

What Is an Executory Contract and What Will Happen to My Executory Contract in Bankruptcy?

Creditor's Rights Toolkit

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This article discusses what may happen to your executory contract during a bankruptcy case.

An executory contract is a contract where both the debtor and the contract counterparty have material ongoing performance obligations.

WHAT WILL HAPPEN TO MY EXECUTORY CONTRACT?

At a high level, a debtor can (1) assume (*i.e.*, retain) the contract (or assume and assign the contract to a third party) provided that the debtor/third party cures any default under the contract and provides adequate assurance of future performance or (2) reject the contract, with rejection being treated as a pre-petition breach of the contract and any damages constituting a general unsecured claim in the debtor's bankruptcy case. Until the debtor either rejects the contract or the court enters an order granting relief, the non-debtor contract counterparty must continue to perform under the contract.

KEY ISSUES

LEVERAGE

Whether a contract counterparty wants the contract assumed or rejected will depend on the facts of the case. It is important to work with experienced bankruptcy counsel to understand leverage points to achieve the contract counterparty's end goal.

NOTICE

The debtor must provide written notice when seeking certain contract-related relief from the Bankruptcy Court, such as assumption, assignment, rejection, or determination of cure amounts, among other things. The time for objecting to that notice may be very short, and if no objection is timely filed, the contract counterparty may waive important rights. Any bankruptcy papers you receive should be reviewed immediately to assess how they may affect your rights.

CURE CLAIM

Before assumption can occur, the contract counterparty will receive notice of the proposed amount needed to cure any default. It is important to carefully review the notice and ensure that the cure claim includes all amounts owed or coming due and not just the amount owed as of the date of the notice and to promptly file an objection with the bankruptcy court regarding any disagreement. Failure to do so may result in the contract counterparty only receiving the amount listed in the notice.

ADEQUATE ASSURANCE INFORMATION

Often what is provided is high level, general, and vague. As such, a contract counterparty may need to promptly file an objection with the bankruptcy court demanding greater clarity to determine adequate assurance.

REJECTION DEADLINE

If the debtor decides to reject the contract, then the contract counterparty must timely file a claim in the bankruptcy case for damages. Failure to timely file a claim can result in a waiver of the rejection claim.

TAKEAWAY

Bankruptcy cases move fast, and a contract counterparty may only have a few days to a few weeks to address issues related to its contract. As such, it is critical that a contract counterparty work with experienced bankruptcy counsel to carefully monitor the case and react timely to protect its rights.

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