HYPOTHETICAL

World's Best Stationary, Inc. ("WBS") is the largest distributor of office stationary products in the United States. Guinea Pig Corporation ("GPC") is a long-standing customer of WBS, purchasing an average of $750,000 in goods from WBS every year. All WBS invoices provide that they must be paid within thirty (30) days of the date of the invoice, which also represents the industry standard for payment of such purchases. During the course of its dealings with WBS, GPC traditionally paid the WBS invoices within twenty (20) days of the invoice date. GPC sends all of its payments for goods purchased from WBS to the following address: World's Best Stationary, Inc., P.O. Box 2250, Louisville, Kentucky 08912.

For the past year, GPC has been experiencing financial difficulties and as a result, has become delinquent on some of its payments to WBS. Due to its size, WBS maintains a bankruptcy department at its Trenton, New Jersey office which handles the administration of all claims by and against WBS customers that have filed for bankruptcy. WBS, concerned about the solvency of GPC, sends letters to WBS on October 1, 2005 and November 1, 2005, which state, in relevant part:

> *Re: Account number 123456*
>
> *To whom it may concern:*
>
> *The above referenced account number is the current account number for Guinea Pig Corporation. Please be advised that all communications regarding the above referenced account number should be sent to us at the following address:*
>
> *World's Best Stationary, Inc.*
> *Attention: Ms. Stacey Whiteout, Bankruptcy Administrator*
> *101 State Street*
> *Trenton, New Jersey 09922*
> *(609) 932-2245*

Despite the delinquency in some of GPC's payments to WBS, WBS continues to sell and ship products to GPC. GPC makes the following payments to WBS (collectively, the "Preference Period Payments"):

Date of Payment	Amount of Payment	Days From Invoice Date
9/22/05	$13,402.21	29
10/3/05	$55,603.76	45
10/28/05	$19,620.98	52
10/31/05	$4,999.99	78
11/12/05	$86,236.99	33
11/25/05	$31,763.44	66
12/10/05	$14,003.03	23
12/20/05	$38,522.56	41

On December 21, 2005 (the "Petition Date"), GPC files a chapter 11 petition in the United States Bankruptcy Court for the Eastern District of Pennsylvania. In its Schedule F, Creditors Holding Unsecured Claims, GPC lists WBS as a non-contingent, non-disputed unsecured creditor holding a claim in the amount of $89,907.65 as of the Petition Date (the "Scheduled Claim"). Notwithstanding the Schedules, WBS records indicate that as of the Petition Date, GPC owes it $120,533.22 for unpaid invoices. On its creditor matrix, GPC lists the WBS address as follows (despite the WBS prior communications to the contrary): World's Best Stationary, Inc., P.O. Box 2250, Louisville, Kentucky 08912. Accordingly, the notice of filing of GPC's bankruptcy case and the notice of bar date get sent to the foregoing WBS P.O. box used for customer payments. The bar date for filing claims in the GPC bankruptcy is set for March 22, 2006. By the time that the notice of filing and bar date reach Stacey Whiteout in the bankruptcy department at WBS, the bar date has passed. Stacey nevertheless files an unsecured proof of claim against GPC in the amount of $120,533.22 (the "Proof of Claim"). On the filed proof of claim, Stacey lists her name and the Trenton, New Jersey address as the name and address where notices in the case should be sent to WBS.

An official unsecured creditors' committee (the "Committee") is appointed in the GPC bankruptcy. WBS is not a member of the Committee. The Committee petitions the bankruptcy court and is granted authority to prosecute avoidance actions on behalf of GPC.

In May of 2006, WBS is contacted by Get Out Now Ltd. ("GON") about purchasing its Scheduled Claim for 23% of its face value. In order to evaluate the merits of the GON offer to purchase the Scheduled Claim, WBS contacts the Committee to request any and all information regarding the status of the GPC bankruptcy and the anticipated distribution to unsecured creditors. The Committee does not respond to the request for information from WBS. WBS elects not to sell the Scheduled Claim to GON.

On August 18, 2006, the Committee files an Omnibus Objection to claims in which it objects to the Proof of Claim filed by WBS as untimely and seeks the reduction of such claim to the amount of the Scheduled Claim. On September 22, 2006, the Committee files a preference action against WBS for the avoidance and return of the Preference Period Payments (the "Preference Action"). In the course of discovery in the Preference Action, WBS demands that the Committee produce any and all information and/or analysis regarding the merit of the claims against WBS, including, without limitation, communications between the Committee and its counsel and work product of Committee counsel.

On December 31, 2006, GPC confirms its liquidating plan of reorganization which provides an estimated 15% distribution to unsecured creditors, subject to the resolution of all of the avoidance actions.

QUESTIONS

1. Which, if any, of the Preference Period Payments are insulated by the ordinary course of business defense?

2. What, if any, defense does WBS have to the objection to its Proof of Claim?

3. On what basis may WBS demand information from the Committee prior to the institution of the Preference Action? On what basis may WBS

demand information from the Committee in the course of discovery in the Preference Action that is *otherwise protected* by one or more privileges? May the Committee successfully protect such material?

