Blakeley & Blakeley LLP

THE TRADE VENDOR QUARTERLY

Summer 2002
www.vendorlaw.com

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

BANKRUPTCY COURTS CONTINUE TO RECOGNIZE THE ESSENTIAL VENDOR DOCTRINE—THE JUDICIAL APPROVAL OF A PREFERENCE

Scott Blakeley
sblakeley@vendorlaw.com

Vendors are wrestling with bankruptcy trustees and liquidating agents in record numbers over the bankruptcy preference. The bankruptcy preference requires a vendor to give back payments received within the 90 days prior to the bankrkuptcy filing, subject to a vendor's defenses such as the subsequent advance and ordinary course of business.

A twist to the preference laws is the recent trend of bankruptcy courts to authorize a debtor in some instances to pay certain vendors post-bankruptcy on account of their pre-bankruptcy claims, the so-called essential vendor or critical vendor. In other words, if the vendor received payment prior to the bankruptcy on account of a delinquent account the vendor may be subject to a preference for the payment. However, if the vendor is selected as an essential vendor by the debtor and the bankruptcy court authorizes the post-bankruptcy payment on the pre-bankruptcy delinquent account, no preference.

Under the essential vendor doctrine, a vendor may find that the product or service it provides a Chapter 11 debtor is essential to continued operations. The uniqueness of the product or service may give the vendor leverage in negotiating post-bankruptcy sales. More and more bankruptcy courts are considering a debtor's request to treat certain vendors as essential and have their pre-bankruptcy claims paid in exchange for post-petition trade credit. A number of bankruptcy courts, from Owens Corning to Bethlehem Steel, to the Warnaco Group, Baldwin Piano, AGA Flowers and Federal Mogul, have recently approved the debtor's request for an essential vendor program. Vendors in the Kmart Chapter 11 proceeding witnessed the bankruptcy court approve Kmart's request to pay Fleming Foods, as well as its liquor and music suppliers, among others. Two bankruptcy courts recently published opinions recognizing the essential vendor program.

The bankruptcy court in the Payless Cashways retail stores Chapter 11 considered the debtor's request to treat certain lumber suppliers as essential vendors (*In re Payless Cashways, Inc., 268 B.R. 543 (Bankr. W.D. Mo. 2001)*).

The essential vendor program provided that in exchange for the debtor's payment of all or part of the vendor's pre-bankruptcy claims, the following terms: the vendor provides standard industry terms, open up to one year following confirmation of a plan of reorganization; critical trade vendor payments would not exceed $10 million. The court's analysis was whether the debtor was able to obtain inventory of similar quality, whether the product was critical to survive, and whether preferring vendors was a better result than shutting down the business.

(continued on page 4)

CONTENTS

BANKRUPTCY COURT CLARIFIES THE ORDINARY COURSE OF BUSINESS PREFERENCE DEFENSE, AND VENDOR PREVAILS

Bradley Blakeley
bblakeley@vendorlaw.com

The recent flurry of chapter 11 filings in the State of Delaware has resulted in thousands of vendors finding themselves, like Armenia Coffee Corporation (Armenia), defending preference actions instituted in The First State. Thanks to Judge Judith K. Fitzgerald, vendors now have a brighter line to use in analyzing their ordinary course of business defense. Judge Fitzgerald ruled in favor of Armenia, finding that Armenia had an ordinary course of business defense to the preference action instituted by the debtor, Brothers Gourmet Coffees, Inc. (Debtor).

In the preference action, the Debtor sought recovery of eight transfers to Armenia totaling more than $800,000 made in the 90 days prior to the petition date. In response, Armenia filed a motion for summary judgment asserting that seven transfers (one was made by wire transfer and not included in the motion) were made in the ordinary course of business.

