



message from partner in charge

It seems like there's always something new to discuss – and this issue takes aim at the recent changes to the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA). Amended Section 546(c) and new Section 503(b)(9) have caused confusion and buzz amongst a variety of interested parties. Attorney Deborah Kovsky-Apap offers readers more insight into these important changes.

I'm also pleased to announce that partners David Stratton and Bob Hertzberg have been named co-chairs of the Corporate Restructuring and Bankruptcy Practice Group. Dave and Bob replace I. William Cohen, who is stepping down after 17 years of leadership. But stepping down doesn't mean stepping back – and I'm delighted to announce that Bill has been elected Vice President of the American College of Bankruptcy – a prestigious, nonprofit, honorary association of bankruptcy and insolvency professionals.

Please join me in congratulating Dave, Bob and Bill in their new roles.

If you have questions about the information contained in this newsletter, call us and we'll do our best to help.

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Much Ado About Nothing (Or Not Very Much): The New Reclamation and Administrative Expense Claims Under BAPCPA

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Introduction

The new provisions regarding reclamation and administrative expense claims under the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) have created considerable buzz among debtors, creditors and the attorneys who advise them. Much has been written about the amended Section 546(c) and new Section 503(b)(9) – though not, unfortunately, by either Congress or the courts. The lack of both legislative history and judicial interpretation has meant that bankruptcy practitioners are still feeling their way through amendments that could signal a sea change in the pre- and post-petition relationship between debtors and their trade vendors – or prove to be merely a tempest in a teapot.

At first blush, it appears that Section 546(c) and Section 503(b)(9) pack a powerful one-two punch, enlarging the rights of creditors that provided goods to a debtor in two important ways. Section 546(c) expands the time for making the reclamation demand from 10 to 45 days, while Section 503(b)(9) grants creditors an administrative expense claim for the value of goods provided to the debtor within 20 days before the commencement of the bankruptcy case, even if the creditor fails to make a written demand for the goods. Together, the two sections would seem to place unsecured creditors that provided goods to the debtor in a far stronger position than under the previous incarnation of the Bankruptcy Code. Yet it is unclear precisely how each section should or will be applied, and Section 546(c) in particular may be of limited utility in practice.

Impact of the Amended Section 546(c) and New Section 503(b)(9)

The overarching question with respect to Section 546(c) and Section 503(b)(9) is not, ‘What on earth was Congress thinking?’ but rather, ‘How will this affect debtors and creditors in practice? Will creditors watch the value of their reclamation claims disappear while they rush to obtain restraining orders? Will debtors be forced to put a halt to business operations while they inventory the goods of reclamation claimants? Will debtors contemplating bankruptcy begin demanding that creditors apply payments to their most recent invoices in order to minimize exposure under Section 503(b)(9)? Will the necessity of paying Section 503(b)(9) claims at confirmation create an insurmountable obstacle to the confirmation of debtors’ plans?’

As a practical matter, little is likely to change under the new sections. Reclamation claims may be rendered worthless – but they were often worthless even under the old Section 546(c) because of the prior rights of a secured lender. The amended Section 546(c) may take away the old Section 546(c)’s alternatives of an administrative expense claim or lien, but Section 503(b)(9) grants twice the administrative priority available under the old Section 546(c). A seller may have to wait until the conclusion of the case in order to receive payment on its Section 503(b)(9) claim,

The greatest import of Section 503(b)(9) is likely to be the requirement under the Bankruptcy Code that Section 503(b)(9) claims, like all administrative expense claims, be paid upon confirmation of the debtor’s plan of reorganization.

but even so it is certainly no worse off than it was before the enactment of BAPCPA.

The greatest import of Section 503(b)(9) is likely to be the requirement under the Bankruptcy Code that Section 503(b)(9) claims, like all administrative expense claims, be paid upon confirmation of the debtor’s plan of reorganization. The existence of significant Section 503(b)(9) claims may prevent some debtors from confirming a plan of reorganization.

As the following practice tips demonstrate, however, planning and foresight on the part of both debtors and credi-

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Private Equity Insight

Key Issues and Trends Facing Dividend Recapitalizations

Pepper Hamilton and PricewaterhouseCoopers are releasing a new study that presents findings from a survey of private equity firms. The study is entitled “Private Equity Insight: Dividend Recapitalizations” and was conducted in association with mergermarket, a research and publishing company.

The report is centered on a survey conducted in late 2006. mergermarket interviewed 75 senior private equity practitioners with a working knowledge of dividend recapitalization processes. Some key findings include:

- 97% of respondents expect to recapitalize portfolio companies in 2007
- The majority of dividend recaps will involve middle market companies
- Most firms are comfortable with post-dividend recap leverage ratios of 3.5 or 4 to 1.