4. If WBS ultimately receives less than a 23% distribution on its allowed claim against GPC, does it have a claim against the Committee for the Committee's failure to provide it with information that would have enabled it to evaluate and accept the offer from GON?

5. Assume that WBS had sold its Scheduled Claim to GON and was still sued by the Committee for the Preference Period Payments. Can the Committee still use § 502(d) to object to the Scheduled Claim after such assignment?

HORNBOOK

I. PREFERENTIAL TRANSFERS

In conjunction with the avoidance provisions of § 550 of the Bankruptcy Code, § 547 permits a trustee or debtor-in-possession to set aside and recover preferential transfers for the benefit of the estate. Section 547(b) defines a preferential transfer as one that satisfies each of the following criteria: (i) prior to the bankruptcy filing, the debtor transfers an interest in property; (ii) the debtor transfers the interest to or for the benefit of a creditor; (iii) the debtor transfers the interest to pay or secure an obligation owed to the creditor prior to the transfer (the "antecedent debt"); (iv) the debtor is insolvent at the time of the transfer; (v) the transfer occurs within ninety days before the bankruptcy petition date (the "preference period"), or, if the transfer is made to or for the benefit of an "insider" of the debtor, within the year prior to the petition date (the "insider preference period"); and (vi) the transfer permits the creditor to receive more than it would have received upon the liquidation of the debtor under the Bankruptcy Code. In granting the trustee broad powers to recover assets transferred to creditors within the preference period, § 547 serves two basic policies: (i) it discourages creditors (particularly those with greater influence over the debtor) from consuming free assets prior to bankruptcy; and (ii) it promotes equal treatment among creditors.

Section 547(c) excludes certain transfers from a trustee's avoidance power even though these transfers meet the conditions set forth in § 547(b). These exceptions include, but are not limited to: (i) a transfer intended to be, and that is in fact, a contemporaneous exchange for new value; (ii) a payment in the ordinary course of a debtor's business of a debt incurred in the ordinary course of the debtor's business or financial affairs; (iii) a transfer of a security interest in connection with a loan that allows a debtor to purchase the collateral for the loan; (iv) a transfer to or for the benefit of a creditor, to the extent that, after the transfer, the creditor gave new value to or for the benefit of the debtor; and (v) the fixing of a statutory lien that is not avoidable under § 545. Congress intended the exceptions contained in § 547(c) to provide "safe harbors" for ordinary business activities that takes place prior to a bankruptcy filing and that do not deplete a debtor's estate.

More specifically, the purpose of the ordinary course of business exception provided for in § 547(C)(2) of the Bankruptcy Code is to protect normal credit transactions that are incurred by the debtor, paid in the ordinary course of a debtor's and transferee's business, and made according to ordinary business terms. Such transactions do not detract from the general purpose of § 547, which is to prevent creditors from pursuing unusual collection actions against a debtor during the debtor's "slide into bankruptcy." H.R. REP. NO. 95-595 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787. Prior to its amendment, Section 547(c)(2) provided that otherwise preferential transfers may not be avoided to the extent that such transfers were: "(A) in payment of a debt incurred by the debtor in the ordinary course of business or financial affairs of the debtor and the transferee; (B) made in the ordinary course of business or financial affairs of the debtor and the transferee; and (C) made according to ordinary business terms." 11 U.S.C. § 547(c)(2). Subsections (A) and (B) have been often referred to as the "subjective" elements of the ordinary course exception, while subsection (C) has been referred to as the "objective" element. *See Paloian v. Quad-Tech, Inc. (In re GGSI Liquidation, Inc.),* 313 B.R. 770, 775 (Bankr. N.D. Ill. 2004); *Katz v. Wells (In re Wallace Bookstores, Inc.)*, No. 02-5414, 2004 Bankr. LEXIS 408, at *40 (Bankr. D. Ky. 2004); *In re Ockerlund Constr. Co.*, 308 B.R. 325, 329, n.1 (Bankr. N.D. Ill. 2004). Until the recent modifications of § 547(c)(2), there had been considerable dispute among courts as to whether subsection (C) of § 547(c)(2) required a showing that the transfer was in the ordinary course of practice in the particular industry generally, in addition to a showing that the transaction was ordinary as between the parties.

With its amendment to § 547(c)(2) in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (the "2005 Act"), Congress has resolved the subjective and objective hurtle decisively by providing that a creditor invoking the ordinary course defense only prove either that (i) the transfer was made in the ordinary course of business or financial affairs of the debtor and the transferee" *or* (ii) the transfer was "made according to ordinary business terms." Thus, as long as a debt is incurred in the ordinary course of business between the parties and the defendant can prove *either* the subjective *or* objective prong, the ordinary course of business defense should be available to creditor defendants under the 2005 Act.

II. CREDITORS' COMMITTEE DUTIES

Creditors' committees' duties are generally outlined in 11 U.S.C. § 1103. Specifically, § 1103(c) provides that a committee may:

1. consult with the trustee or debtor-in-possession concerning the administration of the case;

2. investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and the desirability of the continuance of such business, and any other matter relevant to the case or to the formulation of a plan;

3. participate in the formulation of a plan, advise those represented by such committee of such committee's determinations as to any plan formulated, and collect and file with the court acceptances or rejections of a plan;

4. request the appointment of a trustee or examiner under § 1104 of this title; and

5. perform such other services as are in the interest of those represented.

