GRANTED

No. 99-409

IN THE
Supreme Court of the United States

HARTFORD UNDERWRITERS INSURANCE COMPANY,
Petitioner,
v.
MAGNA BANK, N.A.,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

BRIEF OF *AMICI CURIAE* AMERICAN INSURANCE ASSOCIATION AND NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PA. IN SUPPORT OF PETITIONER

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INTEREST OF THE *AMICI*

Amici curiae American Insurance Association ("AIA") and National Union Fire Insurance Company of Pittsburgh, Pa. ("National Union") respectfully submit this brief in support of the petitioner.[1]

[1] Pursuant to Supreme Court Rule 37.6, *amici curiae* state that no counsel for any party to this dispute authored this brief in whole or in part and no person or entity, other than *amici curiae* and AIA's member companies, made a monetary contribution to the preparation or submission of this brief. Petitioner Hartford Underwriters Insurance Company ("Hartford") is a member of *amicus curiae* AIA.

AIA is a national trade association consisting of over 375 property and casualty insurers. AIA's member companies write workers' compensation insurance throughout the country and account for approximately 42 percent of all such insurance sold by privately-owned insurers. National Union is one of the largest workers' compensation insurers in the country, with direct written premiums of nearly $400 million in 1998. National Union is a member company of American International Group, whose members wrote $1.3 billion in direct premiums for workers' compensation insurance during that same period. AIA has frequently participated as *amicus curiae* in litigation raising issues of importance to workers' compensation insurers.

AIA's members and National Union have a substantial interest in this case because it will determine whether they have an effective remedy for nonpayment of premiums for workers' compensation insurance sold to employers in bankruptcy proceedings. Every state except Texas requires employers, in order to finance workers' compensation benefits paid to injured employees, to purchase workers' compensation insurance or to self-insure. Insolvent businesses do not qualify to self-insure and, if they fail to purchase insurance, may be shut down by state labor departments. Thus, in order for a bankrupt business to continue in operation and attempt to reorganize successfully under chapter 11 of the Bankruptcy Code, it must purchase workers' compensation coverage.

Insurers, however, will be unwilling to underwrite such insurance for an insolvent employer unless there are adequate remedies for collecting premiums where the debtor does not or cannot pay (as occurred in this case). Insurers that write post-petition coverage for bankrupt employers are unsecured creditors. Frequently, the debtor has few if any unencumbered assets out of which to pay unsecured creditors. *See, e.g., United States v. Ron Pair*

Enters., Inc., 489 U.S. 235, 247 n.9 (1989) ("[I]t is not unusual for commercial lenders to obtain a lien on almost all of the debtor's property."). As a result, an insurer's recourse to the debtor's secured assets frequently is the only meaningful remedy for nonpayment of premiums.

The provision at issue in this case, section 506(c) of the Bankruptcy Code, 11 U.S.C. § 506(c) (1994), affords such a remedy. It allows workers' compensation insurers providing post-petition coverage to recover, as claimants for administrative expenses, unpaid premiums out of the debtor's secured assets to the extent the insurance preserves or enhances that collateral. Workers' compensation insurance coverage usually protects the secured creditor's collateral because it facilitates the employer's reorganization as an ongoing business, which tends to maximize the value of its assets. In this case, for example, workers' compensation insurance sold by petitioner Hartford allowed the debtor to continue in business for a period of time sufficient to enable it to sell off parts of the enterprise as viable businesses.

The decision of the Eighth Circuit deprives insurers of any meaningful remedy under section 506(c). Insurers (as well as other administrative expense claimants) are prohibited from seeking an order directly from the bankruptcy court requiring payments out of the secured collateral. Instead, the insurer is placed at the sufferance of the trustee's discretion in deciding whether to pursue the insurer's claim. Unlike the insurance carrier, the trustee has no economic incentive to seek payment aggressively. By the time of nonpayment, the insurance already has been provided and, under the Bankruptcy Code, the trustee generally will take the position that the insurance may not be canceled regardless of nonpayment absent relief by the bankruptcy court from the automatic stay. *See* 11

U.S.C. § 362(a) (1994). Additionally, under state insurance law, nonpayment of premium does not relieve the carrier of its obligation to pay benefits for injuries occurring while the policy was in force, even though the insurer has no premium dollars funding the payment of such claims.

