IN THE UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF ARKANSAS
WESTERN DIVISION

IN RE: WHITE ROCK, INC.,

Debtor.

CASE NO. 01-44553M
CHAPTER 11

ORDER

On August 13, 2001, White Rock, Inc. ("Debtor") filed a voluntary petition for relief under the provisions of chapter 11 of the United States Bankruptcy Code and has since been operating as a debtor-in-possession.

On December 11, 2001, Metropolitan National Bank ("Metropolitan") filed a request to have allowed an administrative claim in the sum of $68,122.97 as attorney's fees and $59,397.00 as security expenses pursuant to 11 U.S.C. § 503(b).[1]

The Debtor filed an objection to the application, and a hearing on the matter was conducted on February 13, 2002, at Little Rock, Arkansas. When the hearing was concluded, the Court took the matter under advisement.

[1]The security expense was amended to the sum of $97,197.00.

The matter is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A), and the Court has jurisdiction to enter a final judgment.

In the application before the Court, Metropolitan contends that it should be allowed as administrative expense its legal fees of $68,122.97 incurred in defending against the Debtor's claim of a leasehold interest in the bank's real property. Metropolitan also requests administrative expense for its out-of-pocket costs of $97,197.00 paid to security services to protect Metropolitan's real property located adjacent to the property occupied by the Debtor.

The following facts are relevant as background. At the commencement of the case, the Debtor claimed a leasehold interest in a tract of land acquired by Metropolitan in a foreclosure suit. The tract was surrounded by or adjacent to other real property acquired in foreclosure by Metropolitan from entities related to the Debtor. The Debtor was in possession of the tract at the time the case was filed and had been in possession for a considerable period pre-petition pursuant to an arrangement with an affiliated company to which the Debtor intermittently paid rent.

From the outset of the case, Metropolitan has claimed no leasehold interest ever existed or that the Debtor's leasehold interest had been previously foreclosed. The Debtor sought and

received a preliminary injunction filed August 28, 2001, allowing it access to its bagging plant located on the property. The parties never fully litigated with regard to the issue of whether a leasehold existed because the Debtor did not attempt to assume the alleged lease within the time limit provided by the Bankruptcy Code, the lease was deemed rejected, and the Debtor agreed to vacate the premises. The Debtor prevailed on the issue of ownership of some substantial improvements located on the real property in question and, by order filed November 13, 2001, was allowed 90 days to disassemble and remove equipment and structures.

DISCUSSION

The Bankruptcy Code provides in relevant part as follows:

> After notice and a hearing, there shall be allowed administrative expenses . . . including . . . the actual, necessary costs and expenses of preserving the estate, including wages, salaries, or commissions for services rendered after the commencement of the case. . . .

11 U.S.C. § 503 (b)(1)(A) (1994).

In general, most courts have determined that for a postpetition debt to qualify as a necessary preservation expense, it must satisfy two requirements: "(1) it must have arisen from a transaction with the estate and (2) it must have benefitted the estate in some demonstrable way." 4 Collier on Bankruptcy ¶ 503.06[3] (Lawrence P. King et al. eds, 15th ed.

rev. 2001)(citations omitted). The administrative claimant has the burden of proof as to both requirements of the statute. In re Section 20 Land Group, Ltd., 261 B.R. 711,716 (Bankr. M.D. Fla. 2000).

Even if a claim meets the requirement of a postpetition transaction, the bankruptcy court has broad discretion in determining whether a claim is an administrative expense. National Labor Relations Bd. v. Walsh (In re Palau Corp.), 139 B.R. 942, 944 (B.A.P. 9th Cir. 1992)(citing In re Dant & Russell, Inc., 853 F.2d 700, 707 (9th Cir. 1988);In re Orvco, Inc., 95 B.R. 724, 728 (B.A.P.9th Cir. 1989)). Section 503(b) should be narrowly construed to maximize the value of the estate for the benefit of all creditors. In re Section 20 Land Group, Ltd., 261 B.R. at 716(quoting In re Colortex Indus., Inc., 19 F.3d 1371, 1377 (11th Cir. 1994)).

In its application for administrative expense, Metropolitan argued that its actions directly contributed to preservation of the estate pursuant to section 503(b)(1)(A), but also relied on an exception to the benefit requirement based on negligence or inequitable conduct of the Debtor.