11 U.S.C. § 1103(c)(1) - (5).

Courts have held that members of a committee have a fiduciary duty to their constituents and are obligated to exercise those powers to protect the interests of their constituents. *See, e.g., In re Kensington Int'l, Ltd.*, 368 F.3d 289, 315 (3d Cir. 2004) (citations omitted); *Westmoreland Human Opportunities, Inc. v. Walsh*, 246 F.3d 233, 256 (3d Cir. 2001), *aff'd in part and rev'd on other grounds, remanded*, 327 B.R. 561 (W.D. Pa. 2005); *Pan Am Corp. v. Delta Air Lines, Inc.*, 175 B.R. 438 (S.D.N.Y. 1994) (creditors' committee owes fiduciary duty to creditors it represents but not to debtor or any other party). This duty obligates them to act with undivided loyalty for the benefit of all of the unsecured creditors, not individual members of the class or to other creditors, the debtor or the estate generally. *Pension Benefit Guar. Corp. v. Pincus, Verlin, Hahn, Reich & Goldstein P.C.*, 42 B.R. 960, 963 (E.D. Pa. 1984); *In re ABC Auto. Prods. Corp.*, 210 B.R. 437, 441 (Bankr. E.D. Pa. 1997). Further, this duty "prohibits members of the creditors' committee from using their position to advance their own individual interests." *In re Nationwide Sports Distrib.*, 227 B.R. 455, 463-64 (Bankr. E.D. Pa. 1998) (citations omitted). Thus, committee members are obligated to avoid conflicts of interest such as acquiring stock of the debtor or engaging in business transactions with the debtor. *See, e.g., Locks v. US Trustee*,

157 B.R. 89 (W.D. Pa. 1993). Similarly, trading of claims by committee members is problematic given that members almost always have material, nonpublic information about the debtor and thus, courts or committees themselves may place restrictions on members trading claims. *See In re Kuhns*, 101 B.R. 243 (Bankr. D. Mont. 1989).

Generally, the duties of a creditors' committee run through the earlier of dismissal, conversion or plan confirmation. However, a committee can continue to exercise certain functions after plan confirmation if necessary to maximize the return to its constituency. *See, e.g., Creditors' Comm. v. Parks Jaggers Aerospace Co. (In re Parks Jaggers Aerospace Co.),* 129 B.R 265 (M.D. Fla. 1991).

The committee has the authority to consult with the debtor-in-possession concerning the administration of the estate and to make recommendations concerning the debtor's business. *See* 11 U.S.C. § 1103(c)(1). Pursuant to § 1103(c)(2), the committee has the authority to investigate the acts, conduct, assets, liabilities and financial condition of the debtor, the operation of the debtor's business and any other matter relevant to the case or to the formulation of the plan. This authority is very broad so as to allow the committee to investigate not only the above but also the reasons for the debtor's financial problems and other claims. This authority also includes the ability to investigate the management and officers of the debtor.

One of the most important roles of the creditors' committee is to negotiate a chapter 11 plan on behalf of its constituency. Specifically, the committee is empowered to participate in the formulation of the plan, advise those represented by the committee of the committee's determination as to a proposed plan and collect and file acceptances and rejections of the plan. 11 U.S.C. § 1103(c)(3).

Pursuant to § 1103(c)(4), the official committee may request the appointment of a trustee or examiner. Further, the catch-all provision codified in § 1103(c)(5) enables the committee to perform other functions as may be necessary to further the interest of its constituency. For example, a committee can object to the allowance of claims thereby increasing the recovery for the remaining creditors.

Section 1109(b) of the Bankruptcy Code gives creditors' committees the right to appear and be heard on any issue arising in the bankruptcy case or any contested matter. *See, e.g., Unsecured Creditors' Comm. v. Marepcon Financial Corp. (In re Bumper Sales, Inc.*), 907 F.2d 1430 (4th Cir. 1990) (creditors' committee has standing to appear and be heard on any motion in a chapter 11 case). Additionally, a committee may initiate a contested matter or an adversary proceeding in its own name. While a committee also has standing to appeal contested matters in which it has appeared even if it is not a named or active party in the matter, there is a split of authority on the issue of whether a creditors' committee may intervene in an adversary proceeding initiated by the debtor. *See, e.g., Southern Pacific Transp. Co. v. Voluntary Purchasing Groups, Inc.*, 227 B.R. 788 (E.D. Tex. 1998) (committee has standing to participate in appeal of confirmation order); *In re Nicolet,* 80 B.R. 733 (Bankr. E.D. Pa. 1988) (dismissing creditors' committee action as duplicative of debtor's action but inviting committee to intervene in that action); *Official Comm. Of Unsecured Creditors of the Florida Group, Inc. v. First Union National Bank of Florida (In re Florida Group, Inc.)*, 123 B.R. 923 (Bankr. M.D. Fla. 1991) (creditors' committee cannot intervene in action filed by debtor). Some courts have held that the committee has an absolute right to intervene while others have held that a committee can intervene only if it qualifies for intervention under Rule 24 of the Federal Rules of Civil Procedure.