AIA and National Union thus seek reversal of the decision below in order to restore to insurers a remedy that was well-established decades ago under pre-Bankruptcy Code practice and that Congress intended to preserve when it adopted section 506(c).[2]

SUMMARY OF ARGUMENT

A debtor's insolvency obviously creates a high risk that post-petition vendors to the debtor will not be paid. Two provisions of the Bankruptcy Code alleviate this risk and thereby encourage suppliers to provide goods and services necessary to preserve the debtor's assets. Section 503(b)(1)(A) gives priority to the payment of "administrative expenses" including "the actual, necessary costs and expenses of preserving the estate . . . ." 11 U.S.C. § 503(b)(1)(A) (1994). However, because the debtor frequently has insufficient unsecured assets out of which to pay such administrative expenses, section 506(c) provides for recovery from the debtor's secured assets of "the reasonable, necessary costs and expenses of preserving, or disposing of, [the secured] property to the extent of any benefit to the holder of such claim." 11 U.S.C. § 506(c) (1994).

Notwithstanding that the very purpose of section 506(c) is to protect the claimant's right to recover administrative

[2] Both petitioner and respondent have consented to the filing of this brief, and their joint letter of consent has been filed with the Office of the Clerk of this Court.

expenses, the Eighth Circuit in this case denied the claimant its remedy of direct recourse to the bankruptcy court and instead gave the trustee exclusive power to decide whether to pursue the claim for expenses. *Hartford Underwriters Ins. Co. v. Magna Bank, N.A. (In re Hen House Interstate, Inc.)*, 177 F.3d 719 (8th Cir. 1999) ("*Hen House*"). The lower court reasoned that the statute's reference to "[t]he trustee" but the omission of any explicit reference to the administrative expense claimant made it clear that "only" the trustee could pursue the claim. *Id.* at 722.

The fundamental flaw in the lower court's decision was its failure to consider the pre-Bankruptcy Code practice in the area of administrative expenses. Congress intended that the Code preserve prior bankruptcy practice except in specific instances where it desired to make a change. Accordingly, in interpreting the Code, this Court has presumed that Congress continued " 'past bankruptcy practice absent a clear indication that Congress intended . . . a departure. . . .' " *Cohen v. De La Cruz*, 523 U.S. 213, 221 (1998) (quoting *Pennsylvania Pub. Welfare Dep't v. Davenport*, 495 U.S. 552, 563 (1990)).

In this case, continuity is not a mere presumption but an expressly-stated legislative purpose. The authors of section 506(c) intended it to "codif[y] current law." H.R. Rep. No. 95-595, at 357 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5787, 6313. This Court thus has recognized that "[t]he Code rule on administrative expenses merely continues pre-Code law." *United Sav. Ass'n v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 379 (1988).

The pre-Code practice contradicts the lower court's interpretation of section 506(c). Claimants for administrative expenses long have been permitted to present their

claims directly to the bankruptcy court rather than through the trustee. *See, e.g., Louisville, Evansville & St. Louis R.R. v. Wilson*, 138 U.S. 501 (1891). The rationale of these decisions was the same as for present day section 506(c): "The most elementary notion of justice would seem to require that services or property furnished" for the "benefit" of property held as collateral "should be paid from" such property "as an 'expense of justice.'" *New York Dock Co. v. S.S. Pozman*, 274 U.S. 117, 121 (1927) (citation omitted).

There is nothing in the language of section 506(c) that unambiguously reflects any congressional intention to change this pre-Code practice. To the contrary, Congress itself characterized that language as preserving the pre-Code practice.