We hope you find **Private Equity Insight: Dividend Recapitalizations** both interesting and informative. You can request a complimentary copy of the entire report, including forewords and commentary by Pepper Hamilton and PricewaterhouseCoopers, by contacting Brian Dolan at dolanb@pepperlaw.com.

Hertzberg and Stratton Become Co-Chairs of Pepper Hamilton's Corporate Restructuring and Bankruptcy Practice

In October 2006, Robert S. Hertzberg and David B. Stratton became co-chairs of the firm's Corporate Restructuring and Bankruptcy Practice Group. They succeeded I. William Cohen, who had served as chairman of the group from 1989 to 2006. Under Mr. Cohen's leadership, the practice group diversified to include all types of clients in the field, including debtors, creditors and committees; and adopted many "best practices" that became models for other practice groups within the firm. Bill will remain an active, full-time member of the group, and will continue to provide leadership in the national bankruptcy and restructuring bar, including service as a Fellow of the American College Bankruptcy.



Robert S. Hertzberg

Bob Hertzberg has practiced in the bankruptcy and restructuring field for more than 25 years. He is the past president of INSOL International (2003-2005), the leading international organization of bankruptcy professionals. Bob also sits on the Sixth Circuit Admissions Council of the American College of Bankruptcy and he has been active in the Turnaround Management Association, the Commercial Law League of America (past chairman of the Bankruptcy Section) and the American Bankruptcy Institute (past chairman of the Central States Workshop Program). Bob is listed in *The Best Lawyers in America* and the International *Who's Who of Insolvency and Restructuring Lawyers*. He received the Consumer Bankruptcy Association's Award of Recognition in 2000 for his accomplishments in the bankruptcy field. Bob graduated in 1979 from Thomas M. Cooley Law School.



David B. Stratton

David Stratton is a member of the firm's Executive Committee and manages the firm's Wilmington, Delaware office. He has had more than 28 years of experience in the bankruptcy and restructuring field, representing a wide range of clients, both as lead counsel and co-counsel in bankruptcy courts in Delaware, Maryland, the Southern District of New York and elsewhere.

He was recognized as one of the leading bankruptcy practitioners in Delaware in the 2004, 2005 and 2006 editions of Chambers USA's *America's Leading Lawyers for Business*. David previously chaired the Commercial Law Section of the Delaware State Bar Association. He graduated *cum laude* in 1978 from the University of Pittsburgh School of Law, where he also served as associate articles editor of the *Law Review*.

When asked about their vision for the practice group, Bob and David said that they are looking forward to working together to build on the excellent platform Bill developed, and that they hope to expand the group significantly.

"We have wonderful lawyers in the group," said David. "We are sure that the future for the group is bright. In particular, we are looking to expand our presence in mid-market debtor and committee cases."

tors can help minimize any negative impact of the new sections.

Practice Tips – 11 USC 503(b)(9)

For Creditors

As soon as possible, a seller should file a motion to compel immediate payment of its administrative expense claim. While it is still not clear when claims under Section 503(b)(9) are to be paid, there are compelling arguments for payment in the ordinary course. Additionally, such a motion may bring the debtor to the negotiating table. Another opportune time to raise the issue of payment of an administrative expense under Section 503(b)(9) is when the professionals in the case are seeking approval of their fee applications. The Sixth Circuit has held that 11 USC 726 requires professionals to disgorge fees in order to make pro rata distributions to creditors at the same priority level. Attorney fee claims and Section 503(b)(9) claims are both administrative expense claims at the same priority level. Thus, a Section 503(b)(9) claimant whose claim has not been paid would have reasonable grounds to object to a professional's fee application. The objection may not succeed – the professional may demonstrate to the court's satisfaction that it will be able to disgorge the fees in the event that the case is administratively insolvent – but the objection may nonetheless give the creditor additional leverage in dealing with the debtor and its counsel.

A seller should also begin its ordinary course analysis as soon as possible, in order to establish both that it is entitled to a claim under Section 503(b)(9), and that it is not liable for a preference and thus not barred by Section 502(d). Until a court rules otherwise, the same ordinary course analysis used under Section 547(c)(2) will probably suffice for Section 503(b)(9) as well.

For Debtors

Before filing, a debtor should assess the total amount that it might owe as administrative expenses under Section 503(b)(9), and budget for that amount, to be held in reserve, in any post-petition financing. Thus, if the expenses are allowed, the debtor will be prepared to meet them either immediately or at confirmation. The debtor also should begin preference and ordinary course analyses early in the case, focusing on those creditors that have or could assert claims under Section 503(b)(9), to determine both whether the seller has made out a prima facie case under Section 503(b)(9), and whether the seller might be liable for a preference that would bar its recovery under Section 502(d).

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