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 APPEAL FROM THE
UNITED STATES COURT OF APPEALS FOR
THE THIRTEENTH CIRCUIT

BRIEF FOR THE PETITIONER

TEAM NUMBER 7
COUNSEL FOR PETITIONER

JANUARY 20, 2022

QUESTIONS PRESENTED

I. Whether a post-petition administrative payment authorized by a bankruptcy court under 11 U.S.C. § 503(b)(9) may operate to increase a creditor's preference exposure by eliminating that creditor's otherwise valid subsequent new value defense under 11 U.S.C. § 547(c)(4)?

II. Under 11 U.S.C. § 365(d)(3), when a monthly rent payment pursuant to a commercial lease comes due after a bankruptcy petition is filed but before that lease is rejected, is the trustee required to perform under the contract or may the trustee prorate the rent payment based on the actual use and occupancy of the premises?

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OPINIONS BELOW

The Thirteenth Circuit Court of Appeal's opinion below can be found at No. 21-0909 and reprinted at Record 2. Both the Bankruptcy Court for the District of Moot and the United States District Court for the District of Moot found for the Trustee, and the Thirteenth Circuit affirmed.

STATEMENT OF JURISDICTION

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

STATUTORY PROVISIONS

This appeal involves various provisions of Title 11 of the United States Code.

Section 547(c)(4) reads:

> (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;

Section 503(b)(9) reads:

> (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.

Section 365(d)(3) reads:

> 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. 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. 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 FACTS

This case appeal arises out of Respondent's attempts to use equitable considerations to circumvent the plain language and fundamental structure of the Bankruptcy Code. As a result, the bankruptcy proceeding underlying this appeal threatens to undercut Congress's principled efforts to reduce the number of unnecessary bankruptcies.

I. FACTUAL HISTORY

A. Touch of Grey and Terrapin Station Enter into an Innovative Franchise Arrangement.

Headquartered in San Francisco, Petitioner Touch of Grey Roasters, Inc., is an American coffee company. R. at 3. Known for its highly rated and award-winning coffees, Touch of Grey has successfully established more than 1900 coffeehouses serving consumers across the world. R. at 3. Respondent Casey Jones is the Chapter Seven Trustee for Terrapin Station, LLC (the "Debtor"). R. at 2. Founded by its sole member, William Tell, the Debtor owned and operated an independent coffeeshop in the Town of Terrapin, Moot for many years. R. at 3.

The events giving rise to the present dispute began five years ago with Touch of Grey's launch of a new series of neighborhood coffeehouses. R. at 4. Touch of Grey's plan for the new neighborhood coffeehouses was simple: revamp and expand existing independent coffeehouses to break into new markets and reach a greater variety of consumers. R. at 4. Through partnership with Touch of Grey, the new coffeehouses would be expanded to sell wider ranges of food, serve night-time alcoholic drinks, and become local venues for live music and poetry readings. R. at 4. Touch of Grey also developed a new line of coffee products for the coffeehouses to sell. R. at 4. To help the local owners preserve the identity and feel of their coffeehouses, and thus avoid alienating their customers, Touch of Grey sold its new line of coffee products under the brand name Dark Star. R. at 4.

Tell agreed for the Debtor to become one of Touch of Grey's neighborhood coffeehouses. The Debtor and Touch of Grey executed two documents to consummate their deal. R. at 4. First, with the Debtor in need of a remodel, Touch of Grey purchased a new warehouse space in downtown Terrapin and leased it to the Debtor (the "Lease"). R. at 4.The Lease was a twenty-year, triple-net lease that required the debtor to pay monthly rent of $25,000. Touch of Grey, as franchisor, and Terrapin Station, as franchisee, also entered into a franchise agreement ("the Agreement"), whereby the Debtor would exclusively sell the Dark Star products that it purchased from Touch of Grey. R. at 4. The new "Terrapin Station Coffeehouse" opened on December 1st, 2018. R. at 5.

B. The Parties' Plan Fails and the Debtor Slides into Bankruptcy.

Despite the best efforts of the Parties, the Debtor's new coffeeshop never got off the ground. The parties' plan to break into the downtown nightlife scene and to avoid alienating the Debtor's previous customers failed. R. at 5. Less than a year after its opening, the Debtor owed Touch of Grey over $700,000 for Dark Star-branded goods. R. at 5. On December 5th, 2019, Touch of Grey sent Terrapin Station a notice of default. R. at 5. Two days later, the parties entered into a forbearance agreement wherein Touch of Grey agreed to forbear from terminating the Agreement in exchange for, among other things, a payment of $250,000. R. at 5.

Just over a week later, the Debtor purchased another $200,000 worth of Dark Star products from Touch of Grey. R. at 5. Despite the outstanding debt, Touch of Grey was willing to sell the goods on credit and documented the sale with an invoice ("the Invoice") dated December 18th. R. at 5. The goods were delivered to Terrapin Station three days later. R. at 6. However, after reviewing year-end numbers, the Debtor filed for bankruptcy just two weeks later.

On January 5th, 2020, the date of the Debtor's bankruptcy petition, the Debtor owed Touch of Grey over $650,000 on invoices for Dark Star goods. R. at 6. Nevertheless, at the first day hearings, the Debtor sought to purchase more Dark Star products. R. at 6. Touch of Grey expressed serious concern to the Bankruptcy Court about Tell's reorganization strategy. R. at 6. The Bankruptcy Court authorized Tell to reorganize the Debtor as a traditional coffeehouse. R. at 7.

As part of its reorganization, the Debtor sought court authorization to pay $200,000 to Touch of Grey claiming that Touch of Grey was a "Critical Vendor." R. at 6. The Debtor further emphasized that Touch of Grey was already entitled to a priority payment of $200,000 under Section[1] 503(b)(9). R. at 6. Sidestepping a fight over the propriety of Critical Vendor payments,[2] the Bankruptcy Court authorized the immediate payment of $200,000 to Touch of Grey as a Section 503(b)(9) administrative expense. R. at 7. The Debtor made the payment, and Touch of Grey resumed extending credit and supplying goods to the Debtor. R. at 7.

For the next four months, the Debtor continued to operate while in bankruptcy. But tragically, the COVID-19 pandemic struck just weeks later and ruined the Debtor's chances of successfully reorganizing. R. at 7. The Debtor permanently closed its doors on May 5th, 2020. R. at 7. After the Debtor shut down, the Debtor converted its case to a Chapter 7 liquidation, and the Respondent was appointed as liquidating Trustee for the Debtor's estate. R. at 8.

C. The Respondent Institutes a Preference Action Against Touch of Grey.

On the Petition Date, the Trustee had preference liability of $50,000 stemming from the $250,000 payment made pursuant to the forbearance agreement. R. at 28. The other $200,000

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[1] The Bankruptcy Code is set forth in 11 U.S.C. §§ 101 *et seq.* Specific sections of the Bankruptcy Code are identified herein as "Section __."

[2] For a discussion of the propriety of Critical Vendor payments generally, see Richard Robinson and Russell Heller, *Keep Your Friends Close, but Keep Your Critical Vendors Closer*, 39-AUG Am. Bankr. Inst. J. 16 (2020).

was protected by the subsequent new value defense under Section 547(c)(4) because of the goods that Touch of Grey shipped to the Debtor before the petition to qualify for that defense. R. at 8.

