



Private Companies Group  
*Approach*

September 2009

Dear Clients and Friends:

Heading into the fourth quarter, we bring you four new stories of recent Private Company client successes from four different industries, all sharing one common trait: *tenacity*. Economic indicators continue to point in various directions; market prognosticators still talk of “green shoots,” as if magic beans were strewn. Yet these stories illustrate that real results take root when a company and its counsel share a singular focus on the goal, and a tenacious, even scrappy ability to figure out how to achieve it. Whether that goal is an alternative source of capital, ways to minimize credit exposure, or a new platform for expanding a start-up venture, these success stories show that hard work, creativity, some patience, and a lot of grit are needed; not magic beans.

We hope you enjoy our third issue of the *Approach*. If you missed our April and June issues, they are posted at [www.schiffhardin.com](http://www.schiffhardin.com), under “Publications.” We welcome any comments or suggestions. Inside we also provide another installment of the “Proactive Creditor Checklist,” focusing on ways to reduce the risk of a “preference” action from your customers’ creditors. The stories featured here and on our Web site are just a few examples of the ways Schiff Hardin’s attorneys work closely with clients to achieve favorable results in often challenging circumstances.

Whether your company is a start-up or a seasoned business organization, our Private Companies Group brings to bear a wide range of specialties in a collaborative, “right-sized” approach to help your business succeed. Our attorneys understand our clients’ diverse businesses, their challenges and risks, and their opportunities. We understand the often intense pressure on their key resources: money, personnel and time. We help our clients thrive in this environment.

*This is the Schiff Hardin Approach.*



**Strong Advocates.**  
**Trusted Advisers.**  
*Lasting Client Relationships.*

Atlanta

Boston

Chicago

Lake Forest

New York

San Francisco

Washington

A specialty foods manufacturer needs cash to grow its business, but the locked credit markets have made funding a challenge.

When a family-owned manufacturer of specialty food products sought capital to grow its business, it turned to Schiff Hardin for help in obtaining the needed funds despite the current credit crunch. Our team assisted the client in restructuring its existing credit facility, and selling and leasing back its main manufacturing location.

Unlike a sales contract, in which the parties need have no further contact after the sale, a lease establishes a relationship between the parties which lasts over the life of the lease. As such, the lease must comprehensively determine the rights and responsibilities of the parties over the lease term. Our attorneys negotiated the lease and the sales contract, worked with the client to determine the tax advantages of the transaction, addressed any environmental issues related to the operation of the manufacturing plant, and provided the expertise needed to consummate the sale. The client now has the necessary funds to expand its business, while its current operations continue at its main plant.

For further information: **Patricia Ullman**, Real Estate  
312.258.5688, pullman@schiffhardin.com  
**Steve Dragich**, Corporate and Securities  
312.258.5692, sdragich@schiffhardin.com



A major industrial products distributor seeks to develop and implement a proactive approach to its credit practices in light of the potential for preference actions.

A major industrial products distributor with customers nationwide often found itself as a defendant in Bankruptcy Court preference actions, due to the increasing rate and speed at which certain of its customers were proceeding to Chapter 7 or 11 filings. The company sought to develop a more proactive approach to its credit practices with such customers, using Schiff Hardin's guidance on how best to structure troubled accounts to minimize the likelihood of a preference action, if not avoid preference litigation risk altogether.

Our attorneys teamed up with the client to outline the key considerations in collecting on aging or troubled accounts receivable. We also provided the client's key credit personnel with an in-depth understanding of the preference statutes and their implementation, adding to the client's knowledge base and enabling it to make better on-the-spot credit decisions without creating additional preference exposure.

Our preference-risk counseling goes beyond run-of-the-mill defenses and includes affirmative steps to seek secondary avenues for repayment if the client is, at a later date, required to disgorge certain payments to a bankrupt entity. For additional information, please see the enclosed "Proactive Creditor" checklist: "Practical Tips to Reduce or Eliminate Your Preference Risk."

For further information: **Jon Vigano**, Restructuring, Bankruptcy and Creditors' Rights  
312.258.5792, jvigano@schiffhardin.com

Schiff Hardin recently assisted a private equity fund-owned portfolio company in successfully negotiating the refinancing of its secured debt and obtaining additional equity capital. The company had been adversely affected by recent developments with its customers' own difficulties in the current economy, and determined its optimal strategy was to refinance its existing debt and seek additional investors. Schiff Hardin advised the client with respect to all corporate, financing and tax issues raised in the transactions. The company secured financing from a new senior lending bank, which replaced the existing lender, and added a mezzanine lender, which also invested additional equity capital in the company, which is now positioned for greater stability and growth.

A portfolio company of a private equity fund needs to refinance its existing secured debt and raise additional equity in a challenging credit market.