What the Eighth Circuit characterized as the "plain meaning" of section 506(c) is really an application of the maxim of statutory interpretation known as *expressio unius est exclusio ulterius*. From the reference to "trustee," the lower court inferred an intention to exclude all others—including the claimants for administrative expenses whose interests are protected by this provision. But the *expressio unius* inference is merely one among many tools of statutory construction. It does not, in itself, discern a statute's plain meaning where other interpretive tools such as pre-Code practice, legislative history and the statutory purposes suggest a contrary interpretation. At worst, the language of section 506(c), properly read in the context of other Code provisions, is ambiguous on the question of a direct remedy for administrative expense claimants. In such instances, this Court consistently has referred to the pre-Code practice, not inferences from inexact statutory language, as the best indicator of legislative intent. That pre-Code practice unambiguously supports the right

of claimants to petition the bankruptcy court directly for payment out of secured assets.

ARGUMENT

I. THERE IS A PRESUMPTION THAT THE BANKRUPTCY CODE CONTINUED PRE-CODE PRACTICE THAT CAN BE OVERCOME ONLY BY UNAMBIGUOUS STATUTORY LANGUAGE TO THE CONTRARY

This Court has crafted a specific rule for interpretation of the Bankruptcy Code. There is a presumption that Congress intended to preserve pre-Code practice unless the applicable provision unambiguously indicates to the contrary. This rule derives from the legislature's intent to maintain continuity in the national bankruptcy system.

"The present text of Title 11, commonly referred to as the Bankruptcy Code, was enacted in 1978 to replace the Bankruptcy Act of 1898 . . . ." *Kelly v. Robinson*, 479 U.S. 36, 44 (1986). Although the Code made many changes in the prior provisions, its purpose otherwise was to preserve the existing bankruptcy system. In order to effectuate this policy of continuity, this Court has refused to " 'read the bankruptcy code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure . . . .' " *Cohen v. De La Cruz*, 523 U.S. at 221 (quoting *Pennsylvania Pub. Welfare Dep't v. Davenport*, 495 U.S. at 563).

In order to overcome this presumption of continuity, the Court has required that the language of the provision in issue be so unambiguous as to compel a result contrary to pre-Code practice. *See United Sav. Ass'n*, 484 U.S. at 380 ("[A] major change in the existing rules would not likely have been made without specific provision in the text of the statute . . . ."); *Kelly v. Robinson*,

479 U.S. at 47 (declining "to hold that the new Bankruptcy Code silently abrogated" judicial decisions "construing the old Act").

To be sure, there have been many differences of opinion concerning whether particular statutory language is so clear-cut as to require a divergence from pre-Code practice. *See, e.g., Dewsnup v. Timm*, 502 U.S. 410 (1992); *Ron Pair Enters.*, 489 U.S. 235. But those decisions finding the statutory language to be ambiguous invariably have looked to the pre-Code practice as the principal guide for interpretation. *See Bank of Am. Nat'l Trust & Sav. Ass'n v. 203 North LaSalle St. Partnership*, 119 S.Ct. 1411, 1417 (1999) ("history is helpful" in understanding the "inexact language of the Code"); *see also Midlantic Nat'l Bank v. New Jersey Dep't of Environmental Protection*, 474 U.S. 494 (1986); *Kelly v. Robinson*, 479 U.S. 36; *United Sav. Ass'n*, 484 U.S. 365. This rule of statutory construction applies in construing section 506 equally as it does in interpreting other provisions of the Code. *See United Savings Ass'n*, 484 U.S. 365 (construing section 506(b)); *Dewsnup v. Timm*, 502 U.S. 410 (construing section 506(d)).

Accordingly, in determining whether section 506(c) permits a claimant to present its claim directly to the bankruptcy court, this Court's method of analysis is well-established. Pre-Code practice should be examined to determine if claimants for administrative expenses were, prior to 1978, permitted to pursue their claims directly. If so, then Congress is presumed to have preserved that remedy unless language in section 506(c) unambiguously indicates that the legislature intended to nullify prior law.

