

### Two New Judges, Two New Opinions: Too Bad for 503(b)(9) Suppliers

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Two judges appointed to the bankruptcy bench in 2006, Hon. **Kevin Gross** in the District of Delaware and Hon. Eric L. Frank in the Eastern District of Pennsylvania, recently handed down what appear to be some of the first decisions to apply §503(b)(9) of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA).<sup>1</sup> Although the new Code section appears to give suppliers new rights and claims, the recent opinions suggest that claims delayed may be claims denied.

BAPCPA created §503(b)(9) of the Bankruptcy Code, which enables creditors who sell goods to debtors in the ordinary course of business within 20 days before the filing of a bankruptcy petition to assert an administrative expense claim. Specifically, the new section provides:

After notice and a hearing, there shall be allowed administrative expenses other than claims allowed under §502(f) of this title, including...

(9) the value of any goods received by the debtor within 20 days before the date of commencement of a case under this title in which the goods have been sold to the debtor in the ordinary course of such debtor's business.

11 U.S.C. §503(b)(9).

Clearly, the elevation of a supplier's claim is a marked improvement over the treatment such claims received under the prior law, where they were simply classified as general, pre-petition claims, which may not be paid in full pursuant to a confirmed reorganization plan. When Congress transformed these claims into coveted administrative claims, it could have completely altered suppliers' treatment by expressly stating that they were also entitled to immediate payment. However, as noted in a recent *ABI Journal* article,<sup>2</sup> §503(b)(9) does not address *when* such claims should be paid. As practitioners know, when a creditor gets paid may very well translate into *whether* a creditor gets paid. Consequently, suppliers and practitioners have been left wondering if Congress intended to give 20-day claimants priority with respect to payment of their claims in addition to the priority in the character of their claims, or if such claims would be paid in connection with the confirmation of a reorganization plan, if confirmation ever occurs.

Reading §503(b)(9) very broadly, suppliers have tried to seek allowance and immediate payment of their claims, hoping to capitalize on the statute's silence, but the recent decisions have rebuffed their efforts.

In *Global Home Products*, Judge Gross considered whether Congress intended to create an immediate right to payment in connection with §503(b)(9) when a 20-day creditor filed a motion for allowance and immediate payment of its §503(b)(9) claim. In its opposition to the motion, the debtor argued that there was no need to deviate from the established rule that administrative claims are payable upon the effective date of a confirmed reorganization plan.

The court noted that the decision regarding the timing of payment of administrative expense claims is normally left to the discretion of the courts. Judge Gross explained that in making the determination regarding the timing of payment of administrative claims, “one of the chief factors courts consider is bankruptcy’s goal of an orderly and equal distribution among creditors and the need to prevent a race to a debtor’s assets.” *Global Home Products, slip op.* at \*3 citing *In re HQ Global Holdings Inc.*, 282 B.R. 169 (Bankr. D. Del. 2002).

To determine if the supplier should be entitled to immediate payment of its §503(b)(9) claim, Judge Gross adopted the three-pronged analysis from *Garden Ridge*. Judge Gross considered: (1) prejudice to the debtors, (2) hardship to the claimant and (3) potential detriment to other creditors. *Global Home Products, slip op.* at \*4.

In order to support its assertion that payment of this administrative claim should be deferred, the debtor offered the testimony of its chief restructuring officer (CRO), who testified that immediate payment of the claim would cause hardship to the debtor because, *inter alia*, it would negatively impact the debtor’s borrowing ability. The debtors did not have sufficient available funds to pay administrative claims, and available funds were needed to finance the debtor’s continuing operations. In response, the supplier did not present testimony regarding the hardship it would suffer if it did not receive immediate payment. Rather, the claimant merely argued that the disparity between its treatment and that of certain critical vendors was tantamount to discrimination among §503(b) creditors.

