Blakeley & Blakeley LLP

THE TRADE VENDOR QUARTERLY

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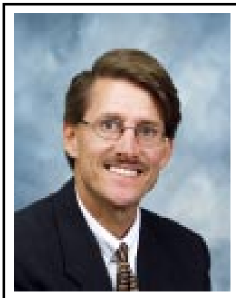
Developments in Commercial, Creditors' Rights, E-Commerce and Bankruptcy Law of Interest to the Credit and Financial Professional

THE MILLENNIUM BUG: ARE YOU SELLING TO A COMPANY ON CREDIT THAT IS VULNERABLE TO Y2K WOES?

Scott Blakeley



A number of consultants and economists, modern day Paul Reveres, warn of the Year 2000 - or Y2K for short - problems. These pundits forecast power failures, stock market chaos and widespread data loss, a virtual temporary breakdown of computerized societies. Is the doomsday talk generated by Y2K real? Is the Y2K problem leading to a worldwide recession, if not addressed? Whether the consequences are as drastic as some predict, or something less, companies are spending huge sums to cure their Y2K problems. In such an environment, what are the real credit risks, both direct and indirect, for a credit executive in assessing an existing customer's credit line, and new open account sales? Will there be widespread defaults by customers on open account sales as a result of Y2K? What steps should a credit executive take with its credit sales in the face of Y2K?

What Is Y2K?

Y2K problems are found in both hardware and software, but are not restricted to computers. Equipment such as phone and voice mail systems, copiers security systems and even cash registers are affected by the date change.

The Y2K problem is a result of early computer programs, written when coding space was a premium, that provide two digits instead of four to designate years. The problem is that many computers and software programs recognize years by only their last two digits -- and, with the shift of centuries, they may identify "00" as 1900 or not recognize it at all. The resulting miscalculations and malfunctions could disrupt virtually all industries.

What Will It Cost?

The costs to correct the Y2K problem is estimated by some at $600 billion or more worldwide, for both private industry and governments. The U.S. government expects to spend $5.4 billion to ensure all of its computers work properly. Underscoring the magnitude on private industry, General Motors, for example, expects to spend $500 million in assessing and fixing the problem. AT&T will spend $350 million in 1998 alone. Aetna Insurance will spend over $195 million over the next two years.

Worldwide Problems

Experts expect that the worst problems to originate overseas, where Y2K awareness is low. Poorer and less sophisticated countries are likely to be hardest hit, and third world customers may be unreliable.

Industry Wide Problems

Y2K may affect virtually all industries, and all segments along the production chain, from manufacturing to distribution to retail. For example, the computer-intensive financial services industry is seen as vulnerable to Y2K, but regulators say banks generally are getting their houses in order. The SEC has cited a number of brokerages firms for failing to timely file reports regarding Y2K compliance. Likewise, telecommunications and transportation are seen as being strongly affected by Y2K.

Litigation

Y2K may be the next litigation bonanza and become a trillion-dollar industry for class action lawyers. A score of lawsuits have already been filed against manufacturers of hardware and software, retailers and consulting firms over alleged losses resulting from Y2K problems. Legal fees could be in the hundreds of millions of dollars. On the horizon are potential suits involving fraud, breach of contract, warranty, liability, personal injury, and a variety of shareholder actions against company directors for failing to prepare for Y2K.

The prospect of widespread litigation has prompted legislative efforts at both the

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THE FAIR CREDIT REPORTING ACT: WHEN MAY IT APPLY TO TRADE CREDITORS AND WHAT STEPS SHOULD TRADE CREDITORS TAKE TO COMPLY?

Scott Blakeley

Thomas Johnson

You learn that your new open account corporate customer has gone out of business. Newspapers report that your corporate customer had orchestrated a bust-out and the president of the company has fled. Most frustrating, you learn too late that the president who orchestrated the bust-out has a personal history of defrauding creditors; and that the president's personal credit history reveals several judgments and a personal bankruptcy. Could you have headed off this problem earlier by obtaining a personal, or consumer, credit report on the president in connection with credit application?

