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No. 21-0909

IN THE SUPREME COURT OF THE UNITED STATES

IN RE TERRAPIN STATION, LLC, *DEBTOR*,

TOUCH OF GREY ROASTERS, INC., *PETITIONER*

v.

CASEY JONES, CHAPTER 7 TRUSTEE, *RESPONDENT*.

ON WRIT OF CERTIORARI FROM THE UNITED STATES

COURT OF APPEALS FOR THE THIRTEENTH CIRCUIT

BRIEF FOR RESPONDENT

QUESTIONS PRESENTED

I. Whether a seller of goods is entitled to reduce its preference exposure pursuant to 11 U.S.C. § 547(c)(4) by the value of goods sold even though that seller of goods has been paid in full for such goods pursuant to 11 U.S.C. § 503(b)(9).

II. Whether a trustee must pay rent due prior to the rejection of an unexpired non-residential real property lease but allocable to the period after the rejection date for a debtor who both ceased operations and vacated the premises on the rejection date under 11 U.S.C. § 365(d)(3).

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OPINIONS BELOW

The Bankruptcy Court for the District of Moot answered both questions presented in favor of Respondent. Petitioner timely appealed both decisions on a consolidated basis to the United States District Court for the District of Moot. The district court affirmed on both issues. On appeal, the United States Court of Appeals for the Thirteenth Circuit affirmed the Bankruptcy Court's decision in favor of Respondent.

STATEMENT OF THE JURISDICTION

The formal statement of jurisdiction is waived pursuant to Competition Rule VIII.

PERTINENT STATUTORY PROVISIONS

The relevant portion of 11 U.S.C. § 547(c)(4) provides:

(c) The trustee may not avoid under this section a transfer—

(4) to or for the benefit of a creditor, to the extent that, after such transfer, such creditor gave new value to or for the benefit of the debtor—

(A) not secured by an otherwise unavoidable security interest; and

(B) on account of which new value the debtor did not make an otherwise unavoidable transfer to or for the benefit of such creditor;

The relevant portion of 11 U.S.C. § 503(b)(9) provides:

(b) After notice and a hearing, there shall be allowed, administrative expenses, other than claims allowed under section 502(f) of this title [11 USCS § 502(f)], 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.

The relevant portion of 11 U.S.C. § 365(d)(3)(A) provides:

(d)

(3)

(A) The trustee shall timely perform all the obligations of the debtor, except those specified in section 365(b)(2) [11 USCS § 365(b)(2)] [subsec. (b)(2) of this section], arising from and after the order for relief under any unexpired lease of nonresidential real property, until such lease is assumed or rejected, notwithstanding section 503(b)(1) of this title [11 USCS § 503(b)(1)]. The court may extend, for cause, the time for performance of any such obligation that arises within 60 days after the date of the order for relief, but the time for performance shall not be extended beyond such 60-day period, except as provided in subparagraph (B). This subsection shall not be deemed to affect the trustee's obligations under the provisions of subsection (b) or (f) of this section. Acceptance of any such performance does not constitute waiver or relinquishment of the lessor's rights under such lease or under this title.

STATEMENT OF THE CASE

The Debtor was founded by its sole member, William Tell ("Tell"), in 2005 for the purpose of establishing a coffeehouse. R. at 3. For several years afterward, the Debtor operated an independent coffeehouse in the Town of Terrapin, Moot. R. at 3.

Petitioner is an international coffee company and coffeehouse chain headquartered in San Francisco, California. R. at 3. There are over 1,900 of Petitioner's coffeehouses all around the world, some of which are corporate-owned stores and others of which are franchised. R. at 3.

As part of its efforts to grow in new markets, and in response to increased consumer demand for local, independent businesses, Petitioner decided to open a series of new "neighborhood coffeehouses" in 2017. R. at 4. The neighborhood coffeehouses would not be branded as Petitioner's stores. R. at 4. Rather, they would quietly be franchised with owners of existing, independent coffeehouses. R. at 4. The neighborhood coffeehouses would sell a new line of coffee products created by Petitioner called "Dark Star," reportedly so that consumers would not immediately realize that, in fact, they were patronizing Petitioner's stores. R. at 4. In addition to selling traditional coffeehouse fare, the neighborhood coffeehouses would provide expanded food offerings and, at night, would offer alcoholic beverages and host live music and poetry readings. R. at 4.

In the fall of 2017, Petitioner approached Tell to see if the Debtor would be interested in franchising a neighborhood coffeehouse in Terrapin. R. at 4. Although the Debtor had a loyal customer base, its earnings had stalled, and its store needed remodeling. R. at 4. Tell was intrigued by the neighborhood coffeehouse concept and the opportunity to partner with an

industry giant like Petitioner. R. at 4. The parties agreed to move forward with the venture. R. at 4.

To facilitate the opening of the new coffeehouse, Petitioner agreed that it would purchase and lease to the Debtor a recently renovated warehouse space located at 5877 Shakedown Street (the "Premises") in the downtown entertainment district of Terrapin. R. at 4. On July 1, 2018, the Debtor, as tenant, and Petitioner, as landlord, entered into a Lease Agreement (the "Lease") for the Premises. R. at 4. The Lease was a twenty-year, triple-net lease that required the Debtor to pay monthly rent in the amount of $25,000, with such rent being "due in advance on the first day of each month." R. at 4. That same day, Petitioner, as franchisor, and the Debtor, as franchisee, entered into a franchise agreement whereby the Debtor would exclusively sell "Dark Star" branded products, which it would purchase from Petitioner. R. at 4.

The buildout of the Premises was completed in November 2018, and the new "Terrapin Station Coffeehouse" opened on December 1, 2018. R. at 5. Simultaneously, the Debtor's original coffeehouse closed. R. at 5. Unfortunately, the new location encountered difficulties from the start. R. at 5. First, an ad hoc group of local independent coffeehouse owners reacted negatively when it learned of the Debtor's affiliation with Petitioner. R. at 5. The group started an effective local advertising campaign that unfavorably characterized the Debtor as "big coffee in disguise." Second, the Debtor's efforts to join the competitive Shakedown Street nightlife scene failed to gain traction. R. at 5.

Burdened by both underperforming sales and above-market rent under the Lease, the Debtor struggled throughout 2019. R. at 5. According to the first day declaration signed by Tell in the Debtor's bankruptcy case, the Debtor was unable to pay its debts as they became due as early as September 2019. R. at 5. Although the Debtor remained current on its rent obligations

under the Lease, by November 1, 2019, it owed Petitioner over $700,000 for Dark Star-branded goods that it had purchased. R. at 5. Troubled by the Debtor's poor performance, Petitioner sent the Debtor a notice of default on December 5, 2019, threatening, among other things, to terminate the franchise agreement. R. at 5.

On December 7, 2019, the parties entered into a forbearance agreement wherein Petitioner agreed to forbear from terminating the franchise agreement in exchange for: (i) a payment of $250,000 from the Debtor on account of the outstanding invoices for Dark Star products, (ii) reaffirmation by the Debtor of its obligations under the Lease, and (iii) a release of any and all claims or causes of action that the Debtor had against Petitioner. R. at 5. That same day, the Debtor made the $250,000 payment to Petitioner. R. at 5.

