

DEBTOR/CREDITOR

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Payment to Subcontractor Recovered

Construction subcontractors are often protected by performance bonds to ensure payment. An unpaid subcontractor can collect from the bonding company. The bonding company's obligation is typically secured by the assets of the general contractor. Thus, the subcontractor is paid by a third party with a superior ability to collect.

A general contractor paid a subcontractor within 90 days prior to filing a bankruptcy petition. The bankruptcy trustee sought to recover the payments as preferences.

The subcontractor defended, arguing that it had given contemporaneous equivalent value for the payment, because the payment extinguished the subcontractor's claim against the bond. Absent the payment from the general contractor, the subcontractor would have been paid from the bond, and the bonding company would have recouped the funds from the general contractor.

A federal appeals court in Richmond rejected the subcontractor's argument, reasoning that the release of the potential bonding company claim against the general contractor was "given" by a third party that was not even aware of the transaction. The subcontractor did not give anything in exchange for the payment it received. *Untied Rentals, Inc. v. Angell*, 592 F.3d 525 (4th Cir. 2010).

Contract Breach Not Discharged

Dr. Garritano was employed by a hospital to operate a health clinic. Under his employment agreement, he was required to collect fees from patients, subtract the expenses of running the clinic and remit the balance to the hospital monthly, together with a report of the revenue and expenses.

Dr. Garritano submitted the monthly reports, but did not send the money. After the hospital terminated his employment, he filed a bankruptcy petition. The hospital

objected to the discharge of the amounts he owed to it, arguing that he caused intentional injury to the hospital.

The bankruptcy judge conceded that claims for breach of contract normally are discharged. However, because the doctor unjustifiably withheld the money he should have turned over, he intended to harm the hospital.

Humility of Mary Health Partners v. Garritano (In re Garritano), 427 B.R. 602 (Bankr. N.D. Ohio 2009).

Bankruptcy to Prevent Successor Liability

If the owner of an insolvent corporation transfers the corporate assets to a new corporation to conduct the same business, the new corporation will be liable for the debts of the old corporation under the theory of "successor liability". A bankruptcy trustee can sell assets free and clear of all creditor claims, including those for successor liability. Is it proper for an owner to use a Chapter 7 case to eliminate successor liability claims through his new corporation's purchase of the assets from the trustee?

A North Carolina bankruptcy judge answered in the affirmative. In order to obtain the maximum value from the sale of assets, the trustee and the court must be able to protect any purchaser from claims of the old corporation's creditors. Even where the purchaser is affiliated with the owner of the debtor company, there is no reason to deny that protection.

In re Remember Enterprises, Inc., 425 B.R. 757 (Bankr. M.D.N.C. 2010).



This newsletter is intended to inform its readers of developments in the area of debtor/creditor relations. It is not legal advice or a legal opinion regarding any specific matter. You should consult a lawyer regarding any questions relating to your particular situation.

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