Upon his appointment, the Respondent commenced a preference action against Touch of Grey for the full $250,000 payment made pursuant to the forbearance agreement. R. at 8. The Respondent argued that the court-approved Section 509(b)(9) payment of $200,000 increased Touch of Grey's preference exposure by $200,000, because the post-petition Section 509(b)(9) administrative expense arose from the same pre-petition transfer of goods that gave rise to Touch of Grey's subsequent new value defense. R. at 9.

D. The Respondent Resists Paying Rent Under the Lease.

A day after the Debtor closed its doors, the Debtor filed a motion to reject the Lease and the Agreement as of May 5th. R. at 7. Touch of Grey supported the Debtors motion to reject the agreements, but moved to compel the payment of May's rent that was due "in advance, on the first day of the month" under the Lease. R. at 8.

The Respondent opposed Touch of Grey's motion to compel payment of May rent. R. at 8. He argued 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. As a result, he contended that the Debtor should pay five days' rent, as opposed to the monthly rent contemplated in the lease. R. at 8.

E. PROCEDURAL HISTORY

The Respondent moved for summary judgment on the preference action and the motion to compel rent. R. at 9. The Bankruptcy Court granted summary judgment for the Respondent on both issues. R. at 9. First, the court ruled that the $200,000 payment it authorized under Section 503(b)(9) eliminated the Petitioner's $200,000 affirmative defense under Section 547(c)(4). R. at

9. Second, the court held that Section 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.

Touch of Grey timely appealed both decisions on a consolidated basis to the United States District Court for the District of Moot. R. at 9. The district court affirmed the Bankruptcy Court. R. at 9. Touch of Grey thereafter timely filed a notice of appeal. R. at 9. The Thirteenth Circuit affirmed the district court. R. at 9. This Court granted Certiorari.

STANDARD OF REVIEW

The questions presented on this appeal are pure issues of law concerning statutory interpretation within the Bankruptcy Code. Thus, the standard of review is de novo. *Texas v. Soileau* (*In re Soileau*), 488 F.3d 302, 305 (5th Cir. 2007).

SUMMARY OF THE ARGUMENT

The concept of a preference is old and simple—when a debtor makes a preferential transfer prior to filing a bankruptcy petition, the trustee has the power to claw back that payment so that it may be shared by the debtor's similarly situated creditors. Everything about Section 547 and the historical concept of preference liability focuses on pre-petition transactions. Yet, the Trustee urges, and the Thirteenth Circuit held, that judicially authorized post-petition administrative payments can create preference liability when none existed before. Applying the logic of the Thirteenth Circuit, when a bankruptcy court authorizes a payment to a creditor under a plan distribution, Wage Order, or Critical Vendor order, the court is simultaneously ordering an increase in that creditor's preference exposure in the likely event that the creditor has also asserted the subsequent new value defense. That cannot be the rule.

This Court should overrule the Thirteenth Circuit's holding and find that post-petition administrative payments cannot increase a creditor's preference exposure because the plain

language of Section 547, the surrounding statutory context, and the important policy goals behind both Section 547 and Section 503 all make clear that the preference window properly closes at the petition.

The Thirteenth Circuit erred again when it allowed the Respondent to prorate the Debtor's rent payment that was due under the parties' Lease. Congress's clear command in Section 365(d)(3) is that a trustee must perform obligations that arise under nonresidential leases until the trustee rejects the lease. Because the language of Section 365(d)(3) is clear and unambiguous, this Court has no reason to head down the often slippery slope of looking to legislative history to interpret a statute. But even if this Court did in this case, the history is entirely consistent with the text. Both make clear that Congress passed Section 365(d)(3) for the express purpose of preventing bankruptcy courts from rewriting the terms of debtor's leases in the name of equity.

The Billing Date approach simply compels trustees to honor Congress's mandate by requiring that trustees honor debtors' commercial leases until those leases are rejected. In contrast, the Proration approach unnecessarily reads ambiguity into Section 365(d)(3). By allowing courts to prorate payments that leases require to be paid in full, the proration approach revives the very evil that Congress sought to extinguish, thus undermining the fundamental goal that the statute was intended to achieve.

Because both the unambiguous plain language of Section 365(d)(3) and its legislative history make clear that Congress intended to protect Lessors and Landlords from having their leases rewritten by courts, this Court should also reverse the Thirteenth Circuit's holding that interprets Section 365(d)(3) to allow for proration and instead adopt the Billing Date approach.

ARGUMENT

This Court should reverse the Thirteenth Circuit's ruling that the post-petition payment of an administrative expense is an "otherwise unavoidable transfer" under Section 547(c)(4)(B). This Court should further reverse the Thirteenth Circuit's decision that Section 365(d)(3) authorizes a Proration approach, and instead adopt the Billing Date interpretation.

I. The Thirteenth Circuit erred by failing to recognize that post-petition administrative payments cannot increase a creditor's preference exposure because transactions affecting preference liability must be made before the petition.

At the heart of the parties' dispute over the meaning of Section 547(c)(4) is whether or not a post-petition administrative payment under Section 503 increases creditor's preference liability under Section 547. Both Sections play key roles in the broader structure of the Bankruptcy Code.

Section 547 establishes the familiar framework of the preference analysis, governing the Trustee's power to avoid certain pre-petition transfers. 11 U.S.C.A. § 547. Section 547(a) defines terms. 11 U.S.C.A. § 547(a). Section 547(b) delineates the elements that make transfers avoidable. 11 U.S.C.A. § 547(b). One of those elements, Section 547(b)(4), establishes the preference period as within 90 days before the petition date, or between ninety days and one year if the creditor was an insider. 11 U.S.C.A. § 547(b)(4). Next, 547(c) codifies nine exceptions that remove certain otherwise unavoidable transfers from the reach of the Trustee. 11 U.S.C.A. § 547(c). One of those exceptions, Section 547(c)(4), is the subsequent new value defense. 11 U.S.C.A. § 547(c)(4). The subsequent new value defense immunizes creditors to the extent that the creditor gave new value on an unsecured basis to the debtor after a preferential transfer. *Id.* Its two subparts, Sections 547(c)(4)(A) and 547(c)(4)(B), limit the defense to when the

subsequent new value extended is secured by an unavoidable security interest, or paid for by an otherwise unavoidable transfer under one of the other eight exceptions in 547(c), respectively. *Id.*

In contrast, Section 503 governs the post-petition allowance and payment of administrative expenses, allowing third parties conducting business with debtors in, or on the eve of, bankruptcy to receive priority payment. 11 U.S.C.A. § 503. Section 503(b) expressly enumerates nine categories of expenses that qualify for priority payment. 11 U.S.C.A. § 503(b). One of those categories, Section 503(b)(9)[3], grants administrative expense status to a seller for the value of any goods sold to the debtor in the ordinary course of the debtor's business and received within twenty days before the commencement of the case. 11 U.S.C.A. § 503(b)(9).

