaint and sees that Manufacturer is being sued, because the transfers it received were from Affiliate but the goods were delivered to Customer. On top of that, Lawyer reviews the filed Proof of Claim, and notices that of the \$100,000 for unpaid goods delivered to Customer, \$75,000 was for goods delivered in the 20 days before the bankruptcy case was filed, so it likely would have been entitled to administrative priority status – i.e., paid in full upon Customer's emergence from bankruptcy – but now it is too late to file a proof of claim for an administrative claim. Worse, Customer's general unsecured claim is only worth pennies on the dollar when negotiating with the Liquidating Trustee regarding Customer's exposure on the fraudulent transfer action, whereas the administrative claim would have been a dollar for dollar offset reducing Customer's liability. This customer cost itself \$75,000 to save \$1,500 in legal fees.

Conclusion: In reality, we were able to convince counsel to the liquidating trustee that they should give the client a credit for its \$75,000 administrative expense claim dollar-for-dollar against the fraudulent conveyance action, even though it would have been untimely if filed. We also successfully argued that the client had valid defenses to the fraudulent conveyance action, including providing "enterprise value" to the affiliate even though the goods were delivered to the customer. But, the client would have saved significant legal fees in the end if it had asked a lawyer to review its proof of claim. It is more than a form.

To discuss this further or for any related topics, please feel free to reach out to:

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