

Is It Fair to Allow New Value Credit for Section 503(b)(9) Invoices?

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In the recent case of *Guiliano v. Mitsubishi Digital Electronics America*, Adv. No. 11-52663(MFW) (Bankr. D. Del. May 1, 2012), the Bankruptcy Court was asked to decide whether a creditor is able to receive full payment on Section 503(b)(9) invoices and use those same invoices as "new value" in the defense of a preference action. The trustee argued that if Mitsubishi's 503(b)(9) administrative claim was not disallowed by Section 502(d), then Mitsubishi would be "double-dipping." While the court passed upon the opportunity to opine upon this issue, it is an interesting one and bears some analysis.

Under Delaware bankruptcy precedent, if such double-dipping is to be prevented, it will not be pursuant to Section 502(d). Generally speaking, Section 502(d) dictates that an entity's claim will be disallowed until the claimant pays the bankruptcy estate for any preference liability. A debtor or trustee can use Section 502(d) to seek disallowance of prepetition claims and a few specifically referenced post-petition claims, but not administrative claims. A Section 503(b)(9) claim is a prepetition claim to the extent that it is a claim for any goods received by the debtor within 20 days before the bankruptcy filing, but it is also given administrative claim priority, thereby excluding it from the reach of Section 502(d).

At least one court outside of Delaware has held that the payment of a 503(b)(9) administrative claim is an "otherwise unavoidable transfer" and, therefore, the underlying invoices cannot be used as new value. See *Circuit City Stores v. Mitsubishi Digital Elec. America*, (In re Circuit City Stores), Adv. Pro. No. 10-3068 (KRH), 2010 Bankr. LEXIS 4398 (E.D. Va. Nov. 30, 2010). Section 547(c)(4) of the Bankruptcy Code sets forth the new-value defense to a preference action. Under that section, in order to assert the defense, a claimant must have provided new value (goods or services on credit) to the debtor after an alleged preferential payment and that new value must not have been paid by an "otherwise unavoidable transfer."

In *Circuit City*, the court examined the applicable avoidance provisions of the Bankruptcy Code and found that none could be used to avoid the payment of the 503(b)(9) claim. Accordingly, the payment of the invoices subject to the 503(b)(9) claim could not be used as new value because the payment of such invoices was an "otherwise unavoidable transfer." The court did not find it significant that the 503(b)(9) claim had not yet been paid by the debtor, because a reserve account had been established to pay the claim in full once the issue before the court was decided.

Has Judge Christopher S. Sontchi already addressed this issue in *Friedman's Inc. v. Roth Staffing Companies*, (In re Friedman's Inc.), Adv. No. 09-50364 (CSS), 2011 Bankr. LEXIS 4500 (Bankr. D. Del. Nov. 30, 2011)? Close enough. In *Friedman's*, the court addressed whether prepetition invoices could be used as new value when most of the invoices had been paid post-petition pursuant to an order allowing payments to critical vendors. The judge held that the filing of the bankruptcy petition "fixes" the analysis of preference liability as of the petition date. Specifically, "neither the post-petition provision of new value by the creditor nor the post-petition payment of unpaid, prepetition new value affects the preference calculation." Whether

the creditor had been paid was not of consequence; only when it had been paid. In this author's humble opinion, Sontchi got it right.

The purpose of Section 503(b)(9) and the new-value defense is to encourage vendors to continue to deal with a debtor as it slides into bankruptcy. When you are dealing with a creditor extending credit to a debtor 20 days before the filing, the creditor either has no idea that the bankruptcy is coming or knows that it is and is continuing to deal with the debtor by choice. Under either scenario, the creditor isn't operating with dubious intent. So, it may just be that I represent more preference defendants than plaintiffs, but I think it's perfectly fair to allow such creditors to "double-dip."

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