

# **Opportunities for Creditors to Recover Postpetition Attorney's Fees in Bankruptcy**

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37th Annual Seminar of the Commercial Law & Bankruptcy Section of the Idaho State Bar  
Burley, Idaho

February 8, 2019

Starting Points:

American Rule. In federal courts, attorney's fees ordinarily are not recoverable by the prevailing party in an action except by contract or statute. *Baker Botts L.L.P. v. Asarco LLC*, 576 U.S. \_\_\_\_\_, 135 S. Ct. 2158 (2015); *Alyeska Pipeline Serv. Co. v. Wilderness Soc'y*, 421 U.S. 240, 257 (1975).

Bankruptcy Rule. There is no general right to recover attorney's fees under the Bankruptcy Code. *Heritage Ford v. Baroff (In re Baroff)*, 105 F.3d 439, 441 (9th Cir. 1997).

## **I. To Obtain a Fee Award, the Creditor Must Request Fees, and Articulate the Basis of the Request.**

It should go without saying that in order for a creditor to recover its fees, the creditor must request fees, and identify the law that supports the request for fees. Absent such a request, the court cannot award fees. So, for example, the plaintiffs in *Murray v. Woodman (In re Woodman)*, 451 B.R. 31 (Bankr. D. Idaho 2011) prevailed in an adversary proceeding against the married debtors. The court held that the creditors' claims were, in fact, nondischargeable.

The prevailing plaintiffs requested an attorney's fee award against the debtors. However, the plaintiffs failed to identify the basis for their request. The court denied the request, holding that "[i]n Idaho, a party claiming attorney's fees must assert the specific statute, rule or case authority supporting its claim." *Woodman*, 451 B.R. at 44. Although the court in *Woodman* did not address in dicta whether the plaintiffs would have recovered their fees had they asserted a valid claim, it appears that they would, in fact, have been awarded fees.

Presumably the vast majority of creditors' claims for postpetition fees in the Idaho bankruptcy court will be premised on the parties' contract, or on the fact that the gravamen of the parties' dispute involved a commercial transaction, entitling the creditor to fees under I.C. § 12-120(3).

## **II. Oversecured Creditors are Entitled to Recover Their Reasonable Postpetition Attorney's Fees as Part of their Secured Claim to the Extent They are Oversecured, if The Claim is Allowable under Contract or State Law.**

11 U.S. Code § 506, entitled "Determination of secured status," provides as follows:

(b) To the extent that an allowed secured claim is secured by property the value of which, after any recovery under subsection (c) of this section, is greater than the amount of such claim, there shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs, or charges provided for under the agreement or State statute under which such claim arose.

"Claim" is used as defined in 11 U.S.C. § 101(5).

The language of section 506(b) is clear. The creditor is entitled to attorney's fees if (1) the claim is an allowed secured claim; (2) the creditor is oversecured; and (3) the fees are reasonable; and (4) the fees are provided for under the agreement or state statute.<sup>1</sup> *In re Hart Creek Ranch, LLC*, 2012 WL 2871720, at \* 3 (Bankr. D. Idaho July 12, 2012) (citing *Kord Enters. II v. Cal. Commerce Bank (In re Kord Enters. II)*), 139 F.3d 684, 687 (9th Cir. 1998).

An oversecured creditor's postpetition attorney's fees are typically quantified in one of two ways. First, the debtor's plan of reorganization can provide for the allowance of the fee request as part of the plan's treatment of the secured creditor's claim.

Alternatively, the parties can engage in a contested matter addressing the amount of attorney's fees included within the allowed secured claim. *See, e.g., Kord Enters.*, 139 F.3d at 686; *In re Smith*, 2016 WL 7496104 (Bankr. D. Idaho Dec. 30, 2016); *Hart Creek Ranch*, at \* 2. In *Smith* and *Hart Creek Ranch*, the creditor filed an amended claim including all of its postpetition attorney's fees.

