Team 26

No. 21-0909

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 2021

IN RE TERRAPIN STATION, LLC, DEBTOR,

TOUCH OF GREY ROASTERS, INC.,

Petitioner,

V.

CASEY JONES, CHAPTER 7 TRUSTEE,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE THIRTEENTH CIRCUIT

BRIEF FOR THE RESPONDENT

Team 26
Counsel 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 the debtor in possession paid for such goods in full pursuant to 11 U.S.C. § 503(b)(9).

II. Whether a trustee must timely perform the obligations of a debtor under 11 U.S.C. § 365(d)(3) by paying rent due prior to the rejection of an unexpired non-residential real property lease but allocable to the period after the effective date of rejection.

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The Thirteenth Circuit Court of Appeals' decision is available at No. 21-0803 and reprinted at R. 2. Both the bankruptcy court and the United States District Court for the District of Moot decided in favor of the Trustee and against Touch of Grey Roasters, Inc. On appeal, the United States Court of Appeals for the Thirteenth Circuit affirmed the bankruptcy court's decision in favor of the Trustee.

STATEMENT OF 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(b) provides:

(b) Except as provided in subsection[] (c) . . . of this section, the trustee may . . . taking into account a party's known or reasonably knowable affirmative defenses under subsection (c), avoid any transfer of an interest of the debtor in property.

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

(2) "new value" means money or money's worth in goods.

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

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

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

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

(d)(3) The trustee shall timely perform all the obligations of the debtor, except those specified in section 365(b)(2), 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;

STATEMENT OF THE CASE

I. FACTUAL HISTORY

Debtor Terrapin Station, LLC ("Terrapin Station") is a coffeehouse, which was founded in 2005 and was successful for several years. R. at 3. Petitioner Touch of Grey Roasters, Inc. ("Touch of Grey") is an "international coffee company" with both franchise and corporate-owned stores. R. at 3. Touch of Grey approached Terrapin Station's owner, William Tell, in the fall of 2017 inviting him to open one of these franchised stores. R. at 3. On July 1, 2018, Terrapin Station and Touch of Grey entered into Franchise and Lease Agreements. R. at 4. Under the Franchise Agreement, Terrapin Station would sell only Touch of Grey's products. *Id.* Under the Lease Agreement, Terrapin Station agreed to a "twenty-year triple-net lease" paying $25,000 "due in advance on the first day of each month." R. at 4. The new franchise opened on December 1, 2018. R. at 5. However, Terrapin Station struggled financially. R. at 5.

Though Terrapin Station continued to pay rent to Touch of Grey, by November 1, 2019, Terrapin Station owed Touch of Grey more than $700,000 for goods it purchased. R. at 5. As a result of this debt, Touch of Grey notified Terrapin Station of default on December 5, 2019. R. at 5. Terrapin Station and Touch of Grey entered into a Forbearance Agreement on December 7, 2019. R. at 5. Under the agreement, Touch of Grey agreed not to terminate the Franchise Agreement. *Id.* In exchange, Terrapin Station paid $250,000 of what it owed to Touch of Grey for goods, reaffirmed its lease obligations to Touch of Grey, and released all claims against Touch of Grey. R. at 5.

On December 18, 2019, Terrapin Station purchased, on credit, $200,000 worth of goods from Touch of Grey. *Id.* Touch of Grey delivered the goods on December 21, 2019. R. at 5–6. However, after lackluster holiday sales, Terrapin Station filed for Chapter 11 bankruptcy on January 5, 2020. R. at 6. On the petition date, Terrapin Station owed unsecured creditors $500,000 and Touch of Grey $650,000 (the $450,000 remaining after the $250,000 Forbearance Agreement payment plus $200,000 for the goods delivered on December 21). R. at 6. Hoping to reorganize, Terrapin Station proposed continuing to sell Touch of Grey's goods in compliance with the Franchise Agreement and moved to pay Touch of Grey $200,000 as a "critical vendor." R. at 6.

The bankruptcy court was unsure whether the Bankruptcy Code ("the Code") authorized critical vendor payments and rejected Debtor's critical vendor argument. R. at 7. However, it allowed the estate to pay Touch of Grey $200,000 as an administrative expense under section 503(b)(9) instead. R. at 7. After receiving this payment, Touch of Grey resumed selling goods to Terrapin Station on credit. R. at 7. However, in March 2020, the COVID-19 pandemic hit, greatly impacting Terrapin Station's ability to operate. R. at 7. As a result, Terrapin Station permanently ceased operations on May 5, 2020, and vacated the premises. R. at 7. The following day, Terrapin Station moved to reject both the Lease and Franchise Agreements under section 365(a). R. at 7. Three days later, Touch of Grey filed a motion with the bankruptcy court seeking to compel Terrapin Station to pay May's rent which had come due on May 1, 2020. R. at 7. Touch of Grey argued that it should be paid May's rent in its entirety under section 365(d)(3) because the rent came due prior to the rejection date of May 5, 2020. R. at 8.

The bankruptcy court held a hearing on May 29, 2020. R. at 8. At that hearing, Terrapin Station converted its Chapter 11 case to a Chapter 7 and the court appointed Casey Jones as Trustee ("Trustee"). R. at 8. The court also granted Terrapin Station's motion to reject the Lease and Franchise Agreement as of May 5, 2020. R. at 8. However, it requested additional briefing on Touch of Grey's request for the entirety of May's rent. R. at 8.

Ultimately, the Trustee objected to Touch of Grey's request for the entirety of May 2020's rent and instead argued that Touch of Grey should only receive prorated rent for the five days in

May that Touch of Grey occupied the premises. R. at 8. Additionally, the Trustee commenced an adversary proceeding against Touch of Grey, seeking to avoid as a preference the $250,000 Forbearance Agreement payment. R. at 8. In response, Touch of Grey sought to reduce its preference exposure under section 547(c)(4) for new value it gave Terrapin Station. R. at 8. Touch of Grey argued it gave Terrapin Station new value by delivering $200,000 worth of goods on December 21, 2019, and that its $250,000 preference exposure should be reduced accordingly. R. at 8.

The Trustee and Touch of Grey did not come to a successful resolution through mediation. R. at 8. Ultimately, because the preference exposure issue was a purely legal question, the parties filed cross-motions for summary judgment. R. at 9. At the hearing on the summary judgment motions, the bankruptcy court also heard arguments for Touch of Grey's request for May's rent. R. at 9.

II. PROCEDURAL HISTORY

The bankruptcy court and the District Court for the District of Moot ruled in favor of the Trustee on both issues. R. at 9. On appeal, the United States Court of Appeals for the Thirteenth Circuit affirmed the decisions of the bankruptcy court and the district court, holding that 1) a creditor cannot reduce its preference exposure by asserting new value under section 547(c)(4) if it has been paid for that new value under section 503(b)(9), and 2) section 365(d)(3) does not require the Trustee to satisfy obligations allocable to the post-rejection period. R. at 9.

STANDARD OF REVIEW

The questions at issue involve statutory interpretation of the Bankruptcy Code and therefore, are solely questions of law. As such, the applicable standard of review is *de novo*. *Texas v. Soileau (In re Soileau)*, 488 F.3d 302, 305 (5th Cir. 2007).

SUMMARY OF THE ARGUMENT

This Court should affirm the Thirteenth Circuit Court of Appeals and find for the Trustee on both issues. A creditor cannot reduce its preference exposure by applying new value under section 547(c)(4) if it was fully paid for that new value as an administrative expense under section 503(b)(9). Section 547(c)(4)(B) prohibits a creditor from doing so because the administrative payment is an otherwise unavoidable transfer. Further, this Court achieves the policy goals and honors the legislative intent behind both sections 547(c)(4) and 503(b)(9) by holding that creditors can assert value under only one.

Additionally, a creditor is not entitled to the entirety of a month's rent if it occupies the premises for less time. Both principles of statutory interpretation and sound policy direct that under section 365(d)(3), a lessor can collect only the prorated amount of rent for the days a debtor occupied the premises before rejecting the lease agreement.