The Preference Action and the Ordinary Course of Business Defense

The Bankruptcy Code vests the debtor (or trustee if one is appointed) with far-reaching powers to avoid transfers of

(Continued on page 5)

FORCE MAJUERE: A METHOD TO ALLOCATE RISK OF NONPERFORMANCE

Richard Ruszat
rruszat@vendorlaw.com

A variety of recent events have renewed the interest of force majeure clauses in contracts. The catastrophic events of September 11 and the continued threat of terrorism, domestic and abroad, are a grim reminder that tragedy does not discriminate. These events only compound common risks associated with conducting business in a cycling domestic economy and unpredictable international markets. The effect of these events requires parties to closely assess their contractual relationships and predict future events to allocate the risk of nonperformance. Today's contracts must contemplate common risks while preparing for events that were once unimaginable.

Defining Force Majeure

Force majeure is a term used to describe a "superior force" event. The purpose of a force majeure clause is two-fold: it allocates risk and puts the parties on notice of events that may suspend or excuse service. The essential requirement of force majeure is that the invoking party's performance of a contractual obligation must be prevented by a supervening event that is unforeseen and not within the control of either party. Typical force majeure events include Acts of God, superceding governmental authority, civil strife, and labor disputes. However, there is no uniform set of events that constitute force majeure. Instead, force majeure remains a flexible concept that permits the parties to formulate an agreement that corresponds to their unique course of dealings and industry idiosyncrasies. Moreover, recent events have increased the necessity to include additional, unthinkable events, such as terrorism and the threat of biological and chemical warfare.

Negotiating a Force Majeure Clause

A party in the negotiation stage of a force majeure clause must scrutinize the events and allocation of risk to assure that the clause is not one-sided or unenforceable. If an event occurs that is not covered or specifically enumerated in a force majeure clause, courts are reluctant to conclude that a contract is unconscionable, and therefore, hold the parties to the benefit of their bargain. Additionally, parties should review the legal effect of enumerating an event in a force majeure clause. For example, a commonly invoked force majeure event is market fluctuation that renders a contract economically unfeasible. A majority of courts refuse to excuse performance on the theory that a contract is no longer profitable.

Drafting a Force Majeure Clause

In drafting a force majeure clause, parties may rely on general clauses or specifically enumerate which events will constitute force majeure. For example, a general force majeure clause may consists of the following language:

"It shall not constitute a material breach,

(Continued on page 6)

F R O M T H E P U B L I S H E R :

<u>The Trade Vendor Quarterly</u> is published by the law firm of Blakeley & Blakeley LLP and is distributed as a service to clients and other parties interested in creditor issues. This information is not intended to constitute legal advice, nor a substitute for legal advice. Blakeley & Blakeley LLP cannot be held responsible for the accuracy of information contained in articles written by guest contributors. Readers' comments and questions are welcome and should be addressed to:

Scott Blakeley of Blakeley & Blakeley LLP,
Wells Fargo Tower,
2030 Main Street, Suite 540,
Irvine, CA 92614.
Phone: 949-260-0611 or Fax: 949-260-0613

or

Home Savings Bank Tower,
660 South Figueroa Street, Suite 1840,
Los Angeles, CA 90017
Phone: 213-385-5815 or Fax: 213-385-5817.

Visit the firm's web site at
www.vendorlaw.com

DERAILING THE TRAIN TO DELAWARE KEEPING CHAPTER 11's IN YOUR HOME JURISDICTION

Doug Cushing,
Jordan Schrader PC

doug.
cushing@jordanschrader.com

The March 2002 *Flash Alert* noted the boost in corporate Chapter 11 filings in Delaware's bankruptcy courts. It also highlighted the burden placed on vendors located elsewhere around the country when the primary business center of a company is not on the East Coast. Given the prima facie venue choice recognizing the state of incorporation of the debtor is the state of the bankruptcy case, a high majority of public companies that will too often result in trade vendors facing long distance burdens attempting to meaningfully participate in the reorganization process.

However, that shouldn't always be the case. Local counsel can make a difference, and in some cases effectively reroute the Chapter 11 proceedings back to the home jurisdiction. Since that battle will be initially litigated in a Delaware bankruptcy court, it is not an easy task, but the cases can be won.

Ernst Home Center, Inc. filed a voluntary Chapter 11 petition in Delaware on July 12, 1996. On behalf of a number of unsecured creditors, the author, along with Dan Caine, now with Ryan Swanson in Seattle, were then engaged to attempt to change the venue to the Western District of Washington where the company was headquartered. A group of landlords filed a similar motion, both being filed approximately five weeks after the petition date. The hearing that followed took place only 10 days later.