Courts have generally permitted a creditors' committee to bring an action in the name of the debtor-in-possession if the committee has standing and is able to establish certain criteria. Where the committee is seeking to bring an action not sponsored by the debtor-in-possession, the action may be maintained if: (i) the committee has a colorable claim against the proposed defendant and standing to bring the action; (ii) the debtor-in-possession has unjustifiably refused to pursue the claim (i.e., an action on behalf of the debtor cannot be maintained if the debtor is currently pursuing the same action); and (iii) the creditors' committee has obtained the permission of the court to initiate the action on behalf of the debtor. *See, e.g.,* 5 *Collier on Bankruptcy* ¶ 1103.05 (15th ed. rev. 2005); *Canadian Pac. Forest Prods., Ltd., v. J.D. Irving, Ltd. (In re The Gibson Group, Inc.)*, 66 F.3d 1436 (6th Cir. 1995). Finally, some plans may give the creditors' committee the right to initiate adversary proceedings in the name of the debtor after confirmation. *See, e.g., 11 U.S.C. 1123(b)(3)(B); Nordberg v. Sanchez (In re Chase & Sanborn*

Corp.), 813 F.2d 1177, 1180 n.1 (11th Cir. 1987) (plan may designate creditor trustee to prosecute adversary proceedings in the name of the debtor).

With the amendment to the Bankruptcy Code in the 2005 Act, Congress has assigned an additional duty for creditors' committees. Section 1102(b)(3) now requires that a creditors' committee provide access to information for creditors holding claims of the kind represented by the committee and solicit and receive comments from such creditors. 11 U.S.C. § 1102(b)(3).

III. NOTICE

Section 342 of the Bankruptcy Code governs notice in a bankruptcy case. Prior to the enactment of the 2005 Act, § 342 consisted of three parts: (i) § 342(a) required the clerk of the bankruptcy court to give notice of the order of relief; (ii) § 342(b) required the clerk to give written notice to an individual whose debts were primarily consumer debts, informing them of the different chapters under which they may file for relief; and (iii) § 342(c) stated that any notice required to be given by a debtor should include the name, address and taxpayer identification number of the debtor, but that failure to include such information would not invalidate the notice. The 2005 Act significantly changes § 342. The majority of the changes simplify the notice process for creditors in consumer bankruptcy cases, but some of the amendments also impact business bankruptcies. Compliance with the new requirements is necessary to ensure effective notice and the efficacy of court orders and deadlines.

Section 342(c) continues to apply to business bankruptcy filings, but the 2005 Act redesignates the former § 342(c) as § 342(c)(1), and adds § 342(c)(2). Section 342(c)(1) changes the taxpayer identification number element so that only the last four digits of the debtor's taxpayer identification number are required to be included in any notice that the debtor is to provide. Section 342(c)(1) also eliminates the clause which previously stated that the failure to provide required information shall not invalidate the legal effect of a notice. One shortcoming of the 2005 Act is that it does not clarify the scope of Section 342(c)(1). The term "notice" is not defined in the Bankruptcy Code, creating ambiguity about whether § 342(c)(1) applies to service of a motion, a summons or other documents.

The 2005 Act creates a new section that allows a creditor to mandate where correspondence should be sent by a debtor. Under new § 342(c)(2)(A), if a creditor supplies a debtor with two communications in the 90 days prior to a bankruptcy filing, and those communications contain the debtor's account number and an address at which the creditor requests to receive correspondence, then required notices from the debtor must be sent to that address and must include the specified account number. When a creditor is precluded by law from sending any communications in the entire 90 day period before the petition, § 342(c)(2)(B) applies. This situation is most likely to arise when the creditor has knowledge that the debtor is represented by an attorney or that there is a prior automatic stay. If § 342(c)(2)(B) applies and the last two notices from a creditor prior to the 90 day prepetition period included a request to send correspondence to an address and an account number, the debtor must send any required notices to such address and include the account number.

Section 342(c)(2) is likely to require interpretation from the bankruptcy courts because it does not specify what constitutes a "request to receive correspondence." Although the word "sent" in the statutory language should prevent it from applying to oral requests. Section 342(c)(2) also should not apply if the debtor is only supplied with an address or an account number, as opposed to both as required by the revised statute. Presumably, communications from collection agencies also do not fall within § 342(c)(2) because those agencies are not the "creditor." 3 Collier on Bankruptcy, ¶ 342.05 (15th Ed. Rev. 2005).

The final provision of § 342(c) states that a notice concerning "an amendment that adds a creditor to the schedules of assets and liabilities" must include the full taxpayer identification number of the debtor in the notice sent to that creditor. In contrast, the copy of such a notice to the court must only include the last four digits of the taxpayer identification number.