First, a creditor cannot use the value of goods it delivered to a debtor to reduce its preference exposure if it received an administrative payment for that value. In bankruptcy, a trustee seeks to maximize the value of the estate for the benefit of all the debtor's creditors. A trustee can undo certain transfers of the debtor's property under the preference provisions of the Bankruptcy Code ("the Code"), including section 547(b). This is called avoidance and ensures that a debtor's property will be equally distributed to its creditors. Once a debtor files for bankruptcy, a creditor must return any transfers that the trustee can avoid under section 547(b). A creditor's preference exposure equals the value of these transfers.

However, a creditor may have a defense it can use to reduce or eliminate its preference exposure. Section 547(c)(4) is available when a creditor gives new value to a debtor after the preferential transfer was made. New value includes goods. A creditor may use the defense to reduce its preference exposure by the amount of new value it gave. However, section 547(c)(4)(A) prohibits the value from being secured by an otherwise unavoidable security interest. Additionally, if the debtor made an otherwise unavoidable transfer on account of the new value, section 547(c)(4)(B) prohibits a creditor from using the defense.

Once bankruptcy is underway, a trustee may pay a creditor for various administrative expenses under section 503(b). If a creditor delivered goods to the debtor in the twenty-one days preceding the debtor filing for bankruptcy, a debtor or trustee can pay the creditor for the value of the goods under section 503(b)(9). Both sections 547(c)(4) and 503(b)(9) serve to protect creditors when their debtors enter financial trouble.

A creditor cannot assert the same value for which it received an administrative expense payment to reduce its preference exposure under section 547(c)(4) because the payment is an otherwise unavoidable transfer, which is prohibited by section 547(c)(4)(B). First, an administrative expense payment is a transfer by the debtor. In section 101(54), the Code defines transfer broadly and courts hold that administrative expense payments are transfers. Transfers from post-petition entities like estates and liquidating trusts are still transfers from the debtor. This is because the value of the transfer originates with the debtor and flows through the estate or trust. Further, if a creditor receives a preferential transfer, delivers new value in goods, and then receives an administrative expense payment in return, such payment is a transfer on account of the new value. Accordingly, an administrative expense payment under section 503(b)(9) is a transfer from the debtor to the creditor on account of the new value given.

Next, a transfer that a trustee cannot avoid under any provision of the Code other than section 547(c)(4) is an otherwise unavoidable transfer. While trustees can avoid transfers under several preference provisions of the Code, a trustee cannot avoid an administrative expense payment under any of them. So, an administrative expense payment under section 503(b)(9) is an otherwise unavoidable transfer.

Section 547(c)(4) permits a creditor to reduce its preference exposure to the extent of new value given only if the debtor did not make an otherwise unavoidable transfer to the creditor on account of that new value. Because an administrative expense payment under section 503(b)(9) is an otherwise unavoidable transfer, a creditor who received such payment cannot use the value for which it was paid to reduce its preference exposure because it fails to satisfy section 547(c)(4).

Additionally, a court achieves the policies Congress intended when it limits a creditor to assert value under either section 547(c)(4) or section 503(b)(9), but not both. Courts cite and legislative history confirms that the primary policy goal of the Code's preference provisions is to treat creditors equally. Strikingly, courts treat creditors unequally when they authorize administrative expense payments because the timing and amount of such payments violate the general bankruptcy rules of creditor priority. Courts conclude that the benefit to debtors and protection for creditors available under section 503(b)(9) justifies this unequal treatment. However, courts must strictly limit this unequal treatment to the extent it is authorized explicitly by the Code.

Courts properly limit this treatment when they hold that creditors may assert new value to receive an administrative expense payment or to reduce preference exposure, but not both. Section

547(c)(4) seeks to recognize when creditors enlarged the estate to the benefit of other creditors. This consideration ensures a creditor who has enlarged the estate will be allowed to reduce its preference exposure to the same extent, which treats that creditor equally in return for its contribution. If a creditor enlarges the estate with new value, but later receives payment under section 503(b)(9) for that value, the estate is no longer enlarged. Therefore, courts would treat the debtor's other creditors unequally if it allowed the creditor to use the value a second time to reduce its preference exposure.

Additionally, courts do not detract from the policy goal of encouraging creditors to work with financially troubled debtors by limiting creditors this way. Some argue that limiting creditors takes creditor protections away, discouraging them from extending credit to debtors they fear are headed for bankruptcy. However, a creditor loses nothing by not using value to reduce its preference exposure if it was already paid for the value as an administrative expense.

This Court properly applies the provisions of sections 547(c)(4) and 503(b)(9), and achieves the policy goals and Congressional intent behind these provisions by precluding creditors from using the same value under both.

The second issue before this Court is whether a lessor is entitled to a full month's rent that came due before a debtor rejected an unexpired non-residential lease agreement but where a portion of that rent is allocable to the period after the rejection date. The Thirteenth Circuit properly held that a lessor is not entitled to a full month's rent under these circumstances. Instead, section 365(d)(3) only permits a lessor to receive the prorated amount of rent for the days on which the debtor occupied the premises before rejecting the lease agreement. Both principles of statutory interpretation and sound policy demand this outcome.

While statutory analysis always begins with the text itself, the text of section 365(d)(3) does not clearly articulate when the lease's obligations arise. While there is no debate that the trustee is obligated to fulfill the lease's obligations in between the petition and rejection date; the section does not unambiguously say whether those obligations arise when billed or if they continuously accrue. While one possible interpretation requires that the trustee strictly perform any obligation that came due in between the petition and rejection dates, an equally, if not more plausible interpretation only requires the trustee to pay the obligation that arises during the time the debtor or trustee was in possession of the property. These differing interpretations are known as the "performance date" rule and the "proration" rule, respectively. Ultimately, the provision's text itself is not sufficiently clear to answer the question of whether a creditor is entitled to a full month's rent.

Statutory analysis does not end with the provision's text and section 365(d)(3) must be read in context with other relevant provisions of the Code. Putting section 365(d)(3) in context with other relevant provisions such as sections 365(g), 502(b)(6), and 502(g) show that this Court should adopt the "proration" rule because to decide otherwise would render those provisions meaningless. Courts rely on this canon of surplusage when one interpretation of a statute renders another provision in the same statutory scheme superfluous.

Sections 365(g), 502(b)(6), and 502(g) clearly show that once a debtor rejects a lease obligation, a failure to honor the obligation is a pre-petition claim under the Code. Adopting the "performance date" rule would allow a lessor to receive rent as a higher priority administrative expense that is allocable to the post-rejection period. Allowing this rule would upset the long-established priority scheme for claims and cannot be the correct result. Instead, to avoid this upset, the Court should adopt the "proration" rule that coherently fits together section 365(d)(3) with sections 365(g), 502(b)(6), and 502(g). Under this approach, while a lessor would receive administrative expense priority status for the rent allocable to the period before the rejection date, it would have a pre-petition claim for the rent allocable to the period after the rejection date, just as the Code intended.

Additionally, while Congress amended the Code in 1984 to include section 365(d)(3), there is no indication in the provision's language that Congress intended to upset the long-established precedent that lessors received *prorated* rent for the post-petition, pre-rejection period as an administrative expense under section 503. That is, up until 1984, lessors were required to file a motion with the bankruptcy court seeking payment as an administrative expense for debtor's obligations that arose during the post-petition, pre-rejection period. Courts generally paid lessors the prorated rent up until the rejection date. Had Congress intended to alter this established practice, it easily could have done so. Yet, there is no language in section 365(d)(3) that suggests Congress intended lessors to receive administrative expense priority status for obligations that are allocable to the post-rejection period.

Finally, in addition to the lack of clear language in section 365(d)(3) supporting the "performance date" rule, the legislative history surrounding this section's enactment also fails to show Congress intended that result. Instead, Congress only indicated that it desired to lessen the financial burden on commercial lessors for the post-petition, pre-rejection period when a debtor still received the lessor's services but did not have to pay rent because of the automatic stay. That is, it intended to assist lessors for a finite, specific period during which the debtor received "free services." However, upon rejection, a debtor is required to immediately vacate the rented premises and as a result, the lessor no longer provides "free services" to the debtor. The lessor should not benefit from a windfall by receiving rent that is allocable to the time after the debtor has vacated the premises. And Congress did not indicate it intended such a result.