On December 18, 2019, the Debtor purchased an additional $200,000 worth of Dark Star products from Petitioner on credit, as set forth on an invoice dated December 18, 2019 (the "Invoice"). R. at 5. In order to induce Petitioner to sell the Debtor such goods, Tell signed a personal guarantee with respect to the Invoice. R. at 6. The goods identified on the Invoice were delivered to the Debtor on December 21, 2019. R. at 6.

After reviewing its disappointing sales numbers from the holiday season, the Debtor filed a petition for relief under Chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for the District of Moot on January 5, 2020 (the "Petition Date"). R. at 6. On the Petition Date, the Debtor was "current" on its obligations to Petitioner under the Lease. However, the Debtor owed Petitioner $650,000 (including the amount due under the Invoice) for goods that it had purchased. R. at 6. The Debtor had no secured debt but owed over $500,000 to other unsecured creditors, some of whom refused to provide the Debtor with goods and services on credit. R. at 6.

The Debtor filed several "first day" motions along with its bankruptcy petition. R. at 6. The motions were supported by the declaration from Tell, wherein he stated that he intended to reorganize the Debtor by returning to traditional coffeehouse operations and hours. R. at 6. He also stated that he hoped to find a sub-lessee for a portion of the Premises, thereby reducing the Debtor's rent burden. R. at 6. The Debtor proposed to continue selling Dark Star-branded products, as it was required to do under the franchise agreement. R. at 6. Counsel for Petitioner appeared at the "first day" hearings and stated that, although her client had serious concerns with the Debtor's reorganization strategy, it was engaged in ongoing, good faith discussions with the Debtor about a path forward. R. at 6.

Two weeks later, the Debtor filed a motion requesting authority to pay $200,000 to Petitioner, asserting that it was a "critical vendor." R. at 6. In support of the motion, the Debtor argued that an ongoing relationship with Petitioner was critical to the Debtor's reorganization plans, and that Petitioner was unwilling to sell goods on credit to the Debtor post-petition absent the payment. R. at 6. The Debtor argued that, notwithstanding the general rule that pre-petition claims should not be paid by a debtor in bankruptcy post-petition, "critical vendor" motions have been met with increasing favor by bankruptcy courts in recent years. R. at 7. The Debtor emphasized that the $200,000 payment would be applied to the Invoice, which was entitled to priority in payment as an administrative expense pursuant to § 503(b)(9). R. at 7.

Therefore, the Debtor posited, other creditors would not be prejudiced by the payment. R. at 7. The United States Trustee opposed the motion, arguing that "critical vendor" payments are not authorized under the Bankruptcy Code. R. at 7. At the hearing, counsel for the newly appointed creditors' committee stated that the committee supported the motion given the importance of Petitioner to the Debtor's reorganization. R. at 7.

After oral argument, the bankruptcy court stated that it was not inclined to approve the "critical vendor" payment, as it was uncertain as to whether such payments are permitted under the Bankruptcy Code. R. at 7. Nevertheless, the court stated that it would award Petitioner an administrative expense under § 503(b)(9) for the value of the goods sold (as reflected on the Invoice) and would allow immediate payment of such administrative expense. R. at 7. Days later, the Debtor made the $200,000 payment to Petitioner. R. at 7. Thereafter, Petitioner resumed selling goods to the Debtor on credit, which allowed the Debtor to continue operating. R. at 7.

Unfortunately, the Debtor's reorganization efforts were anything but successful. R. at 7. The Debtor was forced to temporarily close its doors in March 2020 due to the COVID-19 pandemic. R. at 7. Although the Debtor reopened in April 2020, its customers did not return. R. at 7. On May 5, 2020, the Debtor permanently ceased operations, vacating the Premises and returning the keys to Petitioner. R. at 7. The next day, the Debtor filed a motion with the bankruptcy court to reject the Lease and the franchise agreement with Petitioner as of the date of the motion pursuant to § 365(a). R. at 7.

On May 8, 2020, Petitioner filed a motion seeking to compel payment of the May rent, which became due under the Lease on May 1st. R. at 7. In that motion, Petitioner stated that it did not oppose rejection of the Lease effective May 5, 2020. R. at 8. Nevertheless, it asserted that it was entitled to payment in full for the May rent, pursuant to § 365(d)(3), as such rent came due prior to the date of rejection. R. at 8. Because the bankruptcy courthouse remained closed to the public due to the pandemic, a virtual hearing on both motions was scheduled for May 29, 2020. R. at 8.

At the outset of the hearing on May 29, 2020, the Debtor announced that it was converting its Chapter 11 case to a case under Chapter 7 of the Bankruptcy Code pursuant to § 1112(a). R. at 8. No parties objected to this request, and an order converting the case and appointing the Respondent as the Chapter 7 trustee for the Debtor's estate was entered. R. at 8. At that same hearing, the bankruptcy court granted the Debtor's motion to reject the Lease and the franchise agreement effective as of May 5, 2020. R. at 8. The court did not rule on Petitioner's request for payment of the May rent but instead issued an order requiring additional briefing on the issue. R. at 8.

After retaining counsel, Respondent took an aggressive posture with respect to Petitioner. R. at 8. First, Respondent objected to Petitioner's motion to compel payment for the entirety of the May rent pursuant to § 365(d)(3)(A), arguing that such relief was inequitable to other creditors because the Debtor only occupied the Premises for the first five days of May 2020. R. at 8. Next, Respondent commenced an adversary proceeding seeking to avoid and recover the $250,000 payment that the Debtor had made to Petitioner pursuant to the forbearance agreement as a preferential transfer pursuant to §§ 547(b) and 550(a). R. at 8. Petitioner immediately filed its answer and affirmative defenses asserting, among other things, that it was entitled to reduce any preference exposure by the $200,000 in goods that it sold to the Debtor (as reflected on the Invoice) pursuant to § 547(c)(4). R. at 8.

In lieu of litigation, the parties stipulated to a stay of all proceedings while they attempted to resolve their disputes through mediation. R. at 8. Unfortunately, the mediation was unsuccessful. R. at 8. At a status conference with the court on July 23, 2020, the parties stipulated that because the subsequent new value dispute was purely a legal issue, they would file cross-motions for summary judgment. R. at 9. They also stipulated to hold the hearing on

Petitioner's request for payment of the May 2020 rent at the same time as the hearing on the motions for summary judgment. R. at 9.

After briefing and oral argument, the bankruptcy court ruled in favor of Respondent on both issues. R. at 9. The court concluded that § 365(d)(3) only required the Debtor to pay rent for the five days that it had occupied the Premises prior to rejection. R. at 9. Thus, instead of requiring payment of the full $25,000, the court granted Petitioner an administrative expense in the amount of $4,032.26 for the pre-rejection portion of the May 2020 rent. R. at 9.

In the adversary proceeding, the bankruptcy court granted summary judgment to Respondent, holding that Petitioner could not use the value of the goods reflected on the Invoice as new value to reduce its preference exposure given that the Invoice was paid pursuant to § 503(b)(9). R. at 9. Accordingly, a judgment in the amount of $250,000 was entered in favor of Respondent and against Petitioner. R. at 9.