The movants for such a proceeding bear the burden of proof to establish the four criteria cited in the primary reported cases: (1) the proximity of the court to the interested parties; (2) the location of the debtor's assets; (3) the economics of administering the estate; (4) the relative economic harm to the debtor and other interested parties. *In re Ocean Properties of Delaware,*

(Continued on page 4)

DOES YOUR RECLAMATION DEMAND LETTER SUFFICIENTLY IDENTIFY YOUR GOODS?

Scott Blakeley
sblakeley@vendorlaw.com

News of a major customer's insolvency is frustrating 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 if the customer has not filed bankruptcy, or, if the customer files bankruptcy, a priority claim for the reclaimed goods.

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.

Establishing Your 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 which sufficiently identifies the goods to be reclaimed; and

(4) the debtor had possession of the goods at the time of the reclamation demand or the goods were not in the hands of a buyer in the ordinary course or a good faith purchaser at the time of demand.

Reclaimed Goods Must Be Sufficiently Identified

As noted, one element for a vendor to prevail on its reclamation demand is written demand for the return of the goods which sufficiently identifies the goods to be reclaimed. But what language should the reclamation demand letter contain to sufficiently identify the goods so as to make an effective demand? The bankruptcy court in *In re the Hechinger Investment Company of Delaware,* 274 B.R. 402 (Bankr. D. Del. 2001), considered the debtor's objection to a vendor's reclamation suit contending that the vendor's reclamation demand letter failed to properly identify the goods.

In *Hechinger*, the vendor filed a complaint for reclamation in the bankruptcy court, and the debtor filed a motion to dismiss contending that the reclamation demand letter failed to sufficiently identify the reclaimed goods. The bankruptcy court focused on the vendor's reclamation demand letter. The court noted that the demand letter did not identify the goods, nor did the letter attach documents to identify the goods, such as shipment or delivery dates, invoice numbers or P.O. numbers. The court stated the vendor's burden: "the U.C.C. requires strict compliance with its procedural and substantive rules for reclamation. Moreover, the reclaiming vendor maintains the burden of proof to establish each element of the right to reclamation by the preponderance of the evidence." Hechinger, 274 B.R. at 407. To that end, the court ruled: "the demand must identify the goods as to which reclamation is sought so as to permit their return pursuant to the demand at the time the demand is made. *If the demand fails to be sufficiently detailed to accomplish that purpose, it must of necessity fail as a matter of law."* (citation omitted). *Hechinger*, 274 B.R. at 407.

However, in the context of the debtor's motion to dismiss the reclamation suit, the court found that the vendor's demand letter was sufficient to identify the goods at the time of demand. But the court decided that the vendor had made a "minimal" identification of the goods, and that the vendor had the burden to establish that the debtor was in a position to identify the goods, such as through an inventory control system. That may be a high hurdle, the court observed, given the debtor's nationwide operations and financial difficulty.

Is Your Demand Letter Sufficient?

The *Hechinger* decision reminds vendors to identify the goods being reclaimed to minimize the risk of litigation with the debtor or trustee. The attached reclamation demand letter may be of interest where the customer files bankruptcy.

(Continued on page 6)

FAIR CREDIT REPORTING ACT AND REPORTING AN INDIVIDUAL DELINQUENT ACCOUNT

Scott Blakeley
sblakeley@vendorlaw.com

Should a sole proprietor customer fail to pay, do you report the customer's delinquent account to a credit reporting agency? If so, and you fail to accurately report the delinquent account, may you be liable under the Fair Credit Reporting Act (FCRA)?

The 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. The FCRA insures that credit reporting agencies, and the users of such reports, will respect a consumer's right to privacy by pulling consumer credit reports only after express written authorization from the consumer.