As the exception pertains to trustees' negligence, Collier on Bankruptcy states:

> The Supreme Court addressed the allowability of an administrative claim that did not 'benefit' the estate in the typical sense in Reading Co. v. Brown, a case decided under the former Bankruptcy Act. The Court held that considerations of fundamental fairness and logic required the allowance of a claim of administrative priority for damages resulting from the postpetition negligence of a receiver in a Chapter XI case because such damages were 'actual and necessary costs' of administration. The Court stated that 'actual and necessary costs' should 'include costs ordinarily incident to operation of a business, and not be limited to costs without which rehabilitation would be impossible....

4 Collier on Bankruptcy ¶ 503.06 [3][c][i] (quoting Reading Co. v. Brown, 391 U.S. 471, 483 (1968)).

After Reading, courts have recognized that, in the interest of fairness, some costs ordinarily incident to the operation of the business should be allowed as administrative expense, even if not directly beneficial to the estate. See, e.g., In re B. Cohen & Sons Caterers, Inc., 143 B.R. 27, 29 (E.D Pa. 1992)(holding that postpetition tort claimant was entitled to administrative status in chapter 11 plan).

Metropolitan strenuously argues that the Debtor's claim of a leasehold interest was frivolous and that Metropolitan should be allowed an administrative claim for the cost of defending against a meritless claim. The bank further contends that because the Debtor never had a lease, it committed the tort of trespass, thereby injuring the bank.

As previously stated, the Debtor's claim that it held a leasehold interest that could be assumed and made a part of a reorganization has never been fully litigated, and no decision on the merits adverse to the Debtor has ever been reached. Some preliminary decisions were favorable to the Debtor, but the Debtor eventually abandoned its efforts to assume the lease in question. Therefore, it has not been necessary to rule on this issue even though Metropolitan urged the Court to do so when the Debtor abandoned its attempt to assume an unexpired lease.

Under the "necessary and actual expense" analysis of section 503(b)(1)(A), Metropolitan has not demonstrated any benefit to the estate resulting from the legal services incurred by Metropolitan in attacking the alleged lease. Nor was the cost of a security service to protect Metropolitan's property an actual and necessary cost of preserving the estate. The attorneys' fees and security service costs protected the bank's interests, not those of the estate.

Moreover, the Court cannot conclude, as Metropolitan urges, that these expenses fit within the Reading exception. There is no evidence of damage to Metropolitan's property by the Debtor; rather the expense arose because of the litigation between the parties in protecting their respective interests.

Testimony offered by Metropolitan's employee suggested that a confrontational relationship existed between the parties and that the Debtor's principal may have taken topsoil, furniture, and office equipment from Metropolitan's real property, thereby necessitating the security service to prevent future injury to the property. The Debtor's principal refuted this testimony, and without corroboration, Metropolitan has not met its burden to show that such acts were committed by the Debtor's principal or that they were serious enough to warrant security services costing $97,197.00.

The Court is unaware of any basis under state law to support a claim against the Debtor for these expenses, much less an administrative claim in bankruptcy with a priority over all other unsecured creditors. This scenario is analogous to that of an individual who builds a ten-foot brick wall around his property out of fear of vandalism from his neighbor and then demands judgment from his neighbor for the cost of the wall.

The proper measure of a claim for administrative expense for a lessor whose land is used by the Debtor during the administration of a bankruptcy case is the reasonable rental value of the property used. Reiter v. Fokkena (In re

Wedemeier), 237 F.3d 938, 941 (8th Cir. 2001); Burlington N. R.R. Co. v. Dant & Russell, Inc. (In re Dant & Russell, Inc.), 853 F.2d 700, 707 (9th Cir. 1988) (citations omitted); Williams v. IMC Mortgage Co. (In re Williams), 246 B.R. 591, 594 n.4 (B.A.P. 8th Cir.1999); In re Section 20 Land Group, Ltd., 261 B.R. at 717; In re Longua, 58 B.R. 503, 504 (Bankr. W.D. Wis. 1986).

If, as Metropolitan contends, the Debtor and Debtor's counsel made frivolous arguments to the Court, the bank's remedy is to pursue sanctions pursuant to Federal Rule of Bankruptcy Procedure 9011. See In re Arkansas Communities, Inc., 827 F.2d 1219 (8th Cir. 1987)(affirming bankruptcy court's sanctions of law firm for filing frivolous motions).

Therefore, the Debtor's objection to the administrative claim of Metropolitan is sustained, and the claim is disallowed.

IT IS SO ORDERED.

HON. JAMES G. MIXON
U. S. BANKRUPTCY JUDGE

DATE: 5/16/03

cc: U. S. Trustee
Allen W. Bird, II, Esq.
Stephen B. Niswanger, Esq.