The issue of how to handle the obvious overlap between the time periods in Section 503(b)(9) and Section 547(b) has divided courts. Debtors both sell goods and make payments in the ordinary course of business. Creditors that sell goods to a debtor within Section 503(b)(9)'s twenty-day window have typically received a payment within Section 547(b)'s general ninety-day preference period. Due to this natural interplay, goods received by a debtor within twenty days of bankruptcy frequently gives rise to both an affirmative defense under Section 547(c)(4) and an administrative claim under Section 503(b)(9). Thus, the question then becomes: did Congress intend for the use of Section 503(b)(9) to preclude the use of Section 547(c)(4)?

The text of Section 547 and Section 503 answer this question with a resounding no. "The plain language of Section 547 closes the preference window at the petition, limiting the Section 547(c)(4) defense to new value supplied and payments made before the debtor crosses into bankruptcy." *In re Phoenix Rest. Group, Inc.*, 317 B.R. 491, 496 (Bankr. M.D. Tenn. 2004). Yet in this case, the Thirteenth Circuit held the opposite. As a result, a Section 503(b)(9) payment—

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[3]Section 503(b)(9) was added to the Code in 2005, as part of the Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA").

authorized by the Bankruptcy Court to induce Touch of Grey to continue to extend credit to the Debtor—operated to increase Touch of Grey's preference liability by the exact same amount. R. at 8. By failing to recognize that Section 547 only governs pre-petition transactions, the Thirteenth Circuit erred, misinterpreted Section 547(c)(4)(B), and upended the longstanding rule that transactions affecting preference liability must be made before the petition.

A. Judicially authorized post-petition payments are not "otherwise unavoidable transfers" within the meaning of Section 547(c)(4).

The specific interpretive issue before this Court is whether or not the post-petition payments of an administrative expense are "otherwise unavoidable transfers" within the meaning of Section 547(c)(4)(B). The plain language of Section 547(c)(4), the surrounding context of Section 547, and the legislative history of Section 547(c)(4) make clear that they are not. Section 547(c)(4) in its entirety reads:

> (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.

11 U.S.C. § 547(c)(4). Though Congress did not specify in Section 547(c)(4)(B) when an "otherwise unavoidable transfer" must be made, it cannot be reasonably contended that the statute is completely open ended. If the time period involved is completely open-ended, any payment, made at any time, "could defeat a new value defense." *In re Friedman's Inc.*, 738 F.3d 547, 554 (2013). And logically, if any payment, made at any time, defeats a new value defense,

every judicially authorized post-petition payment on an unsecured pre-petition claim is captured by the rule.

Section 503(b)(9) is one of many times a court may authorize a post-petition payment on a pre-petition claim. In addition to general post-petition distributions on pre-petition unsecured claims, courts have approved “first-day” wage orders that allow payment of employees' pre-petition wages, “critical vendor” orders that allow payment of essential suppliers' pre-petition invoices, and “roll-ups” that allow lenders who continue financing the debtor to be paid first on their pre-petition claims. *See Czyzewski v. Jevic Holding Corp.*, 137 S. Ct. 973 (2017). These priority-violating distributions generally serve significant Code-related objectives. *Id.* Their premise is that successful reorganization makes even the disfavored creditors better off. *Id.* Interpreting Section 547(c)(4)(B) to bring these court-authorized payments into the preference analysis would defeat the point of the payments. “Did Congress really intend there to be no limit to when a payment defeating a new value defense could be made in determining whether a preference has occurred? We think not.” *See Friedman's Inc.*, 738 F.3d at 547.

The better reading of Section 547(c)(4)(B) recognizes that the plain language of Section 547(c)(4), the context of Section 547, and the legislative history of Section 547(c)(4) make clear that Congress fixed preference liability on the date of the petition.

1. The plain language of Section 547(c)(4) limits preference liability to pre-petition transactions.

The starting point of the analysis is the language of Section 547(c)(4)(B). When “the statute's language is plain, the sole function of the courts—at least where the disposition required by the text is not absurd—is to enforce it according to its terms.” *Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 6 (2000). Though Congress did not expressly define when an “otherwise unavoidable transfer” must occur in Section 547(c)(4)(B), Congress's choice

to use the word "debtor" in that Section 547(c)(4)(B) evidences Congress's intent to end the preference analysis on the petition date.

Specifically, Congress chose to use the term "debtor" rather than "debtor in possession" or "trustee" within Section 547(c)(4)(B). *See* 11 U.S.C. § 547(c)(4)(B). Because the "debtor" exists only pre-petition, while the term "debtor in possession" controls the post-petition state of bankruptcy, the Legislature's decision to use "debtor" makes clear that Section 547(c)(4)(B) deals only with pre-petition conduct. At first glance, this inference may appear strained because other parts of the Code refer to "debtors" in the post-petition context. *See Friedman's Inc.*, 738 F.3d 547 (3d Cir. 2013) (declining to focus on the presence or absence of individual words and phrases, in favor of a broader approach looking to the context of the Bankruptcy Code as a whole). However, with a deeper look at the text of Section 547(c)(4) and the substantial body of caselaw interpreting it, the importance of this distinction becomes clear.

The only express temporal requirement in Section 547(c)(4) is that an extension of new value must be made "after the [preferential] transfer." 11 U.SC. § 547(c)(4). But an overwhelming number of courts have held that the use of the specific word "debtor" in Section 547(c)(4) imposes a second temporal requirement on the subsequent new value defense—that the extension of new value also be made before the petition. *See e.g.*, *In re Bellanca Aircraft Corp.*, 850 F.2d 1275, 1284 (8th Cir. 1988) (noting that "post-petition advances are given to the debtor's *estate*, not to the debtor") (emphasis in original); *In re Phoenix Rest. Grp., Inc.*, 317 B.R. at 496 ("Throughout § 547, 'the debtor' refers to the *prepetition* entity that transferred property or engaged in business with the preference defendant.") (emphasis in original); *In re D.J. Mgt. Grp.*, 161 B.R. 5, 6 (Bankr. W.D.N.Y. 1993) ("The phrase 'the debtor' is systematically used throughout the Bankruptcy Code to connote an entity different from 'the estate,' 'the Trustee,' or

'the debtor-in-possession.'"); *In re Sharoff Food Serv., Inc.*, 179 B.R. 669, 678 (Bankr. D. Colo. 1995) ("[T]he specific language 'to or for the benefit of the debtor' [indicates] that the subsequent advances of new value are only those given prepetition, because any post-petition advances are given to the debtor's estate, not the debtor.").

The Code does refer to "debtors" in the post-petition context in other Code sections. However, throughout Section 547 itself, "the debtor" *only* refers to the pre-petition entity that transferred property or engaged in business with the preference defendant. *See Phoenix Rest. Group*, 317 B.R. at 496; *Freidman's Inc.*, 738 F.3d at 555. The additional import placed on this distinction in Section 547 is supported by Congress's use of the disjunctive phrase "debtor or trustee" when defining "new value" in Section 547(a). 11 U.S.C. § 547(a). Dissenting Judge Wier in the court below correctly noted that interpreting the term "debtor" in Section 547(c)(4)(B) to include the trustee would render the phrase "the debtor or the Trustee" superfluous. R. at 2. This Court's "cases express a deep reluctance to interpret a statutory provision so as to render superfluous other provisions in the same enactment." *Pennsylvania Dept. of Pub. Welfare v. Davenport*, 495 U.S. 552, 562 (1990). The plain language of Section 547(a) justifies the extra meaning behind the words "debtor" and "trustee" in Section 547(c) that may not apply in every section of the Code.