On appeal, the United States Court of Appeals for the Thirteenth Circuit affirmed the Bankruptcy Court's decision in favor of Respondent. R. at 21. The Court of Appeals for the Thirteenth Circuit concluded that § 547(c)(4) precluded Respondent from asserting new value for goods subject to a satisfied administrative expense § 503 (b)(9). R. at 10. Additionally, the Thirteenth Circuit stated that § 365(d)(3) does not require the trustee to satisfy obligations allocable to the post-rejection period. R. at 15. In the dissent, Circuit Judge Weir stated that Petitioner's arguments are both consistent with the statutory text and equitable. R. at 22.

STANDARD OF REVIEW

The questions presented are based on statutory interpretation of the Bankruptcy Code and Federal Arbitration Act. As such, this review concerns questions of law and the standard of review for this appeal is de novo. "Fact findings of the bankruptcy court are reviewed under a

clearly erroneous standard and issues of law are reviewed de novo." *Nationwide Mut. Ins. Co. v. Berryman Prods. (In re Berryman Prods.)*, 159 F.3d 941, 943 (5th Cir. 1998).

SUMMARY OF THE ARGUMENT

This Court should affirm the decision of the United States Court of Appeals for the Thirteenth Circuit on both issues presented. The Thirteenth Circuit Court of Appeals correctly concluded that under 11 U.S.C. § 547(c)(4), a creditor is precluded from asserting new value for goods subject to a satisfied administrative expense under 11 U.S.C. § 503(b)(9). The Court of Appeals also correctly concluded that under the Bankruptcy Code, a trustee is not required to pay rent due prior to the rejection of an unexpired, non-residential real property lease but allocable to the period after the rejection date.

Section 547(c)(4) contains no temporal limitation requiring the debtor's payments for new value be made pre-petition. Additionally, a satisfied administrative expense under § 503(b)(9) constitutes an "otherwise unavoidable transfer" by the debtor, rendering the subsequent new value defense under § 547(c)(4) inapplicable. Finally, the underlying policy considerations of the Bankruptcy Code do not permit creditor's to "double dip."

Finally, the Thirteenth Circuit is accurate in finding that a trustee does not have to pay rent due prior to the rejection of an unexpired non-residential real property lease but allocable to the period after the rejection date. A majority of jurisdictions, including the Thirteenth Circuit, have properly held that the "proration" approach is the most honorable approach towards § 365(d)(3)'s legislative history, underlying policies, and statutory text. The "proration" approach interprets situations, like the one at hand, to require only those amounts that accrued during the time the debtor or trustee was in possession of the property arise after the order for relief and

should be assessed against the estate. The use of the "billing date" approach, used by a minority of courts, both undermines and tramples the underlying policies of § 365(d)(3)(A).

ARGUMENT

I. Section 547(c)(4) Precludes a Creditor from Asserting New Value for Goods Subject to a Satisfied Administrative Expense Under § 503(b)(9).

Petitioner cannot both use the "subsequent new value defense" under 11 U.S.C. § 547(c)(4) and be paid in full for that same value under 11 U.S.C. § 503(b)(9). A preference essentially "is an eve-of-bankruptcy transfer to a creditor." *Miller v. JNJ Logistics LLC (In re Proliance Int'l, Inc.)*, 514 B.R. 426, 430 (Bankr. D. Del. 2014) (citations omitted). When a creditor receives a preferential payment, that creditor recovers all of its claim where, "in all likelihood, other unsecured creditors receive less." *Id.* However, under 11 U.S.C. § 547(b), a trustee may, "avoid a [preferential] transfer of an interest of the debtor in property" if certain requirements are met, one of which being that the transfer is made "on or within ninety days before the date of the filing of the petition." § 547(b). Moreover, § 547(b) "focuses on recovering pre-petition transfers made by the debtor to a creditor." *TI Acquisition, LLC v. Southern Polymer, Inc. (In re TI Acquisition, LLC)*, 429 B.R. 377, 380 (Bankr. N.D. Ga. 2010). The burden of proving a transfer is avoidable is placed on the trustee. 11 U.S.C. § 547(g). Section 547(c) provides affirmative defenses for creditors to assert, in certain circumstances, against a trustee who has satisfied the requirements for an avoidable preferential transfer. *See* 11 U.S.C. § 547(c). The creditor has "the burden of proving the nonavailability of a transfer under subsection (c)" of § 547. § 547(g). Particularly, the subsequent new value defense, at issue here, provides that a "trustee may not avoid [a preferential] transfer" that is made –

> (4) to or for the benefit of a creditor to the extent that, after such transfer, such creditor gave new value to or for the benefit of the debtor –
>
> (A) not secured by an otherwise unavoidable security interest; and
>
> (B) *on account of which new value to the debtor did not make an otherwise unavoidable transfer to or for the benefit of such creditor.*

11 U.S.C. § 547(c)(4) (emphasis added).

Similar to § 547(c)(4), another protection afforded to creditors is found in § 503(b)(9) of the Bankruptcy Code, which Congress amended to have included in 2005. *See* Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23, § 1227 (Apr. 20, 2005) ("BAPCPA"). Under § 503(b)(9), a creditor can be provided an administrative expense for "the value of any goods received by the debtor in the ordinary course of such debtor's business." § 503(b)(9).

The issue in the present case deals with the intersection of §§ 547(c)(4) and 503(b)(9) and whether a creditor can assert the subsequent new value defense when there is a satisfied administrative expense. Regarding this specific issue, a majority of bankruptcy courts have correctly answered the question in the negative. *See Beaulieu Liquidating Tr. v. Fabric Sources, Inc. (In re Beaulieu Grp., LLC)*, 616 B.R. 857 (Bankr. N.D. Ga. 2020) (holding a creditor cannot use the new value represented by a satisfied § 503(b)(9) claim to offset its preference liability under § 547(c)(4)); *see also Circuit City Stores, Inc. v. Mitsubishi Digital Elecs. Digit. Elecs. Am., Inc. (In re Circuit City Stores, Inc.)*, 2010 Bankr. LEXIS 4398, at *35 (Bankr. E.D. Va. Dec. 1, 2010) (holding a creditor could not assert the subsequent new value defense because the "creation of the reserve fund constitutes an otherwise unavoidable transfer for the exclusive benefit of [the creditor] on account of its 503(b)(9) claim."); *see also TI Acquisition, LLC v. Southern Polymer, Inc. (In re TI Acquisition, LLC)*, 429 B.R. 377, 385 (Bankr. N.D. Ga.

2010) (holding "[a] creditor that delivered goods to the debtor pre-petition is not entitled to the new value defense under § 547(c)(4) when that creditor has been paid in full by a § 503(b)(9) claim."). With that in mind, Respondent contends that Petitioner is precluded from asserting the subsequent new value defense pursuant § 547(c)(4) because: (A) the statute contains no temporal limitation; (B) the satisfied administrative expense constitutes an "otherwise unavoidable transfer" by the debtor; and (C) the underlying policy considerations of the Bankruptcy Code do not permit creditors to "double dip."