In analyzing whether to extend trade credit to a closely held corporation, a credit executive may wish to review the president's or shareholder's personal credit history. Often the payment history of such a corporation is a reflection of the payment history of the officer or shareholder. Likewise, to reduce risk of non-payment, a credit executive may seek a personal guaranty from a corporation's shareholder or officer, or limited liability corporation's member, before extending commercial credit. In connection with this guaranty, a credit executive may wish to review the guarantor's personal credit history.

Would obtaining such individual credit reports run afoul of federal laws? The Fair Credit Reporting Act ("FCRA") affects how a credit executive may gather information to make these credit decisions. FCRA regulates the use of individual credit reports and credit information. Generally, the collection of business, trade, and commercial credit reports are not covered by FCRA. But does FCRA require a credit executive extending trade credit to a sole-proprietorship, partnership or closely-held corporation to obtain written authorization to obtain an individual's personal credit history, such as the credit history of a corporation's president or shareholder? Does FCRA require written authorization to pull a consumer credit report for an individual guarantying a corporate credit obligation? Before answering these questions, some background of FCRA is considered.

1. FCRA's General Purpose

The FCRA statute concerns only the use of personal consumer credit reports used to evaluate credit in a business transaction. FCRA insures that credit reporting agencies, and the users of such reports, will respect a consumer's right to privacy by authorizing pulling credit reports only in certain approved circumstances.

FCRA's general purpose is:

> "to require that consumer reporting agencies adopt reasonable procedures for meeting the needs of commerce for

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FROM THE PUBLISHER:

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If you have a hot topic affecting the credit and financial professional, e-mail this to Scott.

FILING A PROOF OF CLAIM IS SIMPLE, ISN'T IT?

Bradley Blakeley

More than one credit executive, or even attorney for a vendor for that matter, has mistakenly relied on the familiar "mailbox rule" when filing a proof of claim. It may not be enough to drop your proof of claim in the mailbox and have it post marked on or before the bar date deadline. To insure your proof of claim is timely filed, your proof of claim must be file stamped by the clerk of the bankruptcy court on or before the bar date.

As the court discussed recently in *In re 50-Off Stores, Inc.*, 220 B.R. 897 (Bankrtcy.W.D.Tex. 1998), there is a split of authority among Federal Circuit Courts as to whether the "mailbox rule" applies in the context of filing a proof of claim. The court concluded that "the 'mailbox rule' does not apply to the filing of claims, and that no presumption should be granted to the [claimants] with respect to their contention that they mailed their claims to the bankruptcy court in a timely fashion."

The bar date for you to file a proof of claim is dependent upon whether the case is a Chapter 7 or 11. Generally, in a Chapter 7 case a proof of claim must be filed within 90 days after the first date set for the meting of creditors pursuant to F.R.C.P. 3002(c). If a Chapter 11 case, the bankruptcy court will fix a date within which proofs of claim must be filed pursuant to F.R.C.P. 3003(3).

If you fail to meet the deadline to file your proof of claim, the validity of your claim will depend on whether the case is in Chapter 7 and 11. Late claims are not, generally, permitted in Chapter 7 cases because Bankruptcy Rule 9006(b)(2) expressly excludes application of the "excusable neglect" standard to the deadlines set by Bankruptcy Rule 3002(c). Bankruptcy Rule 3003 which governs the filing of claims in Chapter 11 cases, by contrast, is not excluded by rule 9006(b)(2), so that creditors in Chapter 11 cases may be able to file claims after a court-set bar date, provided they can demonstrate the requisite "excus-

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MAKING YOUR RECLAMATION DEMAND

Scott Blakeley

News of a customer's insolvency can be devastating to a vendor selling on open account. However, the right of reclamation may afford a vendor a cost-effective method of recovery for goods recently shipped.

