



PREFERENCE ACTIONS

PRESENTATION FOR:

**MEDIA FINANCIAL MANAGEMENT
NEWSPAPER COMMITTEE**

**BY:
C. ROBIN SZABO
PRESIDENT
SZABO ASSOCIATES, INC.**

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I. What is a preference action?

- a. It is an action brought by the debtor or trustee to recover dollars that a creditor received prior to the bankruptcy filing.
- b. The preference time frame that the debtor or trustee can assert a claim is two years after the order of relief (filing of the bankruptcy), or one year after a trustee has been appointed, if such appointment occurs before the expiration of the two year period.

II. Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) of 2005 and preference actions:

- a. The new Act changed the venue statute for preference actions. Generally, preference actions of less than \$10,950.00 for bankruptcy cases filed on or before March 31, 2010, or \$11,725.00 for bankruptcy cases filed on or after April 1, 2010,* may now take place only in the district court for the district where the trade creditor resides. This modification helps protect trade creditors from settlement pressure in cases where the cost of defending the payment might exceed the amount of the debt.

* Adjusted every 3 years; next adjustment April 1, 2013

- b. The Act also established a minimum amount subject to avoidance of less than \$5,475.00 for bankruptcy cases filed on or before March 31, 2010, or \$5,850.00 for bankruptcy cases filed on or after April 1, 2010,* (an aggregate amount of transfers during the 90-day reach-back period). The effect of these two modifications is that amounts between \$5,475.00 and \$11,725.00** must be litigated where the trade creditor is located, and amounts less than \$5,475.00 or \$5,850.00** are precluded from being litigated as preferential transfers at all!

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** Depending on the date of the bankruptcy case filing

III. The essential elements:

- a. The initial burden of establishing that a payment is a preference belongs to the trustee. By law, Section 547(b) of the Bankruptcy Code, the trustee cannot establish a preference unless all of the following five elements are met:
 - The payment was made to or for the benefit of the creditor.
 - The payment was made on or within 90 days before the date of the Bankruptcy Petition (or between 90 days and one year before the filing of the petition if the creditor at the time of the transfer was an "insider").
 - The payment was for or on an account for an antecedent debt owed by the customer before the payment was made.
 - The payment was made while the customer was insolvent.
 - Finally, the payment must have enabled the creditor to receive more than it would receive under a Chapter 7 liquidation of the customer's bankruptcy estate.

IV. The preference defenses:

- a. Solvency
- b. Subsequent new value
- c. Contemporaneous exchange for new value
- d. Ordinary course of business

V. What to do:

- a. If you receive a demand for less than \$5,475.00 for cases filed on or before March 31, 2010, or \$5,850.00 for cases filed on or after April, 1, 2010, ignore it.
- b. Determine if your payment meets the five elements for establishing a preference claim.
- c. Do you have any information which would prove that the debtor was solvent at the time the payments were made?
- d. Examine the debtor's payment records.
- e. Determine if the subsequent new value or the contemporaneous exchange for new value defense can be used.
- f. If none of the other defenses can be used, use the ordinary course of business defense.
 - Objective Test – in accordance with industry norms
Or
 - Subjective Test – the specific relationship between the creditor and the debtor
- g. If you are sued, attempt to get a written extension of your answer period, determine if you have preference exposure, then decide whether you or your attorney are going to negotiate a settlement, but in no event allow your answer period to pass.

VI. Preventative steps:

- a. Re-evaluate your customers' creditworthiness annually to alert you to potential problems.
- b. Be aggressive with collections, keeping the payments from your customers as close to terms as possible.
- c. If there is a change in terms with the customer, document it so you can evidence a change in terms.
- d. When a customer files bankruptcy, do a quick review of your potential exposure and if it is greater than \$5,850.00, compile the payment history and credit terms with that customer going back a minimum of 2 years, and secure that data for future use.