



NAVIGATING BANKRUPTCY

AVOIDING COMMON PITFALLS FOR CREDITORS

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1. **Preference Actions**
2. Critical Vendor Status
3. 503(b)(9) Claims

What is a Preference Action?

- A **preference** is a payment (or transfer of value) made by a debtor before filing bankruptcy that unfairly favors one creditor over others
- The bankruptcy trustee (or debtor in possession) can claw back those payments
- Goal = equal treatment of creditors

The 5 Elements of a Preference – Section 547(b)

- To recover a payment, all 5 must be met:
 - Transfer of an interest of the debtor in property
 - Usually a payment – check, ACH, wire
 - To or for the benefit of a creditor/vendor (*i.e.* you)
 - For or on account of an antecedent debt
 - Debt existed before the payment was made
 - Made while the debtor was insolvent
 - Presumed during the 90 days before filing
 - Made within the preference period
 - 90 days before filing (standard creditors)
 - 1 year for insiders
 - That enables the creditor to receive more than in a chapter 7 liquidation
 - Usually satisfied in practice

The Preference Period

- 90 day lookback is the danger zone
- Payments received during this time are at risk
- Key issue – timing matters
 - When was the payment made vs. cleared vs. applied

Common Types of Transfers at Risk

- Check payments – especially if clearing date is within 90 days
- ACH/wire transfers
- Setoffs
- Returned goods or repossessions
- Granting liens shortly before filing

Defenses You Need to Know – Section 547(c)

■ Ordinary Course of Business

- Payment was consistent with:
 - Prior history between you and customer (subjective test)
 - Industry standards (objective test)
- Example – customer always pays in ~ 45 days and this payment fits that pattern

■ New Value Defense

- You shipped goods or provided services after receiving payment
- That “new value” offsets what must be returned
- Critical to track post-payment shipments

Defenses You Need to Know – Section 547(c)

- Contemporaneous Exchange

- Payment was intended to be cash-on-delivery or near-simultaneous
- Not really “credit”

- Subsequent New Value (most common in value)

- Often the strongest defense for trade creditors

Practical Red Flags Before Bankruptcy

- Payments speeding up or slowing down dramatically
- Customer switching to unusual payment methods
- Requests for extended terms or partial payments
- Bounced checks or erratic behavior

How Preference Claims Typically Arise

- Demand letter from trustee or law firm

- Request for
 - Payment history
 - Invoices
 - Contract/terms

- Followed by
 - Settlement demand (often discounted)
 - Lawsuit if not resolved

How to Respond → Strategy Overview

- Don't ignore it – deadlines matter

- Gather
 - Payment history (at least 1 to 2 years)
 - Invoice and shipment data
 - Terms and any changes

- Analyze defenses
 - Ordinary course
 - New value

- Most cases settle, not litigate

Best Practices to Reduce Exposure

- Keep consistent credit terms
- Avoid unusual collection pressure that changes payment patterns
- Track and document
 - Payment timing trends
 - Shipping after payments (for new value)
- Maintain clean records – this is huge for defenses

Key Takeaways

- Preference risk is normal, not a sign you did anything wrong
- Your records and consistency are your best defense
- The new value defense can significantly reduce liability
- Early recognition of troubled accounts helps limit exposure

2026 Court Trends

- Courts are finding that Plaintiffs need to exercise **due diligence** prior to filing a preference complaint
 - Considering a Defendant's affirmative defenses
 - To prevent unnecessary litigation

- This is good news for creditors!

1. Preference Actions
2. **Critical Vendor Status**
3. 503(b)(9) Claims

What is a Critical Vendor?

- A supplier that a debtor asks the court to approve for special treatment
- The debtor argues:
 - We cannot operate without this vendor
- If approved, the vendor may get
 - Payment of prepetition debt (old invoices)
 - Priority treatment going forward

KEY POINT – THIS IS AN EXCEPTION TO THE NORMAL BANKRUPTCY RULES

Why do Critical Vendor Motions Exist?

- Bankruptcy law normally requires
 - Equal treatment of creditors

- But businesses need
 - Goods and services to keep operating

- Courts allow critical vendor treatment to
 - Preserve the business
 - Maximize value for all creditors

When Does This Come Up?

- Usually filed immediately after bankruptcy filing – first day motions
- Debtor identifies vendors they cannot replace easily
- Court may approve
 - Cap on how much can be paid
 - List of approved vendors – sometimes confidential

What Makes a Vendor “Critical”?

- Typical factors:
 - Sole source or had to replace supplier
 - Specialized product or service
 - Long lead times
 - High switching costs
 - Risk of operational shutdown without them

- Translation – Can the Debtor realistically replace you quickly?

What Do You Get as a Critical Vendor?