A. Section 547(c)(4) contains no temporal limitation requiring the debtor's payments for new value be made pre-petition.

Section 547(c)(4) contains no temporal limitations; therefore, the post-petition administrative expense paid pursuant to § 503(b)(9) is part of the preferential analysis and should be used to determine whether the subsequent new value defense applies. "The starting point in statutory interpretation is the language of the statute itself." *Warshauer v. Solis*, 577 F.3d 1330, 1335 (11th Cir. 2009) (quoting *Ardestani v. INS*, 502 U.S. 129, 135 (1991)). "It is well established that 'when the statute's language is plain, the sole function of the courts . . . is to enforce it according to its terms." *Lamie v. United States Tr.*, 540 U.S. 526, 534 (2004) (citations omitted); *see also Conn. Nat'l Bank v. Germain*, 503 U.S. 249, 254 (1992) ("When the words of a statue are unambiguous, then, this first canon is also the last: 'judiciary inquiry is complete.'") (citations omitted)). Notably, in its use of the term "otherwise unavoidable," § 547(c)(4)(B) contains a double-negative, but that fact merely makes the statute complicated, not ambiguous. *In re Check Reporting Serv.*, 140 B.R. 425, 434 (Bankr. W.D. Mich. 1992); *see also In re Circuit City Stores, Inc.*, 2010 Bankr. LEXIS 4398 at *23 ("The use of the double negative in § 547(c)(4)(B) does not render the plain meaning of that portion of the statute ambiguous.").

It is worth noting, there is some debate in bankruptcy courts over whether the new value needs to "remain unpaid" in order for a creditor to establish a defense under § 547(c)(4). *See, e.g., In re Proliance Int'l, Inc.*, 514 B.R. at 431 (explaining there is a jurisdictional split regarding the interpretation and application of § 547(c)(4)(B), where some courts hold that the statute "should be read to mean that the new value *must remain unpaid* at the end of the preference period in order to be used as a defense to a preferential claim," and other courts hold that the statute "does not contain a 'remains unpaid' requirement, rather the court must determine if 'subsequent advances' were made by the creditor."). However, here, the parties have stipulated that new value need not "remain unpaid" for a creditor to establish a defense under § 547(c)(4). R. at 10. Arguably, under the plain language of the § 547(c)(4), that stipulation is a correct following of the defense's requirements. *See Kaye v. Blue Bell Creameries, Inc. (In re BFW Liquidation, LLC)*, 899 F.3d 1178, 1189 (11th Cir. 2018) ("By its plain terms, then, the statute only excludes 'paid' new value that is paid for with 'an otherwise unavoidable transfer.' Therefore, so long as the transfer that pays for the new value is itself avoidable, that transfer is not a barrier to assertion of § 547(c)(4)'s subsequent-new-value defense.")

With regard to the present issue, when reading the text of § 547(c)(4), it can be seen that the statute contains no limitation regarding the time to consider *when* a payment on account of new value must be made. *See* 11 U.S.C. § 547(c)(4); *see also Moglia v. Am. Psychological Ass'n (In re Login Bros. Book Co.)*, 294 B.R. 297, 300 (Bankr. N.D. Ill. 2003) (explaining that § 547(c)(4)(B) "contains no limitation on the time that the repayment of new value . . . must occur."); *see also Hall v. Chrysler Credit Corp. (In re JKJ Chevrolet, Inc.)*, 412 F.3d 545, 553, n.6 (4th Cir. 2005) ("[P]ost-petition transfers may be considered under section 547(c)(4)(B)[.]"). Under the plain language of the statute, it is only required that "(1) any new value given by the

creditor must not be secured by an otherwise unavoidable security interest and (2) the debtor must not have made an otherwise unavoidable transfer to or for the benefit of the creditor on account of the new value given." *In re BFW Liquidation, LLC*, 899 F.3d at 1189 (citing § 547(c)(4)). Moreover, under the statute, "if the debtor makes a preferential payment to the creditor and the creditor thereafter provides the debtor with new value, that new value is a defense to a preference claim so long as the debtor does not make an 'otherwise unavoidable transfer' on account of that new value." *In re Beaulieu Grp., LLC*, 616 B.R. at 866. Therefore, when a payment on account of new value has been made, whether it be pre-petition or post-petition, the inquiry into whether the subsequent new value defense is applicable depends on whether the debtor made an "otherwise unavoidable transfer."

Respondent acknowledges that in *In re Friedman's Inc.*, the Third Circuit expressed the minority view in holding that "where 'an otherwise unavoidable transfer' is made after the filing of a bankruptcy petition, it does not affect the new value defense." 738 F.3d at 549; *see also Commissary Operations, Inc. v. Dot Foods, Inc. (In re Commissary Operations, Inc.)*, 421 B.R. 873, 879 (Bankr. M.D. Tenn. 2010). Be that as it may, Respondent is asking this Court to not endorse the Third Circuit's misplaced and strained analysis of § 547(c)(4). *See id.* at 554 ("[W]e rest this conclusion on the context and policy of the Code, rather than specific language[.]"); *but see In re Beaulieu Grp., LLC*, 616 B.R. at 872–878 (discussing the issues with the conclusion reached by the Third Circuit). Moreover, the facts of the present case are distinguishable from *In re Friedman Inc.*, as the issue was addressed with regard to wage orders, rather than claims under § 503(b)(9). *See id.* at 549 ("[C]an a post-petition payment to a creditor pursuant a Wage Order entered at a debtor's request reduce the creditor's new value defense–and thereby increase preference liability–the same as it would if the payment had been made pre-petition?").

Additionally, Congress knows exactly how to expressly impose temporal limitations and even did so in one of the preference defenses available to creditors. *See* 11 U.S.C. § 547(c)(5) (stating that a trustee is unable to avoid a transfer "that creates a perfected security interest in inventory or a receivable or the proceeds of either . . . *as of the date of the filing of the petition*[.]") (emphasis added); *see also* 11 U.S.C. §§ 502(d), 542(c), 550, 551, 749, 766, 783, 1101. The fact that Congress chose not to impose a temporal limitation in § 547(c)(4) is telling since Congress "does not . . . hide elephants in mouseholes." *Whitman v. Am. Trucking Ass'ns, Inc.*, 521 U.S. 457, 468 (2001). Therefore, this Court can reasonably conclude that § 547(c)(4) contains no temporal limitation because nothing in the statute designates the petition date as the cutoff for determining whether a transfer is "otherwise unavoidable."

Furthermore, any argument that the statute's use of the terms "transfer" or "debtor" impose temporal limitations on § 547(c)(4) are without merit. First, "transfer" is defined broadly to mean "each mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with," among other things, "property . . . or an interest in property." 11 U.S.C. § 101(54)(D). With such a broad definition, a "distribution" made by the debtor's estate post-petition can constitute a transfer. *See In re Beaulieu Grp., LLC*, 616 B.R. at 870 ("Nothing in the definition of 'transfer' excludes distributions."). Second, the use of the term "debtor" rather than "debtor-in-possession" also fails to indicate that § 547(c)(4)(B) refers only to pre-petition activity. To begin, the definition of "debtor" means "person or municipality concerning which a case under this title has been commenced." 11 U.S.C. § 101(13). Moreover, the Bankruptcy Code's definition does not "define a 'debtor' as a pre-petition, as opposed to post-petition, entity." *Friedman's Liquidating Tr. v. Roth Staffing Cos. LP (In re Friedman's Inc.)*, 738 F.3d 547, 555 (3d Cir. 2013) (citing § 101(13)); *see also NLRB v. Bildisco & Bildisco*, 465

U.S. 513, 528, (1984), *superseded by statute,* 11 U.S.C. § 1113, ("[I]t is sensible to view the [Debtor in Possession] as the same "entity" which existed before the filing of the bankruptcy petition."). Therefore, even though the post-petition payment in the present case was made by the "debtor-in-possession," the transfer was made by the same "entity," thus satisfying a transfer by the *debtor* under § 547(c)(4).

