



Feeling the Crunch? How to Manage Distressed Customers in the Uncertainty of COVID-19



COVID-19

Sue Cook | Rozanne Giunta | Dennis Loughlin
May 20, 2020

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Susan M. Cook

40 years of experience in:

- ◆ Bankruptcy, business reorganization
- ◆ Represents clients in distressed automotive supply chain
- ◆ Commercial and business law

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Rozanne M. Giunta

Over 40 years experience in:

- ◆ Bankruptcy, loan workouts, preference claims defense, collection suits, foreclosure actions
- ◆ Automotive, manufacturing, health care industries
- ◆ Representing banks, secured lenders and unsecured creditor committees

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Dennis W. Loughlin

Over 23 years experience in:

- ◆ Corporate counsel in the automotive supply chain with expertise in distressed auto supply and tooling industries
- ◆ Counseling secured and unsecured creditors in all phases of commercial disputes both in and outside of bankruptcy

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Dealing With a Distressed Customer Outside of Bankruptcy

- Prior to the COVID-19 crisis, distress in auto supply, manufacturing, retail and hospitality was increasing due to a variety of factors
- Sometimes the distressed customer is obvious due to media reports, but many times that's not the case
- Watch for indicators of distress
 - Payments not timely or later than course of dealing
 - Over 10 years of a great economy has lulled many
 - Request financials if allowed under contract
 - Actually read the financials you've been given!
 - D&B is sometimes helpful, but many times not
 - Publically traded company? Check the SEC filings
 - Leadership changes, sales of business units/facilities
 - Industry intel

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COVID-19 Hits – Now what?

Many companies' poor financial condition is currently hidden by COVID-19 issues:

- PPP winners and losers
- Lenders reluctant to declare defaults or foreclose
- Landlords precluded from evictions
- Entire industries taken down to zero
- Overall distraction by other COVID-19 issues

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Don't Wait to Act

- Extra vigilance needed, because all the traditional signs still exist, in addition to COVID-19 issues
- As industries come back online, problems will arise quickly, so be prepared
- Understand options and engage professionals



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What to Do if Your Customer is Late (traditionally)

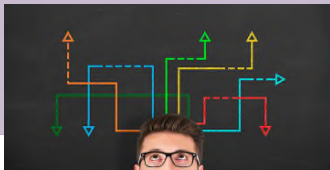
- Supplier does not need to sit idly by and wait for customer to file for bankruptcy
- 2-609 letter to customer seeking adequate assurance may be an option
 - Downside:
 - potential preference liability/litigation
 - need to weigh risks of payment now vs potential disgorgement later
 - Upside:
 - may change payment terms;
 - may shorten contract which has potential positive consequences, especially if bankruptcy is filed thereafter and if you're a sole source supplier
 - Be careful with this option, letter must be carefully drafted; must rely on facts not hunch, but don't be afraid to send it if you've done your due diligence



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Additional Thoughts

- What are your lien options?
- Build a set of facts, then consult with counsel for further intel on your customer or industry



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Dealing With Distressed Customer in Bankruptcy

How am I going to get paid?

- Unpaid prepetition deliveries
- Post-petition deliveries

Bankruptcy Code strives for equal treatment of all creditors in the same class:

- Reality is all suppliers are not treated equally
- Up to supplier to take advantage of Bankruptcy Code sections that allow for special treatment, if allowed by facts and circumstances



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Asserting a Secured Claim

Are you entitled to a secured claim?

- PMSI
- Statutory non-possessory liens like tooling and mold liens
- Possessory liens



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Asserting an Administrative Claim

Administrative claims under the Bankruptcy Code are a special category of claims entitled to priority under certain circumstances

- Covers products delivered post-petition
- Also includes 503(b)(9) claims for delivery of product within 20 days of bankruptcy petition
- Must assert in order to receive this priority
- Differing treatment under confirmed plan vs sale of business – why?



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Administrative Claims (continued)

- When do 503(b)(9) claims get paid?
- 503(b)(9) payment process may be streamlined via a court order...or not
- Different than a proof of claim
- You may be leaving money on the table



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Asserting Reclamation Claims

- Supplier can request reclamation of goods shipped within 45 days prior to bankruptcy petition
- Timing of reclamation claim is important — 45/20 rule
- Reclamation rights are subject to bank liens
- Have parts been incorporated into larger component?



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Importance of Executory Contracts

- Executory contracts are contracts where both parties have duties to perform
- Special status under Bankruptcy Code
- Many supply contracts and purchase orders are executory contracts
- Sole source suppliers may have significant leverage where resourcing is difficult



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Executory Contracts (continued)

- Supplier must ship post-petition unless supply contract terminated pre-petition
- If no executory contract at petition date, no obligation to continue to ship, give credit terms or agree to pricing
- If executory contract, Debtor decides whether to assume or reject supply contract, both result in consequences



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Executory Contracts (continued)

- If executory contract assumed, Debtor must cure pre and post-petition arrears
 - Cleanses preference liability
 - Timing of assumption/rejection can vary greatly
 - While deciding, Debtor must pay post-petition



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Executory Contracts (continued)

- Look at expiration of executory contracts and compare to continued need for parts
- May be opportunities for supplier leverage
- Put the brakes on new contract acceptance process: stop and think
- Contact counsel for strategies to optimize leverage under these facts and circumstances



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Executory Contracts (continued)

- Potential for similar leverage in context of sale of Debtor's business because of requirements to assign executory contracts
- Typically a process in place to assume and assign contracts in a BK sale scenario

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Critical Vendor Status

- Some bankruptcies allow for critical vendors to get paid ahead of unsecured creditors
- Critical Vendor motions typically include a list of proposed critical or sole source suppliers
- Critical vendors may get prepetition debt paid or an administrative claim in exchange for credit terms and/or continued supply during bankruptcy case
- Attractive, but pitfalls exist, so contact counsel


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Questions?



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Conclusion



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Sue Cook | smcook@wnj.com | 248.784.5194
Rozanne Giunta | rgjunta@wnj.com | 248.784.5193
Dennis Loughlin | dloughlin@wnj.com | 248.784.5186

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