IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

In re:	)	
	)	
JEFFERSON COUNTY, ALABAMA,	)	**Case No. 11-05736-TBB9**
a political subdivision of the State of	)	
Alabama,	)	**Chapter 9**
	)	
Debtor.	)	

RESPONSE TO MEMORANDUM IN SUPPORT OF MOTION REQUESTING ALLOWANCE OF ADMINISTRATIVE CLAIMS OF NORFOLK SOUTHERN RAILWAY COMPANY

Jefferson County, Alabama (the "County"), in support of the *Objection of Jefferson County, Alabama to Motion Requesting Allowance of Administrative Claims of Norfolk Southern Railway Company* [Docket No. 2404] (the "Objection")[1] and in response to the *Memorandum in Support of Motion Requesting Allowance of Administrative Claims of Norfolk Southern Railway Company* [Docket No. 2867] (the "Memorandum") filed by Norfolk Southern Railway Company (the "Claimant"), states as follows:

SUMMARY OF RESPONSE

1. The Claimant bases its purported administrative claim on an interpretation of the Eleventh Circuit's decision in *CSX Transportation, Inc. v. Alabama Department of Revenue*, 720 F.3d 863 (11th Cir. 2013), regarding sales taxes levied by the State of Alabama. The County is not a party to the *CSX Transportation* case. The Claimant maintains that if the ruling in *CSX Transportation* stands as to the State of Alabama's sales tax, the Claimant will be entitled to a refund of the County's sales tax. The County does not address the merits of the Claimant's tax

[1] Unless otherwise defined all capitalized terms shall have the meanings provided in the Objection.

refund claim in this response. Solely for the purpose of this response, the County assumes that the Claimant is entitled to a tax refund pursuant to state and federal law and addresses only the issue of administrative priority. The County reserves all rights, claims, and defenses with respect to the Claimant's entitlement and the amount of any tax refund pending resolution of the *CSX Transportation* case. Without limitation, (a) the United States Supreme Court has *CSX Transportation* under review and the Eleventh Circuit's ruling may not stand and (b) no court has applied the *CSX Transportation* ruling to the County's taxes.[2]

2. However, even if the Eleventh Circuit's ruling in *CSX Transportation* survives and is applicable to the County, the Claimant has not sustained its burden of proof for the allowance of an administrative claim in the County's chapter 9 case.

3. First, the Claimant has not established that its purported claim against the County arose postpetition. As set forth below, the alleged accrual of damages under state law does not dictate when a claim arises in bankruptcy.

4. Second, the Claimant solely relies upon the Supreme Court's decision in *Reading Co. v. Brown*, 391 U.S. 471 (1968), for the proposition that administrative claims enumerated in section 503 are only illustrative. The Claimant's reliance on *Reading* is misplaced. *Reading* supports allowing an administrative claim solely under section 503(b)(1)(A) of the Bankruptcy Code, which the Claimant concedes does not apply in the County's chapter 9 case. The policy rationales underlying *Reading* and similar decisions do not apply in a chapter 9 case and provide no basis for administrative priority outside section 503(b)(1)(A).

[2] Section 505 of the Bankruptcy Code does not apply in chapter 9. *See* 11 U.S.C. § 901. However, the Court has jurisdiction to determine administrative claim priority status pursuant to the Plan and section 503(b) of the Bankruptcy Code, notwithstanding any challenge to the Court's jurisdiction to determine the amount or legality of any tax.

5. Accordingly, the Motion requesting allowance of an administrative expense claim pursuant to section 503 of the Bankruptcy Code is due to be denied.

RESPONSE

A. The Applicable Legal Standard.

6. The burden of proof is on the party claiming the administrative expense. *In re Fulwood Enterprises, Inc.*, 149 B.R. 712, 715 (Bankr. M.D. Fla. 1993). A request for payment of administrative expenses enjoys no presumptive validity. *See* 11 U.S.C. § 503; *Fulwood Enters.*, 149 B.R. at 715. The moving party must establish a valid claim that should be charged as a cost of administration under section 503 of the Bankruptcy Code. *See Fulwood Enters.*, 149 B.R. at 715. Administrative expenses are narrowly construed in chapter 9 cases. *See In re County of Orange*, 179 B.R. 195, 201 (Bankr. C.D. Cal. 1995); *see also In re Citation Corp.*, 493 F.3d 1313, 1318 (11th Cir. 2007) ("[W]e must carefully review the legitimacy of [administrative] claims.").

7. As discussed below, the Claimant has not sustained its burden to support an administrative expense claim under section 503 of the Bankruptcy Code.

B. The Claimant Does Not Assert a Postpetition Claim.

8. Administrative expense claims generally must arise postpetition. *See, e.g., In re Hackney*, 351 B.R. 179, 184 (Bankr. N.D. Ala. 2006). Apart from section 503(b)(9), which does not apply to the Claimant, the Bankruptcy Code makes no provision for administrative priority for prepetition claims. The Claimant relies on an assumption that its purported right to tax refunds arose postpetition. However, the Claimant has not met its burden of showing that an alleged tax overpayment made postpetition gives rise to a postpetition claim.