Because § 547(c)(4) is unambiguous, this Court's analysis should end there. *Am. Gen. Fin., Inc. v. Paschen (In re Paschen)*, 196 F.3d 1203, 1207 (11th Cir. 2002) ("When the language of a statute is unambiguous, we need go no further, because we must presume that Congress 'said what it meant and meant what it said.'") (quoting *United States v. Steele*, 147 F.3d 1316, 1318 (11th Cir. 1998)). Meaning, it is unnecessary to "resort to extrinsic evidence, such as legislative history, to discern a statute's meaning if the statue's language is unambiguous." *Id.* However, a look at the statutory development of § 547(c)(4) only bolsters the conclusion that Congress was intentional with its omission of a temporal limitation on when payments made on account of new value must be made. *Cf. In re BFW Liquidation, LLC*, 899 F.3d at 1192 (finding that the statutory development of § 547(c)(4) bolstered the conclusion that new value need not remain unpaid). The predecessor to § 547(c)(4) was "[s]ection 60(c) of the Bankruptcy Act of 1898 (the "Bankruptcy Act"), codified at 11 U.S.C. § 96(c). *In re Beaulieu Grp., LLC*, 616 B.R. at 872. The antecedent statute, in pertinent part, stated "the amount of such new credit *remaining unpaid at the time of adjudication* in bankruptcy may be set off against the amount which would otherwise be recoverable from him." 11 U.S.C § 96(c) (1976) (emphasis added).

Absent evidence to the contrary, it can plausibly be inferred that Congress's omission of a temporal limitation on when payments on account of new value are to be made was intentional because § 60(c) included a temporal limitation that was excluded from § 547(c)(4). *In re*

Beaulieu Grp., LLC, 616 B.R. at 872*; cf. In re BFW Liquidation, LLC*, 899 F.3d at 1191 ("[O]ne can plausibly infer that, by replacing § 60(c)'s 'remaining unpaid' language with new language that omits any such requirement, Congress intended to eliminate § 60(c)'s requirement that new value remain unpaid, and to replace that requirement with something substantively different."). Therefore, this Court should conclude, based on the statute's change in language, that Congress intended for there to be no temporal limitation on when payments made on account of new value are to be made.

Accordingly, because § 547(c)(4) contains no temporal limitation, all this Court must do is determine whether or not payment of an administrative expense under § 503(b)(9) is an "otherwise unavoidable transfer" by the debtor.

B. A satisfied administrative expense under § 503(b)(9) constitutes an "otherwise unavoidable transfer" by the debtor, rendering the subsequent new value defense under § 547(c)(4) inapplicable.

A creditor is unable to assert the subsequent new value defense under § 547(c)(4) because a satisfied administrative expense pursuant to § 503(b)(9) constitutes an "otherwise unavoidable transfer" by the debtor.

As previously discussed, a creditor's ability to assert the subsequent new value defense depends on whether an "otherwise unavoidable transfer" has been made. 11 U.S.C. § 547(c)(4)(B); *see also In re Circuit City Stores, Inc.*, 2010 Bankr. LEXIS 4398 at *23–24 ("[Section] 547(c)(4)(B) of the Bankruptcy Code simply requires a creditor to prove that the new value extended has not been repaid with an otherwise unavoidable transfer.") (citing *Wahoski v. Am. & Efrid, Inc. (In re Pillowtex Corp.)*, 416 B.R. 123, 124 (Bankr. D. Del. 2009)). Notably, the expression "otherwise unavoidable transfer" in § 547(c)(4)(B) refers "to transfers that are unavoidable for reasons other than § 547(c)(4)(B)'s subsequent-new-value defense." *In re BFW*

Liquidation, LLC, 899 F.3d at 1198; *see also Phx. Rest. Grp., Inc. v. Ajilon Prof'l Staffing, LLC (In re Phx. Rest. Grp., Inc.)*, 317 B.R. 491, 499–500 (Bankr. M.D. Tenn. 2004); *In re Check Reporting Servs.*, 140 B.R. at 431-32, 435-36. Therefore, whether a transfer for the benefit of a creditor pursuant a § 503(b)(9) claim is "otherwise unavoidable turns on the provisions of the Bankruptcy Code governing the avoidance powers of a trustee." *In re Circuit City Stores, Inc.*, 2010 Bankr. LEXIS at *26. The sections of the Bankruptcy Code applicable to the inquiry are "11 U.S.C. §§ 544, 545, 547, 548, 549, 553(b) and 724(a)." *Id.*

In particular, § 549 applies to the avoidance of post-petition transfers and is the only section applicable to determine whether the post-petition payment at issue is avoidable. *See* 11 U.S.C. § 549 ("Postpetition transactions"). Under § 549, a "trustee may avoid a transfer of property of the estate (1) that occurs after the commencement of the case; and . . . (2)(B) that is *not* authorized by this title or by the court." *Id.* (emphasis added). In the present case, the post-petition payment made to Petitioner was made pursuant a Court Order after Petitioner was awarded an administrative expense pursuant § 503(b)(9). R. at 7. Therefore, the satisfied administrative expense pursuant to § 503(b)(9) was authorized by the court, making it "otherwise unavoidable" and rendering the subsequent new value under § 547(b)(9) inapplicable. *See Siegel v. Sony Elecs., Inc. (In re Circuit City Stores, Inc.)*, 515 B.R. 302, 314 (Bankr. E.D. Va. 2014) ("As satisfaction of [the creditor's] § 503(b)(9) claim post-petition by [the debtor] "is an 'otherwise unavoidable transfer' . . . § 547(c)(4)(B) of the Bankruptcy Code negates [that claim] for qualification as new value.").

Accordingly, because a satisfied administrative expense under § 503(b)(9) constitutes an "otherwise unavoidable transfer," this Court should find that Petitioner is precluded from asserting the subsequent new value defense under § 547(c)(4).

C. <u>The Underlying Policy Considerations of the Bankruptcy Code Do Not Permit Creditors to "Double Dip."</u>

When taking into consideration the policy goals of the Bankruptcy Code, the "double dipping" that would occur were a creditor allowed to both assert the subsequent new value defense under § 547(c)(4) and be paid in full for that same value under § 503(b)(9) would undercut those goals.