In *Miller v. Trans Union Corp*., 24 Fed.Appx. 422 (C.A. 6th 2001), the plaintiff sought to purchase a vehicle, but was unable to as several banks had denied their application for credit due to negative information contained in their credit reports, which were furnished by Trans Union. The plaintiff alleged that the information contained in their credit reports was false and had been fraudulently reported to Trans Union by certain creditors. The plaintiff sued the creditors under FCRA, and for fraud, requesting monetary damages. The creditors opposed the suit contending that they were not "consumer reporting agencies" as defined by the FCRA.

The court noted that the plaintiff's presented no evidence that the creditors regularly assembled or evaluated consumer credit information in order to furnish consumer reports to third parties, not did the plaintiff's present evidence that the information provided by the creditors to Trans Union was not solely based upon information contained in their own ledgers. The court dismissed the suit.

BANKRUPTCY COURTS CONTINUE TO RECOGNIZE THE ESSENTIAL VENDOR DOCTRINE...

(continued from page 1)

The court noted that the debtor could not otherwise obtain trade credit, that the creditors' committee did not oppose the request, and that the essential vendor program provided the debtor the opportunity to restock its shelves. The court rejected the Office of the United States Trustee's argument that should the debtor convert to Chapter 7, the essential vendor would have to return the payment as a preference.

In another recent bankruptcy court decision, *In re Wehrenberg, 260 B.R. 468 (Bankr. Mo 2001)*, the debtor, who operated a chain of move theatres, requested to pay prepetition claims of critical vendors. Certain film companies holding unsecured claims refused to continue to provide films to the debtor unless the claims were paid. The court agreed, noting: "Payment of the prepetition claims of these vendors as set out in the Debtor's motion is necessary to realize the possibility of a successful reorganization. . . the Court may authorize the payment of prepetition claims when such payments are necessary to the continued operations of the Debtor." *Wehrenberg*, 260 at 468.

The courts application of the necessity doctrine continues to evolve. Debtors more frequently request courts' approval of the necessity program, and courts are more receptive. Where the doctrine is approved, courts reason, both the debtors and creditors stand to gain something. The A necessary@ vendor benefits by receiving early payment on its prepetition claim. The debtor and its vendors benefit by receiving needed product on credit, which may lead to a successful reorganization. A vendor being deemed an essential vendor can have a dramatic impact on the account. The credit professional is not forced to wait what may turn out years for uncertain payment from a reorganizing debtor.

In exchange for the vendor being paid in full, the debtor conditions the vendor extending comparable credit terms postpetition. Below is the type of letter that a debtor often requests its essential vendor to sign:

(Continued on page 5)

DERAILING THE TRAIN TO DELAWARE KEEPING CHAPTER 11's IN YOUR HOME JURISDICTION

(Continued from page 2)

Inc., 95 BR 304 (1988); *In re Commonwealth Refinancing Co.,* 596 F2d 1239 5th Cir 1979, *cert. den.* 444 US 1045 (1980).

The primary focus of our challenge focused on the debtor's own information. This included the filed schedules, the list of the 20 largest creditors, filed reports of stores to be closed, previously filed 10-Qs on file with the SEC, and other generally available public information.

Corporate records reflected that *Ernst* had been incorporated in Washington in 1894 and its state of incorporation transferred to Delaware in 1993. It depicted itself as a Northwest corporation, as its principal locations were in the states of Washington, Oregon and Idaho, but its operations and stores did extend through a number of other western states. At the time of filing, the overwhelming majority of the stock was owned by a New York/New Jersey based investment group. The corporate officers remained in Seattle, Washington, and all the stores which were initially to be closed were in the Western states.

Outlining the makeup of the debtor's creditor base was very important in persuading the court that a change of venue was appropriate. The unpublished decision highlighted the material which we gleaned from the debtor's filed schedules. Our analysis showed that half the 20 largest creditors were west coast based and overall 40% of the unsecured creditors reflected Washington addresses. An additional 35% came from the other Western states. The court's opinion highlighted that creditor concentration. Judge Walsh noted particularly that if there were preference or avoidance actions filed, they would very likely be filed against parties entitled to seek transfer of venue on a case-by-case basis if the entire matter were not shifted to Washington. Similarly, the leaseholder group demonstrated that lease rejection disputes were likely to require non-Delaware locales focusing on non-Delaware choices of law.