II. UNDER PRE-CODE PRACTICE CODIFIED IN SECTION 506(c), THIRD PARTIES HAD A DIRECT REMEDY FOR RECOVERY OF THEIR EXPENSES FROM SECURED COLLATERAL

"Section 506(c) was intended by Congress as a codification of the long, but somewhat inconsistent, line of cases decided under (and, in some instances, prior to) the former Bankruptcy Act expressing and applying the equitable principle that a lienholder may be charged with the reasonable costs and expenses incurred by the estate that are necessary to preserve or dispose of the lienholders collateral to the extent that the lienholder derives a benefit as a result." 4 Lawrence P. King, *et al., Collier on Bankruptcy* ¶ 506.05, at 506-126 (15th ed. rev. 1999); *see also* H.R. Rep. No. 95-595, at 357, *reprinted in* 1978 U.S.C.C.A.N. at 6313; *United Sav. Ass'n*, 484 U.S. at 379 ("The Code rule on administrative expenses merely continues pre-Code law."). That "pre-Code law" allowed claimants who provided services during bankruptcy or receivership to bring claims directly against secured collateral.

This rule was established long ago. One of the earliest cases was *Louisville, Evansville & St. Louis R.R. v. Wilson*, 138 U.S. 501 (1891), where this Court authorized an attorney to recover $300 from the sale proceeds of collateral in payment for legal services that enabled the recovery and rental of train engines to the benefit of the security holders. The Court held that the attorney had a direct right of recovery against the property where the receiver lacked the capacity or will to pursue the claim:

> [W]hen he [the receiver] has not acted, and the question is presented to the court as to the liability of the property for any claim, the court is not foreclosed by the order of appointment [of the receiver],

> but may consider and determine equitably the extent of liability of the property to such claim, and what its rights of priority may be. Hence, as the receiver did not pay this claim, the parties in interest may rightfully challenge its priority, even if it were within the very letter of the order of appointment of the receiver.

Id. at 506. The rationale for this rule under pre-Code practice was the very same unjust enrichment principle as embodied in section 506(c): "We think it may fairly be held that the [secured] party who takes the benefit of such a service [by an administrative claimant] ought to pay for it; and that equity may properly decree payment therefor." *Id.* at 507.

A similar ruling was made in *In re Rotary Tire & Rubber Co.*, 2 F.3d 364 (6th Cir. 1924). Brokers who provided insurance during the bankruptcy sought direct recovery of premiums against the sale proceeds of the insured property, even though the property was subject to a $35,000 mortgage. *Id.* at 364. The lower court held, and the Sixth Circuit affirmed, that the brokers were entitled to priority for premiums because the insurance preserved the value of the mortgaged property. *Id.*[3]

[3] Other pre-Code decisions also allowed claimants other than the trustee to bring claims directly against secured property. *See, e.g., National Acceptance Co. v. District No. 1, Progressive Mine Workers of Am. (In re Chapman Coal Co.)*, 196 F.2d 779, 781 (7th Cir. 1952) (union brought successful petition to obtain first lien on previously-secured assets of corporation for wages incurred to preserve the assets); *County of Clark v. United States*, 284 F.2d 885, 886 (9th Cir. 1960) (court did not question right of county to seek recovery of tax claim from sale proceeds subject to tax lien of United States, but denied recovery to county on the basis that taxes were "of no benefit to the United States"); *First W. Sav. & Loan Ass'n v. Anderson*, 252 F.2d 544, 550 (9th Cir. 1958) (court held that attorney as well as trustee entitled to first lien on secured property for fees for services rendered); *United States v. Henderson*, 274 F.2d 419, 422 (5th Cir. 1959) (both trustee and attorneys were parties to action for recovery of fees from mortgagee's collateral); *In re Louisville Storage Co.*, 21 F. Supp. 897 (W.D. Ky. 1936), *aff'd*, 93 F.2d 1008 (6th Cir. 1938) (employee of debtor prevailed in his request seeking to charge his wages against the lienholder, as did trustee and attorneys who sought recovery of their fees and expenses); *Citizens & Southern Nat'l Bank v. Mullins (In re Bolton Rd. Med. Ctr.)*, 433 F. Supp. 369, 371 (N.D. Ga. 1976) (both trustee and his attorneys were parties to proceeding for recovery of expenses against secured property); *In re Alaska Plywood Corp.*, 166 F. Supp. 423, 425 (D. Alaska 1958) (both trustee and stockholders committee requested and received priority against mortgaged assets superior to that of secured creditors).

