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**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF KANSAS**

In re:

**CONVEYOR TECHNOLOGY GROUP,
INC.,**

DEBTOR.

**CASE NO. 02-22743-7C
CHAPTER 7**

**ORDER DETERMINING THAT FORMER DEBTOR-IN-POSSESSION
HAS STANDING TO SEEK TO SURCHARGE COLLATERAL
UNDER 11 U.S.C.A. § 506(C)**

This matter was before the Court on December 19, 2003, on the debtor's motion to surcharge certain administrative expenses against sale proceeds pursuant to 11 U.S.C.A. § 506(c). Creditors Bank of Belton, Hibernia Capital Corporation, and E.S. Bankest, LC, through a court-appointed receiver, objected to the motion. At the hearing, the debtor appeared by counsel Carl R. Clark of Lentz & Clark, P.A. The Bank of Belton appeared by counsel Eric Johnson of Spencer Fane Britt & Browne LLP. Hibernia appeared by counsel Gene A. DeLeve of Berman, DeLeve, Kuchan & Chapman, L.C. The receiver for creditor E.S. Bankest, LC, appeared by counsel Gregory Garno. Case trustee Eric C. Rajala appeared pro se. During the hearing, the Court announced its decision that the debtor still had standing to pursue its motion despite the conversion of this case from Chapter 11 to Chapter 7. The Court is issuing this order now to reduce that ruling to writing and to provide a more detailed explanation of the Court's reasoning.

FACTS

Conveyor Technology Group, Inc., filed a Chapter 11 bankruptcy case in August 2002. In November 2002, the Court approved the debtor's motion to hire Equity Partners, Inc. (hereinafter EPI), as a broker to help sell the debtor's assets, or to help with other reorganization efforts. In January 2003, the debtor applied for permission to sell substantially all its assets at auction, free and clear of liens and encumbrances, pursuant to § 363 of the Bankruptcy Code, with each lien to attach to the proceeds of the sale of the assets subject to the lien. The application stated that the debtor would place all sales proceeds in an account pending further order of the Court, but also said that EPI would be paid for its services immediately on the conclusion of any sales.

EPI marketed the debtor's assets for sale at auction in March 2003. The assets were divided into eight groups for the auction, but only five of the groups drew bids that were accepted. Bank of Belton bought the debtor's real estate (usually referred to as "Parcel A" in the pleadings) with a credit bid of \$625,000. Three groups of office, shop fabrication, and field installation equipment (usually referred to as "Parcels B, C, and D") were sold for \$240,000. A group of proprietary products and patents (usually referred to as "Parcel E") was sold for \$500,000. The groups that were not sold were: (1) one ("Parcel F") of patents and other items related to the "Rabbit System," (2) another ("Parcel G") of patents and other items related to the "Tow Bar Shock Absorber," and (3) a final group ("Parcel H") of miscellaneous inventory not included in any of the other groups. The Court has not been informed whether these last three groups were later sold or otherwise disposed of.

Two days after the auction, without formally moving for approval of the sales, the debtor submitted orders approving the sales at the prices mentioned, and Judge Flannagan (who has since retired) signed them. Each order indicated that the sale it covered would close some time after entry of the order. One order approved the sale of the three equipment groups, and a second order approved the sale of the group of proprietary products and patents for \$500,000. A third order approved the sale of the real estate to a third party if it met certain requirements by the day before the order was signed (which it did not do), but otherwise to Bank of Belton for its credit bid. This order provided that the bank would credit its secured claim against the real estate for the amount of its bid minus real estate taxes to the date of closing, which it was to pay. The first two orders also authorized the debtor to pay fees to EPI from the sale proceeds.