Moreover, identical words and phrases within the same statute should be given the same meaning as a matter of statutory consistency. *See e.g.*, *Powerex Corp. v. Reliant Energy Servs., Inc.*, 551 U.S. 224, 232 (2007). The facts of the present case are a perfect example of why that principle matters. Here, Touch of Grey received a post-petition payment and subsequently extended new value to the Debtor. Under the Trustee's approach, the post-petition payment reduces Touch of Grey's subsequent new value defense, but Touch of Grey's post-petition

extensions of new value have no effect. In essence, the Trustee asks this Court to construe the word "debtor" to mean one thing in Section 547(c)(4) and something different in one of its subparts. "Logically, and as a matter of statutory consistency, the Trustee's argument fails." *See In re Murray*, No. 04-13611, 2007 WL 5595447, at *2 (Bankr. M.D. Tenn. June 6, 2007).

2. The remainder of Section 547 clarifies that the preference window closes on the date of the petition.

The provisions surrounding Section 547(c)(4)(B) shed additional light on what Congress intended Section 547 to mean. This Court has been abundantly clear that courts construing the Code are not to "be guided by a single sentence or member of a sentence, but look to the provisions of the whole law, and to its object and policy." *Kelly v. Robinson*, 479 U.S. 36, 43 (1986). A provision that may seem ambiguous in isolation is often clarified by the remainder of the statutory scheme because only one of the proposed meanings produces a substantive effect that is compatible with the rest of the law. *See United Sav. Ass'n of Texas v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 371 (1988). When Section 547 is read as a whole, numerous contextual indicators bolster the conclusion that post-petition transfers are irrelevant to the preference analysis.

Right off the bat, Section 547 is entitled "Preferences." *See* 11 U.S.C.A. § 547. That suggests that it concerns transactions occurring within the preference period, which is by definition pre-petition. *See Friedman's Inc.*, 738 F.3d at 555 ("It would make sense that the calculation of the amount of the preference, and application of any new value reduced by subsequent transfers, would relate to that time period."). In contrast, Section 549 is entitled "Postpetition Transactions," and, as its title implies, that provision deals with only post-petition conduct. *See* 11 U.S.C.A. § 549. Congress, by placing Section 547(c)(4)(B) within Section 547, indicated that Section 547(c)(4)(B) looks only to pre-petition events.

Next, Section 547(b)(5)'s liquidation test, which is used to determine if a challenged transfer is avoidable, is conducted on the petition date. That test requires courts to compare the payment received by a creditor during the preference period with what the creditor would have received if the payment had not been made and the debtor's assets were liquidated and distributed to creditors. *Alvarado v. Walsh (In re LCO Enters.)*, 12 F.3d 938, 942 (9th Cir. 1993). Again, Congress did not expressly say when this test should be performed. 11 U.S.C. § 547(b)(5). However, courts have consistently held that the liquidation analysis should be conducted as of the date the bankruptcy petition is filed. *See Palmer Clay Prods. Co. v. Brown*, 297 U.S. 227, 229 (1936); *In re Falcon Prods., Inc.*, 381 B.R. 543, 547 (Bankr. App. 8th Cir. 2008) (noting that "Supreme Court precedent requires that the hypothetical liquidation test be conducted as of the petition date"). Thus, extending the preference analysis past the petition date would be inconsistent with the essential elements of a preference. *See Freidman's Inc.*, 738 F.3d at 556.

Even worse, if this Court interprets Section 547(c)(4)(B) to include post-petition payments, the calculation of preference liability begins to fluctuate depending on when a preference action is filed. *Id.* The statute of limitations for preference actions begins to run on the petition date. 11 U.S.C. § 546(a). If Congress had intended to allow for post-petition transactions to affect the impact on the estate, it likely would have crafted a different statute of limitations. *See Freidman's Inc.*, 738 F.3d at 556. Hinging the value of an avoidance action on when the Trustee decides to bring that action injects an entirely unnecessary element of gamesmanship and uncertainty into the preference process.

Finally, the inclusion of the phrase "as of the petition date" in Section 547(c)(5) further bolsters this analysis. The Thirteenth Circuit below concluded that the inclusion of this language

in an analogous provision leads to "the inescapable conclusion that the statute contains no temporal limitation whatsoever." R. at 14. However, the Thirteenth Circuit failed to consider both the purpose and the effect of this language—to create a "net-results" rule. *See Floating Liens in Inventory and Receivables (Code § 547(c)(5))*, § 66:30, 4 NORTON BANKR. L. & PRAC. 3d. (Oct. 2021) ("The rationale for the test is that the sum of all transactions during the relevant preference period should be netted out to determine whether there has been a preferential effect."). In contrast, that language would be superfluous in Section 547(c)(4) because Section 547(c) is not a net-results rule. *See Matter of Toyota of Jefferson, Inc.*, 14 F.3d 1088, 1092 (5th Cir. 1994) (noting that because Section 547(c)(4) requires new value to be given by the creditor *after* the preferential transfer to the creditor, it is not a net-results rule). Thus, Section 547(c)(5), like every other provision in Section 547, only serves to further emphasize the natural conclusion that Congress intended the preference analysis to end on the date of the petition. See *Friedman's Inc.*, 738 F.3d at 556 ("On balance, we believe that the policy of improvement of position prior to the petition date is central to the concept of preference.").

In sum, these contextual clues clarify that the preference analysis concludes on the petition date. Section 547(c)(4)(B), like any other statutory provision, must be read with the rest of Section 547. Reading Section 547 as a whole establishes the petition date as the outer limits of its reach. Such a reading avoids creating conflict among the various provisions of the Code and allows Legislative intent concerning preferences to be upheld.

3. Congress did not intend to erase the pre-Code practice of fixing liability on the petition date with the passage of Section 547(c)(4) or Section 503(b)(9).

The history of the subsequent new value defense reinforces the conclusion that Section 547(c)(4) does not extend to post-petition events. This Court has explicitly noted that it will not

read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure. *Cohen v. de la Cruz*, 523 U.S. 213, 221(1998). Esteemed Professor Countryman described the pre-Code practice as follows:

> Old section 60c provided, from its enactment in 1898, that if a creditor had been preferred 'and afterward in good faith gives the debtor further credit without security of any kind for property which becomes a part of the debtor's estate, the amount of such new credit *remaining unpaid' at bankruptcy* 'may be set off against the amount' of the preference that the trustee recovers.

See Vern Countryman, *The Concept of A Voidable Preference in Bankruptc*y, 38 VAND. L. REV. 713, 781 (1985); *see also* Bankruptcy Act of 1898, Ch. 541, § 60, 30 Stat. 544 (1898).

As the language above clearly demonstrates, Section 60(c) limited the preference analysis to the petition date. When Congress replaced the language "remaining unpaid at bankruptcy" with the phrase "otherwise unavoidable transfer" in Section 547(c)(4)(B), Congress simply eliminated the requirement that the new value have to remain unpaid. Congress deleted the old "remaining unpaid" requirement because it allowed a debtor to defeat a creditor's new value defense with a payment that could later be avoided by the Trustee. *See* Harris P. Quinn, *The Subsequent New Value Exception under Section 547(c)(4) of the Bankruptcy Code—Judicial Gloss Is Creditors' Loss*, 24 MEM. St. U. L. REV. 667, 681 (1994) (criticizing courts still requiring new value to remain unpaid after the enactment of Section 547(c)). Indeed, the parties here have stipulated, and the Thirteenth Circuit agreed, that new value no longer must remain unpaid to trigger the subsequent new value defense. R. at 10.