For the reasons set forth above, the Court should adopt the "proration" rule, not the "performance date" rule.

ARGUMENT

This Court should affirm the Thirteenth Circuit Court of Appeals and hold that a creditor cannot reduce its preference exposure by applying new value under section 547(c)(4) if it was fully paid for that new value as an administrative expense under section 503(b)(9). Additionally, this Court should affirm the Thirteenth Circuit and hold that a lessor is entitled to only a prorated amount of rent for the days a debtor occupied the premises before rejecting the lease agreement under section 365(d)(3).

1. The Thirteenth Circuit properly held that Touch of Grey cannot use the value of goods it delivered to Terrapin Station to reduce its preference exposure under section 547(c)(4) because it was paid for that value as an administrative expense under section 503(b)(9).

Touch of Grey cannot reduce its preference exposure with new value under section 547(c)(4) because it received payment under section 503(b)(9) for that value, rendering it unable to satisfy the elements of section 547(c)(4). In bankruptcy, a trustee can avoid (undo) some transfers of the debtor's property that happened before the debtor declared bankruptcy. 11 U.S.C. §§ 544; 547(b). A trustee can avoid transfers to creditors made during the preference period if certain conditions are met. 11 U.S.C. § 547(b). A trustee can avoid these transfers, known as preferences, to ensure creditors receive equal distributions of the bankruptcy estate. *Merit Mgmt. Grp., LP v. FTI Consulting, Inc.*, 138 S. Ct. 883, 888 (2018). A creditor's preference exposure is the value of transfers it receives from the debtor during the preference period which the trustee may avoid. *See In re Proliance Int'l, Inc.*, 514 B.R. 426, 430 (Bankr. D. Del. 2014).

However, even when a trustee satisfies section 547(b), entitling it to avoid a preferential transfer, a creditor may reduce or limit the trustee's avoidance to the extent the creditor has a defense enumerated in section 547(c). 11 U.S.C. §§ 547(b), 547(c). *See also* 11 U.S.C. § 550(a). This includes the new value defense enumerated in section 547(c)(4). A creditor must meet certain conditions to use this defense. 11 U.S.C. § 547(c)(4). First, a creditor must give new value to the debtor after receiving a transfer that the trustee can avoid. *Id.* New value includes "money's worth in goods." 11 U.S.C. § 547(a)(2). Next, the new value cannot be "secured by an otherwise unavoidable security interest." *Id.* (c)(4)(A). Finally, the debtor cannot make "an otherwise unavoidable transfer" to the creditor "on account of [the] new value" given. *Id.* (c)(4)(B). If these conditions are met, a creditor can reduce its preference exposure by the amount of new value it gave.

Additionally, a trustee may request and the court can authorize a trustee to pay a creditor for various administrative expenses, even if such payment violates bankruptcy law's general creditor priority rules. One allowable expense pays a creditor for the value of goods it delivered to the debtor in the twenty-one days preceding the petition date on which the debtor filed for bankruptcy. 11 U.S.C. § 503(b)(9).

Courts properly interpret and apply the overlapping sections 547(c)(4)(B) and 503(b)(9) when they hold that administrative payments are otherwise unavoidable transfers. Lower courts disagree about when a creditor receives an otherwise unavoidable transfer for new value pursuant to section 547(c)(4)(B) such that it cannot assert the value under the statute to reduce its preference exposure. Early courts interpreted section 547(c)(4)(B) to require that the new value remain unpaid at the time the debtor files for bankruptcy. *E.g.*, *In re Bishop*, 17 B.R. 180, 183 (Bankr. N.D. Ga. 1982). Here, the parties stipulated that new value need not remain unpaid for Touch of Grey to be able to reduce its preference exposure. R. at 10, n.5. Under the proper approach, a creditor who receives an administrative expense payment for value cannot reduce its preference exposure under section 547(c)(4) with that same value.

Here, the Trustee seeks to avoid as a preference $250,000 Terrapin Station paid Touch of Grey. The parties stipulated that the payment meets the requirements for trustee avoidance under section 547(b). R. at 9, n.3. Touch of Grey seeks to reduce this preference exposure under section 547(c)(4) with new value it gave to Terrapin Station. R. at 8. The record confirms that Touch of Grey gave Terrapin Station $200,000 of new value. R. at. 5–6. However, Touch of Grey cannot reduce its preference exposure by asserting this new value because it received an administrative expense for that value. More specifically, Touch of Grey cannot satisfy the elements of section 547(c)(4) and prohibiting Touch of Grey from reducing its preference exposure achieves the policy goals Congress intended with both statutes.

A. *Touch of Grey cannot satisfy the elements of section 547(c)(4) and so it cannot reduce its preference exposure.*

Touch of Grey satisfies several but not all of the requirements to reduce its preference exposure under section 547(c)(4). Creditors have nine defenses that preclude trustees from avoiding preferential transfers "under this section." 11 U.S.C. § 547(c). "This section" refers to section § 547, and so where applicable, these defenses preclude a trustee from avoiding transfers by using section 547(b). *See id.* Reducing preference exposure under section 547(c)(4) precludes a trustee from avoiding transfers "to or for the benefit of a creditor." 11 U.S.C. § 547(c)(4). Here, the Trustee seeks to avoid the $250,000 payment to Touch of Grey. At the time of the payment, Terrapin Station owed Touch of Grey more than $700,000 for goods it purchased on credit. After defaulting on this debt, Terrapin Station paid Touch of Grey $250,000 under a Forbearance

Agreement. This payment was a transfer to the creditor, and Touch of Grey satisfies the first portion of section 547(c)(4).

Next, section 547(c)(4) precludes avoidance only "*to the extent* that, *after* such transfer, such creditor gave *new value* to or for the benefit of the debtor." 11 U.S.C. § 547(c)(4) (emphasis added). This means a creditor may reduce the trustee's avoidance or preclude it altogether, to the extent of the amount of new value the creditor gave the debtor after the preferential transfer. *In re Check Reporting Servs.*, 140 B.R. 425, 430–431 (Bankr. W.D. Mich. 1992). Here, after the preferential $250,000 Forbearance Payment, Touch of Grey delivered $200,000 worth of goods to Terrapin Station, which qualifies as new value given to the debtor. R. at 6. So, Touch of Grey seeks to reduce the Trustee's avoidance of the $250,000 Forbearance Payment to the extent of $200,000. R. at 8. This would permit the Trustee to avoid only $50,000 of the Forbearance Payment and allow Touch of Grey to retain $200,000.

However, Touch of Grey must satisfy two additional conditions to reduce its preference exposure under section 547(c)(4). The new value Touch of Grey delivered was not secured by an otherwise unavoidable security interest, satisfying the condition in section 547(c)(4)(A). *See* R. at 5–6. Similarly, the parties stipulated that Touch of Grey has no other defense against trustee avoidance under section 547(c) besides the new value defense. *Id.* However, Touch of Grey fails to satisfy section 547(c)(4)(B) which requires that it give new value "on account of which . . . the debtor did *not* make an otherwise unavoidable transfer" to the creditor. 11 U.S.C. § 547(c)(4)(B) (emphasis added). After Touch of Grey delivered the new value, Terrapin Station *did* make an otherwise unavoidable transfer to the creditor on account of the new value when it paid Touch of Grey an administrative expense payment.