Reclamation is the right of a seller to recover possession of goods delivered to an insolvent buyer. The remedy of reclamation is needed when an unsecured vendor is unable to retrieve goods or stop them in transit. A reclaiming vendor need not prove fraud, although the premise of reclamation is that the vendor was defrauded. Under the common law and the old Uniform Sales Act, the seller could only exercise its reclamation rights if it proved the buyer obtained delivery by misrepresenting its solvency. However, the Uniform Commercial Code (UCC) has expanded this remedy where the buyer does not misrepresent solvency.

Elements of a Reclamation Claim

Courts have settled upon the following elements to establish a valid reclamation claim under the Bankruptcy Code:

(1) the seller sold goods on credit to the debtor in the ordinary course of business of both;
(2) the seller delivered the goods to the debtor at a time when the debtor was insolvent;
(3) the seller made a written demand for the return of the goods within ten, or in certain cases twenty, days after the goods were delivered to the debtor; and
(4) the debtor had possession of the goods at the time of the reclamation demand or the goods were not inthe hands of a buyer in the ordinary course or a good faith purchaser at the time of demand.

Steps For a Successful Reclamation

Reclamation Letter

A vendor initiates reclamation by delivering a reclamation letter (*see letter attached*) within ten days, or in certain cases twenty days, after the goods were delivered. The reclamation letter should include a detailed description of the merchandise in question, a statement of the delivery date to the debtor, and a demand for the immediate return of the goods. The reclamation letter should also demand an accounting. An accounting is crucial, because the right to reclaim may be defeated by the debtor's resale of the goods to a buyer in the ordinary course of business.

If the accounting is not delivered or not accurate, the vendor should be prepared to immediately demand a right to inspect both the inventory on hand the books and records pertaining to sales of said goods for the period between the date of delivery of the goods and the date of the reclamation letter. The letter should be delivered to the debtor by facsimile and certified mail.

Initiating Proceedings

If the buyer files a bankruptcy proceeding prior to the preparation of the reclamation letter (or at any time thereafter) the seller should promptly contact debtor's counsel in order to stipulate with debtor either to the immediate return of the goods or for the debtor to sell the goods, provided the seller is granted an administrative claim or a lien under the Bankruptcy Code. Courts are divided as to whether a reclaiming vendor may simply rely on a proper and timely notice, or must initiate an adversary proceeding, to enforce its rights. The risk the vendor faces if it fails to seek court enforcement of its reclamation right is that it cannot meet its burden of proving that the goods subject to the reclamation demand were in the possession of the debtor at the time such demand was made.

If there are no bankruptcy proceedings, the seller must initiate legal action in state court pursuant to the UCC. The seller should bring a complaint for replevin and a writ of attachment against the proceeds of any sale of goods protected by the reclamation demand.

Special Problems For Vendors

Insolvency At The Time Of Delivery Of The Goods

A vendor has the burden to establish that the debtor was insolvent at the time the debtor received the goods. The UCC's definition of insolvency is expansive. The UCC defines insolvency as an entity "who either has ceased to pay his debts in the ordinary course of business or cannot pay his debts as they become due or is insolvent within the meaning the federal bankruptcy law." The Bankruptcy Code, on the other hand, adopts only a balance sheet test to determine solvency. An entity is insolvent if "the sum of such entity's debts is greater than all of such entity's property, at a fair valuation." Unfortunately for vendors, most courts have determined the Bankruptcy Code to require the customer to be insolvent within the more restrictive definition set forth in the Bankruptcy Code.

Possession Of Goods

Courts strictly enforce the requirement that the goods be in the possession of the debtor when reclamation is demanded. If the debtor has transferred the goods to a good faith purchaser before the reclamation demand is made, the reclaiming vendor loses all reclamation rights to the goods.