The pre-Code rule in bankruptcy was itself based on a more general principle that "the cost of protecting a fund in court is everywhere recognized as a dominant charge on that fund." *Adair v. Bank of Am. Nat'l Trust & Sav. Ass'n*, 303 U.S. 350, 360-61 (1938). This principle "applies even in ordinary bankruptcy proceedings since the secured creditor benefits from the disbursement." *Id.* at 361 (footnote omitted). The Court has described the power to charge expenses against court-protected property as "an *in rem* jurisdiction springing from possession of the property which is necessary in order that the court may adequately care for the property." *Warren v. Palmer*, 310 U.S. 132, 139 (1940).

In applying this longstanding principle outside of bankruptcy, this Court did not limit the remedies for recovery to actions by court representatives on behalf of the claimant but also allowed the claimant to proceed directly against the secured parties whose collateral was benefited. *New York Dock Co. v. S.S. Poznan*, 274 U.S. 117 (1927), is an exemplar of this direct remedy. A vessel with cargo was seized by a United States marshal and held in his custody while docked at a wharf. The wharf owner then sought recovery of payment for his services from the proceeds of the ship's sale. Respondents, the

owners of the cargo who held liens on the ship, objected. *Id.* at 118-19.

Reversing the Second Circuit, the Court held that the wharf owner was entitled to preferential payment from the proceeds prior to any distribution to the lienholders:

> The most elementary notion of justice would seem to require that services or property furnished upon the authority of the court or its officer, acting within his authority, for the common benefit of those interested in a fund administered by the court, should be paid from the fund as an 'expense of justice.'

Id. at 121 (citation omitted). For present purposes, the salient feature of the Court's holding was its permission for the wharf owner to bring its claim directly rather than through the government official who administered the collateral (the marshal). The Court emphasized that it was applying the "familiar rule of courts of equity when administering a trust fund or property *in the hands of receivers.*" *Id.* (emphasis added).

In sum, the pre-Code bankruptcy practice, derived from general equity practice, allowed administrative expense claimants such as Hartford to proceed directly to bankruptcy court to obtain payment out of the collateral of secured creditors so long as the goods or services provided by the claimant had protected that collateral. This was an integral feature of the pre-1978 practice that Congress intended to preserve in section 506(c).

III. THE LANGUAGE OF SECTION 506(c) REFLECTS NO INTENTION TO RESTRICT PRE-CODE PRACTICE ON CLAIMANT REMEDIES

Nothing in the language or history of section 506(c) provides any indication that Congress desired to deny claimants a direct remedy for recovery of administrative

expenses even though they had such a remedy under prior law. The legislative history, far from evidencing any intention of changing prior law, indicates that Congress intended to preserve it. Nor does the plain meaning of the statutory language, read in the context of related provisions, compel a conclusion at odds with the pre-Code practice and legislative history.

The Eighth Circuit's decision is premised almost entirely on the canon of statutory construction referred to as *expressio unius est exclusio alterius.* The lower court read the reference in section 506(c) to the trustee, combined with the failure to explicitly mention the claimants on whose behalf the trustee acted, as making it "clear and unambiguous" that the claimant lacks a direct remedy. *Hen House*, 177 F.3d at 723. In reaching that conclusion, the Eighth Circuit erroneously elevated one among many tools of statutory construction to trump other maxims of legislative construction that point to a contrary interpretation.