By eliminating the requirement that new value remain unpaid, Congress did not abrogate the pre-Code rule that the preference analysis ended at the petition. If Congress had intended Section 547(c)(4) to modify the pre-Code rule that the subsequent new value exception ended on the petition date, "the intention would be clearly expressed, not left to be collected or inferred

from disputable considerations of convenience in administering the estate of the bankrupt." *In Midlantic Nat'l Bank v. New Jersey Dept. of Env't Prot.*, 474 U.S. 494, 501 (1986); *see also Whitman v. Am. Trucking Assocs.*, 531 U.S. 457, 468 (2001) ("Congress...does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions—it does not, one might say, hide elephants in mouseholes.").

In sum, if Congress wanted to change the venerable understanding that preference liability is fixed on the petition date, it would have said so. Congressional silence does not justify such a drastic departure from the well-established preference liability framework. Congress could have amended Section 547(c)(4) when it passed Section 503(b)(9) to prevent the application of both to the same payment, but Congress did not. *In re Commissary Operations, Inc.*, 421 B.R. 873, 879 (Bankr. M.D. Tenn. 2010). Unless and until Congress makes such a decision, courts must follow the current direction that the Bankruptcy Code provides. *See Kawaauhau v. Geiger*, 523 U.S. 57, 64 (1998). An examination of the policy goals underlying both statutes reveals why Congress has declined to do so.

B. Closing the preference window at the petition best serves the congressional policy underlying Sections 547(c)(4) and 503(b)(9).

Reading Section 547(c)(4)(B) to preserve the distinction between pre-petition and post-petition transactions best serves the public policy goals espoused by both Section 547(c)(4) and Section 503(b)(9). The Thirteenth Circuit held the opposite, reasoning that allowing Touch of Grey to claim a benefit under both Sections for the same conduct would be inconsistent with bankruptcy's goal of equality. R. at 15. In reality, allowing Touch of Grey to utilize both Sections fulfills the policy underlying both—to give debtors the best opportunity to avoid bankruptcy.

At bottom, both Sections encourage creditors to do business with distressed debtors. *In re Commissary Operations, Inc.*, 421 B.R. at 876. Any rule authorizing a priority payment may be said to conflict with the policy of equal treatment. *See Union Bank v. Wolas*, 502 U.S. 151, 161 (1991). However, a successful reorganization makes all creditors better off. *See In re Kmart Corp.*, 359 F.3d 866, 872 (C.A.7 2004) (discussing the justifications for Critical Vendor orders). In turn, a priority payment may fulfill the central Code policy of maximizing the value of the bankruptcy estate. *See Toibb v. Radloff*, 501 U.S. 157, 163 (1991) (recognizing "maximizing the value of the bankruptcy estate" as a goal of the Code).

By requiring creditors to choose one or the other, the Thirteenth Circuit actually undermined the central purpose of both. Reading Section 547(c)(4)(B) to only capture pre-petition events is entirely consistent with Congress's decision to create two independent financial incentives for creditors to continue extending risky credit to debtors teetering on the brink of bankruptcy.

<u>1. Depriving creditors of the benefit that Congress conferred on them in 503(b)(9) and 547(c)(4) chills their willingness to deal with troubled businesses.</u>

Congress enacted both Section 547(c)(4) and Section 503(b)(9) of the Code to enhance the rights of creditors selling goods to struggling debtors before bankruptcy. Nothing in the plain language of either Section indicates any congressional intent for creditors to be limited to using one or the other. Interpreting the use of one to preclude the use of the other would undermine the policy of both by making creditors less likely to extend credit to a troubled business.

The policy of Section 547(c), not that of the general avoidance provision, is relevant here. The cases holding that the Code's policy in favor of "equality" reigns supreme have lost sight of the true policy objectives underlying Section 547(c). *See Freidman's Inc.*, 738 F.3d at 560. As the Eighth Circuit Court of Appeals correctly recognized:

> The general avoidance portion of the Bankruptcy Code was intended to 'facilitate the prime bankruptcy policy of equality of distribution among creditors of the debtor.' Nevertheless, the subsequent advance rule, section 547(c)(4), 'was not enacted to ensure equitable treatment of creditors, *but rather is intended to encourage creditors to deal with troubled businesses*.'

In re Bellanca Aircraft Corp., 850 F.2d at 1280 (citations omitted) (emphasis added).

Lining up neatly with Section 547(c)(4), Section 503(b)(9) seeks to encourage trade creditors to continue to extend credit to a debtor potentially heading for bankruptcy. *In re Arts Dairy LLC*, 414 B.R. 219, 220 (2009) Conversely, it also discourages abuse by debtors who seek to acquire goods at a time when it is known that bankruptcy is imminent and that payment for the goods will not have to be tendered. *Id.*

Alleviating the financial pressure that would result if creditors were to force an ailing company to pay for supplies up-front prevents unnecessary bankruptcies *In re New York City Shoes, Inc.*, 880 F.2d 679 (3d Cir. 1989). Requiring creditors to choose between asserting a Section 503(b)(9) claim and preserving its subsequent new value defense chills their willingness to do business with troubled entities. *See In re Commissary Operations, Inc.*, 421 B.R. at 879 (noting that imposing such a choice "would work a disservice on Congress' inherent policy goals when enacting" both provisions).

Congress was free to confer two independent benefits on sellers of goods that continue to support distressed businesses to further the same goal. Congress did confer those benefits. The identical policies underlying each Section support reading Section 547(c)(4)(B) in a manner that gives effect to both.

2. Reading Section 547(c)(4)(B) to capture post-petition payments interferes with post-petition policies and practices.

Pre-petition transactions and post-petition transactions are governed by different rules for a reason. Interpreting Section 547(c)(4(B) to include post-petition disbursements in the preference analysis interferes with the orderly rules that govern post-petition conduct. The court-authorized priority payment of $200,000 in this case operating to allow for its own claw-back demonstrates this point perfectly.

The preference analysis need not account for post-petition activity because when the petition is filed, the bankruptcy court assumes control of the debtor-creditor relationship. *Friedman's Inc.*, 738 F.3d at 561. Things are fundamentally different after the debtor becomes a bankruptcy estate under the administration of the court and is subject to the scrutiny of creditors, committees, the U.S. Trustee, and others*. See In re Phoenix Rest. Grp., Inc.*, 317 B.R. at 497–98. A holding that blends the orderly rules governing pre- and post-petition invites conflict between those rules. *Id.* (noting that bankruptcy policies collide and uncertainty flourishes if preference defense analysis under Section 547(c)(4) slides past the petition).