A central policy of the Bankruptcy Code is "[e]quality of distribution among creditors[,]" and per that policy, "creditors of equal priority should receive pro rata shares of the debtor's property." *Begier v. IRS*, 496 U.S. 53, 58 (1990). With regard to the purpose behind § 547, the Supreme Court has articulated two underlying policies. *See Union Bank v. Wolas*, 502 U.S. 151, 161 (1991) ("First, by permitting the trustee to avoid pre-bankruptcy transfers that occur within a short period before bankruptcy, creditors are discouraged from racing to the courthouse to dismember the debtor during his slide into bankruptcy. . . . Second, and more important, the preference provisions facilitate the prime bankruptcy policy of equality of distribution among creditors[.]"). Moreover, the purpose of the enactment of the preference defenses is "to encourage creditors to continue doing business with such debtors under usual practices." *In re Beaulieu Grp., LLC*, 616 B.R. at 857. In essence, the purpose of the subsequent new value defense "is to preserve the policy objectives underlying preference provisions of the Bankruptcy Code." *In re TI Acquisition, LLC*, 429 B.R. at 384. The subsequent new value defense fosters such objectives because the defense is limited "to the extent by which the bankruptcy estate has been enhanced by the creditor's actions." *Id.*

First, because there has been payment on account of the new value with an "otherwise unavoidable" transfer, effectively no new value has been given to the estate. "The subsequent new value defense reflects the understanding that when a debtor makes a preferential payment to

the creditor—thereby depleting the pool of funds available to other creditors—that pool is replenished when the creditor subsequently provides new value to the debtor." *In re Beaulieu Grp., LLC*, 616 B.R. at 875. Notably, the "status quo" is maintained when a debtor makes an avoidable payment on account of the new value. *Id.* However, here when the Debtor paid Petitioner $200,000 pursuant to the § 503(b)(9) claim, the estate was no longer enlarged by the delivery of goods identified on the "Invoice" it received from Petitioner. *See In re TI Acquisition, LLC*, 429 B.R. at 384 ("If the estate is not enlarged, no new value has been given. Thus, [creditor's] delivery of goods to Debtor pre-petition enlarged the Debtor's estate. Upon full payment to [creditor], the Debtor's estate is no longer enlarged by the delivery.").

Second, § 503(b)(9) does not affect a creditor's incentives to work with distressed debtors. It is true that creditors' knowledge of the subsequent new value defense available under § 547(c)(4) "encourages continued commerce with the debtor." *Id.* at 384-85 (citing *In re Commissary Operations, Inc.*, 421 B.R. 873, 879 (Bankr. M.D. Tenn. 2010)). However, a creditor never knows, when it ships goods pre-petition, whether a debtor will file for bankruptcy within twenty days of receiving the shipment. *Id.* at 385. Meaning, a creditor does not know if it will be able to assert a claim under § 503(b)(9). *Id.* Therefore, "[f]rom the creditor's pre-petition perspective, there is no difference in incentive if the new value defense the creditor may have relied on is lost as a result of a § 503(b)(9) claim." *Id.* Additionally, as seen in the present case when Petitioner continued to trade with the Debtor after receiving full payment for the "Invoice" pursuant a § 503(b)(9) claim, "paying creditors in full for their claims is the ultimate method of encouraging them to continue to trade with the debtor." *Id.*

Finally, not allowing a creditor to both assert the subsequent new value defense and be paid in full for that same value is the best way to promote equality among creditors. Here, if

Petitioner were allowed to reduce its preference liability under the subsequent new value defense, even though it has already received payment in full for that same value, other unsecured creditors would be penalized. *See In re Beaulieu Grp., LLC*, 616 B.R. at 877. If this Court allowed this "payment plus" treatment, the pool of funds available to other unsecured creditors would be diminished because it would have decreased by $200,000 since that is the amount Petitioner's preference liability would be decreased by. *See id.*

Ultimately, "[t]he overriding goal of equality of distribution is undercut if such creditors are treated as 'payment plus' or 'priority plus' creditors while other unsecured creditors, including those who have had to return preferential payments are penalized by the decrease in the pool of funds available for distribution[.]" *Id.* Here, Petitioner is an unsecured creditor that has received full payment for a shipment of goods that it made twenty days prior to the debtor's bankruptcy filing. R. at 6. There is no reason that Petitioner should be allowed to offset its preference liability based on that same value, at the expense of the Debtor's other unsecured creditors. Such an outcome would undermine the policy of "equality among creditors," by allowing certain creditor's to "double dip." *See MMR Holding Corp. v. C&C Consultants (In re MMR Holding Corp.)*, 203 B.R. 605, 609 (Bankr. M.D. La. 1996) ("[U]navoidable post-petition transfer[s] on account of new value extended subsequent to a preference *should* limit the use of § 547(c)(4) by the amount of the unavoidable transfer, as without a reduction in the new value offset, the transferee would be receiving double use of the new value[.]").

In sum, like the courts below, this Court should find that Petitioner is precluded from asserting the subsequent new value defense under § 547(c)(4) because there is a satisfied administrative expense pursuant § 503(b)(9).

II. A Trustee Does Not Have to Pay Rent Due Prior to the Rejection of an Unexpired Non-Residential Real Property Lease but Allocable to the Period After the Rejection Date.

A bankruptcy trustee does not have to pay a debtor's rent when it is due prior to the rejection of an unexpired non-residential real property lease but allocable to the period after the rejection date. 11 U.S.C. § 365(d)(3)(A), along with the entire Bankruptcy Code, is grounded in equity and fairness. *See Young v. Higbee Co.*, 324 U.S. 204, 210 (1945) ("[H]istorically one of the prime purposes of the bankruptcy law has been to bring about a ratable distribution among creditors of a bankrupt's assets; to protect the creditors from one another."); *Howard Delivery Serv., Inc. v. Zurich Am. Ins. Co.*, 547 U.S. 651, 655 (2006) ("[T]he Bankruptcy Code aims, in the main, to secure equal distribution among creditors.").

The Thirteenth Circuit, along with the majority of other jurisdictions, has properly held that the "proration" approach is the most honorable approach towards § 365(d)(3)'s legislative history, underlying policies, and statutory text. To the contrary, the "billing date" approach both undermines and tramples the underlying policies of § 365(d)(3)(A). Therefore, this Court should affirm the Thirteenth Circuit.

A contract is executory "if 'performance remains due to some extent on both sides.'" *Mission Prod. Holdings, Inc. v. Tempnology, LLC*, 139 S. Ct. 1652, 1658 (2019). The Bankruptcy Code allows a bankruptcy trustee to, "subject to the court's approval, . . . assume or reject any executory contract or unexpired lease of the debtor." 11 U.S.C. § 365(a). "Section 365(a) enables the debtor (or its trustee), upon entering bankruptcy, to decide whether the contract is a good deal for the estate going forward." *Mission Prod. Holdings, Inc.*, 139 S. Ct. at 1658. If the trustee feels the contract is a good deal, she will act by "fulfilling [the debtor's] obligations while benefiting from the counterparty's performance." *Id.* If the trustee feels the

contract is a bad deal, she will reject the deal, "repudiating any further performance of [her] duties." *Id.* Decisions to accept or reject executory contracts are routinely approved by bankruptcy courts under the deferential business judgment rule. *Id.*

Armed with the power to accept or reject executory contracts, "[t]he trustee shall timely perform all the obligations of the debtor . . . arising from and after the order for relief under any unexpired lease of nonresidential real property, until such lease is assumed or rejected, notwithstanding section 503(b)(1) of this title." 11 U.S.C. § 365(d)(3)(A). The point of contention within § 365(d)(3)(A) is identifying exactly when an obligation arises. The lower courts have taken two distinct approaches. The majority of courts interpret § 365(d)(3)(A) as requiring the "proration" approach, which "provides that only those amounts that accrued during the time the debtor or trustee was in possession of the property 'arise after the order for relief' and should be assessed against the estate.'" *In re Furr's Supermarkets, Inc.*, 283 B.R. 60, 62 (B.A.P. 10th Cir. 2002). A minority of courts defer to the "billing date" approach, interpreting § 365 (d)(3)(A) as requiring that "obligations under a lease 'arise' when they are billed and must be paid in full irrespective of whether the obligations accrued before or after the order for relief." *Id.*

The Thirteenth Circuit and the Bankruptcy Court for the District of Moot have elected to adopt the "proration" approach. It is well understood, and this Court firmly believes, that "bankruptcy courts . . . rule correctly most of the time." *Bullard v. Blue Hills Bank*, 575 U.S. 496, 507 (2015). This Court should keep that same spirit of confidence in the courts below and hold that a bankruptcy trustee does not have to pay a debtor's rent when it is due prior to the rejection of an unexpired non-residential real property lease but allocable to the period after the rejection date.