Expressio unius is nothing more than a possible negative inference to be drawn from the mention of one thing but not another. But "[n]ot every silence is pregnant" and thus *expressio unius* is not an absolutist rule of statutory construction. *Illinois Dep't of Public Aid v. Schweiker*, 707 F.2d 273, 277 (7th Cir. 1983); *see also El Paso Natural Gas Co. v. Neztsosie*, 119 S. Ct. 1430, 1439 (1999) ("[n]ow and then, silence is not pregnant"). For instance, this Court has held that maxims such as *expressio unius* have " 'long been subordinated to the doctrine that courts will construe the details of an Act in conformity with its dominating general purpose.' " *Herman & MacLean v. Huddleston*, 459 U.S. 375, 387 n.23 (1983) (citation omitted): *see also El Paso Natural Gas Co. v. Neztsosie*, 119 S. Ct. at 1438 (rejecting "most zealous

application of the maxim *expressio unius est exclusio alterius*").

Expressio unius is, rather, only one of several methods available to interpret section 506(c). *See, e.g., Lindh v. Murphy*, 521 U.S. 320, 337 (1997) (Rehnquist, C.J., dissenting) (criticizing majority decision because it "relies on one canon of statutory interpretation, *expressio unius est exclusio alterius*, to the exclusion of all others"). In addition to ignoring pre-Code practice, the Eighth Circuit failed to consider other principles of statutory construction that regularly have been applied by the Court in bankruptcy cases. In particular, " '[w]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion.' " *Bates v. United States*, 522 U.S. 23, 29-30 (1997) (quoting *Russello v. United States*, 464 U.S. 16, 23 (1983)).

There are several provisions in the Bankruptcy Code where Congress inserted the term "only" to restrict the eligibility of parties to participate in bankruptcy proceedings. For example, with respect to the most important eligibility question under bankruptcy law—who may be a debtor—section 109(a) provides that "*only* a person that resides or has a domicile, a place of business, or property in the United States, or a municipality, may be a debtor under this title." 11 U.S.C. § 109(a) (1994) (emphasis added). Subsection (b) through (f) of section 109, which define the entities that are eligible for relief under the various chapters of the Bankruptcy Code, also uniformly use the word "only" to restrict eligibility. 11 U.S.C. § 109(b)-(f). Similarly, section 321(a), governing eligibility of trustees, states that "[a] person may serve as trustee in a case under this title *only* if such person" meets the requirements set forth therein. 11 U.S.C. § 321(a) (emphasis added). And section 702(a) provides that "[a] creditor may vote for a candidate for trustee *only* if such creditor" meets various requirements. 11 U.S.C. § 702(a) (emphasis added).

Sections 109, 321 and 702 illustrate that Congress used the term "only" when it wanted to be clear about its exclusion of all but the named parties from eligibility for coverage under the Code. Undoubtedly, this was because the plain meaning of "only" is exclusionary, that is, the term is synonymous with "solely" or "exclusively." *Webster's Third New International Dictionary* 1577 (1981); *see also Black's Law Dictionary* 1089 (6th ed. 1990) ("only" means "solely," "exclusive," "nothing else or more").

Congress' approach when it wanted to limit remedies or eligibility is confirmed by its selective usage of the term "only." The word "only" did not appear in any of the Bankruptcy Act provisions that were the predecessors to sections 109, 321 and 702(a). See 11 U.S.C. § 2a(1) (repealed); 11 U.S.C. § 45 (repealed); 11 U.S.C. § 44a (repealed). Congress' deliberate amendment of these provisions to insert the word "only" but its omission in others indicates a conscious decision to make the former provisions exclusive but the latter provisions nonexclusive. *Cf. Patterson v. Shumate*, 504 U.S. 753, 758 (1992) (when Congress meant to refer to state law under the Bankruptcy Code, it used the term "state law").

Thus, the omission of the modifier "only" when the trustee is mentioned in section 506(c) strongly suggests that Congress did not intend to limit the claimant from direct recourse to the bankruptcy court. Rather, if Congress had wanted to change pre-Code practice and deny a direct remedy to administrative expense claimants, "one would expect Congress to have made unmistakably clear

its intent to" do so by providing that "only" the trustee could seek recovery. *Cohen v. De La Cruz*, 523 U.S. at 222.