One problem particularly relevant here arises from the fact that post-petition disbursements require court authorization. *See, generally*, 11 U.S.C.A. § 549. Authorizing a post-petition payment to a creditor that also increases that creditor's preference liability is giving with one hand and taking away with the other. *Friedman's Inc.*, 738 F.3d at 561 (observing the problems with allowing a debtor to seek and obtain permission to pay wages to a staffing company one week and then sue that company for a preference the next). Addressing this unfairness, one court described the severity of the problem as follows:

> Because the debtor-in-possession convinced the Court that [certain creditors] were so critical to the operation of the Debtor's business and the company's reorganization efforts, special treatment was carved out for this particular group of creditors. Now the Trustee would undo what the Court approved...[t]he mixed message that such a ruling would send for future bankruptcies is problematic, and

> the harm that could come to future debtors from this approach is of great concern to the Court.

In re Murray, Inc., 04-13611, 2007 WL 5595447, at *2 (Bankr. M.D. Tenn. June 6, 2007).

The facts of this case are strikingly similar. The debtor-in-possession here convinced the Bankruptcy Court that Touch of Grey was critical to the operation of the Debtor's business and reorganization efforts. R. at 6–7. The creditors' committee was in favor of the payment being made, and as a result, the Bankruptcy Court carved out special treatment for Touch of Grey. R. at 7. Now, the Trustee would undo what the Bankruptcy Court approved by penalizing the vendor for accepting the administrative payment and continuing to do business with a debtor in bankruptcy. That cannot be the result that the Legislature intended.

3. Claiming a Section 503 expense is not a "windfall."

As a final matter, Touch of Grey receiving benefits under Section 547(c) and Section 503(b)(9) for the same transaction is not a "windfall" to Touch of Grey. Every dollar received by Touch of Grey was for goods actually provided, and Touch of Grey's continued extensions of credit to the Debtor allowed it to continue its reorganization efforts for four additional months.

More fundamentally, this Court presumes that Congress passed Section 503(b)(9) with full knowledge of Section 547(c)(4). *See United States v. Brown*, 879 F.3d 1043, 1049 (9th Cir. 2018); *In re Vills. at Castle Rock Metro. Dist. No. 4*, 145 B.R. 76, 83 (Bankr. D. Colo. 1990). As discussed above, "when 11 U.S.C. § 503(b)(9) was added, Congress did not amend 11 U.S.C. § 547(c)(4) to include a new subsection reducing new value by the amount of any § 503(b)(9) claim." *In re Commissary Operations, Inc.*, 421 B.R. at 879. Characterizing a creditor claiming

two benefits under two independent Code provisions as a "windfall" is misleading.[4] *See Friedman's Inc.*, 738 F.3d at 549.

By replenishing the debtor's estate during the preference period, creditors provide the estate with the best chance to avoid bankruptcy, while effectuating congressional intent. *See In re Commissary Operations, Inc.*, 421 B.R. at 878. "Even if the creditor receives a limited post-petition payment on its 503(b)(9) claim to cover the 'value' of the goods, the debtor-in-possession has realized the mark-up profit on the re-sale of the goods...and can fill an order to its customers' satisfaction." *Id.* A creditor providing this support to a struggling debtor is the precise outcome that Congress sought to achieve; ruining this outcome ruins the purpose of the provisions entirely.

Because both the text of Section 547 and the policy behind it support limiting the reach of Section 547(c)(4)(B) to pre-petition events, this Court should reverse the Thirteenth Circuit's holding and allow Touch of Grey to offset its preference liability with the Section 503(b)(9) payment authorized by the Bankruptcy Court. Such a decision furthers the goals of bankruptcy and ensures uniformity in the application of the Code's provisions.

II. The Thirteenth Circuit again erred by not adopting the Billing Date interpretation of Section 365(d)(3), which simply requires the Trustee to perform under a lease until rejection.

Section 365(d)(3) stands for the unambiguous and unremarkable proposition that Trustees must perform the obligations arising under commercial leases until they reject them. However, the statute does not define when an obligation arises. Courts are surprisingly split on this issue, opting for either the "Billing Date" approach or the "Proration" approach. The former holds that

[4] As a more general matter, it should be noted that these provisions give the creditors priority at the end of a case, not a right to immediate payment. It is not always so clear whether the creditors actually enjoy priority. *See* Richard M. Hynes & Steven D. Walt, *Inequality and Equity in Bankruptcy Reorganization*, 66 U. KAN. L. REV. 875 (2018).

obligations arise when the lease says that they do. The latter suggests that obligations accrue daily, such that they can be prorated between the prerejection and postrejection periods. The first gives effect to the statute's plain language, while the second does violence to it in the name of equity.

The Lease in the present case stated that monthly rent was due "in advance on the first day of each month." R. at 4. The Lease was not rejected until May 5th. Under the Billing Date approach, the Trustee simply must do what the Lease would have required the Debtor to do: pay May's rent, because it came due before the Trustee rejected the Lease. As Circuit Judge Wier succinctly stated in his dissent below: "the analysis is that simple." R. at 28.

Because the Billing Date approach effectuates the command of unambiguous statutory language, finds support in the history of the Bankruptcy Code, and best serves the public policy goals that led to its passing, the Thirteenth Circuit erred by failing to adopt it.

A. The meaning of "obligations arising under any unexpired lease" in § 365(d)(3) is not ambiguous in the context of a lease that requires payment of one month's rent in advance before rejection.

The task of resolving the dispute over the meaning of Section 365(d)(3) begins where all such inquiries must begin: with the language of the statute itself. *U.S. v. Ron Pair Enters., Inc.*, 489 U.S. 235, 241 (1989). "In this case it is also where the inquiry should end, for where, as here, the statute's language is plain, 'the sole function of the courts is to enforce it according to its terms.'" *Id.* (citing *Caminetti v. United States*, 242 U.S. 470, 485 (1917)). Because the plain language of Section 365(d)(3) is unambiguous, "judicial inquiry is complete." *Rubin v. United States*, 449 U.S. 424, 430 (1981). The full text of Section 365(d)(3) reads:

> 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.

11 U.S.C. § 365(d)(3) (emphasis added).

Section 365(d)(3) is not ambiguous and the plain language of the statute only leads to one reasonable interpretation: a trustee is required to perform the lease in accordance with its terms. Thus, Section 365(d)(3) instructs courts to "look to the terms of the lease to determine both the nature of the 'obligation' and when it 'arises.'" *In re Montgomery Ward Holding Corp.*, 268 F.3d 205, 209 (3d Cir. 2001).

<u>1. The word "obligation" in Section 365(d)(3) refers to the legal duties imposed by the underlying contract.</u>

The word "obligation" in Section 365(d)(3) refers to the legal obligations imposed by the underlying lease. *See HA-LO Industries, Inc. v. Centerpoint Props. Tr.*, 342 F.3d 794, 799 (7th Cir. 2003) (noting that rent obligations are governed by Section 365(d)(3) of the Bankruptcy Code and the terms of the parties' lease). Section 365 does not define obligation. *See* 11 U.S.C. § 365. Because the Code does not define obligation, the word has its ordinary meaning. *Asgrow Seed Co. v. Winterboer*, 513 U.S. 179, 187 (1995). The essential meaning of the word obligation is "something that you must do because of a law, rule, promise, etc." *See Obligation*, *Merriam-webster.com*, https://www.merriam-webster.com/dictionary/obligation (last visited Jan. 10, 2022). Thus, in the context of a lease contract, an obligation is something that one is legally required to perform under the terms of the lease. *In re Montgomery Ward Holding Corp.*, 268 F.3d at 209.