The debtor-in-possession and the unsecured creditors committee opposed the motion, citing the "national committee, the east coast based reorganization consulting firm, and the initial activity post-petition before the court in Delaware." Finding the consultant's resume noted its "national practice" the court found that limitation of little impact. The judge also distinguished the *Ernst* situation from a previous decision in Delaware in the *Pik 'N Pay* case, a multi-state retailer, where only one large national creditor, NationsBank, not teams of landlords and unsecured creditors sought the change. He further contrasted the typical leased site in *Pik 'N Pay* which were small retail spaces of only a few thousand square feet to the multi-acre sites in *Ernst,* a big style box retailer. This disparate impact in terms of the relative loss to the creditor was also of concern to the court in terms of the unsecured creditor's objection to Delaware venue. He evaluated the scope of the losses as likely to be of high impact on those creditors. This was a significant basis in his view requiring transfer to Washington to let the local court handle the reorganization.

The opposition, as one might expect, contended that the costs of requiring those national parties that would be involved to travel to the west coast would increase the overall costs of administering the case. These objections were summarily rejected by the court which stated "If the cost of overcoming that disadvantage is some additional administrative expense to the estate, then that is a small price to pay for an even playing field." That final note was of particular benefit to the moving creditors as well in our later motion brought in the Western District of Washington for reimbursement of attorney's fees to the two groups of creditors. Despite continued strident opposition from the debtor-in-possession, the court allowed recovery of attorneys fees from the estate for both local and Delaware counsel for the two groups of creditors which had brought the motion to change venue.

True national entities will continue to justifiably remain in the Delaware courts, but vendors in the hinterlands should not be afraid to make the fight when the factual case can be presented, particularly in those instances where the debtor's historical documentation will effectively pin them down to a different venue.

Doug Cushing is an attorney with Jordan Schrader PC. He may be contacted by e-mail at doug.cushing@jordanschrader.com

BANKRUPTCY COURT CLARIFIES THE ORDINARY COURSE OF BUSINESS PREFERENCE DEFENSE, AND VENDOR PREVAILS

(Continued from page 1)

assets and monetary transactions prior to a bankruptcy filing. The power to avoid preferential transfers is one of the most powerful weapons a trustee has. The Bankruptcy Code defines a preference expansively to include nearly every transfer by an insolvent debtor 90 days prior to bankruptcy. The purpose of the preference provision is two-fold. First, vendors are discouraged from racing to the courthouse to dismember a debtor, thereby hastening its slide into bankruptcy. Second, debtors are deterred from preferring certain unsecured creditors by the requirement that any unsecured creditor that receives a greater payment than similarly situated unsecured creditors disgorge the payment so that like creditors receive an equal distribution of the debtor's assets.

Not all transfers made within the preference period are avoidable. To protect those transactions which replace value to the bankruptcy estate previously transferred, the Bankruptcy Code carves out seven exceptions or defenses to the trustee's recovery powers. The most commonly asserted exception by trade creditors is the ordinary course of business defense. That defense protects payments, in all or part, received by an unsecured creditor within 90 days of the bankruptcy from recovery where the creditor establishes certain elements detailed below. The policy supporting the ordinary course of business defense is two-fold: (1) protect customary transactions, and (2) encourage creditors to continue to extend credit to financially troubled debtors, possibly helping the debtor avoid bankruptcy.

To qualify for the ordinary course of business defense, a creditor must establish that the payment is ordinary as between the parties and that the payment is ordinary in relation to prevailing business standards. The court determines a debtor's ordinariness of payments through comparison with prevailing business standards, which includes common terms used by other trade creditors in the same industry facing similar problems.

Ordinary Course Prevails

In its ruling, the *Brothers Gourmet Coffee* Court first examined whether the transfers were made within the ordinary course of business between the parties (the subjective analysis). The Debtor argued that Armenia stepped up its collection efforts during the preference period such that the payments were not made in the ordinary course of business. The record reflected that prior to the preference period, Armenia made calls to Debtor concerning payment related to 50 percent of its orders, but, during the preference period, called regarding five out of seven orders. However, the Court found that the change was not material.