Another relevant maxim of statutory interpretation is that "equivalent words have equivalent meaning when repeated in the same statute." *Cohen v. De La Cruz*, 523 U.S. at 220 (citing *Ratzlaf v. United States*, 510 U.S. 135, 143 (1994)). For example, in *Patterson v. Shumate*, the Court noted that its construction of the term "applicable nonbankruptcy law" as used in section 541(c)(1), to include both federal and state law, "accords with prevailing interpretations of that phrase as it appears elsewhere in the Code." 504 U.S. at 758-59 n.2.

The "prevailing view" of other provisions of the Code worded similarly to section 506(c) is that non-trustees have the right to seek relief directly rather than through the trustee only. For example, the "avoidance" provisions of the Code uniformly provide that "*the trustee . . . may* avoid" various liens and transfers without express reference to any other party in interest. 11 U.S.C. §§ 544(a), 545, 547(b) (1994); 11 U.S.C.S. § 548(a) (Supp. 1999); 11 U.S.C. § 549(a) (1994) (emphasis added).[4] A majority of circuit courts, nevertheless, have held that creditors and their committees may bring such avoidance actions. *See Canadian Pac. Forest Prods. Ltd. v. J.D. Irving, Ltd. (In re Gibson Group, Inc.)*, 66 F.3d 1436, 1438 (6th Cir. 1995) (granting individual creditor right to bring suit under sections 547 and 548 to recover

[4] "Avoidance" provisions authorize recovery, on behalf of the bankruptcy estate, of certain improper or unauthorized transfers of money or liens made by a debtor to third parties. For example, § 547 authorizes the recovery of preferential transfers made within 90 days (or in the case of insiders, one year) before the bankruptcy petition. The other provisions cited above address unperfected liens (§ 544), statutory liens such as those for rent (§ 545), fraudulent transfers (§ 548) and unauthorized post-petition payments (§ 549).

preferential or fraudulent conveyances); *Coral Petroleum, Inc. v. Banque Paribas-London*, 797 F.2d 1351, 1362-63 (5th Cir. 1986) (unsecured creditors committee had right to bring action under section 547); *Unsecured Creditors Comm. of Debtor STN Enters., Inc. v. Noyes (In re STN Enters.)*, 779 F.2d 901, 904 (2d Cir. 1985) (committee had right to bring preference action); *Official Unsecured Creditors Comm. of Suffola, Inc. v. United States Nat'l Bank (In re Suffola, Inc.)*, 2 F.3d 977, 979 n.1 (9th Cir. 1993) (same).

Finally, this Court has held that *expressio unius* "cannot properly be applied to a situation . . . where the remedial purposes of the Act[] would be undermined by a presumption of exclusivity." *Herman & MacLean v. Huddleston*, 459 U.S. at 387 n.23. That would be true here. Section 506(c) is an exception to the general rule that "the expenses associated with administering a bankruptcy estate are not chargeable to a secured creditor's collateral or claim, but must be borne out of the unencumbered assets of the estate." *See* 4 Lawrence P. King, *et al.*, *Collier on Bankruptcy* ¶ 506.05, at 506-125. The purpose of this exception "is the prevention of a windfall to the secured creditor: a secured creditor should not reap the benefit of actions taken to preserve the secured creditor's collateral without paying the cost." *Id.*

That purpose would be thwarted if the party protecting the collateral cannot sue directly to recover payment but must rely on the trustee's discretionary decision to assert the claim. The trustee lacks the same economic incentive as the claimant to pursue recovery. "[I]f the trustee does not have available funds to pay the claimant, the trustee has no economic incentive to seek a recovery under Section 506(c) with respect to amounts that will be paid over to the claimant. As a result, the secured creditor may

obtain a windfall at the expense of the unpaid claimant." 4 Lawrence P. King, *et al.*, *Collier on Bankruptcy*, ¶ 506.05, at 506-142-43.

This case is an example of this disincentive. The trustee had little reason to press Hartford's claim because the automatic stay provision in section 362 may have prevented Hartford from canceling the insurance and because Hartford was obligated to pay claims under the policy even in the event of nonpayment of premium. An interpretation of section 506(c) as precluding the claimant from asserting its claim in bankruptcy court would thus be inconsistent with the equitable principle underlying this provision—prevention of unjust enrichment. *See Kelly v. Robinson*, 479 U.S. at 49 ("There is an overriding consideration that equitable principles govern the exercise of bankruptcy jurisdiction.").