For further information: **Alex Young**, Corporate and Securities  
312.258.5737, abyoung@schiffhardin.com  
**Kevin Knohl**, Finance  
312.258.5789, kknohl@schiffhardin.com  
**Bob Pluth**, Tax  
312.258.5535, rpluth@schiffhardin.com



EveryBlock LLC ([www.everyblock.com](http://www.everyblock.com)) is a Web-based start-up that provides online news on a hyper-local level. The company was founded in Chicago in 2007 through a grant from the John S. and James L. Knight Foundation. EveryBlock.com scours the Internet for local news and publicly available information and organizes it geographically for users, down to a city-block level. The site currently gathers data for 15 major U.S. metropolitan areas.

An on-line news start-up company needs advice in transitioning from being funded through a journalism grant to exploring different commercial options and a potential strategic sale.

With its grant coming to an end earlier this summer, EveryBlock needed to find a new funding source to continue building its site and underlying technology. The founders turned to Schiff Hardin's Private Companies Group for assistance. Our attorneys provided advice in confirming its intellectual property rights and evaluating potential venture capital investment and acquisition opportunities. Our intellectual property attorneys also provided knowledgeable counsel with respect to EveryBlock's open source code and the still-developing arena of Internet copyright law. Ultimately EveryBlock agreed to be acquired by MSNBC.com, and Schiff Hardin handled the negotiations and successful closing of the sale. The deal provides EveryBlock.com with a solid financial backing to enable its founders to expand the site's growth and innovation as part of a broader strategic platform, at the same time providing its founders with liquidity from the sale.

For further information: **Matt Galo**, Corporate and Securities  
312.258.5643, mgalo@schiffhardin.com  
**Chris Bollinger**, Intellectual Property  
312.258.5724, cbollinger@schiffhardin.com  
**Rob Sieland**, Corporate and Securities  
312.258.5619, rsieland@schiffhardin.com



Schiff Hardin is a client-focused, general practice law firm with offices in Atlanta, Boston, Chicago, Lake Forest, Illinois, New York, San Francisco, and Washington, D.C. With attorneys admitted to practice in 31 states and six countries, Schiff Hardin offers a diversified practice covering almost every legal discipline, with the broad reach to meet the needs of domestic and international clients.

Our Corporate and Securities Group, which includes the Private Companies Group, provides a full range of services for private and public companies throughout the United States and abroad, from start-up businesses to Fortune 500 corporations. Our tradition of excellence in service to our clients — many of whom we have enjoyed working with for decades — enables us to anticipate their legal needs and provide solutions to help them drive their businesses.

For comments or further information about our Private Companies Group or the services described in this issue of the *Approach*, please contact your regular Schiff Hardin attorney or any of the attorneys listed inside, or **Steve Dragich** (312.258.5692, [sdragich@schiffhardin.com](mailto:sdragich@schiffhardin.com)) or **Matt Galo** (312.258.5643, [mgalo@schiffhardin.com](mailto:mgalo@schiffhardin.com)). If you would like to receive this publication in electronic form, please visit our Web site to sign up.

Please visit our Web site to learn more about Schiff Hardin.

[www.schiffhardin.com](http://www.schiffhardin.com)



© 2009 Schiff Hardin LLP All rights reserved.

This publication has been prepared for the general information of clients and friends of the firm. It is not intended to provide legal advice with respect to any specific matter. Under rules applicable to the professional conduct of attorneys in various jurisdictions, it may be considered advertising material. Tax Matters: The advice contained in this memorandum is not intended or written to be used, and cannot be used by a taxpayer, for the purpose of avoiding penalties that may be imposed on the taxpayer under law.

# The Proactive Creditor Checklist:

## Practical Tips to Reduce or Eliminate Your Preference Risk

This checklist provides some guidance to reducing or eliminating your potential preference exposure in actions commenced under Section 547 of the United States Bankruptcy Code or under similar state laws. It is not a comprehensive list of available preference defenses and other options to defeat a preference claim or complaint. Rather, this checklist is a practical guide that you can use proactively to reduce or eliminate your potential preference exposure.

### 1. What is a Preference? The More You Know, the More Protected You Are.

- Typically, a preference claim is a payment disgorgement lawsuit, generally initiated in Bankruptcy Court by a debtor or trustee, to collect payments made by a bankrupt company to its vendor/creditor. Some states also have their own preference laws.
- Congress intended Section 547 of the Bankruptcy Code (which governs preference actions) to remove some perceived inequities when a troubled company elects to pay certain creditors but not others during the period leading up to bankruptcy.
- A preference lawsuit must be commenced within two years after a company files for bankruptcy protection.

be a preference, it must be made on account of a pre-existing debt. When you are paid in advance, the debt has not yet been incurred. We recommend payment by wire transfer for this reason.