Section 342(g) governs notice that is ineffective. Section 342(g) does not apply to any notices by a debtor that are outside the ambit of § 342(c). As a result, any notices that are not required by the Bankruptcy Code, rules, court order or other applicable laws are beyond the scope of § 342(g). When § 342(g) applies, however, an ineffective notice shall not be effective until such notice is "brought to the attention of the creditor." The term "brought to the attention"

is defined by exclusion. Section 341(g)(1) only states that if a creditor has established reasonable procedures, so that notices received by the creditor are delivered to the correct person or organizational subdivision, then an ineffective notice is not "brought to the attention" of such creditor until it reaches that person or department. The effect of § 342(g) is to give protection to creditors who have developed reasonable procedures when unreasonable notice is given, such as mailing notice of a bankruptcy case to a sales employee in an unrelated facility. *Id.* at ¶ 342.08.

Section 342(g) also limits the liability of a creditor who does not receive effective notice. Pursuant to § 342(g)(2), a creditor who has not received effective notice may not face a monetary penalty for a violation of the § 362 automatic stay or the § 542 or § 543 turnover requirements. Section 342 does not impact the discharge of debts or violations of the discharge injunction, nor does it preclude other remedies against the creditor or other entities. *Id.*

In the short-term, the changes to § 342 are likely to cause uncertainty over whether notice is adequate, particularly when notice was sent to an address other than the one specified by a creditor under § 342(c)(2). In such a case, a creditor may seek to file a proof of claim after the bar date for filing proofs of claim has passed. A creditor may then attempt to utilize Bankruptcy Rule 9006(b)(1), which allows a court to enlarge the time period for doing an act, even if the request for enlargement is made after the time period specified in the otherwise applicable statute or rule. A request for an enlargement of time must be made by motion, and cause must still be shown.

CASE SUMMARIES

A. PREFERENTIAL TRANSFERS

***In re Tolona Pizza Products Corporation,* 3 F.3d 1029 (7th Cir. 1993)**

The United States Court of Appeals for the Seventh Circuit broke new ground in 1993 with its decision in *In re Tolona Pizza Products Corporation*. In *Tolona Pizza*, the court held that the third requirement of the ordinary course exception - that the transaction be in conformity with "ordinary business terms" - means only that the terms be within the "*range* of terms that encompasses the practices in which firms similar in some general way to the creditor in question engage." *Id*. at 1033 (emphasis added). Therefore, the court reasoned, "only dealings so idiosyncratic as to fall outside that broad range should be deemed extraordinary and therefore outside the scope of the [ordinary business terms requirement]." *Id*. (citations omitted). *Tolona Pizza* inspired a number of other decisions which emphasized the relationship between the debtor and the transferee as paramount in the assessment of "ordinary business terms."

Fiber Lite Corporation v. Molded Acoustical Products, Inc.
***(In re Molded Acoustical Products, Inc.)*, 18 F.3d 217 (3d Cir. 1994)**

In *In re Molded Acoustical Products, Inc.*, the United States Court of Appeals for the Third Circuit held that the longer the relationship between the parties, the greater is the court's flexibility in looking beyond industry standards and using the parties' relationship as the more important factor in determining what constitutes ordinary business terms. *See also Big Wheel Holding Co., Inc. v. Federal Wholesale Co. (In re Big Wheel Holding Co., Inc.)*, 223 B.R. 669 (Bankr. D. Del. 1998) (citing *Molded Acoustical* and holding that payments were ordinary course even though made after recipient made reclamation demand and ceased shipping product to the debtor).

***Risk Management Alternatives, Inc. v. Scharffenberger (In re Allegheny Health Education & Research Foundation)*, 2005 U.S. App. LEXIS 4200 (3d Cir. Mar. 11, 2005)**

In *In re Allegheny Health Education & Research Foundation*, the defendant argued that it was not required to present evidence of "ordinary business terms" with respect to standard industry practice under § 547(c)(2)(C) because the length and consistency of its prepetition relationship with the debtor made such proof unnecessary under *Molded Acoustical*. The court

of appeals rejected this view of *Molded Acoustical* and held that even creditors with longstanding prepetition relationships must present *some* evidence that their prepetition dealings with the debtor fall within a range of ordinary business terms for the relevant industry. In affirming the order of the district court, the Court of Appeals noted that "while a creditor may, under the right circumstances, depart substantially from the relevant industry's norm for credit terms, it is possible for even longstanding credit terms to 'depart so grossly from what has been established as the pertinent industry's norms that they cannot be seriously considered usual and equitable with respect to other creditors.'" *Id.* at *8 (citing *Fiber Lite Corp. v. Molded Acoustical Products, Inc. (In re Molded Acoustical Products, Inc.)*, 18 F.3d 217 (3d Cir. 1994)).