In *Hart Creek Ranch*, part of the secured creditor's fees were incurred in unsuccessfully prosecuting a motion to convert the chapter 11 case to chapter 7. The fees incurred in this effort formed part of the Court's award of attorney's fees, thereby showing that an oversecured creditor's claim for fees under the agreement do not become disallowable merely because the creditor did not prevail. In other words, section 506(b) does not incorporate a "prevailing party" test. Nonetheless, "where services are not reasonably necessary or where action is taken because of an attorney's excessive caution or overzealous advocacy, courts have the right and the duty, in the exercise of their discretion, to disallow fees . . . under § 506(b)." *Hart Creek Ranch* at \*5 (quoting *In re Lauderville*, 2012 WL 78713, at \*3 (Bankr. D. Mont. Jan. 11, 2012)).

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<sup>1</sup> The words "or State statute" were added to section 506(b) in 2005. *See generally In re Astle*, 364 B.R. 735, 739-41 (Bankr. D. Idaho 2007).

In determining the amount of a reasonable fee under section 506(b), federal law controls. *Hart Creek Ranch*, at \*4. The creditor bears the burden of establishing the reasonableness of the fees. *In re Staggie*, 255 B.R. 40, 52 (Bankr. D. Idaho 2000).<sup>2</sup>

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<sup>2</sup> The factors that govern the determination of the reasonableness of a particular fee are beyond the scope of this article.

### **III. Unsecured Creditors are Entitled to Recover Their Reasonable Postpetition Attorney's Fees if Allowable Under Contract or State Law.**

Under Ninth Circuit law, “[w]hen a bankruptcy court adjudicates a dispute arising from a contract claim, it must apply state law unless the bankruptcy code provides otherwise.” *Rubenstein v. Ball Bros., Inc. (In re New England Fish Co.)*, 749 F.2d 1277, 1280 (9th Cir. 1984). In particular, the court has instructed that state law governs a party’s right to recover attorney’s fees in bankruptcy litigation if state law, and not federal bankruptcy law, provides the rule of decision in the action. *Krommenhoek v. A-Mark Precious Metals, Inc. (In re Bybee)*, 945 F.2d 309, 315 (9th Cir. 1991).

However, pursuant the so-called *Fobian* rule, the creditor was not entitled to its attorney’s fees if the substance of the parties’ dispute was governed by bankruptcy law.

Where a contract or statute provides for an award of attorneys’ fees, a creditor may be entitled to such fees in bankruptcy proceeding. Such an award is governed by state law. However, where the litigated issues involve not basic contract enforcement questions, but issues peculiar to federal bankruptcy law, attorney’s fees will not be awarded absent bad faith or harassment by the losing party.

*Fobian v. W. Farm Credit Bank*, 951 F.2d 1149, 1153 (9th Cir. 1991) (citations omitted).

In *Travelers Cas. & Sur. Co. v. Pacific Gas & Elec. Co.*, 549 U.S. 443 (2007), the Supreme Court overruled *Fobian*. The Supreme Court concluded that there was no statutory basis to the *Fobian* rule: “the Code says *nothing* about unsecured claims for contractual attorney’s fees incurred while litigating issues of bankruptcy law.” 549 U.S. at 453 (emphasis in original). The court also noted, but declined to explore, the question of whether an unsecured creditor’s claim for attorney’s fees was to be disallowed under section 506(b) by implication. The Supreme Court made this decision on the grounds that the issue had not been raised in the lower courts.

The Ninth Circuit’s principal response to *Travelers* is found in *Infonet Mgmt. v. Centre Ins. Co. (In re SNTL Corp.)*, 571 F.3d 826 (9th Cir. 2009). In *SNTL*, the Ninth Circuit simply adopted the 9th Circuit BAP opinion which had been entered below. 380 B.R. 904 (9th Cir. BAP 2007). The Ninth Circuit held that section 506(b) has no relevance insofar as the allowance of attorney’s fees to an unsecured creditor is concerned. In other words, the fact that a secured creditor is entitled to its postpetition attorney’s fees under section 506(b) does not mean that an unsecured creditor is not entitled to his postpetition attorney’s fees. The allowability of an unsecured creditor’s postpetition attorney’s fees is subject to section 502, not 506. *SNTL* held that to the extent that the creditor had a right to attorney’s fees under state law or the contract, the creditor was entitled to recover its postpetition attorney’s fees. The court also made clear that the claim for postpetition attorney’s fees was part of the creditor’s prepetition claim, not a postpetition (administrative) claim.