Here, the Lease required the Debtor to pay the full monthly rent, $25,000, "in advance on the first day of each month." R. at 4. By doing so, the Lease indisputably obligated the Debtor to pay rent in twelve monthly payments, each due on the first day of each month. Because the

Lease defined the Debtor's rent obligation as monthly installments, the text of the Lease directly contravenes the Trustee's argument that the Debtor's rent obligation accrued daily. *See In re Duckwall–ALCO Stores*, 150 B.R. 965, 976 n. 23 (D.Kan. 1993) (rejecting the proration approach because the lease at issue did not provide for payment of taxes to the landlord as they accrued).

2. An obligation requiring a debtor to pay one month's rent in advance on a fixed date unambiguously arises on the day that payment is due under the lease.

The question of when an obligation "arises" for the purposes of Section 365(d)(3) is unambiguously answered when a lease requires the payment of one month's rent in advance on a fixed date. This is the precise scenario that Congress had in mind when it passed Section 365(d)(3) to relieve landlords of the uncertainty of collecting rent fixed in the lease "'in full, promptly, and without legal expense' during the awkward post-petition prerejection period." *HA-LO Indus., Inc.*, 342 F.3d at 799.

The Thirteenth Circuit erred, like other courts adopting the Proration approach, when interpreting Section 365(d)(3) to be ambiguous because it does not say when an obligation "arises." R. at 17. Identifying when an obligation "arises" may indeed be unclear in cases where the lease at issue fails to specify an obligation's payment date. But when, as here, a lease simply requires the payment of one-month's rent on the first day of the month, the plain language of Section 365(d)(3) unambiguously commands a finding that the obligation "arose" when the obligation came due. *See In re Koenig Sporting Goods, Inc.*, 229 B.R. 388, 392 (B.A.P. 6th Cir. 1999) *aff'd*, 203 F.3d 986 (6th Cir. 2000) (holding that the meaning of "obligations ... arising ... under any unexpired lease" in § 365(d)(3) is not ambiguous in the narrow context of a lease that required payment of one month's rent in advance the day before rejection.).

Tellingly, every circuit court considering this issue in the context of post-petition rent has come to this same conclusion. *See In re Burival*, 406 B.R. 548, 553 (Bankr. App. 8th Cir. 2009), *aff'd*, 613 F.3d 810 (8th Cir. 2010) ("The language is clear: the debtor shall timely perform all obligations arising from and after the order for relief until the lease is assumed or rejected."); *HA-LO Indus., Inc.*, 342 F.3d at 799; *In re Koenig Sporting Goods, Inc.*, 229 B.R. 388 at 41; *Montgomery Ward*, 268 F.3d at 212.

In contrast, one of the most influential cases articulating the rationale for the Proration Approach addressed a situation where a landlord was seeking to recover a year's worth of back-taxes under Section 365(d)(3). *See Matter of Handy Andy Home Improvement Ctrs., Inc.*, 144 F.3d 1125 (7th Cir. 1998). These non-rent expenses, for which Handy Andy was liable under the terms of the lease, had in part accrued prepetition while Handy Andy occupied the premises, but were billed to Handy Andy after the start of the post-petition period and prior to Handy Andy's rejection of the lease. *Id.* at 1126. Writing for the *Handy Andy* court, Judge Posner held that the back-taxes should be prorated, reasoning that that the tax obligation could realistically be said to have arisen piecemeal every day of the year. *Id.* at 1127.

A careful reading of *Handy Andy* actually supports the application of the Billing Date approach here. When analyzing the plain language of Section 365(d)(3), Judge Posner stressed that the legislative history of Section 365(d)(3) was illuminating. *Id.* He wrote "To give relief to landlords, Congress passed section 365(d)(), which takes them out from under the 'actual, necessary' provision of 503(b)(1) and allows them during that awkward postpetition prerejection period *to collect the rent fixed in the lease*." *Id.* at 28 (emphasis added). He further emphasized that the language of Section 365(d)(3) should be read in light of its context, which "consists not

merely of other sentences *but also of the real-world situation to which the language pertains*." *Id.* at 1128 (emphasis added). In his words, "[w]hen context is disregarded, silliness results." *Id.*

Judge Posner's rule is an imminently reasonable one. And when the real-world situation presented is a landlord attempting to collect rent fixed under the lease, both the context and the legislative history bolster what the plain language of the statute says: the Billing Date approach applies.

Less than ten years after *Handy Andy*, the Seventh Circuit arrived at this same conclusion when it adopted the Billing Date approach in the context of post-petition rent. *See HA-LO Indus., Inc.*, 342 F.3d at 798 (observing that *Handy Andy* does nothing to diminish the statutory protection afforded landlords for purely post-petition and prerejection obligations to pay rent). This Court should do the same.

B. Applying the Billing Date approach in the post-petition rent context is entirely consistent with the public policy goals and legislative history of Section 365(d)(3).

As alluded to above, the application of the Billing Date approach is not only supported by the plain language of Section 365(d)(3), it also best effectuates the legislative policy behind the statute as expressed in Section 365(d)(3)'s legislative history. The Bankruptcy Code was amended in 1984 to provide relief to Lessors/Landlords who had suffered under non-residential real property leases under prior law. Virtually all courts have agreed it was designed to alleviate the burdens that prior bankruptcy law placed on landlords by requiring timely compliance with the terms of the lease. *See Montgomery Ward*, 368 F.3d at 210. What the Thirteenth Circuit characterizes as inequitable is in reality Section 365 working exactly as it should.

1. The Bankruptcy Code was amended to provide relief to Lessors/Landlords getting burned on non-residential real property leases.

Congress gave trustees a single unremarkable and unambiguous command in Section 365(d)(3): honor commercial leases until you reject them. The Thirteenth Circuit's desire for equality is overridden by Congress's intent to provide special treatment for nonresidential landlords. *See Burival*, 406 B.R. at 553–55. The legislative history of the amendments makes this purpose clear. Senator Orrin Hatch, a conferee on the Original Act, described the purpose of the bill as follows:

> The 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. *This timely performance requirement will insure that debtor-tenants pay their rent, common area, and other charges on tim*e pending the trustee's assumption or rejection of the lease.

In re Krystal Co., 194 B.R. 161, 165 (Bankr. E.D. Tenn. 1996) (quoting the Statement of Senator Hatch, H.R. Rep. No. 882, 95th Cong., 2d Sess. *reprinted in* 1984 U.S.C.C.A.N. 576) (emphasis added). These remarks make no mention of the concepts of accrual or proration. *Id*. Instead, the legislative history makes clear that the statute was enacted to ameliorate the financial burden borne by lessors of nonresidential property during the period in which trustees decided whether to assume a lease. *In re P.-A. Trading Co.*, 27 F.3d 401, 403 (9th Cir. 1994).

Specifically, Section 365(d)(3) shifted the burden of indecision from the landlord to the debtor. *Id.* Prior to 1984, the Code created a "Neverland" between the filing of a bankruptcy case and the debtor's decision to assume or reject a lease wherein lease obligations were gutted by the equitable considerations underlying Section 503(b). *See In re Koenig Sporting Goods, Inc.*, 229 B.R. at 393 (discussing "Neverland" and the notions of "necessity," "reasonableness," and "benefit" at play under Section 503(b)); *In re Oreck Corp.*, 506 B.R. 500, 504, 509 (Bankr. M.D.