i. **The administrative expense payment was a transfer by the debtor.**

Here, the administrative expense payment was a transfer by the debtor to the creditor. The Code defines transfer broadly and includes "each mode, direct or indirect, absolute or conditional, voluntary or involuntary" of disposing of property. 11 U.S.C. § 101(54); *accord In re Beaulieu Grp., LLC*, 616 B.R. 857, 870 (Bankr. N.D. Ga. 2020). A payment qualifies as a transfer. *See In re Circuit City Stores, Inc.*, No. 08-35653, 2010 WL 4956022, at *6 (Bankr. E.D. Va. 2010). In *In re Beaulieu Grp., LLC*, a liquidating trust reserved funds to make an administrative expense payment to a creditor. 616 B.R. at 870. The court held that the future administrative expense payment was a transfer. *Id.* at 870–71. Additionally, the court held that this transfer by the trust was a transfer by the debtor. *See id.* The court reasoned that the debtor ultimately made the administrative expense payment, which merely passed through the trust. *Id.* Here, the estate is similar to the trust in *Beaulieu* because Terrapin Station's assets pass through the estate for distribution to creditors. So, even though the payment came from the estate, Terrapin Station made a direct transfer of property from a debtor to a creditor when it paid Touch of Grey the $200,000 administrative expense payment.

ii. **Terrapin Station made the transfer on account of new value given.**

Next, Terrapin Station made the administrative expense payment to Touch of Grey on account of the new value given. Touch of Grey gave $200,000 of new value to Terrapin Station when it delivered goods. R. at 8, 12. Terrapin Station made the payment on account of that same $200,000 value. R. at 7. Therefore, Terrapin Station made and Touch of Grey received the administrative expense payment on account of the new value given.

iii. **A transfer that a trustee cannot avoid under any provision of the Code is an otherwise unavoidable transfer.**

Courts properly hold that a creditor has not received an otherwise unavoidable transfer, thereby satisfying section 547(c)(4)(B), when the creditor has not received a transfer that the trustee can avoid under a provision of the Code other than section 547(c)(4). While previous courts held that new value given must remain unpaid at the petition date to satisfy this condition, later courts discredited this approach. *Compare, e.g.*, *In re Formed Tubes*, 46 B.R. 645, 646 (Bankr. E.D. Mich. 1985) *with In re IRFM, Inc.*, 144 B.R. 886, 893 (Bankr. C.D. Cal. 1992). By contrast, some courts hold that otherwise unavoidable means unavoidable under a defense enumerated in section 547(c) other than the new value defense in section 547(c)(4). *E.g.*, *In re Bishop*, 17 B.R. at 183. However, more recently, courts conclude that a transfer a trustee cannot avoid under any provision of the Code outside of section 547(c)(4) is an otherwise unavoidable transfer. *E.g.*, *Circuit City*, 2010 WL 4956022, at *8.

Congress intended the phrase "otherwise unavoidable" to mean transfers that the trustee cannot avoid under any provision of the Code other than section 547(c)(4). If Congress wanted to limit otherwise unavoidable transfers to transfers that are unavoidable by way of a section 547(c) defense, Congress could have written section 547(c)(4)(B) to read "on account of which new value the debtor did not make a transfer unavoidable *under this section* to or for the benefit of such creditor," as it used the phrase "under this section" in section 547(c). *Compare* 11 U.S.C. § 547(c) *with* 11 U.S.C. § 547(c)(4)(B). Instead, Congress directed that a creditor not receive a transfer that was *otherwise unavoidable* on account of the new value given. 11 U.S.C. § 547(c)(4)(B). Rather than limit relevant transfers to those under *this section*, section 547, Congress described transfers more broadly to reference any transfer that a trustee cannot avoid otherwise. *See id.*; *accord Check Reporting*, 140 B.R. at 434–36 (paying heed to the "artful articulation" set forth by Congress when enacting section 547(c)(4) and holding "otherwise unavoidable" to mean unavoidable by way of a

Code provision other than section 547(c)(4)) (citing *In re Fulghum Constr. Corp.*, 706 F.2d 171, 174 (6th Cir. 1983)); H.R. REP. NO. 95-595, ch. 4, at 177–78 (1977). Accordingly, courts properly conclude that otherwise unavoidable transfers are transfers that the trustee cannot avoid under any provision of the Code other than section 547(c)(4).

iv. **The administrative expense payment Touch of Grey received was an otherwise unavoidable transfer.**

Finally, the administrative expense payment is an otherwise unavoidable transfer because a trustee cannot avoid it under any provision of the Code. Trustees can avoid preferential transfers under several avoidance provisions of the Code. Also, trustees can avoid certain transfers made before the debtor files a petition for bankruptcy. 11 U.S.C. §§§ 544 (trustee can avoid certain voidable transfers), 548 (trustee can avoid fraudulent transfers), 553(b) (trustee can avoid certain offsetting transfers); *accord Circuit City*, 2010 WL 4956022, at *8. Here, however, the estate made the payment after the petition date, so these avoidance provisions do not apply.

Additionally, a trustee can avoid certain transfers that are liens. 11 U.S.C. §§ 545, 724(a); *accord Circuit City*, 2010 WL 4956022, at *8. Because the payment Touch of Grey received is not a lien, these avoidance provisions do not apply. Finally, a trustee can avoid certain transfers made after the petition date, including transfers "not authorized" by the Code or the court. 11 U.S.C. § 549; *accord Circuit City*, 2010 WL 4956022, at *8. Terrapin Station made the payment after the petition date, but because both section 503(b)(9) and the bankruptcy court authorized the payment, this avoidance provision does not apply. Because the Trustee cannot avoid the payment to Touch of Grey under any avoidance provision of the Code, the administrative expense payment was an otherwise unavoidable transfer.

This Court should hold that Touch of Grey cannot reduce its preference exposure by applying new value under section 547(c)(4) because it fails to satisfy the statute's elements. Touch of Grey received an otherwise unavoidable transfer from the debtor on account of the new value it gave when it received an administrative expense payment for that value. Accordingly, Touch of Grey fails to satisfy section 547(c)(4)(B) and it cannot reduce its preference exposure with the new value.

B. A Court achieves the policy goals Congress intended when it prohibits a creditor from reducing its preference exposure under section 547(c)(4) with value for which it received an administrative payment.

This Court achieves the policy goals underlying the Code by prohibiting Touch of Grey from reducing its preference exposure under section 547(c)(4). Consistently, courts cite the policy goals of treating creditors equally and encouraging creditors to work with financially troubled debtors when interpreting section 547(c)(4). A court best achieves these policy goals when it prohibits a creditor from reducing its preference exposure with value for which it was paid.

i. Courts treat creditors equally when they prohibit a creditor from asserting new value under section 547(c)(4) if it has received an administrative payment for that value.

This Court should prohibit Touch of Grey from reducing its preference exposure because in doing so this Court will treat Terrapin Station's creditors equally. Congress stated that the primary bankruptcy policy achieved by the Code's preference provisions is treating creditors equally. H.R. REP. NO. 95-595. This Court endorses that view. *Union Bank v. Wolas*, 502 U.S. 151, 161 (1991). The Code's preference provisions allow trustees to avoid transfers that would unequally elevate one creditor's position at the expense of other creditors. *Merit Mgmt. Grp.*, 138 S. Ct. at 888; *accord In re Kroh Bros. Dev. Co.*, 930 F.2d at 648, 652 (8th Cir. 1991). But the defenses in section 547(c) allow creditors to keep such transfers when it would be fairer to do so. *See In re Ladera Heights Cmty. Hosp.*, 152 B.R. at 964, 969 (Bankr. C.D. Cal. 1993). Section 547(c)(4) treats a creditor who gave new value equally by reducing its preference exposure by the amount of the new value given. *See, e.g.*, *In re Phoenix Rest. Grp.*, 317 B.R. 491, 495–96 (Bankr. E.D. Tenn. 2004). Otherwise, that creditor will have surrendered value to the estate, benefitting the estate's other creditors by increasing the asset pool from which claims will be paid, at its own expense. *Beaulieu*, 616 B.R. at 875, 877. Accordingly, courts aim to treat creditors equally when interpreting and applying section 547(c)(4). *E.g.*, *Circuit City*, 2010 WL 4956022, at *6; *Phoenix Rest. Grp.*, 317 B.R. at 497.

a. Courts must restrict the inherently unequal treatment that administrative payments confer on creditors to the bounds authorized by the Code when calculating preference exposure.