Additionally, the Debtor admitted that the average time between invoice due date and payment date in the pre-preference period was approximately 32.69 days and the average time between invoice due date and payment date in the preference period was approximately 33.71 days. The Court found that the difference of one day was not material and the payments during the preference period were within the range of payments made in the pre-preference period. Accordingly, the Court found that Armenia met its burden on the issue of the subjective test.

The Court also found the transactions were made according to ordinary business terms (the objective analysis). The Debtor contended that Armenia had not provided any specific data regarding the ordinary business terms in the coffee industry. However, the Court disagreed. Instead, the Court found that Armenia's declarant was an expert whose opinion was offered as to the experience of payment for orders in the coffee industry, and that the transactions between the Debtor and Armenia were ordinary within the industry. The Court found that the Debtor produced no evidence to refute the expert's opinion, and summary judgment was granted on the section 547(c) issues.

As found in *Brothers Gourmet Coffee*, a small difference between pre-preference period and preference period collection practices and timing of payments may not still allow you to prevail on the ordinary course of business defense. The Court provides ammunition for the vendor to negotiate the preference complaint.

BANKRUPTCY COURTS CONTINUE TO RECOGNIZE THE ESSENTIAL VENDOR DOCTRINE—THE JUDICIAL APPROVAL OF A PREFERENCE

(Continued from page 4)

ACKNOWLEDGMENT BY ESSENTIAL TRADE VENDOR

[Name of Essential Trade Vendor] is in receipt of [relevant debtor's] purchase order or invoice ________ requesting shipment of [describe requested goods by type, quantity and price] (the "Goods") or delivery of services ("Services") which was/were received by us on ______________, 2002, at those places set forth in the Purchase Order or Invoice. (If the Purchase Order requires multiple delivery dates and/or locations, we have attached a schedule of such information to this Acknowledgement.) We hereby acknowledge and agree that shipment of the Goods or Services will be in accordance with Customary Trade Terms and the Order Granting Debtors Authority for Payment of Prepetition Trade Claims of Essential Trade Vendors entered by the Court.

[Name of Essential Trade Vendor]
By:_______________________
Printed Name:______________
Title:______________________
Date:______________________

DOES YOUR RECLAMATION DEMAND LETTER SUFFICIENTLY IDENTIFY YOUR GOODS?

(Continued from page 3)

BANKRUPTCY RECLAMATION DEMAND LETTER

[*date*]

VIA FACSIMILE AND OVERNIGHT MAIL
[OR, HAND DELIVERY]

[*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 **[Vend*or*]** (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 segregation and return of all the ***[Reference 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. Invoices attached*]**. 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 Executive*]

EXHIBIT "A"

FORCE MAJUERE*:* *A METHOD TO ALLOCATE RISK OF NONPERFORMANCE*

(Continued from page 2)

and neither party shall lose any rights hereunder or be liable to the other party for damages or losses, on account of failure of performance by the defaulting party, if the failure is the result of a natural disaster, national emergency, the act or omission of a third party, or similar event outside of a party's control."

A prudent force majeure clause specifically enumerates the events that will prevent performance and entitle a party to suspend or excuse an obligation. For example, a specific and contemporary force majeure clause may consists of the following language:

"Neither party shall lose any rights hereunder or be liable to the other party for damages or losses, except for payment obligations, on account of failure of performance by the defaulting party if the failure is the result of an Act of God (e.g., fire, flood, inclement weather, epidemic, or earthquake); war or act of terrorism, including chemical or biological warfare; labor dispute, lockout, strike, embargo; governmental acts, orders, or restrictions; failure of suppliers or third persons; or any other reason where failure to perform is beyond the reasonable control, and is not caused by the negligence, intentional conduct or misconduct of the defaulting party, and the defaulting party has exercised all reasonable efforts to avoid or remedy such force majeure. The defaulting party must provide written notice of the force majeure event to the remaining parties within two (2) business days of such event."