#### IV. Attorney's Fees in Stay Relief Litigation

A secured creditor does not waive its right to recover attorney's fees under section 506(b) merely by failing to include a request for fees in the stay relief motion itself. *In re Rupert*, 2004 WL 4960311 (Bankr. D. Idaho Dec. 23, 2004).

*Rupert* held that oversecured creditors' rights to recover attorney's fees for prosecuting a stay relief motion are governed by section 506(b). Thus, where, in *Rupert*, the creditor had the right to recover its attorney's fees under contract in the event of bankruptcy, the reasonable attorney's fees incurred by the secured creditor in prosecuting its stay relief motions was part of its allowed secured claim. Moreover, the fact that the creditors filed four unsuccessful motions did not mean that its fees were unreasonable.

The fact that the *Rupert* creditor prevailed, however, does not mean that every oversecured creditor will succeed in including its attorney's fees in prosecuting a stay relief motion as part of its allowed claim. The secured creditors in *In re Lopez*, 349 B.R. 671, 679-80 (Bankr. D. Idaho 2006) did not recover its fees. The distinction between the *Rupert* creditor and the *Lopez* creditors was that the former had the benefit of an express provision in her note covering fees in a bankruptcy case while the latter did not. In *Lopez*, the court held that a more general clause awarding the lender fees "in case of suit hereon or foreclosure," did not entitle the creditor to fees for moving for stay relief or moving to dismiss.

This author has been unable to locate an Idaho case examining whether a creditor other than an oversecured creditor can recover its attorney's fees for prosecuting a stay relief motion. That is, this author has been unable to locate an Idaho case addressing whether an undersecured or unsecured creditor's claim for postpetition fees incurred in litigating a stay relief motion are allowable under section 502.

In *Johnson v. Reghetti (In re Johnson)*, 756 F.2d 738 (9th Cir. 1985) the Ninth Circuit held generally that attorney's fees could not be awarded incurred in a stay relief contested matter. In *Johnson*, the chapter 11 debtors defeated the creditor's stay relief motion. The debtors sought to recover fees. The court denied the debtors' fee request. The basis of the court's decision was that a contested stay relief motion was a summary bankruptcy proceeding, which was neither an action "on the contract" nor an action under state law. The court held that: "the state law governing contractual relationships is not considered in stay litigation." 756 F.2d at 740.

*Green Tree Servicing LLC v. Giusto*, 553 B.R. 558 (N.D. Cal. 2016) held that *Johnson* remained good law notwithstanding *Travelers*. *Green Tree*, like *Johnson*, held that a debtor who prevailed on a stay relief motion could not recover its attorney's fees in defeating the stay relief motion because the note's provision for fees did not apply since the contested matter was not related to the enforceability of the note.

*Rupert* and *Johnson/Green Tree*, then, potentially seem contrary to one another, in that one allows fees for stay relief motions and the other does not. One distinction, clearly, is the fact that it was the secured creditor seeking fees in *Rupert* and it was the debtors seeking fees in *Johnson* and *Green Tree*. Another important distinction is that *Rupert* is a section 506(b) case while *Johnson* and *Green Tree* rely on neither section 506(b) nor 502.

It would certainly be anomalous if the creditor were entitled to fees for unsuccessfully prosecuting a stay relief motion per the rule of *Rupert* and the debtor/trustee were entitled to fees for successfully prosecuting a defense to the stay relief motion on the grounds of the contract or state law because it was the prevailing party. In that context, perhaps *Johnson/Green Tree* is the right result.

Resolution to this issue apparently awaits further developments.