- If your customer won't pre-pay, negotiate for cash-on-delivery (C.O.D). While not as good as a pre-payment, it is an available defense, preferable to payment on terms.
- If all else fails, cash in hand is better than nothing at all. It is better to collect as much as you can before your customer's bankruptcy filing, shifting the burden to your customer (or its trustee in bankruptcy) to sue you for the return of allegedly preferential payments (where your customer has to spend money and meet a burden of proof), than to be left with a general unsecured claim against your customer in its bankruptcy case.

### 2. Aging Accounts Receivable Strategy — Stay on Top of Aging Accounts.

- Track accounts receivable aging carefully. Though admittedly challenging, strive to keep payments from customers within terms.
- A sharp spike in collection efforts may increase your risk. Apply collection efforts consistently for any past due account. Establish and comply with a collection policy and use only approved methods and language (remember, e-mail is permanent and threats can increase preference exposure).
- Payment in advance is an absolute defense to a preference claim and is one of the best ways to eliminate preference exposure. For a payment to

### 3. New Account Strategy — Advance Planning Can Protect Against Future Challenges.

- Obtain a security deposit. Obtaining and holding a security deposit affords protection because, where you have the theoretical right to offset against the security deposit unpaid amounts that were otherwise paid in the months leading up to bankruptcy, you have a preference defense.
- Obtain a guarantee. Either through a parent guarantee or a personal guarantee from an officer or principal of your customer, a properly drafted guarantee provides an alternative source to collect on any payments you may have to disgorge.



- ❑ Take a security interest in the goods sold. Taking a security interest early in your relationship with your customer will help reduce your preference risk once the relationship begins to experience some credit fatigue – at which time it is nearly impossible to get a security interest from this same customer. If you are secured over the value of the payments that a bankrupt company is attempting to disgorge, you will most likely not have to return any payment. Be sure you are properly perfected.
- ❑ Review your customary invoice terms and conditions and revise them to permit you to shorten payment terms and implement other credit protections when your customer's receivable begins to age.
- ❑ When negotiating a long-term supply agreement, establish a credit limit maximum that gives you flexibility to lower the credit limit in the event payment arrearages occur. Be sure to enforce such terms when necessary.
- ❑ When opening a new account, ensure the department responsible for opening the account includes as much information as possible about the customer, particularly the customer's full and proper legal name. This helps greatly when your customer and 10 of its subsidiaries share the same first word.
- ❑ Investigate your customer's credit-worthiness. Ask your customer for a balance sheet and other financials. Check publicly available credit reports.

#### 4. Customer Bankruptcy Strategy — Protect Now Against the Litigation Ambush That Is Two Years Away.

- ❑ Preserve all payment history for three years prior to the bankruptcy filing date. Preference litigation often occurs almost two years after a bankruptcy filing occurs. Designate an appropriate custodian of bankruptcy debt records.
- ❑ Print and retain copies of invoices and bills of lading (or other proof of delivery) for items identified during the payment history.
- ❑ Generate an accounts receivable history. Print and retain copies of all invoices, both paid and unpaid, for the duration of the relationship with your customer.
- ❑ Issue a reclamation letter and a 503(b)(9) administrative claim demand letter (time is of the essence with these letters). A reclamation letter demands the return of goods shipped to the customer within 45 days before bankruptcy. A 503(b)(9) claim is a claim for payment in full of all goods shipped to the customer in the ordinary course of business within 20 days before bankruptcy.
- ❑ Perform a preference analysis to determine your risk of exposure and to understand your defenses.
- ❑ Review your customer's credit file to determine whether a personal guarantee exists. Consider providing the guarantor(s) with immediate notice.



### Restructuring, Bankruptcy & Creditors' Rights Group

Louis T. DeLucia  
212-753-7853  
ldelucia@schiffhardin.com

Patricia J. Fokuo  
312.258.5657  
pfokuo@schiffhardin.com

Tiffany R. Redding  
312.258.5529  
tredding@schiffhardin.com

Jon C. Vignano  
312.258.5792  
jvignano@schiffhardin.com

Alyson M. Fiedler  
212-745-9531  
afiedler@schiffhardin.com

Eugene J. Geekie, Jr.  
312.258.5635  
egeekie@schiffhardin.com

Heidi H. Rowe  
312.258.5534  
hrowe@schiffhardin.com

John S. Worden  
415.901.8764  
jworden@schiffhardin.com

J. Mark Fisher  
312.258.5710  
mfisher@schiffhardin.com

Barry S. Hyman  
312.258.5721  
bhyman@schiffhardin.com

Jason M. Torf  
312.258.5791  
jtorf@schiffhardin.com