- Potential benefits
 - Payment of prepetition balance (in full or partial)
 - Better payment terms post-petition
 - Continued business relationship

- But –
 - Not automatic
 - Often comes with conditions

Common Conditions Imposed on Vendors

- If you accept critical vendor status, you may have to
 - Continue supplying goods/services
 - Maintain or restore customary trade terms
 - Agree not to –
 - Change pricing
 - Tighten credit terms
 - Possibly waive certain rights

KEY WARNING = YOU'RE TRADING FLEXIBILITY FOR PAYMENT

Risks and Tradeoffs

- You may
 - Lock yourself into unfavorable terms
 - Be forced to extend credit again

- If the company fails anyway
 - You could face new exposure

- Some payments may be
 - Less than 100% of what you're owed

Negotiation Opportunities

- This is where you can have influence

- You can push for
 - Shorter payment terms – e.g. COD or shortned cycle
 - Payment plans on old debt
 - Guarantees of ongoing payment
 - Clear limits on future exposure

- Don't assume terms are fixed – there is often room to negotiate

What if You are NOT Chosen as a Critical Vendor?

- You typically
 - Do NOT get paid prepetition amounts

- But
 - You can still negotiate informally
 - You can decide whether to continue supplying

- Practical reality
 - Some non-critical vendors still have leverage

Practical Red Flags

- Watch for
 - Sudden outreach from customer about “importance”
 - Requests to continue shipping without payment
 - Vague promises of “being taken care of in bankruptcy”

- If you hear you’re “critical” – verify it through counsel or filings

How to Respond

- Quickly assess
 - Your leverage – are you truly critical?
 - Replacement risk

- Gather
 - Outstanding balance
 - Contract terms
 - Dependency details

- Coordinate with
 - Legal term – internally or outside counsel

Best Practices

- Know your strategic accounts ahead of time
- Track
 - Customer dependency on your product
- Document
 - Unique aspects of your offering
- Have a playbook ready before bankruptcy happens

Key Takeaways

- Critical vendor status is an opportunity – but not free money
- It's a negotiation, not a guarantee
- You are trading
 - Payment on old debt... FOR
 - Commitment going forward
- Know your leverage before you agree

Remember!

- Status as a critical vendor does not protect you from preference demands
 - Can try to negotiate this “away” – but almost impossible to do!

1. Preference Actions
2. Critical Vendor Status
3. **503(b)(9) Claims**

What is a 503(b)(9) Claim?

- A 503(b)(9) claim gives priority status to certain unpaid invoices
- Applies to
 - Goods received by the debtor
 - Within 20 days before bankruptcy filing
- It is an administrative expense claim → higher priority than general unsecured claims
- Translation → you may get paid ahead of most other creditors

Why it Matters

- Normal unsecured claims often recover little – or nothing
- 503(b)(9) claims
 - Must be paid in full to confirm a plan – in most cases
- This can turn
 - A write off → into a meaningful recover

The Key Requirements – *ALL MUST BE MET*

- Sale of Goods (NOT Services)
 - Must be tangible goods
 - Services do not qualify
 - Mixed contracts may need allocation

- Goods Received by the Debtor
 - Focus is on receipt, not shipment
 - Delivery date matters more than invoice date

Timing is Everything

- Key dates to track
 - Shipment Date – Not Enough
 - Delivery/Receipt Date – CRITICAL
- If goods arrive on day 21 → no 503(b)(9)
- This is where most mistakes happen

What Qualifies as “Goods”

- Generally includes
 - Inventory
 - Raw materials
 - Finished products

- Gray areas
 - Software
 - Electricity
 - Custom/manufactured items

- Courts may vary – when in doubt, analyze closely

How to Assert a 503(b)(9) Claim

- Debtor usually sets a bar date (deadline)

- You must –
 - File a request or proof of claim
 - Identify qualifying invoices

- Include
 - Invoice dates
 - Delivery/receipt proof
 - Amount claimed

Common Documentation Needed

- Invoices
 - Bill of lading
 - Proof of delivery (POD)
 - Shipping records
 - Customer acknowledgments
-
- If you can't prove delivery timing, you may lose the claim

Interaction with Preference Claims – IMPORTANT

- You might face
 - A preference demand
 - AND have a 503(b)(9) claim

This is a strategic opportunity!

Common Pitfalls

- Including services (not allowed)
- Using invoice date instead of delivery date
- Missing the bar date
- Poor documentation of receipt
- Not coordinating with legal/finance teams

Practical Strategy

- Immediately identify
 - Shipments within 20 days pre-filing

- Flag
 - High-value deliveries

- Coordinate internally
 - Credit + AR + legal

- Track both
 - 503(b)(9) opportunity
 - Preference exposure

Best Practices (Before Bankruptcy Happens)

- Maintain strong...
 - Delivery tracking systems

- Keep...
 - Clean accessible records

- Understand...
 - Which customers create the most exposure

- Build a rapid response checklist...

Best Practices (Before Bankruptcy Happens)

- 503(b)(9) is a priority claim – use it
- Delivery date drives everything
- Documentation = success or failure
- It can offset losses everywhere – like preferences
- Act quickly – deadlines matter

QUESTIONS?



THANK YOU!

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