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Column

Last in Line

***28 HOOPS OF FIRE: FILING PROOFS OF CLAIM IN THE MULTI-DEBTOR CASE**

Lisa Sommers Gretchko

Howard & Howard Attorneys P.C. Bloomfield Hills, Mich. lgretchko @howardandhoward.com

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It is now tougher than ever to be an unsecured trade creditor. The reclamation remedy has been virtually eviscerated because debtors so rarely have equity in their inventory. Trade liens that I have reviewed recently are so watered-down that they lack the protection and information that trade creditors deserve. Critical-vendor motions favor a select few unsecured creditors, but at the expense of all the others. As if to add insult to injury, the claims procedures in recent large, multi-debtor bankruptcy cases make it more difficult (and more expensive) than ever before for unsecured creditors to simply file a proof of claim.

In most bankruptcy cases, creditors file the proof of claim at the bankruptcy court, which maintains the claims register or claims docket; thus, the creditor simply sends (or takes) the proof of claim to the bankruptcy court (together with an extra copy and a return envelope), and asks the court to return a time-stamped copy once the claim is filed. In large multi-debtor bankruptcy cases, however, the number of claims can overwhelm the bankruptcy court. Thus, it is now common-place for the bankruptcy court to enter a Claims Procedure Order appointing an independent claims agent with whom all proofs of claim are to be filed. At first, claims procedure orders seemed relatively innocuous; they identified the claims bar date and the claims agent. Lately, however, the claims procedure orders in large multi-debtor cases seem to have taken on a life of their own.

In a recent large multi-debtor chapter 11 case, the debtors' schedules and statements of affairs admitted that the debtors use an "integrated bookkeeping system," meaning that the debtors' books and records are in such a state that even the debtors cannot determine *which* debtor entity is responsible for *which* creditor's claim. Nevertheless, the claims procedure orders entered in that case required *each creditor* to file a *separate* proof of claim against *each* debtor that *might* owe it money. (If a proof of claim listed multiple debtors, the claims procedure order promised to treat that claim as if it was filed only against the first debtor named in the claim.)

Some creditors will have contracts or invoices containing the identity of the debtor and the amount owed, in which case this debtor-specific requirement is not a problem. Ironically, however, many of the trade creditors who conducted the most business with the debtors may be the most ill-equipped to know exactly *which* of the multiple debtors might owe them money. The advent of electronic data systems has revolutionized the manner in which large multi-debtor conglomerates deal with their principal vendors, and the transactions among them are increasingly paperless. Consequently, there might not be any paper invoices between a principal vendor and the debtors: Instead, each has a computer that "talks to" the computer of the other. Thus, the trade creditor that may have sold goods to *all* of the debtors' numerous locations may find itself in the unenviable position of not knowing *which* of the multiple debtors is actually responsible to pay the claim. In this scenario, the claims procedure order requires the trade creditor to file a proof of claim against *each* of the multiple debtors.

In chapter 11 proceedings, the creditor's first instinct might be to seek assistance from counsel for the creditors' committee. Counsel for the committee, however, is just as frustrated as the creditor and has no better information than the debtors. Indeed, in this scenario, committee counsel will advise that the *safest* way to proceed is to file a proof of claim against each of the

multiple debtors for the total amount of the claim, together with an explanatory statement indicating that the creditor is uncertain *which* of the debtors is responsible for all or any portion of the claim. Although this might seem like just an inconvenience, it is very difficult to explain to the trade creditor *why* it needs to sign and file so many claim forms: Frankly, it makes lawyers look like we are creating busy work at our client's expense.

The volume of transactions between a principal vendor and many related debtors renders it virtually impossible to attach all of the invoices to the proof(s) of claim; instead, the creditor usually attaches a summary or list of the invoices to the proof of claim. Even in the world of paperless transactions, however, the creditor's counsel must take time to review that list. In reviewing such a list recently, I noticed two different formats in the invoice numbers, and when I questioned my trade creditor client about this difference, I learned that one invoice format was generated by a sister company which was, in fact, a *separate* corporation with a *separate* body of paperless transactions with the debtors. Of course, the claims procedure order also required the sister company to file a proof of claim against *each* of the debtors, even though the debtors had never heard of the sister company.

By the time your client recovers from writer's cramp, he or she wants to fire you. However, your skills are needed to ensure that all required proofs of claim are timely and properly filed. Although the claims procedure order relieves the bankruptcy court of this administrative burden, the claims agent can also become overwhelmed by the sheer volume of claims and may be unable to return a time-stamped copy of the filed proof of claim before the claims bar date. Consequently, your client (who has taken the trouble to sign and file a proof of claim against *each* debtor) might not receive the written confirmation it desires *before* the claims bar date that all of its proofs of claim have been timely and properly filed. This is simply unacceptable to most clients, especially those with large claims.