Notably, the Code authorizes courts to treat creditors unequally to benefit debtors and protect creditors by authorizing administrative expense payments under section 503(b)(9). *See In re Plastech*, 394 B.R. 147, 151 (Bankr. E.D. Mich. 2008) (stating that "[section] 503(b)(9) results in disparate treatment" of similarly situated unsecured creditors). However, the balanced policy goals of benefitting debtors and protecting creditors justify the inequality of administrative expense payments. First, the prospect of payment under section 503(b)(9) may encourage creditors to continue doing business with financially troubled debtors. *E.g.*, *In re Arts Dairy, LLC*, 414 B.R. 219, 220 (Bankr. N.D. Ohio 2009). If a creditor suspects a debtor is headed for bankruptcy, it may be more willing to keep delivering goods on credit if it knows it can recoup the value as an administrative expense. *E.g.*, *In re Commissary Operations, Inc.*, 421 B.R. 873, 879 (Bankr. M.D. Tenn. 2010). Consequently, debtors benefit from administrative expense payments by having continued access to credit.

Second, administrative expense payments prevent debtors from abusing provisions of the Code. *Arts Dairy*, 414 B.R. at 220. A debtor who knows bankruptcy is imminent cannot plan to order goods on credit, file for bankruptcy, and then avoid making payment on the goods. *Id.* This is because section 503(b)(9) statutorily requires the debtor to pay for qualifying goods post-petition. 11 U.S.C. § 503(b)(9). Accordingly, these payments protect creditors from debtor abuse. However, to provide benefit and protection under section 503(b)(9) and still adhere to the overarching goal of treating creditors equally, courts must strictly limit unequal treatment to the extent explicitly authorized by the Code.

b. Courts balance the unequal treatment of creditors when they account for the extent to which the estate is enlarged by value given.

Courts strike this balance when they account for the extent to which a creditor enlarged the estate by new value. When a creditor gives new value, it enlarges the estate. *See TI Acquisition*, 429 B.R. 377, 384 (Bankr. N.D. Ga. 2010). A court recognizes this by allowing that creditor to reduce its preference exposure by the amount it enlarged the estate with new value. *See* 11 U.S.C. § 547(c)(4); *accord Ladera Heights*, 152 B.R. at 969; *Kroh Bros.*, 930 F.2d at 652; *Phoenix Rest.*, 317 B.R. at 495; *Circuit City*, 2010 WL 4956022, at *6. Therefore, a court ensures a creditor is treated equally by determining the extent to which it enlarged the estate. *Kroh Bros*, 930 F.2d at 653, 654.

However, when a debtor or the estate pays for that new value, the estate is no longer enlarged. *Check Reporting*, 140 B.R. at 433; *accord Phoenix Rest.*, 317 B.R. at 495; *Kroh Bros*, 930 F.2d at 654. If the estate is no longer enlarged, the creditor cannot assert any new value to reduce its preference exposure. *E.g.*, *TI Acquisition*, 429 B.R. at 384 ("If the estate is not enlarged, no new value has been given."); *accord Kroh Bros*, 930 F.2d at 653, 654. Finally, when a creditor gives new value to a debtor after a preferential transfer, but later receives an administrative expense payment for that value, the estate is no longer enlarged by the new value. *See TI Acquisition*, 429 B.R. at 385; *accord Circuit City*, 2010 WL 4956022, at *6, *9. Accordingly, a creditor cannot assert value that did not enlarge the estate to reduce its preference exposure because to do so would be "inequitable and contrary to [section 547(c)(4)]. *Id.*

c. Touch of Grey no longer enlarged the estate after being paid an administrative expense and therefore cannot reduce its preference exposure.

Here, Touch of Grey cannot reduce its preference exposure under section 547(c)(4) with the new value it gave Terrapin Station because that value no longer enlarges the estate. Touch of Grey enlarged the estate to the extent of the $200,000 of goods it delivered. *See* R. at 5–6. However, Terrapin Station made an administrative expense payment to Touch of Grey for the goods. *See* R. at 6–7. Accordingly, Terrapin Station's estate is no longer enlarged by the new value Terrapin Station gave. Because the estate is no longer enlarged by $200,000, Touch of Grey cannot assert this value to reduce its preference exposure under section 547(c)(4).

d. Courts honor congressional intent by accounting for the enlargement of the estate.

Courts adopting this approach comport with Congressional intent to preserve the principles of the net result rule. While abrogated by the Code, the rule allowed a creditor to offset its preference exposure to the extent it gave new value to the debtor during the preference period. *Jaquith v. Alden*, 189 U.S. 78, 82–83 (1903). When Congress enacted the Code, it retained principles of the rule while prescribing a different formula in section 547(c)(4) for calculating the extent to which a creditor could reduce its preference exposure. *In re Garland*, 19 B.R. 920, 926 (Bankr. E.D. Mo. 1982) (citing H.R. REP. NO. 95-595) (concluding that Congress intended "to retain at least the principles behind the [net result] rule in section 547(c)(4)" but recognizing that the statute precluded the direct application of the net result rule because section it prescribes a formula for calculating a creditor's preference exposure). Congress added a timing element to the new formula by requiring new value to be given *after* the preferential transfer, rather than any time during the preference period. *See id.* at 925–26. However, Congress retained the net enlargement approach. *See id*. The new formula directs courts to consider the extent to which a creditor enlarged the estate by giving new value to the debtor after a preferential transfer. *See id.*; 11 U.S.C. § 547(c)(4). Therefore, courts adhere to the principles of the net result rule as Congress intended by accounting for net enlargement of the estate when calculating preference exposure.

e. This Court should prohibit Touch of Grey from reducing its preference exposure to treat Terrapin Station's other unsecured creditors equally.

Prohibiting Touch of Grey from reducing its preference exposure balances the unequal treatment that the administrative expense payment has on Terrapin Station's other creditors. In bankruptcy, unsecured creditors must file claims and wait for those claims to be paid by the estate. *See* 11 U.S.C. §§ 501, 502, 362(a); *accord In re Edelman*, 237 B.R. 146, 148, 149 n.5, (B.A.P. 9th Cir. 1999). Often, unsecured creditors receive less than 100 cents on the dollar for their claims. *Beaulieu*, 616 B.R. at 877. An administrative expense payment pays an unsecured creditor for what would otherwise be part or all of its unsecured claim, dollar for dollar. *Id.* If the estate is unable to pay unsecured claims dollar for dollar, that creditor fares better than its debtor's other unsecured creditors who will not receive full payment on their claims. *Id.* Additionally, administrative expense payments are paid to unsecured creditors relatively quickly while other unsecured creditors must wait. *Id.* Allowing an unsecured creditor who receives an administrative expense payment to use that value to reduce its preference exposure exacerbates this unequal treatment. *Id.*; *accord TI Acquisition*, 429 B.R. at 385.

Additionally, allowing a creditor to use the same value under both sections 503(b)(9) and 547(c)(4) allows that creditor to benefit twice from a single quantity of value it gave the debtor. Like an administrative expense payment, reducing preference exposure under section 547(c)(4) offsets part of an unsecured creditor's claim, dollar for dollar. When creditors use the same value under both statutes, they "double dip." *In re Terrapin Station v. Jones*, No. 20-0803, 15 (13^{th} Cir. 2021); *accord TI Acquisition*, 429 B.R. at 385. This defeats the preference provisions of the Code that aim to treat creditors equally. *TI Acquisition*, 429 B.R. at 385. Accordingly, this Court should treat Terrapin Station's other unsecured creditors equally and prohibit Touch of Grey from reducing its preference exposure.

ii. **Creditors will continue to work with financially troubled debtors because they will still be sufficiently protected.**

This Court should prohibit Touch of Grey from reducing its preference exposure because it will not discourage creditors from working with financially troubled debtors by doing so. Section 547(c)(4)(7) encourages creditors to continue working with financially troubled debtors because it protects creditors by reducing preference exposure. *E.g.*, *Check Reporting*, 140 B.R. at 436, 437; *Kroh Bros.*, 930 F.2d at 650–51 (8th Cir. 2004). However, the *T.I. Acquisition* court highlighted that the "ultimate method of encouraging [creditors] to continue" extending credit to financially troubled debtors is to fully pay creditors' claims in bankruptcy. 429 B.R. at 385. This is exactly what administrative expense payments do. *Id.* Administrative expense payments pay a creditor for what would otherwise be part or all of its unsecured claim against the estate, dollar for dollar. *Beaulieu Grp,* 616 B.R. at 877. An unsecured creditor can hope for no better scenario than having its claim, or at least part of it, paid in full. It follows that when a creditor receives an administrative expense payment for value it gave, it no longer needs to assert that value to reduce its preference exposure, just as it no longer needs to file a claim against the estate for that debt. As such, limiting a creditor to assert the value under either section 503(b)(9) or section 547(c)(4) provides the creditor sufficient protection to encourage it to continue working with its debtor.