Reclamation Where There Is A Secured Creditor

Courts have taken conflicting views as to whether an existing inventory lender primes a reclaiming vendor's claim. One view is that the existence of a senior lien on goods merely subordinates the reclaiming vendor's rights to those of the lienholder, i.e., it does not extinguish the vendor's right of reclamation. Those courts allowing administrative claims to reclaiming vendors notwithstanding the value of the lienholder's collateral have done so on the grounds of "fairness."

On the other hand, some courts have determined that a secured creditors rights will extinguish all of the reclaiming vendor's rights. Therefore, only those goods that were sold to the debtor prior to the filing were subject to any security interest.

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WHEN 100 CENTS ON THE DOLLAR IS NOT ENOUGH: PRESENT VALUE ANALYSIS AND CHAPTER 11

Scott Blakeley

The primary purpose of a Chapter 11 case is the negotiation between a debtor and its unsecured creditors of a plan of reorganization which restructures the debtor's finances and provides the basis for repaying creditors. However, Chapter 11 plans are notorious for repaying unsecured creditors something significantly less than the face amount of their claims.

The Ninth Circuit Court of Appeals, in *In re Perez*, recently faced the issue of whether a plan that proposed to pay unsecured creditors 100 cents on the dollar over 5 1/2 years, without interest, was confirmable. The *Perez* court applied a basic principle of modern finance, present value analysis, to Chapter 11 and held that as the plan did not compensate certain unsecured creditors for the lost time value of their money, it did not pay their claims in full. The debtor, who held a junior interest, proposed to retain property which rendered the plan unconfirmable (if junior creditors or shareholders make a substantial "new value" contribution, yet senior creditors are not paid in full, such a plan may be confirmable - but this issue is beyond the scope of this article.) Before considering the *Perez* ruling, an overview of the plan process in Chapter 11 as it affects unsecured creditors is considered.

The Disclosure Statement

A debtor has the exclusive right to file a plan of reorganization during the first 120 days after the bankruptcy filing (although this may be terminated by parties in interest upon a showing of "cause"), and upon the filing of a plan, this "exclusivity period" is extended for an additional 60 days for voting purposes. Prior to any vote on a plan, a debtor proposing a plan must first obtain bankruptcy court approval of a disclosure statement. The purpose of the disclosure statement is to provide impaired creditors with adequate information as to their treatment under a plan so they may make an informed decision when they cast their votes.

The Plan of Reorganization

A plan of reorganization is the vehicle by which a debtor discharges its prepetition obligations and provides the method for repayment of its obligations. Generally, the hallmark of the plan process is flexibility, and creditors can agree to any treatment of their claims. A plan segregates creditors' claims into classes and describes how such creditor classes are to be treated. The plan must state whether the creditor class is impaired or unimpaired. A creditor class is impaired if the plan alters its legal rights (e.g., creditors within the class will not be paid according to the terms of their respective agreements with the debtor).

Voting to accept or reject a plan is limited only to those creditors impaired under the plan. An impaired creditor class is deemed to have accepted the plan if the plan is approved by at least two-thirds in dollar amount <u>and</u> one-half in number of voting creditors in that class. Those creditors in an accepting creditor class that reject the plan are protected by what is called the "best interests of creditors test" which requires that rejecting creditors receive as much under the Chapter 11 plan as they would in a Chapter 7 liquidation.

A plan may be confirmed by one of two methods. The most common method is by consent, e.g., all impaired creditor classes vote to accept the plan. Another method is by "cramdown," wherein at least one impaired creditor class votes to accept the plan, the plan does not discriminate unfairly and is fair and equitable as to each impaired creditor class that rejects the plan. In other words, the cramdown provides for confirmation of a plan notwithstanding its rejection by one or more impaired creditor classes.

"Cramdown" and Unsecured Creditors

A cramdown plan meets the fair and equitable test in one of two situations.

