



## Circuit court allows post-petition attorney fees as unsecured claims

By Rob Coughlin, Erik Schneider and Patrick MacDonald

Joining the other U.S. Courts of Appeal that have ruled on the issue before, the United States Court of Appeals for the Fourth Circuit recently allowed a creditor's unsecured claim for attorneys' fees incurred after the filing of a bankruptcy petition where payment was provided for in a pre-petition contract.<sup>1</sup> This is an important decision that offers assuring news to indenture trustees, whose unsecured claims for post-petition fees and expenses have been challenged in various bankruptcy courts notwithstanding that their payment may be expressly provided for in the indenture. Indenture trustees should be aware that the question will also be heard by the Third Circuit in the coming months.

### Both lower courts disallowed unsecured claim for post-petition attorney's fees and expenses

SummitBridge National Investments III, LLC ("SummitBridge"), the holder of three secured promissory notes made by Ollie William Faison, the debtor in bankruptcy, appealed decisions by the Bankruptcy Court and the District Court for the Eastern District of North Carolina disallowing its unsecured claim for post-petition attorney's fees and expenses. SummitBridge was the assignee of the promissory notes, which were secured by sufficient collateral to cover the outstanding principal and pre-petition interest on the notes, as well as a portion of post-petition interest and attorney's fees. To the extent that it incurred post-petition attorney's fees in excess of the value of its collateral, SummitBridge filed an unsecured claim for recovery of those fees based on the terms of the promissory notes, which provided that the debtor agreed to pay "all costs of collection, including but not limited to reasonable attorneys' fees."

The debtor objected to SummitBridge's claim in the Bankruptcy Court, arguing that the Bankruptcy Code does not allow unsecured claims for post-petition attorney's fees or costs. The Bankruptcy Court agreed with the debtor's objection, and SummitBridge appealed the order to the

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<sup>1</sup> *SummitBridge National Investments III, LLC v. Ollie William Faison*, No. 17-2441, U.S.C.A. 4<sup>th</sup> Cir. (Decided February 8, 2019).

United States District Court, which affirmed the Bankruptcy Court's decision. SummitBridge then appealed to the Fourth Circuit.

## **The Fourth Circuit reverses**

The Fourth Circuit overruled both lower courts. Guided by the presumption articulated in the U.S. Supreme Court's 2007 decision in *Travelers Casualty & Surety Co. of America v. Pacific Gas & Electric Co.*, 549 U.S. 443 (2007) that "claims enforceable under applicable state law will be allowed in bankruptcy unless they are expressly disallowed,"<sup>2</sup> the Fourth Circuit rejected arguments by the debtor that § 502(b) and § 506(b) of the Bankruptcy Code bar creditors from asserting unsecured claims for post-petition attorneys' fees arising out of pre-petition contracts.

In its analysis, the Fourth Circuit rejected the debtor's argument that SummitBridge's "claim" as of the "date of the filing of the petition" was either nonexistent, or had to be viewed as zero, because the fees and expenses were incurred post-petition. The court disagreed, noting that "claim" is broadly defined under the Code and includes contingent rights to payment. "What matters is that the *right* to those fees arose pre-petition, when Faison signed the promissory notes in question."<sup>3</sup>

The court was also unconvinced by policy arguments raised by the debtor that only unsecured creditors, not secured (but under-secured) creditors like SummitBridge, should be allowed to assert unsecured claims for post-petition attorneys' fees, finding that the argument "has no basis in the text of the relevant Code provisions. What matters under § 502 and § 506(b) is the status of a given claim, not the status of the creditor asserting it."<sup>4</sup>

Having examined each challenge against the *Travelers* presumption that claims enforceable under state law are to be presumed allowable unless expressly disallowed in the Bankruptcy Code, the court concluded that there is no such express disallowance of unsecured claims for post-petition attorneys' fees arising out of pre-petition contracts. Invoking what it described as a basic principle of federal bankruptcy law "that state law governs the substance of claims, Congress having generally left the determination of property rights in the assets of a bankruptcy estate to state law," the court emphasized that allowing creditors, like SummitBridge, who have bargained specifically for attorneys' fees in pre-petition contracts enforceable under state law, is fully consistent with that principle.

## **Looking ahead**

A similar case is currently pending in front of the United States Court of Appeals for the Third Circuit, involving Tribune Media, as debtor, and the Indenture Trustee for a series of the debtor's unsecured subordinated notes.<sup>5</sup> In that case, the Delaware Bankruptcy Court disallowed the Indenture Trustee's counsel fees and expenses because it interpreted the omission of under-secured and unsecured attorney's fees and expenses from §506 to be an intentional decision by Congress to disallow such claims by unsecured creditors.<sup>6</sup>

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<sup>2</sup> *Travelers* at 452.

<sup>3</sup> *SummitBridge* at 8.

<sup>4</sup> *SummitBridge* at 15.

<sup>5</sup> *In re Tribune Media Company et al.*, No. 18-3793, U.S.C.A. 3<sup>rd</sup> Circuit (2019).

<sup>6</sup> *In re Tribune Media Company et al.*, No. 08-13141 (KJC), Bankr. Del. (Nov. 19, 2015).

These decisions highlight the importance of indenture trustee protective provisions in governing agreements. With each favorable decision, trustees gain further confidence that their claim for attorneys' fees and expenses incurred in connection with a debtor bankruptcy will be an allowed claim against the estate, so long as the proper protective language is included in the governing document.

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