Here, the prospect of an administrative expense payment encouraged Touch of Grey to continue working with Terrapin Station. Touch of Grey continued extending credit to Terrapin Station after other creditors stopped, even when Terrapin Station was in default. R. at 6. However, once Terrapin Station filed for bankruptcy, Touch of Grey demanded an administrative expense payment before it would extend more credit. R. at 7. Then, after being paid in full, Touch of Grey resumed extending credit to Terrapin Station. *Id.* The prospect and successful receipt of the payment encouraged Touch of Grey to continue working with financially troubled Terrapin Station. True, some creditors are not sufficiently familiar with sections 503(b)(9) or 547(c)(4) to be encouraged by these provisions to continue working with financially troubled debtors. However, being an "award-winning," international company with nearly 2,000 locations worldwide, Touch of Grey is precisely the type of sophisticated creditor these Code provisions encourage. *See* R. at 3.

This Court should prohibit Touch of Grey from asserting new value under section 547(c)(4) to reduce its preference exposure. Most importantly, Touch of Grey fails to satisfy section 547(c)(4)(B) because it received an otherwise unavoidable transfer for the value when it received an administrative expense payment. Additionally, this Court achieves the policy goals Congress intended by disallowing Touch of Grey from reducing its preference exposure. This Court should affirm the Thirteenth Circuit.

2. **The Thirteenth Circuit properly held that a trustee is not required under section 365(d)(3) to pay rent that came due prior to the rejection of an unexpired non-residential real property lease but allocable to the period after the effective date of rejection.**

The Code provides a Chapter 7 bankruptcy trustee with significant discretion to act on behalf of the debtor's estate. *See* 11 U.S.C. § 704(1) (listing the wide-ranging duties of the trustee). The Code governs the role of a trustee and sets forth the guidelines under which the trustee can operate. *See* Hon. Steven Rhodes, *The Fiduciary and Inst. Obligations of a Chap. 7 Bankruptcy Tr.*, 80 AM. BANKR. L.J. 147, 149 (2006). Ultimately, the trustee will utilize the Code's procedure to maximize the value of the estate and then distribute the estate's assets to the debtor's creditors. *See Comm. Futures Trading Com'n v. Weintraub*, 471 U.S. 343, 352 (1985); *see also Otte v. U.S.*, 419 U.S. 43, 53 (1974) (stating the Code aims to keep "fees and administrative expenses at a minimum so as to preserve as much of the estate as possible for the creditor").

One example of how a trustee acts on behalf of the debtor's estate to maximize its value is under section 365(a). That section provides that a trustee (or debtor-in-possession[1] pursuant to section 1107(a)) may "assume or reject any executory contract or unexpired lease of the debtor." 11 U.S.C. § 365(a). When debtors file for bankruptcy, they may still be subject to agreements that the parties have not yet fully performed. *See Executory*, Black's Law Dictionary (11th ed. 2019) ("to be performed at a future time; yet to be completed"). The trustee has the option to decide whether this outstanding contract or unexpired lease is a "good deal" for the estate or not. *Mission Prod. Holdings, Inc. v. Tempnology, LLC*, 139 S. Ct. 1652, 1658 (2019). If the trustee determines it to be a "good deal," the trustee will assume the contract or lease and perform its obligations. *Id.* However, should the trustee decide the contract or lease is not a "good deal" for the estate, the trustee will reject it. *See In re Columbia Gas System Inc.*, 50 F.3d 233, 238 (3rd Cir. 1995) (discussing that an outstanding agreement represents for the estate "both an asset (the counterparty's performance) . . . and a liability (the debtor's performance)").

If the trustee assumes the contract or lease, the counterparty will benefit from the obligations under the contract by receiving administrative expense status. *See* 11 U.S.C. §§ 503(b),

[1] Though Terrapin Station, as debtor-in-possession, originally rejected the lease while it was still under Chapter 11, once the court converted the case to Chapter 7 and appointed a trustee, the trustee's goal became to maximize the estate's value.

507(a)(1) (providing that administrative expenses have the highest priority over all other unsecured claims against a debtor's estate). However, if the trustee rejects the contract or lease, the counterparty to the agreement has only a pre-petition claim against the debtor's estate for breach of damages under section 365(g), rather than a post-petition claim dating to the actual rejection date. *See* 11 U.S.C. § 365(g) (providing that "the rejection of an executory contract or unexpired lease. . . constitutes a breach of such contract or lease— (1) immediately before the date of filing the petition"); *see also NLRB v. Bildisco & Bidilsco*, 465 U.S. 513, 531 (1984) (noting that post-petition claims receive a higher priority than pre-petition claims).

Ultimately, because the Code provides only the counterparty with a pre-petition unsecured claim for the damages resulting from the debtor's nonperformance, it will only likely receive a small fraction of that claim's value. *Mission Prod. Holdings, Inc. v. Tempnology, LLC*, 139 S. Ct. at 1652. The counterparty will receive only a small portion because it will share pro-rata with all other unsecured creditors in the remaining assets of the estate after the trustee pays off higher priority claims. *See* 11 U.S.C. § 726(a) (providing for how property of the estate will be distributed to debtor's creditors).

While this decision to reject or assume the contract or lease may significantly impact how much the counterparty is paid from the estate, the trustee's decision is given a high level of deference under the business judgment rule. *See NLRB v. Bildisco & Bidilsco*, 465 U.S. at 523. Additionally, while given a high level of deference, if the trustee does not act quickly enough, the Code automatically deems the lease or contract rejected. *See* 11 U.S.C. §§ 365(d)(1), 365(d)(4)(A).

Within section 365, subsection (d)(3) deals specifically with unexpired non-residential real property leases. *See* 11 U.S.C. § 365(d)(3). It requires that the trustee "timely perform all obligations required under the lease. . . arising from and after the order for relief under any unexpired lease. . . until such lease is assumed or rejected, notwithstanding section 503(b)(1) of this title." *Id.* That is, during the time between when a debtor files a bankruptcy petition but before the trustee assumes or rejects the unexpired lease, the trustee must perform the lease's obligations. Yet, this section does not clearly articulate *when* those obligations arise.

Courts are divided on when these obligations arise, and two different approaches have emerged. A slight majority of courts have adopted the "proration" rule. *See, e.g, In re GCP CT School Acquisition, LLC*, 443 B.R. 243, 255 (Bankr. E.D. Mass. 2010); *In re Handy Andy Home Improvement Ctrs.*, 144 F.3d 1125, 1127 (7th Cir. 1998); *In re Furr's Supermarket*, 283 B.R. 60, 62 (B.A.P. 10th Cir. 2002). Courts adopting this rule have concluded that obligations continuously arise on each day a debtor occupies the premises between the petition and rejection dates. *See In re Furr's Supermarket*, 283 B.R. at 62 (holding that the trustee is only obligated to pay the "amounts that had accrued during the time the debtor or trustee was in possession of the property").