First, a cramdown plan is fair and equitable if an unsecured creditor class receives property with a present value equal to the full amount of its claims as of the effective date of the plan. Present value analysis is employed where a plan dictates payment on claims over time. The rationale supporting present value analysis is that a dollar received today is more valuable than a dollar received six months from today as a dollar received today can be invested and earn interest. Where a plan provides for a creditor class to be paid over time, the claims are discounted to present value to determine whether the deferred payments actually result in full payments to the creditor class. The discount rate is determined by courts who use the interest rate a debtor would pay as a borrower of a like amount on like terms in the commercial loan market as a benchmark.

Second, a cramdown plan is fair and equitable if no junior creditor class or shareholder class retains or receives anything where a senior creditor class rejects the plan and is not being paid in full, the so-called "absolute priority rule".

The **Perez** *Case Facts*

A creditor (the "Creditor") obtained an unsecured judgment against Perez (the "Debtor"), who responded by filing a personal Chapter 11 bankruptcy. The Debtor's plan classified the Creditor's claim with other unsecured creditors. Because the Creditor's claim was so large, he controlled the vote of his class. The Creditor voted to reject the plan, which caused the class to reject the plan.

The Creditor objected to his treatment under the plan. While the plan stated that it offered 100 cents on the dollar for his claim, the Creditor complained that because the plan provided for deferred payments on his claim (payment over 67 months without interest), it did not actually result in full payment. The Ninth Circuit discounted the payment stream the Creditor was to receive in the future to present value and found the Creditor was not compensated for the lost time value of his money. Since under the

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WHEN 100 CENTS ON THE DOLLAR IS NOT ENOUGH: PRESENT VALUE ANALYSIS AND CHAPTER 11 (Continued)

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proposed plan the Creditor was not actually offered 100 cents on the dollar, yet provided that the Debtor would retain certain property, the Ninth Circuit found the absolute priority rule was violated. As a result, confirmation of the plan was denied.

Conclusion

The plan of reorganization process in Chapter 11 has built-in protections for an unsecured creditor class that rejects a plan. The Ninth Circuit opinion states that a cramdown plan is not confirmable unless the objecting unsecured creditor class is paid in full as of the effective date of the plan, in present value dollars, in a case where junior creditors or shareholders receive or retain anything. In other words, objecting unsecured creditor classes whose claims are to be paid over time are entitled to market-rate interest in such situations.

MAKING YOUR RECLAMATION DEMAND (Continued)

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A Lien Versus A Claim In The Bankruptcy Case

The vendor should insist upon a lien on the assets of the bankruptcy estate, rather than an administrative claim. An administrative claim will not get satisfied if the bankruptcy case is administratively insolvent. A vendor's lien under the Bankruptcy Code is measured by the price realized by the debtor for the goods sold. As such, an agreement as to the amount of the lien or claim is advisable, so as to avoid recovering less than the resale price of the goods.

[date]

VIA FACSIMILE AND OVERNIGHT MAIL

[Debtor]

Re: [***Debtor's Case Name***]

Dear [***Debtor's Officer***]:

This letter constitutes a notice of demand for the return of certain goods purchased by the above-captioned debtor ("Debtor") from [***Creditor***] (the "Seller"). Please take notice that pursuant to [***State***] Commercial Code 2702, 11 U.S.C. section 546(c), and by virtue of the Debtor's insolvency, the Seller hereby demands the return of all the [***description of goods***] (the "Goods") currently in your possession and delivered to you on or after [***Delivery Date***] pursuant to the invoices, dated [***Invoice Date and Invoices Numbers***]. Unless you authorize the return of the Goods immediately, further appropriate measures will be taken.

Please contact the undersigned immediately to make arrangements to allow the Seller to reclaim the Goods. I look forward to hearing from you shortly.

Sincerely,

[***Credit Manager***]

EXHIBIT "A"

THE MILLENNIUM BUG: ARE YOU SELLING TO A COMPANY ON CREDIT THAT IS VULNERABLE TO Y2K WOES? (Continued)

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state and federal level to limit the scope of liability suits against manufacturers and retailers. In October, 1998, President Clinton signed into legislation an act to encourage more complete disclosure and exchange of information about year-2000 computer problems and technical solutions.