***Gatti v. CEBCO (In re Deliland Foods Corporation)*,**
2005 U.S. Dist. LEXIS 5258 (D. Del. Mar. 31, 2005)

Industry standards under § 547(c)(2)(C) of the Bankruptcy Code also formed the central issues for the district court in *In re Deliland Foods Corporation*. In *Deliland Foods*, the debtor was unable to get supplies for its deli business as a result of numerous prepetition defaults. The defendant, a deli supply broker, agreed to supply the debtor, provided that the debtor paid the broker within seven days of delivery. For one such payment, the debtor's check delivered within the seven day period bounced. The debtor proceeded to wire funds to the broker within fourteen days after the goods were delivered (*i.e.*, seven days after the bank returned the debtor's original check). The bankruptcy court found that the debtor paid within the ordinary course of business. On appeal, the district court affirmed this decision and rejected the plan administrator's argument that the bounced check/wire transfer was *per se* outside the range of ordinary business terms. Rather, the district court noted that the parties entered into their arrangement at a time when the debtor's financial distress was an established fact. The court noted that, under these circumstances, "[a] bounced check, followed by a wire transfer shortly thereafter, cannot be considered so idiosyncratic as to fall outside the broad range in which similar firms engage." *Id.* at *6 (citing *United States Trustee v. First Jersey Securities (In re First Jersey Securities)*, 180 F.3d 504, 513 (3d Cir. 1999)).

***Morris v. Sampson Travel Agency, Inc.* *(In re US Interactive, Inc.)*, 321 B.R. 388 (Bankr. D. Del. 2005)**

The court in *In re US Interactive, Inc.*, found unpersuasive the industry standard evidence presented by defendant. In *US Interactive*, the defendant provided employee travel booking and meeting setup services to the debtor over an 18-month period prior to the petition date. Prior to the preference period, the defendant paid all invoices promptly and in full. From the outset of the preference period, the debtor began making partial payments ranging from between 27 to 90 days late.

The defendant's primary defense was that the payments were made in the ordinary course of business and that the course of conduct fell within the broad range of conduct for ordinary course transactions contemplated by the Seventh Circuit in *Tolona Pizza.* Citing the applicable Third Circuit variation of *Tolona Pizza* as set forth in the *Molded Acoustical* case, the plaintiff argued and the court accepted that the relatively brief (18 month) duration of the parties' business relationship required a greater emphasis on objective industry norms. On this factor the bankruptcy court found the defendant lacking – noting in particular that the defendant's expert failed to provide any statistics or other objective industry data to prove compliance with the industry norm. *Id.* at 394.

B. CREDITORS; COMMITTEE DUTIES

***In re Kensington Int'l, Ltd.*, 368 F.3d 289 (3d Cir. 2004)**

In a quintet of asbestos-related bankruptcies, creditors of two of the debtors filed petitions pursuant to 28 U.S.C. § 455(a), which sought the recusal of the judge presiding over the consolidated cases. The creditors posited that in appointing five non-judicial advisors consisting of lawyers, retired state court judges and professors with prior experience in asbestos litigation, the presiding judge had "created a perception in the mind of the reasonable person that his impartiality could be questioned," thus mandating his disqualification. *Id.* at 296. The United States Court of Appeals for the Third Circuit remanded the proceedings while retaining jurisdiction, and on remand, the presiding judge denied the recusal motions both on the merits and on timeliness grounds.

Though § 455 does not contain an express requirement of timeliness, the presiding judge found that case law suggests that parties seeking disqualification under § 455(a) should do so in a timely manner. Determining that the petitioners either knew or should have known long ago about two particular advisors' participation in one of the bankruptcies, but waited until much later to act on that information, the presiding judge found the motions seeking recusal were untimely. In his written opinion, the presiding judge found that the parties seeking recusal had either constructive or imputed knowledge prior to the date they claimed they learned of the advisors' participation in the bankruptcy.

Upon review of the presiding judge's disposition of the petitions, the Third Circuit rejected the judge's argument that the petitioning parties had constructive knowledge of the advisors' participation in the bankruptcy, as it found that the judge never communicated such participation to the parties. The presiding judge argued that knowledge could be imputed to one of the petitioners through the law firm serving as lead counsel for the unsecured creditors' committee in one of the five bankruptcies. A member of the firm serving as lead counsel had testified to receiving an e-mail disclosing one of the advisors' appointment in another of the five bankruptcies. The presiding judge asserted that this constituted notice to the petitioners in the first bankruptcy because the unsecured creditors' committee and the law firm representing it owed a fiduciary duty directly to the petitioners to disclose such information.

The Third Circuit found that while the unsecured creditors' committee in the first bankruptcy represented the petitioners' interests in the second bankruptcy, "it is established that a creditors' committee owes a fiduciary duty to the unsecured creditors as a whole, not to the individual members." *Id.* at 315 (citations omitted). "So while the Committee had a duty to represent the collective interests of the unsecured creditors, it did not have the authority to bind each individual creditor. This stands in stark contrast to the attorney-client privilege . . . . ." *Id.* The Third Circuit opined that actual knowledge is required to question a judge's impartiality under § 455(a). It concluded that because the petitioners did not have actual knowledge of the conflict with the advisors, their petition were not untimely when made.