**V. The Non-Debtor Party to an Executory Contract is Entitled to Recover Its Postpetition Attorney's Fees as Part of the Debtor's Cure, to the Extent Available Under the Contract or State Law.**

The non-debtor party to an executory contract is entitled to recover its attorney's fees as part of the debtor's assumption, if the creditor is entitled to recover its fees either under the terms of the contract or under state law. *See In re Shangra-La, Inc.*, 167 F.3d 834, 849 (4th Cir. 1999) (cure under section 365(b)(1)(B) must include attorney's fees when the fees are allowable under the terms of the lease or under state law); *Lacey v. Westside Print Works, Inc. (In re Westside Print Works, Inc.)*, 180 B.R. 557, 564 (9th Cir. BAP 1995) (same); *In re Sterling Mining Co.*, 2009WL 2589401, at \*8. n.37 (Bankr. D. Idaho Aug, 21, 2009).



## **VI. The Non-Debtor Defendant in An Adversary Proceeding is Entitled to Its Attorney's Fees Incurred in the Adversary Proceeding, if Allowable Under State Law.**

If the trustee sues a non-debtor party in an adversary proceeding, and the non-debtor party prevails, it is entitled to recover its attorney's fees if such fees would be awarded under state law, either pursuant to the contract or under I.C. § 12-120(3). *Hopkins v. Saratoga Holdings, LLC (In re Colvin)*, 2008 WL 1957855 (Bankr. D. Idaho 2008).

In *Colvin*, the trustee brought an adversary proceeding to recover on a contract claim against three non-debtors. The non-debtors were apparently not creditors of the estate. The trustee lost; the non-debtors prevailed. The court awarded the defendants their reasonable attorney's fees under I.C. § 12-120(3). The court did not award the defendants their attorney's fees under the contract because the contract contained no attorney's fee provision. All indications from the opinion are that the attorney's fee award would be entitled to administrative expense priority.

Similarly, if the debtor sues a non-debtor party in post-petition litigation, and the non-debtor party prevails, the non-debtor party is entitled to attorney's fees if allowable under state law. *Beach v. Wells Fargo Bank, N.A.*, 2011 WL 4963003 (Bankr. D. Idaho Oct. 19, 2011).

In *Beach*, the plaintiffs were the chapter 7 debtors. They sued the defendant after the petition was filed for violating the federal Truth in Lending Act and the Idaho consumer protection act. The defendant removed the case to the bankruptcy court, and ultimately prevailed.

The court awarded the defendant its fees under the terms of the parties' loan documents. As in *Colvin*, the *Beach* court suggested that the defendant's fee claim would be a postpetition, not a prepetition, claim. Nonetheless, the bankruptcy court held that it would not enter orders enforcing the defendant's recovery of the fee claim against the debtors. 2011 WL 4963003, n.26. The basis of that ruling was not clear.

*Beach* raises by implication, but does not expressly address, the question of whether a party who wins a lawsuit with debtor, and then obtains an award of fees, holds a prepetition claim subject to discharge or a postpetition claim that is not subject to the discharge injunction. The leading cases appear to be *Boeing North Am., Inc. v. Ybarra (In re Ybarra)*, 424 F.3d 1018 (9th Cir. 2005) and *Siegel v. Fed. Home Loan Mortg. Corp.*, 143 F.3d 525 (9th Cir. 1998). Those cases hold that where the debtor voluntarily commences the litigation postpetition, or where the debtor "return[s] to the fray" on a postpetition basis to continue prepetition litigation, the non-debtor party is entitled to recover its postpetition costs and fees from the debtor regardless of the discharge. In *Ybarra*, the debtor had commenced litigation against her former employer prepetition. After she filed her chapter 7 bankruptcy petition, she wrestled the cause of action away from the trustee pursuant to an exemption, and refused a settlement offer. The Ninth Circuit held that Ybarra had "returned to the fray," and, accordingly, the former employer's postpetition attorney's fees were not subject to the debtor's discharge. *But see High Country Bed & Breakfast, Inc. v. Amresco Independence Funding, Inc. (In re High Country Bed & Breakfast*,

*Inc.*), 02.2 I.B.C.R. 89 (Bankr. D. Idaho May 13, 2002) (denying administrative expense claim treatment to defendant's fees incurred in adversary proceeding regarding prepetition contract).