More Bankruptcies

Y2K may be the cause of bankruptcy in a number of business failures. For many companies that are in financial straits and with scarce financial resources, updating their systems to be Y2K compliant is impossible. A number of manufacturers throughout the country are requiring their vendors to complete detailed questionnaires that demonstrate they are Y2K compliant. A fortress mentality may emerge shortly where companies that cannot demonstrate Y2K compliance will be excluded as a supplier, for example. These companies that do not have the cash flow to become Y2K compliance may find themselves with out their primary customers.

Steps To Protect Your Credit Sales In The Face Of Y2K

Y2K may impact your credit decisions both directly and indirectly. Over the next 18 months, Y2K may become the next excuse a credit executive hears for non-payment of an account.
How may you assess the Y2K risk? With potential customers, and a public company, review the most recent quarterly report (10Q) or annual report (10K) filed with the Securities and Exchange Commission. What disclosures are made regarding Y2K compliance. Has the potential customer identified problems and taking steps to cure them. Will the problems be cured, without interrupting its ability to pay your extension of credit? At this time, there is not a nationally approved certification to indicate that a company has complied with standards to become Y2K compliant. However, 10Q and 10K disclosures will provide a sense of direct credit risk. Included in your Y2K analysis for the potential customer is indirect credit risk. Analyze whether the potential customer is in an industry susceptible to Y2K problems. For example, is the potential customer a hardware or software manufacturer that may be the target of significant litigation. Is the potential customer a distributor in which a majority of revenues are from third world countries, which countries are especially susceptible to Y2K.

As to indirect credit risks, there may be a domestic credit crunch as a result of Y2K when banks balk at lending to companies that seem vulnerable to Y2K woes. Banks reportedly are toughening lending terms for customers that have excessive Y2K risk. Banks are writing a covenant into new loans, requiring borrowers to anticipate possible Y2K problems. Banks may use this covenant for calling a loan or terminating a loan. A credit executive should be aware of this risk with a potential customer, as the credit executive does not want to see its goods foreclosed on by the customer's lender because of the customer's Y2K woes.

With closely held companies, a credit executive should request in his or her credit application that the potential customer disclose Y2K compliance. Confirm that the potential customer has established a budget for Y2K and assigned people to the project. With potential customers, unless it is clear that the customer is Y2K compliant or has the wherewith to become compliant, and that indirect risks discussed are minimal, consider taking collateral, personal or corporate guarantees, letters of credit, to back up the immediate credit risk until the Y2K risk passes.

With your existing customers and credit lines, consider classifying your customers Y2K risk. Those classified with greater direct and indirect risk should be monitored closely in the coming months. Perhaps with some customers, consider taking collateral, personal or corporate guarantees, letters of credit, to back up the immediate credit risk until the Y2K risk passes.
Also, as more and more credit departments are paperless, consider maintaining a printout of your accounts to protect from your own Y2K problems. As a result of computer glitches, your receivable records may crash, or may contain serious errors with your customers' payment history. It should be noted that for the credit executive reporting customer delinquencies to public reporting agencies, in the event Y2K interferes with the credit executives own accounts receivables, the information which the credit executive reports may be in error. In the event that the customer has difficulty obtaining credit because the credit executive supplied inaccurate information, there may be consequences.

On the positive side, the best disasters are predictable, as the case may be with Y2K, and allow you the opportunity to prepare. Whether Y2K turns out to be mere media hype or results in widespread customer defaults in the coming months, the cliche planning for failure is better than failing to plan is appropriate for the credit executive in 1999.

THE FAIR CREDIT REPORTING ACT: WHEN MAY IT APPLY TO TRADE CREDITORS AND WHAT STEPS SHOULD TRADE CREDITORS TAKE TO COMPLY? (Continued)

(continued from page 2)

> consumer credit, personnel, insurance, and other information in a manner which is fair and equitable to the consumer, with regard to the confidentiality, accuracy, relevancy, and proper utilization of such information in accordance with the requirements of this [Act]."