***Westmoreland Human Opportunities, Inc. v. Walsh*, 246 F.3d 233 (3d Cir. 2001)**

In *Westmoreland*, a non-profit organization became the recipient of grant monies under the federal Supportive Housing Program and had executed a Supportive Housing Grant Agreement with the Department of Housing and Urban Development ("HUD") as a part of this arrangement. Several months after entering into this relationship, the organization filed a chapter 11 petition. The defendant, another non-profit organization, was one of the debtor's largest creditors and a member of the unsecured creditors' committee. While on the committee, the defendant, without notifying either the committee or the bankruptcy court, assumed the debtor's position as recipient of these federal grant monies, executing a Supportive Housing Grant Agreement Amendment with HUD.

The trustee sued the creditor, alleging that it had breached its fiduciary duty to the committee constituents by assuming the debtor's interest in the grant relationship as it did. The creditor defendant responded that the debtor's interest in the grant relationship was not property of the bankruptcy estate and thus no fiduciary duty on the part of the defendant had been triggered. The bankruptcy court disagreed, holding the interest in the grant relationship to be part of the bankruptcy estate, and finding that the defendant had violated its fiduciary duties. The district court affirmed this ruling.

On appeal by the creditor, the United States Court of Appeals for the Third Circuit disagreed with the lower courts' determination that the debtor's interest in the grant relationship was property of the estate. However, the court found that neither the district court nor the bankruptcy court addressed the issue of whether, despite the fact that the debtor's interest in the grant relationship was not property of the bankruptcy estate, the defendant's assumption of the debtor's interest in that relationship, without notice to committee members or the bankruptcy court, violated the fiduciary duty it owed to the committee constituents. Accordingly, the Third Circuit remanded the case for a determination of that issue. On remand, the bankruptcy court concluded that a fiduciary duty does exist between a committee member and an unsecured creditors' committee in relation to that committee member's actions regarding a transaction involving debtor's property not considered part of the bankruptcy estate. *See Walsh v. Westmoreland Human Opportunities, Inc. (In re Life Service Systems, Inc.)*, 279 B.R. 504

(Bankr.W.D. Pa. 2002), *aff'd in part and rev'd on other grounds, remanded*, *Westmoreland Human Opportunities, Inc. v. Walsh,* 327 B.R. 561 (W.D. Pa. 2005).

***Pension Benefit Guar. Corp. v. Pincus, Verlin, Hahn, Reich & Goldstein P.C.*, 42 B.R. 960 (E.D. Pa. 1984)**

In *Pension Benefit*, a creditor that was excluded from receiving a distribution pursuant to the debtor's plan of reorganization brought a malpractice action against the law firm that served as counsel to the creditors' committee of the plaintiff's class of creditors. The defendant sought summary judgment on the grounds that no attorney-client relationship existed between it and the creditor plaintiff. The defendant argued that it was counsel to the creditors' committee and not to the plaintiff individually, as counsel to a creditors' committee often finds itself taking positions adverse to individual members of the class. The defendant also cited 11 U.S.C. § 1103(b), which provides that counsel to a creditors' committee may not represent any other entity in connection with the case, so long as it is employed by the committee. The defendant expressed concern that imposing a fiduciary relationship between creditors' committee counsel and individual creditors would open counsel to attack by creditors dissatisfied with their distribution under a plan.

The court disagreed, noting that a creditors' committee owes a fiduciary duty to the creditors and must safeguard as much as possible the rights of all creditors. While the court found no specific obligations enumerated in the Bankruptcy Code or case law, it did reiterate "that a broad sense of equity and fiduciary duty pervades the entire bankruptcy administration and that counsel to a creditors' committee undertakes the obligation to represent the interests of the entire class fairly." *Id.* at 963 (citations omitted). The court saw no undue harm in finding the existence of an attorney-client relationship between creditor committee counsel and the individual creditor, and imposed an obligation to utilize "care, skill, prudence, and diligence" in the performance of their obligations. *Id.* at 964. Thus, while the court did not find an obligation on the part of the committee counsel to maximize the interest of any individual creditor, it did find an obligation to exercise due care in administering the distribution of the assets. Accordingly, the court denied the defendant's motion for summary judgment, as well as the plaintiff's cross-motion.

C. NOTICE

In re: GST Telecom, Inc.
2002 WL 1737445 (D. Del. 2002)

In *GST Telecom*, the State Board of Equalization of California (the "Board") alleged that it did not receive adequate notice of the bar date for all tax claims by governmental entities. The bar date was March 31, 2001. Prior to the bar date, the debtor sent notice to the address listed for the Board on the debtors' service list, which was: "State of California, Board of Equalization, P.O. Box 942879, Sacramento, CA 94279." The correct mailing address designated by the Board was: "State of California, Board of Equalization, MIC 29, P.O. Box 942879, Sacramento, CA 94279-0001."

On February 15, 2002, the Board filed a postpetition administrative expense request for the payment of tax due on postpetition sales. The debtor asserted that the claim was untimely because it was made nearly one year after the bar date. The Board argued that the court should excuse the untimely filing because the Board failed to receive proper notice of the bar date.

