

# BANKRUPTCY ALERT

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## SUPREME COURT RULING LIMITS CHARGES AGAINST LENDER'S COLLATERAL

On May 30, 2000, the U.S. Supreme Court ruled that only a bankruptcy trustee may surcharge a secured lender's collateral for the payment of administrative expenses. *Hartford Underwriters Insurance Company v. Union Planters Bank, N.A.*, 120 S. Ct. 1942 (2000). The decision limits charges against a lender's collateral for the reasonable, necessary costs and expenses of preserving or disposing of the lender's collateral during a bankruptcy case to those sought by the bankruptcy trustee, which also includes a Chapter 11 debtor in possession.

The *Hartford* case involved a debtor that owned and operated restaurants as a Chapter 11 debtor in possession. The debtor's case ultimately failed and resulted in a Chapter 7 liquidation. However, during the case's Chapter 11 administration, Hartford provided workers' compensation insurance on an unsecured basis. Upon conversion, the estate was administratively insolvent. As a result, Hartford sought to surcharge the lender's collateral, which included real and personal property where the restaurants were operated, in order to recoup the premiums it advanced to the debtor.

Despite Hartford's attempts to use proceeds from the sale of the lender's collateral to pay its unsecured claim, the Supreme Court denied Hartford's claim and ruled that only a trustee has authority to seek payment of its claim from a

lender's collateral based upon the plain language of Section 506(c), which provides that, "[t]he trustee may recover from property securing an allowed secured claim. . ." The Court found this language to be exclusive and not applicable to any other party in interest.

The result of the *Hartford* decision is that only a trustee or debtor in possession may attempt to surcharge a lender's collateral. This appears to be good news for secured lenders. However, what remains to be seen is whether this will be a disincentive to those wishing to do business with debtors in possession.

The Court's decision does not address the propriety of an unsecured creditor's demand on the debtor to seek a surcharge on collateral if the estate is administratively insolvent. A logical result of the *Hartford* decision would be for administrative claimants to begin demanding agreements to surcharge before providing goods and services to a debtor. From the lender's perspective, this would be tantamount to a postpetition financing without court approval. Whether such an agreement would be enforceable remains unanswered by the *Hartford* decision, but will no doubt be the subject of further discussion and possible court challenge.

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