Moreover, force majeure clauses may include language that is industry specific. The construction industry, for example, may incorporate a clause to suspend or excuse performance obligations if its failure to perform is caused by subcontractors, materialmen, or carriers. Likewise, if the contract concerns internet and online services, a force majeure clause may include events such as server failures, software glitches, and copyright or labor disputes. The upside of drafting a force majeure clause is the ability to apply it to the unique circumstances of the parties.

Invoking a Force Majeure Clause

Generally, a party may invoke a force majeure clause if an enumerated event occurs that is out of the party's control and prevents performance of a contractual obligation. The burden of proof is on the party seeking to invoke the force majeure clause. The force majeure event may either suspend or excuse a party's performance. It is imperative that the party invoking a force majeure clause provide written notice to the other party. This permits the party that is not in default to mitigate against the effects of a force majeure event.

Protecting Against a Force Majeure Event

As the definition implies, it is impossible for the party invoking a force majeure clause to avoid an event from interfering with its performance on a contractual obligation. Accordingly, it is imperative that the parties negotiate a clear and concise force majeure clause that allocates risk and provides predictability to permit a party to expeditiously respond to a force majeure event. Additionally, the affected party may mitigate against the effect of a force majeure event at the onset of the contract. For example, a party should consult an insurance broker to determine whether insurance is available to cover financial losses stemming from a force majeure event. If the stakes are high, then insuring performance may limit or prevent adverse consequences associated with nonperformance. Moreover, develop a "B" plan to soften the landing of a party's nonperformance. If the contract involves services or supplies, find an alternative source in advance. The bottom line is to limit losses.

RECENT ENGAGEMENTS AND ACTIVITIES

Blakeley & Blakeley LLP Recent Engagements and Activities for Summer 2002

Blakeley & Blakeley continues to represent its vendor clients in the areas of creditor rights, commercial litigation and collection, preference defense, credit documentation, bankruptcy and out-of-court workouts.

- ◊ Scott spoke to **CFDD** regarding recent developments with the **Fair Credit Reporting Act.**
- ◊ Scott spoke to **NACM/Chicago-Midwest** in San Antonio, Texas regarding **The Corporate Meltdown of Enron**.
- ◊ Scott spoke to **CMA Business Credit Service's Medical Products Group** regarding **Bankruptcy and Creditors' Rights.**
- ◊ Scott spoke to the **National Business Credit Exchange's Wall Coverings Industry Group** in Las Vegas regarding the **Necessity Doctrine and Defending the Preference Action.**
- ◊ Scott spoke to **National Association of Credit Management's** members regarding **Escheatment**.
- ◊ Scott spoke to the **NACM/Conneticut's Copper and Aluminum Traders and Lead Manufacturers** in Las Vegas regarding the **Necessity Doctrine and Defending the Preference Action.**
- ◊ Scott Blakeley spoke to the **National Food Group** in Las Vegas regarding **Bankruptcy and Antitrust**.
- ◊ Scott spoke to **National Electrical Distributing Credit Association** regarding the **Necessity Doctrine and Defending the Preference Action.**
- ◊ Scott spoke at the **NACM Credit Congress** in Las Vegas regarding the **Electronic Credit Department**.

KEEPING THE CREDIT AND FINANCIAL PROFESSIONAL
INFORMED OF LEGAL DEVELOPMENTS
VISIT OUR WEBSITE @
www.vendorlaw.com

The Trade Vendor Quarterly is distributed via E-Mail. ***The Trade Vendor Quarterly*** is a free publication prepared by the law firm of Blakeley & Blakeley LLP for clients and friends in the commercial credit and financial community. Please complete the following:

Representative to Receive Newsletter: ______________________________

Company Name: ______________________________

E-Mail Address: ______________________________

Telephone: ______________________________

Facsimile: ______________________________

Mailing Address: ______________________________

____

____

Others to Receive Newsletter: ______________________________

____

Please forward the information via:

E-mail: sblakeley@vendorlaw.com

Fax: 949/260-0613

Mail: Scott Blakeley
Blakeley & Blakeley LLP
Wells Fargo Tower
2030 Main Street, Suite 540
Irvine, CA 92614
Direct Line: 949/260-0612