Another Ninth Circuit case distinguishes *Ybarra*. *Picerne Constr. Corp. v. Castellino Villas, A.K.F., LLC* (*In re Castellino Villas, A.K.F., LLC*), 836 F.3d 1028 (9th Cir. 2016). In *Castellino Villas*, the creditor and the chapter 11 debtor litigated, postpetition, the creditor's prepetition mechanic's lien claim. The creditor prevailed. The creditor then sought administrative expense treatment for its attorney's fees. The bankruptcy court found in favor of the debtor, holding that the creditor's fee claim was a prepetition claim. The district court and the Ninth Circuit affirmed. The courts held that under the circuit's "fair contemplation" test, it could be reasonably contemplated as of the petition date that the creditor had a contingent claim for attorney's fees, thus mandating treatment as a prepetition claim.

## **VII. The Non-Debtor Plaintiff in Dischargeability Litigation is Entitled to Recover its Attorney's Fees from the Debtor, if Allowable Under State Law.**

While *Fobian* was good law, the non-debtor plaintiff in dischargeability litigation was not entitled to recover its attorney's fees when it prevailed in the adversary proceeding. *Jenkins v. Sroufe (In re Sroufe)*, 261 B.R. 35 (Bankr. D. Idaho 2001); *Idaho First Nat'l Bank v. LeMaster (In re LeMaster)*, 147 B.R. 52 (Bankr. D. Idaho 1992).

After *Travelers* overruled *Fobian*, the law changed. After *Fobian*, "the inquiry must be whether the creditor plaintiff would be entitled to fees in state court for establishing those elements of the claim which the bankruptcy court finds support a conclusion of nondischargeability." *Kilborn v. Haun (In re Haun)*, 396 B.R. 522, 528 (Bankr. D. Idaho 2008) (citing *Cohen v. de la Cruz*, 523 U.S. 213 (1998)).

Thus, in *Haun*, Judge Myers examined whether the litigation involved a contract that was commercial in nature within the meaning of I.C. 12-120(3). In *Haun*, the court held that the contract at issue was a commercial contract. Accordingly, the court awarded the creditor his attorney's fees against the debtor. 396 B.R. at 531. See also *Johnson v. Hunt (In re Hunt)*, 2009 WL 2169884 (Bankr. D. Idaho Jul. 15, 2009) (where contract that was the basis of the plaintiff's nondischargeability claim constituted a commercial transaction, court awards prevailing plaintiffs their attorney's fees against the debtor).<sup>3</sup>

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<sup>3</sup> Presumably where the debtor prevails in the nondischargeability litigation, she would be able to recover her attorney's fees from the losing plaintiff, if the gravamen of the lawsuit was a commercial transaction within the meaning of I.C. § 12-120(3). Query what would happen were the creditor to prevail in the sense that it recovered a money judgment, but the debtor were to prevail in the sense that the claim were deemed to be dischargeable. Presumably the court would hold that neither party prevailed and award fees to neither litigant.

## VIII. A Creditor Can Recover Its Attorney's Fees as Administrative Expense in Some Circumstances.

Section 503 of the Bankruptcy Code provides as follows:

- (b) After notice and a hearing, there shall be allowed administrative expenses,  
... including  
...
  - (3) the actual, necessary expenses, other than compensation and reimbursement specified in paragraph (4) of this subsection, incurred by—
    - (A) a creditor that files a petition under [section 303 of this title](#);
    - (B) a creditor that recovers, after the court's approval, for the benefit of the estate any property transferred or concealed by the debtor;
    - (C) a creditor in connection with the prosecution of a criminal offense relating to the case or to the business or property of the debtor;
    - (D) a creditor, ... in making a substantial contribution in a case under chapter 9 or 11 of this title;
  - ...
    - (4) reasonable compensation for professional services rendered by an attorney ... of an entity whose expense is allowable under subparagraph (A), (B), (C), (D), or (E) of paragraph (3) of this subsection, based on the time, the nature, the extent, and the value of such services, and the cost of comparable services other than in a case under this title, and reimbursement for actual, necessary expenses incurred by such attorney ...;

This provision allows a creditor to prove an administrative expense claim against the estate in the amount of its expenses, including attorney's fees, when the creditor makes certain types of contributions to the bankruptcy case. Of course, an administrative expense claim is a postpetition claim entitled to priority treatment under section 507.