However, other courts have adopted the stricter "performance date" rule, which requires a trustee to strictly perform any obligation that came due under the lease in between the petition and rejection date. *See e.g., In re Montgomery Ward Holding Corp.*, 268 F.3d 205, 208–12 (3d Cir. 2001); *In re Koenig Sporting Goods, Inc.*, 203 F.3d 986, 990 (6th Cir. 2000). For example, if a lease agreement required a debtor to pay in advance on the first of the month and the trustee rejected the lease on the second day, the trustee is obligated to pay the full month's rent, even if ninety-seven percent of that rent is allocable to a period after the rejection date when the debtor no longer has a right to possession of the premises. *See In re Koenig Sporting Goods, Inc.*, 203 at 990; *see* 11 U.S.C. § 365(d)(4) (requiring debtor to vacate premises upon rejection). Congress could not have intended such a result.

Petitioner argues that this Court should follow the "performance date" rule, saying section 365(d)(3) requires that trustees strictly perform any obligation that came due post-petition but pre-rejection, irrespective of when the trustee rejected the lease. R. at 8. Yet, that argument fails to recognize that statutory interpretation does not occur in a contextual vacuum. *See Gundy v. United States*, 139 S. Ct. 2116, 2126 (2019) (stating that the Court "interprets statutory provisions. . . by reading the text in 'context' and in light of the statutory 'purpose'"). Indeed, when considering section 365(d)(3) in context with the Code and its purpose, this provision clearly only requires that the trustee's obligations extend until the time of rejection. Using traditional tools of statutory interpretation, including "the canons of construction, the legislative history, and the underlying purposes and policies of the Bankruptcy Code," the Court of Appeals for the Thirteenth Circuit correctly concluded that the Trustee for Terrapin Station is not required to pay rent for the entirety of May 2020 and instead, must pay only the rent that accrued through May 5, 2020, the effective date of rejection. R. at 17.

A. When read in isolation, section 365(d)(3) is ambiguous, which precludes a plain meaning argument that the provision clearly requires the trustee to strictly perform all obligations that arise prior to rejection.

First, statutory analysis begins with the text itself. *See Ross v. Blake*, 578 U.S. 632, 638 (2016). Additionally, the words in the provision at issue must be given their ordinary meaning unless Congress has expressly defined a term. *See Asgrow Seed Co. v. Winterboer*, 513 U.S. 179, 187 (1995) ("When terms used in a statute are undefined, we give them their ordinary meaning."). Ordinary meaning denotes that the words in the statute should be interpreted as they are commonly understood. *See Nix v. Hedden*, 149 U.S. 304, 307 (1893) (relying on "ordinary usage" to determine that tomatoes are regarded as vegetables, not fruits).

Again, section 365(d)(3) reads: "The trustee shall timely *perform all obligations* required under the lease. . . *arising from and after the order for relief* under any unexpired lease. . . *until such lease is assumed or rejected*, notwithstanding section 503(b)(1) of this title." 11 U.S.C. § 365(d)(3) (emphasis added). Congress has not explicitly defined operative terms such as "arising" or "obligations." As such, they must be construed using their ordinary meanings. Yet, giving these terms their ordinary meanings does not clearly resolve *when* an obligation to perform arises.

i. Relating section 365(d)(3)'s undefined terms "arising" and "obligations" produces two reasonable interpretations indicating that the provision is ambiguous.

An obligation is generally understood to mean "any duty imposed by law, promise, contract, relations of society, courtesy, kindness, etc." *Obligation*, Black's Law Dictionary (11th ed. 2019). Yet, section 365(d)(3) does not clearly answer when this "duty imposed by law" arises; and relating "arising" to "obligations" can produce two plausible meanings.

One common definition of "arise" includes "to begin to occur or to exist; to come into being." *Arise*, merriam-webster.com (Jan. 18, 09:10 PM), https://www.merriam-webster.com/dictionary/arising. This definition highlights that the term can be "understood in either an absolutist or accrual sense." *In re Ames Dept. Stores, Inc.*, 306 B.R. at 67. That is, an obligation can "come into being" either at a fixed time, such as when a lessee receives a bill for rent, or an obligation can "begin to occur" continuously over time, such that the obligation continuously arises on each day the debtor occupies the premises. Each of these are plausible interpretations. Petitioner argues the obligation which the Trustee must perform "came into being" when the debtor received the bill for May's rent, prior to the rejection of the lease. However, the language in section 365(d)(3) is not written as clearly as Petitioner suggests, and instead, could just as easily lend support for the "proration rule" by saying the obligation "begins to occur" each day the debtor occupies the premises.

ii. Section 365(d)(3)'s phrase "until such lease is assumed or rejected" may be modified by either "perform" or "obligations," which adds to its ambiguity.

Whether the term "arising" is to be understood in an absolutist or accrual sense is not the only means of ambiguity within this provision's text. The phrase "until such lease is assumed or rejected" and its potential modifiers further this ambiguity. This phrase can either modify "perform" or "obligations." *In re Ames Dept. Stores, Inc.*, 306 B.R. at 67. If this phrase modifies "perform," then the trustee is required to strictly perform any obligation under the lease until it is rejected. *Id.* This interpretation lends itself more favorably to the "performance date" rule, as the obligation of May's full month rent bill would "come into being" prior to the lease being rejected. Yet, it is not obvious that this provision should be read that way. Instead, the phrase may modify "obligations." *Id.* Under that reading, the trustee's requirement to perform the lease's obligations would end when the lease is rejected. *Id.* In this case, the Trustee would fulfill the obligations of May's rent that "begin to occur" each day the debtor occupies the premises until the Trustee has rejected the lease. This interpretation supports the "proration rule." As the provision does not clearly state whether the phrase modifies "perform" or "obligations," it does not clearly and unambiguously answer the issue at hand.

B. The "proration" rule better comports with the statutory interpretation principle that a provision should be read in view of its statutory context.

Though section 365(d)(3) itself is ambiguous and does not clearly answer whether Petitioner should receive rent for all of May 2020 or only the first five days of the month, there are other methods of ascertaining the provision's meaning. First, statutory interpretation is not cabined to only the provision's text, but the provision at issue must be situated within the overall Code framework. *See King v. Burwell*, 576 U.S. 473, 492 (2015) (stating the Court must "[bear] in mind the 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" (quoting *Utility Air Regul. Grp. v. EPA*, 573 U.S. 302, 318 (2014))). This whole act rule assumes that the provisions of a statute fit together into a coherent whole. *See, e.g, FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 121 (2000) (stating that the Court must interpret a provision to create a "symmetrical and coherent. . . [statutory] scheme"). This assumption of coherence adds to the inference that not only does the statute use language consistently and coherently, but that the provisions functionally work together to accomplish the statute's objectives.

Here, section 365(d)(3) should be construed while also considering sections 365(g), 502(g) and 502(b)(6), all of which show that unperformed obligations after rejection of a contract or lease as pre-petition general unsecured claims. *See In re Ames Dept. Stores, Inc.*, 306 B.R. at 65. Section 365(g) provides that a counterparty to a rejected "executory contract or unexpired lease" has a pre-petition breach of contract claim. 11 U.S.C. § 365(g). The amount of this claim is calculated under section 502. Within that section, subsections (b)(6) and (g) can be read together to further establish that "claims for an estate's failure to honor obligations after rejection [are] pre-petition, and not administrative, claims." *In re Ames Dept. Stores, Inc.*, 306 B.R. at 68.

While subsection (g) provides that a claim resulting from rejection is treated as a pre-petition claim, (b)(6) then statutorily caps the amount of the lessor's allowed claim. 11 U.S.C. § 502(g), 502(b)(6). The purpose of this rent cap is "to balance the interests of [lessors] and unsecured creditors by allowing a [lessor] to receive compensation for losses suffered from a lease termination while not permitting a claim so large as to prevent general unsecured creditors from recovering from the estate." *In re MDC Systems, Inc.*, 488 B.R. 74, 82 (Bankr. E.D. Pa. 2013). Viewing section 365(d)(3) in light of this goal, the Code creates a coherent statutory scheme that strikes a careful balance between a lessor's interest in receiving payment for the post-petition, pre-rejection period without upsetting the trustee's goal of minimizing administrative costs and maximizing the estate for all unsecured creditors.