See 15 U.S.C. § 1681b.

2. What is a Credit Report

A credit report may be any written or oral communication bearing on a consumer's credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living. The Report must be either used or expected to be used, or it must have been collected in whole or in part, for a "permissible purpose."

3. Written Authorization is Required Except For a Legitimate Business Purpose

FCRA as a general rule requires a trade credit grantor to obtain written authorization, i.e., permission, from an individual to run a consumer credit report. There is an exception to the statute, however, where authorization is not required. A consumer credit report may be obtained without authorization from the consumer if there is a legitimate "business purpose" in connection with a transaction initiated by the consumer.

A "business transaction" under FCRA refers to an exchange of goods or service for money. The general language of this subsection is extremely broad and seems to suggest that any "business need" would be sufficient to allow a credit executive to pull a consumer credit report without authorization from the individual, such as a corporation's president. On the other hand, the courts have limited the scope of the phrases "business need" and "business transaction," holding that "business transactions" include only those types of transactions described in other parts of the statute. Most courts have limited "business transactions" to those involving (a) <u>the extension of credit</u>, or (b) <u>the collection of debt</u>.

For example, in *Wrigley v. Dun & Bradstreet, Inc.*, subscribers of Dun & Bradstreet sought credit information regarding Wrigley Construction company in connection with Wrigley's application for the extension of trade credit. Dun & Bradstreet provided information about the company and also personal information regarding the criminal convictions and bankruptcy of the owner of Wrigley. Consent from the owner was never obtained. In a lawsuit by the owner against Dun & Bradstreet, the court held that FCRA does not extend coverage to a consumer's "business transactions." The Court ruled in favor of the credit reporting agency, finding no violation of FCRA and, thus, no liability.

Regarding debt collection efforts, one appellate court held it generally proper to obtain a consumer report in connection with debt-collection litigation. The Court reasoned that the "lawsuit involves the collection of a debt, [therefore] the attorney is likely to procure the consumer report for a purpose analogous to those enumerated in § 1681b." *Duncan v. Handmaker*, 149 F.3d 424 (6th Cir. 1998). As the goal or purpose of a lawsuit moves outside debt collection, it is less likely although not impossible that an attorney will obtain the report for a purpose that is within FCRA.

4. Notification if Credit Is Declined Based Upon the Credit Report

FCRA requires that a credit grantor provide notice to the *consumer* if the credit grantor is denying credit, or otherwise taking adverse action with respect to the credit application, based upon the information obtained in the credit report. Thus, a credit grantor will provide notice to the company of the denial of credit; the credit grantor must also provide notice to the president, shareholder or guarantor with respect to whom the credit report was obtained.

The notice can be oral, in writing, or electronic. The credit grantor is required to provide the name, address and telephone number of the consumer reporting agency. In addition, the credit grantor must state that the consumer reporting agency did not make the adverse credit decision and such agency is unable to provide the consumer with the specific reasons why the adverse credit decision was taken. Finally, the credit grantor must notify the consumer of the consumer's right to obtain a free copy of the consumer report and "an indication" of the 60 day period that the consumer has to obtain such free copy. Notice must also be provided of the consumer's right to dispute with the consumer reporting agency the accuracy or completeness of any information in the consumer report.

5. Penalties for Violating FCRA

In the consumer context, the private enforcement provisions of FCRA permit a consumer to bring civil suit for wilful noncompliance with the FCRA, with no ceiling on the amount of punitive damages. In the consumer context the consumer may sue for negligent noncompliance, for actual damages sustained. The consumer may also seek to recover the consumer's reasonable attorneys' fees, as determined by the court. The reported judicial decisions applying FCRA penalty provisions to business transactions are scant. However, there is no exception in the statute and, thus, no basis to believe that the penalty provisions of FCRA would not apply to business transactions. In addition, criminal penalties may also be assessed including fines and imprisonment against any person who knowingly and willfully obtains a consumer report under false pretenses.