The court held that the Board did not receive proper notice. The court reasoned that even though the debtor sent the notice of the bar date to the address on the schedule of liabilities, that address was supplied by the debtor. The debtor had an obligation to ensure that they sent the notice to the correct address because the Board did not supply the address. If the Board had supplied the address to which the notice was sent, the court stated that it would have ruled that notice was sufficient. In dicta, the court also noted that the address of the Board was easy to find because it was available on the internet. The court further stated that small differences in an address can render notice insufficient, particularly when the notice is sent to a large organization. As a final matter, the court noted that actual notice can cure defective notice, but because there were unresolved factual issues regarding actual notice, the court did not rule on whether the notice was so cured.

Pioneer Investment Services Co. v. Brunswick Associates Limited Partnership
507 U.S. 380 (1993)

The leading case on the excusable neglect standard of Rule 9006 is *Pioneer*, which addressed a split in the courts of appeals on the proper interpretation of the term "excusable neglect." Some circuits had followed a strict standard, requiring that the cause of the delay was due to circumstances beyond the control of the party filing the motion. Other courts had adopted a more liberal interpretation of excusable neglect, relying on a test that involved balancing the equities. *Pioneer* was a chapter 11 case in which an attorney representing several unsecured creditors filed proofs of claim on behalf of his clients 20 days after the bar date. The Supreme Court held that the excusable neglect standard of Rule 9006(b)(1) is not limited to situations in which the delay is caused by circumstances beyond the control of the party filing the proof of claim. In reaching this conclusion, the Court reasoned that "Congress plainly contemplated that the courts would be permitted, where appropriate, to accept late filings caused by inadvertence, mistake, or carelessness, as well as by intervening circumstances beyond the party's control." *Id.* at 395. The Court went on to hold that:

> Because Congress has provided no other guideposts for determining what sorts of neglect will be considered 'excusable,' we conclude that the determination is at bottom an equitable one, taking account of all relevant circumstances surrounding the party's omission. These include . . . the danger of prejudice to the debtor, the length of the delay and its potential impact on judicial proceedings, the reason for the delay, including whether it was within the reasonable control of the movant, and whether the movant acted in good faith.

Id.

In re Spring Ford Industries
2003 WL 21494002 (Bankr. E.D.Pa 2003)

The four-factor test the court enunciated in *Pioneer* provides a standard that depends on the equities of each case. Subsequent cases have tried to reconcile *Pioneer's* holding with the continued need to avoid prolonged administration of title 11 cases. In *Spring Ford*, the Bankruptcy Court evaluated a creditor's late filing of two proofs of claims in a chapter 11 case. The debtor corporation filed its petition for relief on April 2, 2002, and the bar date for filing

proofs of claim was July 2, 2002. The creditor, Paxar Corporation ("Paxar"), admitted that the debtor sent timely notice of the bar date (the "Notice") to its plant in Sayre, Pennsylvania (the "Sayre Facility"). Paxar's Sayre Facility handled customer service, sales and correspondence. The preparation of proofs of claim was historically handled by the White Plains, New York office (the "White Plains Facility"). Consistent with that practice, the Notice was forwarded from the Sayre Facility to the White Plains Facility.

During this period Paxar was relocating certain corporate and accounting offices from the White Plains facility to Miamisburg, Ohio (the "Miamisburg Facility"). At some point at the end of July or beginning of August, the Notice was forwarded to the Miamisburg Facility, which had been delegated the proof of claim function. Prior to the Notice being sent to the Miamisburg Facility, Paxar had prepared a proof of claim dated July 1, 2002 ("Claim One"). Claim One was received by the court on August 6, 2002. Paxar claimed that the relocation of the proof of claim preparation function to the Miamisburg Facility was responsible for its failure to timely file Claim One since the Notice was internally misdirected to the White Plains Facility. Paxar contended that this operational problem constituted "excusable neglect" so as to allow a late filing.

In evaluating Paxar's claim, the court first noted that the burden of proof rests with the petitioner claiming excusable neglect. The court also noted that the Third Circuit had elucidated several examples that would suffice to warrant a late filing of a proof of claim in *In re Cendant Corporation Prides Litigation*. Those examples included "the failure of claimants to receive notice, illness, misrouted mail, intervening company name changes, or short internal mail systems delays." *Id.* at *3, citing *In re Cendant Corporation Prides Litigation*, 233 F.3d 188, 197 (3d Cir. 2000). According to the Court in *Spring Ford*, the threshold question in finding excusable neglect is whether or not the reason for the missed bar deadline is neglect. Given that Paxar was aware of the transfer of the business and accounting functions, the court held that the failure to file Claim One at the time it was prepared reflected poor judgment and carelessness that qualified as neglect. Thus, the court proceeded to analyze whether the neglect was excusable under the *Pioneer* standard.

While most of the delay in filing Claim One was attributable to misrouted mail and a corporate reorganization, some part of it was attributable to the internal failure to transmit the Notice directly to the correct office. Thus, the Bankruptcy Court noted that Claim One presented a close question, because while *Cendant* appears to recognize misrouted mail as justifying a late filing, *Pioneer* cautions that office upheaval does not constitute excusable neglect. Nonetheless, the court found that there was no prejudice to the debtor, and that the brevity of the delay also mitigated against a harsh result. Therefore, the Bankruptcy Court found excusable neglect as to Claim One.