Therefore, requiring a trustee to pay a lessor rent that is allocable to this post-rejection period would render these provisions meaningless and upset this careful statutory balance. *In re Ames Dept. Stores, Inc.*, 306 B.R. at 70. The lessor's claim for rent that is allocable to the post-rejection period would supersede other creditors and receive a higher priority status, which is contrary to the purposes of sections 365(g), 502(g) and 502(b)(6). *Id.* Essentially, this recharacterization of what the Code has provided as a pre-petition claim into an administrative claim violates the Code's long established priority scheme. *In re NETtel Corp., Inc.*, 289 B.R. 486, 492–93 (Bankr. D.D.C. 2002). As such, the "proration rule" better allows these provisions to fit together coherently with section 365(d)(3).

C. The canon of construction that the Code should not be read to erode established bankruptcy practice absent a clear signal from Congress indicates that the "proration" rule is the correct reading of section 365(d)(3).

While fitting section 365(d)(3) coherently with other provisions in the Code supports the view that the "proration" rule is the better reading of section 365(d)(3), the canon of construction not "to erode past bankruptcy practice absent a clear indication" from Congress, also shows that "performance date" rule has no place here. *Cohen v. de la Cruz*, 523 U.S. 213, 221 (1998). Prior to section 365(d)(3)'s enactment in 1984, lessors had to request that debtors' lease obligations that arose during the post-petition, pre-rejection period be paid as administrative expenses under section 503. *See, e.g.*, *In re Keyboard Center, Inc.*, 9 B.R. 472, 474 (Bankr. D. Conn. 1981). During that time, courts would generally allow lessors to receive as an administrative expense, prorated rent for the post-petition, pre-rejection period, as long as it was not unreasonable. *See Palmer v. Palmer*, 104 F.2d 161, 163 (2d. Cir. 1939); *In re Dunwoody Village Sporting Goods, Inc.*, 11 B.R. 493, 494 (Bankr. N.D. Ga. 1981).

As courts granted lessors prorated rent up until, but not beyond the lease rejection date, it is evident that courts set precedent supporting the "proration rule." The fact that Congress possessed the ability, but chose not to, include language in section 365(d)(3) stating rent allocable to the post-rejection period should be considered an administrative expense highlights its likely satisfaction with this rule. While some courts are reluctant to find meaning in Congressional silence, sometimes silence is significant. *See Blue Chips Stamps v. Manor Drug Stores*, 421 U.S. 723, 733 (1975). Here, the longstanding application of the "proration" rule during this post-petition, pre-period, coupled with Congress's years-long analysis and debate over the 1984 amendments, clearly show it had ample opportunity to raise the issue and make its displeasure known with the "proration" rule known. Yet, it did not.

Ultimately, the language in section 365(d)(3) in no way clearly shows that Congress intended to do away with this precedent. Indeed, Congress showed it did not intend for lessors to receive rent payments allocable to the post-rejection period when it enacted section 365(d)(4), which requires a trustee to surrender the premises back to the lessor immediately upon rejection If the debtor is no longer entitled to the lessor's services, the lessor is not entitled to rent allocable to the period post-rejection. The legislative history surrounding section 365(d)(3)'s enactment shows exactly that and fails to show that Congress intended to adopt the "performance date" approach.

D. The legislative history surrounding section 365(d)(3)'s enactment fails to show Congress intended to adopt the "performance date" approach.

The legislative history surrounding the enactment of section 365(d)(3) shows that Congress did not intend to grant commercial lessors a windfall by allowing them to collect rent allocable to the period after the lease rejection date. Instead, Congress simply intended to lessen the financial burden on commercial lessors for providing services to a debtor who had filed bankruptcy but had not yet rejected or assumed an unexpired lease. Although the usefulness of legislative history in showing Congressional intent is debated among courts and practitioners alike, here, the legislative history clearly supports that Congress intended the "proration" rule when enacting section 365(d)(3). *See D.C. v. Heller*, 554 U.S. 570, 605 (2008) (stating that legislative history is "considered persuasive *by some*. . . because the legislator who heard or read those statements presumably voted with that understanding") (emphasis added).

Often there is a gap in time between when a debtor files for bankruptcy and the trustee rejects the lease.[2] Prior to 1984, this gap posed special problems for commercial lessors because during the post-petition, pre-rejection period, the lessor was often forced to provide current services—the use of its property, utilities, security and other services—without current payment." 130 CON. REC. (1984), *as reprinted in* 1984 U.S.C.C.A.N. 576, 599. That is, the automatic stay would prevent lessors from being able to evict bankrupt debtors and those debtors would not automatically pay rent. *Id.*

Instead, as previously mentioned, commercial lessors had to petition the bankruptcy court for an order designating rent during this period as an administrative expense, which was a time-consuming and cumbersome process. *See In re Keyboard Center, Inc.*, 9 B.R. 472, 474 (Bankr. D. Conn. 1981). This process was made more difficult by the restrictive standards used to determine what qualifies as an administrative expense. *See* § 503(b)(1) (requiring that an administrative expense be "the actual, necessary costs and expenses of preserving the estate"). *See also Lerner Stores Corp. v. Elec. Maid Bake Shops*, 24 F.2d 780, 782 (5th Cir. 1928) (stating whether a claim is paid an administrative expense is also largely within the discretion of the bankruptcy courts).

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[2] For example, here, the Terrapin Station initially filed for Chapter 11 bankruptcy in January of 2020 hoping to reorganize; however, it took an additional four months for it to take stock of its economic prospects and decide to reject the lease. R. at 6, 7.

In 1984, Congress enacted section 365(d)(3) to remedy this financial burden on commercial lessors. While there is no doubt that Congress intended this section to aid commercial lessors' financial difficulty when its lessee files for bankruptcy, there is no indication in the Congressional history that Congress intended to grant lessors a windfall by allowing them to receive rent allocable to the post-rejection date. Instead, Congress noted it was concerned specifically with this post-petition, pre-rejection period because the lessor would be required to provide services without payment. *See* 130 Con. Rec. (1984), *as reprinted in* 1984 U.S.C.C.A.N. 576, 599.

Yet, that concern does not apply after the rejection date. In fact, upon rejection, the debtor is required to vacate the premises and would no longer receive any services, let alone "free services," from the lessor. *See* 11 U.S.C. § 365(d)(4). Additionally, upon rejection, the lessor can find a new tenant for the space previously occupied by the debtor. For example, if a trustee rejects the lease on the second of the month and the lessor finds a new tenant for the space within that month, the lessor could essentially double dip under the "performance date" rule. That is, the lessor would receive a full month's rent from the debtor's estate as an administrative expense and rent from the new tenant. Congress did not provide any indication that it intended this result.

While Congress indicated that trustees should perform the lease's obligations "at the time required in the lease," that statement is not enough to garner support for the "performance date" rule. 130 Con. Rec. (1984), *as reprinted in* 1984 U.S.C.C.A.N. 576, 599. Just as a statutory provision cannot be read in isolation, that statement cannot not read in isolation. *See In re Handy Andy Home Improvement Ctrs., Inc.*, 144 F.3d at 1128 (stating "when context is disregarded, silliness results"). Critically, that statement was made in the context of Senator Hatch highlighting the problems for lessors during the post-petition, pre-rejection period. *See* 130 Con. Rec. (1984), *as reprinted in* 1984 U.S.C.C.A.N. 576, 599. Ultimately, the statement likely only meant that lessors should receive payments for the "current services" provided during that interim period. That statement on its own does not support the "performance date" rule.

CONCLUSION

The Bankruptcy Code should not be used as vehicle for certain creditors to gain unfair windfalls at the expense of other creditors as Touch of Grey attempts to do so here. Instead, the Court should 1) prohibit Touch of Grey from asserting new value under section 547(c)(4) to reduce its preference exposure and 2) adopt the "proration" rule, prohibiting Touch of Grey from receiving rent allocable to the post-rejective period as an administrative expense.