In weighing the evidence, Judge Gross found the CRO persuasive regarding the potential prejudice to the debtor if the administrative expense claim was to be paid immediately. The court concluded that the prejudice to the debtors outweighed any prejudice to the claimant, and denied the motion for immediate payment. The court also noted that its decision benefits other creditors because it preserves an equitable distribution to other administrative claimants at a later date. Further, the court was concerned that granting one §503(b)(9) supplier’s request for immediate payment might cause a snowball effect on the other debtor’s cash flow suppliers who either have already filed motions or were entitled to do so.

Like Judge Gross, Judge Frank confronted an aggressive supplier asserting its §503(b)(9) rights in the *Bookbinders’ Restaurant* case. In an opinion issued merely one week after *Global Home Products*, Judge Frank also denied the supplier’s request for immediate payment.

Judge Frank held that the timing for payment of §503(b)(9) claims was within the discretion of the bankruptcy court. The court concluded that nothing in the language of §503(b)(9), neither expressed or implied, entitled a claimant to immediate payment. Like Judge Gross, Judge Frank found that the court should exercise its discretion guided by considerations of prejudice to the debtor, hardship to the claimant and the potential detriment to other creditors. *Bookbinders’ Restaurant Inc., slip op.* at \* 1.

The §503(b)(9) supplier argued that it should be paid immediately because the debtor was paying post-petition trade creditors in the ordinary course and it maintained that it should not be treated differently than those creditors. The court rejected the claimant's "equal protection" argument, noting that the supplier had offered no support for its contention that a §503(b) claimant had a right to be paid contemporaneously with post-petition creditors paid in the ordinary course. Specifically, the court stated that the claimant:

has presented no authority supporting the proposition that a holder of an administrative expense allowed under §503(b) has an unqualified legal entitlement to be paid at the same time as post-petition creditors who are being paid in the ordinary course pursuant to 11 U.S.C. §363(c)(1). Indeed, such a holding would be contrary to the cases discussed above which treat the subject of actual payment of allowed administrative expenses as a discretionary matter for the court. And, as I have previously observed, there is nothing in the text of §503(b)(9) or the legislative history that suggests a §503(b)(9) allowed administrative expense is entitled to more favorable treatment than other allowed administrative expenses so as to justify an exception to the general rule. That said, there might be circumstances in which it would be inequitable or inappropriate to permit a debtor to pay certain administrative expenses but not others. In such a case, the court can order the bankruptcy estate representative to pay the unpaid allowed administrative expenses. It is possible that this is such a case. However, before I can make that determination, a hearing is necessary so that the debtor's reasons for the disparate treatment can be aired.

*Bookbinders' Restaurant Inc., slip op. at \* 5.*

The court went on to clarify that such post-petition creditors are paid pursuant to §363(c)(1), not §503(b)(1). The court further explained that the treatment of §503(b)(9) claimants is consistent with that of unpaid, allowed §503(b) administrative expense claims, which is precisely the treatment that the post-petition creditors would receive if they were not paid by the debtor.

## **Conclusion**

The decisions suggest that (1) courts may be reluctant to read §503(b)(9) to confer onto claimants a right to immediate payment absent extraordinary facts that compel, and finding that the supplier would be prejudiced beyond the usual harm caused by bankruptcy delays, and (2) that the question of the timing of the payment of an allowed administrative expense will continue to remain in the sound discretion of the court.

<sup>1</sup> *In Re Global Home Products LLC*, Case No. 06-10340, 2006 WL 3791955 (Bankr. D. Del. Dec. 21, 2006) and *In re Bookbinders' Restaurant Inc.*, Case No. 06-12302, 2006 WL 3858020 (Bankr. E.D. Pa. Dec. 28, 2006).

<sup>2</sup> Routh, Ryan T., "Twenty-day Claims: The Anticipated and Unanticipated Consequences of Code §503(b)(9)," *ABI Journal*, Vol. XXV, No. 9, p. 24, November 2006.