The burden of proving entitlement to benefit of an administrative expenses is on the claimant. *Einstein/Noah Bagel Corp. v. Smith (In re BCW West, L.P.)*, 319 F.3d 1166, 1172 (9th Cir. 2003); *In re Korn*, 352 B.R. 228, 240 (Bankr. D. Idaho 2006).

Petitioning creditors can recover their attorney's fees if they file the petition and an order for relief is entered on the basis of their petition. Bankruptcy Code §§ 503(b)(3)(A), 503(b)(4).

Creditors can recover their attorney's fees from the estate if they make a "substantial contribution" to a chapter 9 or chapter 11 case. Bankruptcy Code §§ 503(b)(3)(A), 503(b)(4).

The principal test of a substantial contribution to the reorganization is the "extent of the benefit to the estate." *Cellular 101, Inc. v. Channel Commc'ns, Inc. (In re Cellular 101, Inc.)*, *Christian Life Ctr. Litig. Def. Comm v. Silva (In re Christian Life Ctr.)*, 821 F.2d 1370, 1373 (9th Cir. 1987). The benefits conferred by the claimant must be direct and not "incidental" or "minimal," and must outweigh the benefits received by the claimant. Further, the claimant's actions must foster, rather than retard, progress of the reorganization. *Cellular 101*, 377 F.3d at 1096-98.

A strict reading of sections 503(b)(3) and (4) would require that a party could recover attorney's fees under subsection (4) only if the party also recovered other expenses under subsection (3). The Ninth Circuit Bankruptcy Appellate Panel has rejected that reading as "absurd." *North Sports, Inc. v. Knupfer (In re Wind 'n Wave)*, 328 B.R. 176, 182 (9th Cir. BAP 2005). Accordingly, a party can recover its attorney's fees under section 503(b)(4) even if that is the only expense it has incurred. *Id.*

## **IX. Fees Can Be Awarded as Sanctions.**

In *In re Frantz*, 2016 WL 4581405 (D. Idaho Aug. 31, 2016), the district court affirmed an award of sanctions to a creditor in the amount of \$49,000 against debtor and debtor's counsel. In *Frantz*, the bankruptcy court awarded sanctions under its inherent power to do so pursuant to section 105(a) of the Bankruptcy Code. The court can also enter a sanctions award against a debtor under Bankruptcy Rule 9011. *Wallace v. Hayes (In re Wallace)*, 2013 WL 782721 (Bankr. D. Idaho Feb. 27, 2013).

## **X. Fees Can Be Awarded in Claim Objection Proceedings.**

When an unsecured creditor is entitled to its attorney's fees pursuant to the contract or state law, it can recover postpetition attorney's fees as part of its allowed unsecured claim. *Infonet Mgmt. v. Centre Ins. Co. (In re SNTL Corp.)*, 571 F.3d 826 (9th Cir. 2009). Surprisingly, the author was unable to find an Idaho case, but an unsecured creditor should be entitled to recover its attorney's fees incurred in a claim objection proceeding, if the creditor has a valid claim for fees under the parties' contract or under I.C. § 12-120(3). *See generally In re Canyon Mgmt., LLC*, 2015 WL 435049 (Bankr. D. Idaho Feb. 2, 2015) (declining to award the prevailing creditor fees incurred in a claim objection proceeding, but seemingly acknowledging that an unsecured creditor would have the right to recover attorney's fees in a claim objection proceeding where a right to fees would exist under I.C. § 12-120(3)); *In re West One Mineral, Inc.*, 96.1 I.B.C.R. (Bankr. D. Idaho 1996) (same).

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