A. The Text of § 365(d)(3) is Ambiguous, Requires Further Analysis Beyond its Plain Language, and is Best Honored by the "Proration" Approach.

The text of 11 U.S.C § 365(d)(3)(A) is ambiguous on its face. The statute states that "[t]he trustee shall timely perform all the obligations of the debtor . . . arising from and after the order for relief under any unexpired lease of nonresidential real property, until such lease is assumed or rejected, notwithstanding section 503(b)(1) of this title." § 365(d)(3)(A). There are two parts of § 365(d)(3)(A) that are ambiguous: the term "arising" and the phrase "until such lease is assumed or rejected."

The term "arising," undefined by the Bankruptcy Code, is susceptible to at least two different meanings. "It can be either an absolute occurrence or something that is continuing to accrue." R. at 17. Indeed, an obligation "may arise as it is accrued, or it may arise when the landlord submits the bill to the debtor-tenant." *In re Phar-Mor, Inc.*, 290 B.R. 319, 324 (Bankr. N.D. Ohio 2003). Just as with the rest of the Bankruptcy Code, Congress neglected to provide instruction on both how to interpret the term "arising" and when a debtor's obligation arises under § 365(d)(3)(A). *See In re Montgomery Ward Holding Corp.*, 268 F.3d 205, 213 (3d Cir. 2001) (Mansmann, J., dissenting) ("[T]he statute says nothing about how to determine when the obligation arises. . . . An obligation attributable to a particular time may well be said to 'arise' at that time, and an obligation that accrues over time may be said to 'arise' as it accrues, without doing violence to the statutory language.").

Similarly, the phrase "until such lease is assumed or rejected" may be interpreted in two different ways. The phrase could be interpreted to modify either the word "perform" or "obligations." If the phrase modifies "perform," § 365(d)(3)(A) could be construed as mandating the completion of any payment due under a lease until that lease is assumed or rejected; if the phrase modifies "obligations," § 365(d)(3)(A) could be construed as meaning that

the trustee's duty to perform the obligation in question ceases upon rejection. *See In re Ames Dep't Stores, Inc.*, 306 B.R. 43, 67 (Bankr. S.D.N.Y 2004) ("And (2) 'until such lease is assumed or rejected' can be construed to modify (a) 'perform'—in which case it would support an absolutist view, inconsistent with prorating—or (b) equally or more plausibly, 'obligations'—in which case prorating would be necessary and appropriate.").

It is true that the "starting point in every case involving construction of a statute is the language itself." *Id.* at 66. However, "'text is only the starting point,' especially when the language is ambiguous." *Id.* Furthermore, "[s]tatutory language . . . cannot be construed in a vacuum." *Roberts v. Sea-Land Servs., Inc.*, 566 U.S. 93, 101 (2012). Rather, when it comes to interpreting the Bankruptcy Code, "we must not be guided by a single sentence or [part] of a sentence, but look to the provisions of the whole law, and to its object and policy." *In re Ames Dep't Stores, Inc.*, 306 B.R. at 66. Indeed, "[i]t is a fundamental canon of statutory construction that the words of a statute must be read in their context and with a view to their place in the overall statutory scheme." *Roberts*, 566 U.S. at 101.

The "proration" approach, rather than the "billing date" approach, is the scheme that is most true to the ambiguous statutory text of § 365(d)(3)(A). There is no doubt that the term "arising" is "susceptible of being used in an accrual sense: a rental obligation arises under the lease based on the corresponding period of occupancy under the lease." *In re NETtel Corp.*, 289 B.R. 486, 490 (Bankr. D.D.C. 2002). Commonsensically, "[a] landlord's entitlement to compensation for occupancy at a fixed periodic rate relates to the actual days the tenant was entitled to occupancy . . . ." *Id.* This indicates that the landlord's entitlement to such compensation "can be said to arise on each occupancy day." *Id.* Here, the Debtor moved out of the premises on May 5th, 2020. R. at 7. Just like the Bankruptcy District Court for the District

of Columbia found in *In re NETtel Corp.*, this Court should find that "the Base Rent, the obligation at issue, 'could realistically be said to have arisen piecemeal every day.'" *Id.* A correct statutory interpretation of § 365(d)(3)(A) commands as much.

Finally, even if this Court were to find that the text of § 365(d)(3)(A) was clear and unambiguous, it should still reject the "billing date" approach and embrace the "proration" approach. "Courts 'must look beyond the language of the statute . . . when[,] . . . although the statute is facially clear, a literal interpretation would lead to internal inconsistencies, an absurd result, or an interpretation inconsistent with the intent of Congress.'" Victoria Kothari, *11 U.S.C. § 365(d)(3): A Conceptual Status Argument for Proration*, 13 Am. Bankr. Inst. L. Rev. 297, 315 (2005). "When context is disregarded, silliness results." *In re Handy Andy Home Improvement Ctrs., Inc.*, 144 F.3d 1125, 1128 (7th Cir. 1998); *see, e.g., In re NETtel Corp.*, 289 B.R. at 490 ("Under the [billing] date approach, a trustee would be obligated to pay for a full year's rent that came due immediately after the order for relief even if the lease were rejected prior to the commencement of the year of occupancy covered by the payment. Congress did not likely intend such absurd results."). Here, following the "billing date" approach would result in both silliness and absurdity by requiring the Debtor to pay for eighty-four percent of a leasing period from which it did not benefit. Congress did not intend this result.

B. The Historical Application, Legislative History, and Underlying Policies of § 365(d)(3)(A) Mandate Application of the "Proration" Approach.

The historical application, legislative history, and underlying policies of § 365(d)(3)(A) all indicate that interpreting § 365(d)(3)(A) as requiring the "proration approach" is the correct analysis.

First, prior to the promulgation of the Bankruptcy Code, courts overwhelmingly applied the "proration" approach to rejections of unexpired leases of nonresidential real property as well

as other situations. *See* Kothari, *supra* at 304 ("Further, it was pre-Code practice to prorate any post-petition real estate taxes obligations provided for in the lease."); *see also In re Handy Andy Home Improvement Centers, Inc.*, 144 F.3d at 1128; *In re Furr's Supermarkets, Inc.*, 283 B.R. at 68–69; *In re Ames Dep't Stores, Inc.*, 306 B.R. at 65; *In re GCP CT Sch. Acquisition, LLC*, 443 B.R. 243, 254–55 (Bankr. D. Mass. 2010); *In re NETtel Corp.*, 289 B.R. at 490; *In re Child World, Inc.*, 161 B.R. 571, 574 (S.D.N.Y 1993). This is of high importance because "tracing the immediate post-petition landlord-debtor relationship from pre-Code practice through section 365(d)(3) provides a historical reference for judicial interpretation of Congressional intent where the plain language does not suffice, and in this case supports adoption of the proration or accrual method." Kothari, *supra* at 304.