6. Trade Creditors Should Comply With FCRA As a Precautionary Measure

Don't be the test-lawsuit. As noted, FCRA as a general rule requires a trade credit grantor to obtain written authorization from an individual to run a consumer credit report. However, where an individual intends to guarantee the credit of a company, FCRA appears to provide an exception which allows the trade credit grantor to run a consumer credit report on the guarantor without authorization if there

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FILING A PROOF OF CLAIM IS SIMPLE, ISN'T IT? (Continued)

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able neglect."

After determining the bar date, the next step to filing your claim is to obtain the proper proof of claim form. The form (Form #B-10) may be obtained by contacting the intake section in the appropriate divisional office. The court will mail you a proof of claim within 24 hours of your request at no cost. The form should be completed in its entirety, and, to avoid a possible objection, invoices or other documentation detailing your claim should be attached.

Next, comes the actual filing of the claim. Your may file your proof of claim through the mail. The original proof of claim along with two copies, one which is to be file stamped and returned to you for your records, should be included. In addition, if filing by mail, include a self addressed stamped envelope with postage. The U.S. Mail should be avoided unless you have extra time before the bar date. Even then, it is better practice to use an overnight service which can be easily tracked to confirm receipt by the court. Address the envelope to the in-take clerk of the court and be sure that you have the proper address, as some courts have two addresses, e.g. Los Angeles Division.

If filing within a week or less of the bar date, it is wise to contact an attorney service to file your claim. An attorney services is a company made up of dispatchers and couriers who specialize in these sorts of tasks. Most bankruptcy courts will accept facsimile signatures for the proofs of claim, so you can fax the proof of claim along with the supporting documentation, to the service who can then copy the document and file it, often on the very same day. Be sure to confirm with your attorney service whether or not you need to later file your original signature page as some courts require.

In addition to filing the document, you may also chose to send copies of your claim to the trustee, if one is appointed, the Office of the United States Trustee and the Debtor. While this is not required under the Bankruptcy Code, it may help to head-off an objection to your claim in the future and, as we all know, avoiding objections is one of the primary goals.

THE FAIR CREDIT REPORTING ACT: WHEN MAY IT APPLY TO TRADE CREDITORS AND WHAT STEPS SHOULD TRADE CREDITORS TAKE TO COMPLY? (Continued)

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is a "business purpose" for running such report.

However, there is little case law interpreting the "business purpose" exception of FCRA. In light of this, we recommend trade credit grantors obtain written permission to run a consumer credit of the individual guarantor and the insider of a company so as to protect the trade credit grantor from becoming a test-lawsuit. A credit executive should obtain written permission by including the following type of authorization language in the business credit application and personal guarantee form.

a. FCRA Authorization Contained in Trade Credit Application

A credit executive extending trade credit should include the following language in his or her trade credit application to authorize obtaining consumer credit reports on the corporation's individual insiders or LLC's individual members. This language could be included as a separate form, or addendum to accompany the application for trade credit:

The undersigned consents to [*insert: Name of Your Business*] obtaining a consumer credit report on _________ [*insert name of the sole proprietor/ President/Officer of closely held company*] for the purpose of evaluating the creditworthiness of __________ [*insert name of the sole proprietor/President/Officer of closely held company*], in connection with this Application.

Signed By:

____

[*type here name of sole proprietor/ President/Officer of closely held company*]

b. FCRA Authorization Contained in Personal Guarantee

A credit executive requiring a personal guarantee for extensions of trade credit should include the following language in his or her personal guarantee form to authorize obtaining a consumer credit report from the guarantor.

The undersigned consents to [*insert: Name of Your Business*] obtaining a consumer credit report on _________ [*insert name of the guarantor*] for the purpose of evaluating the creditworthiness of _________ [*insert name of the guarantor*], in connection with an application for business credit.

Signed By:

____

[*type name of guarantor here*]