On August 19, 2003, counsel filed the debtor's motion, pursuant to § 506(c), to surcharge certain administrative expenses against the proceeds of the March auctions, and amended it the next day to add another expense. The amended motion seeks \$74,193.04 in employee wages, \$2,000 to reimburse a woman who paid for insurance on the debtor's property pending the sales, \$22,849.55 in fees and expenses for the debtor's counsel, and \$3,510.75 in fees and expenses for the Unsecured Creditors Committee's counsel, a total of \$102,553.34. The case was converted to Chapter 7 on August 22. As indicated, Hibernia, the Bank of Belton, and the receiver for E.S. Bankest, LC, all objected to the surcharge motion. Among other things, they raised the preliminary question of the debtor's

standing to seek to surcharge their collateral in light of the termination of the debtor's status as a debtor-in-possession on conversion of the case.

Disputes also arose about the debtor's plans to pay EPI's fees, and the Court held a hearing on the surcharge motion and the EPI disputes on November 19. The Court gave the parties time to submit any additional authorities they might wish to on the question of the debtor's standing to seek to surcharge the secured creditors' collateral under § 506(c). Only the debtor and Hibernia submitted further support for their positions on that question.

DISCUSSION AND CONCLUSIONS

Section 506(c) of the Bankruptcy Code provides: "The trustee may recover from property securing an allowed secured claim the reasonable, necessary costs and expenses of preserving, or disposing of, such property to the extent of any benefit to the holder of such claim." In *Hartford Underwriters Inc. Co. v. Union Planters Bank, N.A.*,¹ the United States Supreme Court considered whether an insurance company that did not know its customer was a Chapter 11 debtor and had provided the debtor with workers' compensation coverage despite the debtor's failure to make all the required payments could apply to surcharge collateral under this provision after the bankruptcy case was converted to Chapter 7. The Court ruled that the insurance company could not invoke § 506(c).² Hibernia and the Bank of Belton contend the *Hartford* decision bars the debtor's attempt to invoke the provision here, while the debtor argues that the case is factually distinguishable because the

¹530 U.S. 1 (2000).

²530 U.S. at 4-14.

motion there was filed after the case was converted while the debtor filed the present motion before conversion.

This Court agrees with the debtor that *Hartford* is distinguishable from this case but for a somewhat different reason. The insurance company in *Hartford* not only was not the Chapter 7 trustee but had also never been the Chapter 11 debtor-in-possession. The Supreme Court pointed out in a footnote that § 1107 authorizes debtors-in-possession to use § 506(c) by giving them the rights and powers of a trustee.³ In this case, the debtor clearly was authorized to invoke § 506(c) at the time expenses connected with the March 2003 sales were being incurred. The parties have not cited, and the Court has not found, any case concerning a debtor's attempt as the former debtor-in-possession to surcharge collateral.

The Court is convinced that the debtor has standing to bring the surcharge motion in this case. The expenses were all incurred and the collateral sought to be surcharged was sold while the debtor was the debtor-in-possession. Indeed, given the five months that passed from the time the auction took place until the case was converted, the debtor's motion might, if filed quickly, have been resolved before the conversion. While § 348(e) provides that conversion "terminates the service of any trustee" serving in the case before conversion, nothing in the section suggests that conversion automatically undoes anything that the debtor did while it was exercising its debtor-in-possession powers as trustee. Of

³530 U.S. at 6, n. 3.

course, this provision would preclude the debtor from seeking to surcharge collateral for activities performed after conversion, but that is not what is happening here. Absent controlling authority to the contrary, the Court believes it is fair to allow the debtor to pursue its surcharge motion now.

The parties should recognize that the Court does not mean to suggest that it has already decided that the claimed expenses are recoverable under § 506(c), only that it has decided the debtor still has standing to pursue the motion. The creditors' objections to the debtor's standing to bring the § 506(c) motion are hereby denied.

IT IS SO ORDERED.

Dated at Topeka, Kansas, this _____ day of June, 2004.

DALE L. SOMERS
BANKRUPTCY JUDGE

CERTIFICATE OF SERVICE

The undersigned hereby certifies that true and correct copies of the above **ORDER DETERMINING THAT FORMER DEBTOR-IN-POSSESSION HAS STANDING TO SEEK SURCHARGE COLLATERAL UNDER 11 U.S.C.A. § 506(C)** were mailed via regular U.S. mail, postage prepaid, on the _____ day of June, 2004, to the following:

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