



obtaining a security interest is another handy tool. In fact, there are statutory provisions that automatically provide you with a shipper's lien and warehouseman's lien for goods that you are holding in your possession. There are limitations to those liens and the statutory steps must strictly be followed, but they are a good place to start. With the correct documentation, you can even expand those liens to secure payments owed for goods which were previously shipped and already delivered.

Although it is preferable to be a secured creditor, there are other tools available to help enhance your position. For instance, you could require a deposit from the customer. Similar to the way you keep your gas tank full, you want to require that your customer's deposit be kept at a certain level, and "topped off" if used. That is known as an "evergreen deposit." Another option is to require the customer to provide you with a standby letter-of-credit, which can be presented to the issuing bank for payment if the customer fails to pay. Also, if there is a financially stable, credit-worthy owner of the customer company, or a parent corporation, you could ask for a guarantee from that owner or parent company. And finally, there are certain statutory provisions which provide you with other rights. For example, in certain circumstances, a party to a contract or purchase/service order may require the other party to provide adequate assurance that they will be able to perform. The statutes may also allow you to stop goods in transit when certain conditions are met.

Alternatively, you may find that you would like to apply your brakes. Review your contracts, purchase and service orders, and terms and conditions, as they may contain termination provisions which can serve as your "brakes." Your brakes may become particularly important if you become concerned that a customer might file for bankruptcy protection. Contracts terminated *prior* to bankruptcy generally cannot be resurrected, but if you wait until a bankruptcy is filed, you may be stuck, even if your contract is in default. Bankruptcy may allow your customer to cure any defaults and to "assume" and/or assign that contract, and you could be forced to continue doing business with your customer or an assignee of your customer. Consider revising contracts with distressed customers to reduce your exposure in anticipation of a possible bankruptcy, such

as tightening payment terms or default provisions. Be cautious, though, as taking any unusual activity in the 90 days before a bankruptcy could subject you to a “claw-back” claim for any payments made to you during that time frame.

Another helpful tool is to address the issue of a customer’s bankruptcy as soon as you become aware that one has been filed. If your customer files for bankruptcy, engage counsel early to protect your position and preserve your rights. For the same reasons you would take a truck in for servicing when an issue arises, you should bring a customer’s bankruptcy filing to legal counsel so that they can address any issues that may prove problematic down the road. Beware of the “automatic stay” which is immediately effective upon a bankruptcy filing. The automatic stay requires you to stop all collection activity. Moreover, it restricts you from terminating contractual rights. You can maximize your recovery in the bankruptcy process by timely filing all available claims you may have. These include unsecured claims for goods or services provided prior to the bankruptcy filing. You might additionally have some priority claims (which will be paid before most other claims) by taking the steps suggested in the first part of this article. One other avenue for payment in a bankruptcy action is to be named as a critical vendor. That designation will provide you with priority treatment, allowing you to get paid *in full* on your prepetition claims in exchange for continuing to do business with the debtor. Monitor the bankruptcy, as a sale of your customer’s assets can affect you. You could find yourself doing business with a buyer of your customer. Be sure that your security position is not jeopardized by the debtor’s post-petition financing. Sometimes post-petition lenders will be given rights which trump other pre-existing rights and interests. Furthermore, you will want to make sure that the expense for paying for your continued service during the bankruptcy action is included in the debtor’s budget. A bankruptcy attorney can help you maneuver through all these processes.

Finally, you should also evaluate your risk of getting sued by a bankrupt debtor. As we mentioned above, the Bankruptcy Code permits payments which were made by a debtor during the 90-day window leading up to the bankruptcy action to be “clawed back.” This can result in claims and lawsuits being brought against anyone

who received a payment during that time frame. They are known in the bankruptcy world as “Preference Claims.” Preference Claim actions may be filed as much as *three years* after the bankruptcy filing. There are defenses you can assert, but you need to make sure that valuable information and documents necessary for your defenses are not lost over time. Three years is a long time. To protect your information, you should put a “litigation hold” in place as soon as a customer has filed for bankruptcy.

In sum, with some vigilant monitoring of the financial strength of your customers, taking some preventative action, and taking any steps that may be available at the first signs of financial trouble, you can likely enhance your position and reduce your potential exposure. And, finally, if you suspect a customer may be spiraling toward bankruptcy, it is always wise to consult a bankruptcy attorney to assist you in developing a strategy to both protect your position as well as insulate yourself against exposure.

If you have questions or need assistance, please reach out to the author of this article or any attorney with Frost Brown Todd’s [Bankruptcy & Restructuring](#) practice.

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