Conversely, an interpretation of section 506(c) as denying a direct remedy to claimants is not necessary, as the lower court reasoned, to prevent preferential treatment of one claimant compared to other claimants or other unsecured creditors. *Hen House*, 177 F.3d at 723; *see also Ford Motor Credit Co. v. Reynolds & Reynolds Co. (In re JKJ Chevrolet, Inc.)*, 26 F.3d 481, 484 (4th Cir. 1994). The Code expressly affords the administrative expense claimant a priority over pre-petition unsecured creditors. 11 U.S.C. § 507(a).

Nor would affording a direct remedy to claimants such as Hartford give them a preference over other administrative expense claimants not contemplated by the Code. Numerous bankruptcy courts have recognized that, "from a practical standpoint," equality of treatment among administrative claimants "does not exist." *In re Vernon Sand & Gravel, Inc.*, 109 B.R. 255, 257 (Bankr. N.D. Ohio 1989). This is because so-called "operational payments" made by the trustee or debtor in the ordinary

course of business—for example, for employee wages, utilities, supplies and taxes—are paid in full during the course of the bankruptcy proceeding. *Id.*; *see also In re Lochmiller Indus., Inc.*, 178 B.R. 241, 247 (Bankr. S.D. Cal. 1995); *Guinee v. Toombs (In re Kearing)*, 170 B.R. 1, 7 (Bankr. D.D.C. 1994); *In re Telesphere Communications, Inc.*, 148 B.R. 525, 531 (Bankr. N.D. Ill. 1992). Such payments are treated as final and not subject to later disgorgement; otherwise, if these expenses were subject to a pro-rata reduction, businesses operating under chapter 11 could not retain employees, use outside vendors or pay for utilities. *Vernon Sand & Gravel*, 109 B.R. at 257. The result is a "de facto" preference for operational payments, which are paid in full when services are rendered, over other administrative expenses. *Telesphere Communications*, 148 B.R. at 531. Indeed, if the insurance premiums owed to Hartford had been paid in a timely manner, there would have been no question that Hartford would have been entitled to keep the money—notwithstanding any inequality of treatment that would have resulted.

More generally, concerns about preferential treatment do not apply where the source of the funds to pay the claimant is secured collateral rather than unencumbered assets, as is the case under section 506(c). The principle of equitable distribution applies only to distribution of *unencumbered* assets, and not to the proceeds of *collateral*. *See, e.g., United Sav. Ass'n v. Timbers of Inwood Forest Assocs., Ltd. (In re Timbers of Inwood Forest)*, 793 F.2d 1380, 1387 (5th Cir. 1986), *aff'd*, 484 U.S. 365 (1988). This in part explains why creditors with oversecured claims are entitled to recover interest (which comes from collateral) notwithstanding preferential treatment of the secured creditor while undersecured creditors are not since the payment would come from unencumbered assets to the detriment of other unsecured creditors.

Cf. Ticonic Nat'l Bank of Sprague, 303 U.S. 406, 411-12 (1938) (holding that doctrine of equal distribution does not apply when source of payment is *res* subject to lien rather than unencumbered assets).

In summary, the lower court's exclusive reliance on *expressio unius* was misplaced for several reasons. The inference of exclusionary intent is inconsistent with the more explicit wording Congress used in other Code provisions where it wanted to restrict the rights of a party in interest. The Eighth Circuit's reading also squarely conflicts with the equitable and remedial objective of section 506(c), which was to insulate volunteer sellers to the debtor from the risk of nonpayment. Of most importance, nothing in the language of section 506(c) contradicts Congress' stated intent of preserving pre-Code practice, including the direct remedy afforded to administrative expense claimants.

CONCLUSION

The judgment of the Eighth Circuit should be reversed.

Respectfully submitted,

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