Tenn. 2014) (observing that lessors commonly faced disallowance, reduction, or delayed payment of post-petition rents depending upon debtor's use of the property, market value of the leased premises, solvency of the debtor, and the simple fact that administrative expenses had no immediate payment requirement).

By passing Section 365(d)(3), Congress intentionally placed the burden on the debtor to reject the lease before some onerous payment comes due. *In re Krystal Co.*, 194 B.R. at 164. Only the Billing Date approach fulfills this intent by making the unrejected leases binding on the Debtor until rejection. Addressing the inherent flaws in the Proration Approach, one commentator pronounced:

> [U]nder a nonbinding lease approach, the burden shifts to the lessor to move to compel an early election so as to avoid the risk of not collecting the full rent should the [debtor-in-possession] vacate part or all of the premises, or if the court finds the contract rate to be unreasonable...only by adopting a binding lease approach will a court allocate the burdens as envisioned by Congress.

Joshua Fruchter, *To Bind or Not to Bind - Bankruptcy Code S 365(d)(3): Statutory Minefield*, 68 AM. BANKR. L.J. 437, 464 (1994).

By adopting the Proration approach, the Thirteenth Circuit failed to give effect to the policy decisions made by Congress when it enacted Section 365(d)(3). The legislative history and plain language of Section 365(d)(3) make the congressional intent behind the statute clear. The Thirteenth Circuit's concern for the most equitable result must yield to the text of the Code. *See Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 206 (1988) (instructing that equitable powers of bankruptcy courts can only be exercised within the confines of the Bankruptcy Code).

2. The Billing Date interpretation creates a bright-line test that cuts both ways.

While the Thirteenth Circuit characterizes the Billing Date approach as a pro-creditor rule, the reality is that the Billing Date approach often operates to harm creditors as much as it

helps them. The essence of the Billing Date interpretation is that obligations accrue all at once, or not at all, depending on the date that payment became due under the lease. Whether this all-or-nothing rule operates to harm or benefit a creditor turns entirely on the date of the petition.

Only when the petition is filed before the rent obligation accrues does the Billing Date approach benefit the landlord. In this case, Section 365(d)(3) operated to help Touch of Grey because the Debtor filed the petition before rent was due and failed to reject the Lease until four days after the obligation arose. R. at 8. If the Debtor would have rejected the Lease just a week earlier, Section 365(d)(3) would provide no benefit to the landlord. Had the Debtor filed its petition after the rent obligation accrued, Section 365(d)(3) would have operated to deny Touch of Grey any administrative priority at all regardless of how long the Debtor stayed in possession.

The consequences of this interpretation can be heavy. *See, e.g.*, *In re Oreck Corp.*, 506 B.R. at 504. In *In re Oreck Corp*, the Lease stated that all rent was due and payable in advance of the first of each month. *Id*. The Debtor filed a Chapter 11 petition on May 6th. *Id.* At the petition date, the Debtor had not yet paid the Creditor for the May rent that accrued pre-petition on May 1st. *Id.* The Creditor sought to recover the prorated rent for the twenty-five days of May in which the Debtor occupied the premises as a debtor-in-possession. *Id.* However, because rent obligation arose before the petition, the *Oreck* court rejected the Creditor's entire administrative expense claim. *Id.*

Both the result in *Oreck* and the result here are compelled because unambiguous language binds everyone equally. *See In re Appletree Mkts. Inc.*, 139 B.R. 417 (Bankr. S.D. Tex. 1992) (applying the Billing Date approach despite concluding that the equities may have required a different result). If the *Oreck* landlords had been in the same position as Touch of Grey is here, they might have urged this Court to find Section 365(d)(3) to be clear and

unambiguous. *See In re The 1/2 off Card Shop,* Inc., No. 00-48425-WS, 2001 WL 1822419, at *3 (Bankr. E.D. Mich. Mar. 7, 2001) (noting that the Billing Date interpretation can "cut both ways"). Similarly, if the Debtor here would have been in the same position as the debtors in *Oreck*, it might have done the same as well. But either way, "parties cannot waive the flag of statutory ambiguity only when it suits them." *Id.*

At its core, the Billing Date approach effectuates the intent of Congress regardless of the way it cuts in any given case because it removes the cloud of uncertainty that formerly surrounded the post-petition prerejection window. *In re Oreck Corp.*, 506 B.R. at 504 (noting that the inequitable outcome reached under the statute was not offensive because it achieved the goals of the statute). This clarity benefits both the debtor and lessor because each knows when the obligation arises, and if they want to avoid that obligation, each knows when they would have to act in order to do so. *Id.*

3. The Billing Date interpretation puts the ball in the debtor's court.

Finally, the Trustee's equitable arguments to circumvent Section 365(d)(3)'s plain language fall flat considering that Section 365(d)(3) places the Debtor in control of its own fate. Congress granted debtors and trustees control over when leases are rejected and when voluntary bankruptcy petitions are filed. *See* 11 U.S.C. § 301; 11 U.S.C. § 365(a). Thus, when a debtor sits on its hands and waits to reject a lease until its monthly rent obligation accrues, equity, as well as the plain language of the statute, favors full payment to the creditor. *In re Koenig Sporting Goods, Inc.*, 203 F.3d at 989 (disagreeing that "policy considerations," "equity," and "common sense" compelled the adoption of the proration approach); *see also HA-LO Industries, Inc.*, 342 F.3d at 800 (concluding that equity favored full payment because the debtor elected to reject the lease one day after its monthly obligation accrued).

In this case, the Debtor rejected the lease a mere four days after its rent obligation came due. R. at 8. The Debtor's circumstances did not change over that four-day period. R. at 7. Nothing precluded the Debtor from rejecting the lease before May began, yet the Debtor waited until the first week of May to seek rejection. Imposing the costs of that delay on the Debtor is exactly what Congress intended by passing Section 365(d)(3). *See Krystal Co.*, 194 B.R. at 164.

In sum, the Thirteenth Circuit erred by interpreting Section 365(d)(3) to create a proration approach in the face of unambiguous language requiring otherwise. The Billing Date interpretation of Section 365(d)(3) fits perfectly with the statutory language and breathes life into a policy choice that Congress clearly intended to make. Congress's intent to bind trustees to the obligations arising under unexpired commercial leases forecloses any inquiry into whether or not that rule produces an equitable result in every case. As this Court has so often reminded us:

> [W]e do not sit to assess the relative merits of different approaches to various bankruptcy problems. It suffices that the natural reading of the text produces the result we announce. Achieving a better policy outcome—if what petitioner urges is that—is a task for Congress, not the courts.

Hartford Underwriters Ins. Co., 530 U.S. at 13.

CONCLUSION

In this case, Touch of Grey attempted to avail itself of three benefits that Congress plainly intended it to have. In each instance, the courts below denied Touch of Grey those benefits. But when Congress plainly bestows a benefit on a creditor in a Code provision, bankruptcy courts may not deny that benefit in the name of equity. For the reasons stated, this Court should reverse the decision of the Thirteenth Court of Appeals.