Even when Congress promulgated the Bankruptcy Code in 1978, payments owed under rejected nonresidential property leases that were awarded administrative expense priority under § 503(b) "should not [have] exceed[ed] the fair and reasonable rental value." *In re Dant & Russell, Inc.*, 853 F.2d 700, 707 (9th Cir. 1988). The amount of the claim was limited to "the 'portion of the leased property' that is actually used or occupied." *Id.* (citing *In re Thompson*, 788 F.2d 560, 562 (9th Cir. 1986)). Indeed, courts had the discretion to "choose to fix a different amount based on the debtor-in-possession's actual use" of the leased property. *Id.* This, of course, is premised on the maxim that the "debtor-in-possession or trustee's liability for actual use and occupancy is not compensatory but rather is founded upon the equitable principle of preventing unjust enrichment." *Id.* In summary, courts have instituted a "'long-standing practice [under § 503(b)(1)] of prorating debtor-tenant's rent to cover only the post-petition, pre-rejection period, regardless of billing date.' Thus, the pre-Code practice of proration continued during the early years of the Code." Kothari, *supra* at 305.

Second, the legislative history surrounding § 365(d)(3)(A) instructs that the "proration" approach is the one which Congress desired. There is no doubt that it was Congress's intention "[t]o give relief to landlords" by "allow[ing] them during that awkward post-petition prerejection period to collect the rent fixed in the lease." *In re Furr's Supermarkets, Inc.*, 283 B.R. at 67. However, Congress only intended § 365(d)(3)(A) "to put landlords on an equal footing, not to grant them a windfall at the expense of other creditors." *In re Ames Dep't Stores, Inc.*, 306 B.R. at 69. Indeed, "[a]llowing landlords to recover for items of rent which are billed during the postpetition, prerejection period, but which represent payment for services rendered by the landlord outside this time period, would grant landlords a windfall payment, to the detriment of other creditors, without any support form the legislative history." *In re GCP CT Sch. Acquisition, LLC*, 443 B.R. at 254—55. Instead, "the logic of requiring debtor-tenants to pay for the 'current services' their landlords must provide during the postpetition, prerejection period dictates that to the extent such payments consist of rent, they should be prorated to cover only the postpetition, prerejection period." *Id.* at 254.

The legislative history of § 365(d)(3)(A) captures Senator Orrin Hatch's sentiments that, when debtors reject a lease and vacate the premises, "the other tenants often must increase their common area charge payments to compensate for the trustee's failure to make the required payments to the debtor." 1984 U.S.C.C.A.N. 576, 599. Senator Hatch expresses that, "[t]he bill would lessen these problems by requiring the trustee to perform all the obligations of the debtor under a lease of nonresidential real property at the time required in the lease." *Id.* However, even though there existed congressional intent "to do away with prejudice to landlords, . . . there is no indication of a corresponding intention to grant landlords a windfall, especially at the expense of other creditors." *In re Ames Dep't Stores, Inc.*, 306 B.R. at 70. Hence, if a court

followed the "billing date" approach, the un-prorated rent amount "would be paid by the Chapter 7 estate before payments to any other administrative claimant or creditor. Had this been the intent of Congress, it would have enacted conforming amendments to sections 503 and 507 along with the amendment to § 365(d)." *In re Furr's Supermarkets, Inc.*, 283 B.R. at 69. These aforementioned reasons are why courts are exceedingly reluctant "to adopt an interpretation of section 365(d)(3) that is so at odds with its true legislative purpose and common sense." *In re Ames Dep't Stores, Inc.*, 306 B.R. at 80.

Third, the underlying policies of § 365(d)(3)(A) favor the "proration" approach. It is important to understand that § 365(d)(3)(A) is grounded in fundamental fairness. *Id.* at 69. Therefore, it makes sense that "Congress enacted § 365(d)(3) to ensure that landlords would not be disadvantaged by providing post-petition services to the debtor." *Id.* Nevertheless, "[p]ost-rejection [p]rorating is required to avoid extending section 365(d)(3) beyond its intended effect, and to achieve fairness for other creditors." *Id.* at 65. The focus is not just on the Creditor in this case, but on all creditors. *See In re Child World, Inc.*, 161 B.R. at 574 ("The policy behind this statutory scheme is to facilitate the efforts of the trustee or debtor in possession to rehabilitate the business for the benefit of all the estate's creditors."). Indeed, "there is no indication that Congress meant . . . to give landlords favored treatment for any class of prepetition debts." *In re Handy Andy Home Improvement Ctrs, Inc.*, 144 F.3d at 1128.

For the foregoing reasons, the historical application, legislative history, and underlying policies of § 365(d)(3)(A) vehemently reject the "billing date" approach and mandate application of the "proration" approach.

C. The Legislative History and Underlying Policies of the Entire Bankruptcy Code Mandate Application of the "Proration" Approach.

The legislative history and underlying policies of the entire Bankruptcy Code discourage application of the "billing date" approach and calls for application of the "proration" approach. Historically, bankruptcy courts have been deemed courts of equity. *See In re Enron Corp.*, 333 B.R. 205, 218 (Bankr. S.D.N.Y. 2005) (citing *In re Westgate–California Corp.*, 642 F.2d 1174, 1177 (9th Cir.1981) ("In addition, 'bankruptcy courts are empowered [by the common law concept of the equitable doctrine] to subordinate claims where the subordination will promote a just and equitable distribution of the bankruptcy estate.'"). "The Bankruptcy Code aims, in the main, to secure equal distribution among creditors." *Howard Delivery Serv., Inc.*, 547 U.S. at 655. Furthermore, "one of the prime purposes of the bankruptcy law has been to bring about a ratable distribution among creditors of a bankrupt's assets; to protect the creditors from one another." *Young*, 324 U.S. at 210.

By implementing the "billing date" approach, this Court would "elevate the claims of landlords for the post-rejection period of all of the estate's other creditors—a result exactly contrary to the plain meaning, and purpose, of sections 365(g) and 502(g)." *In re Ames Dep't Stores, Inc.*, 306 B.R. at 70. Applying the "proration" approach does not raise these concerns. Furthermore, contrary to the spirit of the Bankruptcy Code, "[t]he [billing] date approach in applying § 365(d)(3) often converts what would be prepetition debt (attributable to either pre-order-for-relief occupancy or post-rejection occupancy) into an administrative claim, thereby violating the principle of creditor equality and distorting the priority and distribution provisions of other sections of the Bankruptcy Code." *In re NETtel Corp.*, 289 B.R. at 492—93. Until Congress specifically advises such a diversion from the Bankruptcy Code's previous practices, this Court is discouraged from deviating. *See Pennsylvania Dep't of Pub. Welfare v. Davenport*,

495 U.S. 552, 563 (1990) (stating the Court "will not read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure.").

Because of the Bankruptcy Code's deep roots in equitable doctrine and fundamental fairness, this Court should interpret § 365(d)(3)(A) as requiring the "proration" approach.

CONCLUSION

For the foregoing reasons, this Court should affirm the decisions of the Court of Appeals for the Thirteenth Circuit on both issues and find in favor of Respondent.

Respectfully submitted,

Team 14

Counsel for Respondent

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