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When an Israeli Vendor Discovers Its American Customer is Insolvent

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Each day creditors across the globe receive the bad news that a customer is not paying its debts or is otherwise insolvent. Israeli creditors, whether lenders or vendors, are no exception. Knowing what to do can limit exposure and maximize recovery of debts owed by the insolvent party.

Often, foreign creditors have little knowledge of the procedures and remedies available to them under American law, or of the variety of strategies which they may employ. Their business lawyers may be equally vague about the intricacies of American insolvency law. The esoteric nature of the law, coupled with distance and the amount in question, may discourage such creditors from exploiting available remedies even when the expense of doing so may be relatively modest.

Here are some basics for the Israeli practitioner to know:

Typically, if a customer has filed a petition under American federal bankruptcy law, they will have done so under one of two relevant Chapters of the Bankruptcy Code. The customer, now a debtor, will often file pursuant to Chapter 7 (liquidation) and a Trustee will be appointed to receive and evaluate claims. Alternatively, a Debtor may file under Chapter 11 (reorganization), and while the Chapter 11 Debtor remains in possession and operating, a committee of creditors may be appointed to oversee the reorganization on behalf of unsecured creditors.

It is important to note that, creditors are not necessarily treated equally in the context of American bankruptcy and insolvency counsel should review whether a claim may be entitled to priority status, whether and how to file a proof of claim or appropriate motion, and examine potential claims against the creditor under various clawback theories. Where a creditors' committee is to be appointed, joining the committee may have significant benefits for the creditor, but it must act promptly to indicate its willingness to join.

Creditors in Israel should also be aware that, under U.S. federal law, the filing an involuntary petition against an American debtor is possible. Such a petition may be possible where the debtor is generally failing to pay its

debts as they become due or is “balance sheet insolvent”. If the debtor has 12 or more creditors, 3 petitioners are needed to jointly file such a petition. While involuntary bankruptcy can be an excellent tool, it can be a slippery slope and should be undertaken with scrupulous caution.

Creditors already pursuing a claim against a company which subsequently files bankruptcy under U.S. federal law should immediately cease further enforcement actions and consult counsel, as the filing triggers an automatic stay which prohibits continuation of collection activities until permitted by the bankruptcy court.

Insolvency isn’t always governed by federal law and the United States Bankruptcy Code. Depending on the situation, state law remedies such as Assignments for the Benefit of Creditors (ABC), receiverships under state law, and out of court workouts may be employed. These mimic the procedures and priorities of the bankruptcy code but are sometimes more efficient, less costly and more appropriate.

Securing the advice of local counsel who specialize in bankruptcy and creditors’ rights is important. Posing questions to such specialized counsel costs nothing and may result in significant benefits.

Please note that this is a general overview of developments in the law and does not constitute legal advice. Nothing herein creates an attorney-client relationship between the sender and recipient. If you have questions regarding these provisions, or any other aspect of bankruptcy law, please contact Michael Traison at 312.860.4230.

Practices

- Bankruptcy and Creditors' Rights

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