Strategies for Protecting Your Claim

When faced with this situation, the creditor's counsel needs to be proactive. First, in the large multi-debtor case, creditor's counsel should call the claims agent and *ask* how quickly a time-stamped copy of the filed claim will be returned. If the claims agent's response is unsatisfactory, then you need to get creative. If your client is located in the same city as the claims agent, perhaps you can have the client hand-deliver the proofs of claim to the claims agent and wait for the claim to be filed, and the time-stamped copies returned. If this is not an option, ask the claims agent if there is a particular person in the claims agent's office to whom you can send the claim(s) to have them filed with the time-stamped copy returned via overnight courier. Alternatively, you might want to use your ABI Directory to locate bankruptcy counsel in the geographic vicinity of the claims agent, so that you can send the proofs of claim to that attorney, and he or she can then hand-file the proofs of claim with the claims agent, obtain the *29 time-stamped copies and send them to you. The expense associated with this last option is usually nominal, although it is the most expensive of these three alternatives.

Ironically, the vendor's compliance with the letter of the claims procedure order ensures that the debtors will file a claim objection alleging that the multiple proofs of claim are duplicative, and that only one of them should be allowed. If the multi-debtor bankruptcy cases have been substantively consolidated, then perhaps there is merit to the claim objection, and a quick settlement can be reached. In the absence of substantive consolidation, however, it would appear that this claim objection is in error, and that the debtors and the claimant will have a lot of reconciliation work ahead of them. Such an objection, however, is extremely aggravating to the trade creditor who has simply complied with the claims procedure order. In many situations, the trade creditor must now go to the additional expense of hiring counsel admitted to practice in the court in which the bankruptcy is pending, just to sign a response to the claim objection and handle the courtroom aspects of the claim objection.

This whole scenario would be bad enough if the debtor consolidated all of its objections to the trade creditor's claims into one objection. In my experience, however, this is not done. Debtor's counsel will file one claim objection to deal with duplicate claims, and subsequent claim objections to deal with other issues, such as the debtors' inability to identify the vendor (which arises when the trade creditor *and its sister company* use just one name when selling to the debtors), reconciliation errors in the amount of the claim, etc. In one recent case, my client was the target of at least three different claim objections before its claim was resolved and allowed.

Perhaps debtors (and their counsel) lose sight of the fact that their bankruptcy can have a devastating ripple-effect on the debtors' principal vendors. Certainly, some of these principal vendor/claimants are enormous by any measure, and their financial survival does not depend on the outcome of the debtors' bankruptcy. Other vendors, however, are smaller companies who grew based on their business relationship with their large customer that just filed bankruptcy and, from their perspective, the bankruptcy proceedings of a large customer means that the vendor's own future might be in peril. The claims process should not be crafted or enforced in a way that further traumatizes these vendors.

Because the purpose of chapter 11 is to enable the debtors to successfully reorganize, it would seem that, *especially* in reorganization cases, the debtors' counsel should try to craft a claims procedure order (and implement a claims-objection process) that is as painless and inexpensive as possible for the trade creditors whose support the reorganized debtor needs in order to succeed post-chapter 11. For example, in the multi-debtor case in which the *debtors* do not know which entity is responsible to which creditor, a special procedure could be crafted for any creditor whose transactions with the debtors render the creditor similarly unable to determine which of the debtors are responsible to pay the claim. After all, the debtors know the identity of their large vendors and which of them conduct business with the debtors via paperless transactions. (In fact, there is often a separate agreement between the debtors and the large vendors as to the computer equipment and systems that each is required to maintain in order to ensure that their technology is compatible so that their computers can "talk to" one another to streamline the vendor's delivery of products, and the debtors' payment for that product.) Perhaps a separate claim form could be crafted for the principal vendors *57 that fall into this category to alleviate the need for them to file a proof of claim against *each* of the multiple debtors. Perhaps the debtors could structure a reconciliation process and claim-objection process that reconciles *all* objections thereto in *one* claim objection, instead of piecemeal objections that test the patience and fortitude of the trade creditor.

Another way to alleviate the burden that the claims process tends to impose on trade creditors is to require the claims agent to either e-mail or fax written confirmation of the filing of the proof of claim very quickly after the proof of claim is filed, so that creditors receive quick written confirmation that the claim was properly and timely filed without having to go to the expense of hiring separate counsel in the geographic vicinity of the claims agent to ensure that the claim was filed before the claims bar date (unless, of course, the creditor waits until the day before the bar date.) Perhaps bankruptcy courts could amend their local rules (or perhaps bankruptcy judges could modify their application in the multi-debtor case, at least for the initial parts of the claim-objection process), so that the creditor is not required to hire local counsel to sign pleadings or to appear on claims objections. Often, the large vendor has already consulted a lawyer before preparing and filing the initial proof of claim; thus, court rules requiring *local* counsel to sign pleadings and participate in the claims-objection process simply add an additional layer of expense to be borne by the trade creditor.

The bottom line is that the current claims process in the large multi-debtor bankruptcy case is a complex labyrinth in which creditors are required to jump through hoops of fire simply to get their claims filed and allowed. Especially in the chapter 11 context, it is counterproductive for debtors' counsel to make the claims process unnecessarily difficult for the trade creditor with a large claim because the debtors need the support of those very creditors throughout the chapter 11 process (and thereafter) if they are to survive. Although unsecured trade creditors may still be "last in line," the claims process should not be designed to make it more difficult or more expensive for them to gain a foothold on that lowly rung of bankruptcy's priority ladder.

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