9. While state law generally determines the existence of a claim based on a cause of action, federal law determines when a claim arises for bankruptcy purposes. *See Johnson v.*

Home State Bank, 501 U.S. 78, 83 (1991) (holding that the question of whether an interest is a claim for bankruptcy purposes is "to be resolved by reference to the 'text, history and purpose' of the Bankruptcy Code" (citations omitted)). The definition of "claim" under the Bankruptcy Code includes contingent and unmatured rights to payment. *See* 11 U.S.C. § 101(5). This broad definition ensures that "all legal obligations of the debtor, no matter how remote or contingent, will be able to be dealt with in the bankruptcy case." *In re Hassanally*, 208 B.R. 46, 50 (BAP 9th Cir. 1997) (quoting legislative history); *see also Epstein v. Official Comm. Of Unsecured Creditors of Estate of Piper Aircraft (In re Piper Aircraft)*, 58 F.3d 1573, 1576 (11th Cir. 1995).

10. In the Eleventh Circuit, the postpetition accrual of damages does not convert to administrative priority status a claim based upon a prepetition event or transaction. *See Piper*, 58 F.3d at 1577; *In re Bill Heard Enters., Inc.*, 400 B.R. 813, 824, n.26 (Bankr. N.D. Ala. 2009) (discussing the modified prepetition relationship test called the "*Piper* test"). The Eleventh Circuit specifically has rejected the "accrued state law claim test." *Piper*, 58 F.3d at 1576 n.3. Accordingly, a claim arises prepetition if the acts giving rise to liability occur prepetition, regardless of when the injury is suffered or a right to payment accrues. *See Stone v. Kmart Corp.*, No. 2:06-CV-302-WKW, 2007 WL 1034959 (M.D. Ala. Mar. 30, 2007) (plaintiff had remote prepetition claim for malicious prosecution against debtor at time of plaintiff's arrest despite fact that criminal prosecution was dismissed postpetition); *In re Pan Am. Hosp. Corp.*, 364 B.R. 839 (Bankr. S.D. Fla. 2007) (wrongful death claim resulting from prepetition medical treatment was prepetition claim despite fact that patient died postpetition); *In re Kirkpatrick*, 206 B.R. 663 (Bankr. M.D. Fla. 1997) (attorneys' fees awarded pursuant to federal statute were prepetition claim based on prepetition lawsuit); *In re CD Realty Partners*, 205 B.R. 651 (Bankr. D. Mass. 1997) (citing *Piper* and holding that statutory withdrawal liability for retirement plan funding was prepetition claim despite fact that debtor's withdrawal liability arose

postconfirmation); *In re Charter Int'l Oil Co.*, No. 3:06-ap-00179-GLP, 2007 WL 879176 (Bankr. M.D. Fla. Mar. 14, 2007) (creditor had prepetition claim for exposure to debtor's products even though creditor was not diagnosed with disease until after petition); *In re Krause, Inc.*, Adv. No. 01-6574, 2005 WL 6487214 (Bankr. N.D. Ga. July 11, 2005) (creditor had prepetition claim against debtor arising from prepetition and postpetiton purchase of defective ladders even if damages may have been incurred postpetition).

11. Each of the alleged bases for the Claimant's purported claim against the County occurred prepetition. The County imposed and collected sales tax from the Claimant before the County filed bankruptcy. The statute under which the Claimant challenges the County's sales tax – the Railroad Revitalization and Regulatory Reform Act of 1976 (the "4-R Act") – predates the County's bankruptcy. *See CSX Transp.*, 720 F.3d at 871 (holding that the State of Alabama's sales tax violates the 4-R Act). The litigation the Claimant brought to challenge the state's sales tax, which involved a nearly identical challenge to the state sales tax as in *CSX Transportation*, predates the County's bankruptcy. *See Norfolk S. Ry. Co. v. Ala. Dept. of Revenue*, 550 F.3d 1306 (11th Cir. 2008). The postpetition occurrences the Claimant alleges - the Eleventh Circuit ruling in *CSX Transportation* and the Claimant's alleged payment of taxes - are not the events that give rise to any claim, rather, they are mere contingencies or accruals based on prepetition transactions or relationships.

12. Based on the foregoing, the relationship, events, and transactions giving rise to the Claimant's assertion that it does not owe the County's sales tax arose before the County's bankruptcy. The Claimant's argument that a portion of damages for payment of alleged invalid taxes accrued postpetition, based on its alleged overpayment of taxes disputed as a result of prepetition events, provides no basis for administrative priority. Accordingly, under *Piper* and

applicable law, the Claimant has a prepetition claim against the County, notwithstanding any postpetition accrual of damages.

13. Moreover, the Claimant has not factually established its entitlement to an administrative expense claim. The exhibits attached to the Motion do not establish when tax obligations accrued. As discussed above, the payment date does not necessarily control. Furthermore, the Claimant assumes, without any justification or citation, that administrative expense claims in a chapter 9 case are based on the filing date as opposed to the date of the order for relief. *See* 11 U.S.C. § 921. The County does not further address these fact issues because the Claimant is not entitled to a priority claim as a matter of law, but reserves all rights, claims, and defenses.

14. The Claimant has provided no authority or analysis to support its assumption that its disputed claims arose postpetition. Accordingly, the Motion is due to be denied.

C. *Reading* Does Not Apply to the County's Chapter 9 Case.

15. Even if the Claimant has a postpetition claim, the Motion is still due to be denied. The Claimant relies solely on the Supreme Court's *Reading* decision to support assertion of administrative priority. This reliance is misplaced as a matter of law and policy.

16. In *Alabama Surface Mining Commission v. N.P. Mining Co. (In re N.P. Mining Co.)*, 963 F.2d 1449 (11th Cir. 1992), the Eleventh Circuit recognized that section 503(b)(1)(A) may include "nonlisted" administrative expense claims based upon the use of the word "including" in subsection (b)(1)(A). 963 F.2d at 1452. The *N.P. Mining* court also alluded to the possibility of "nonlisted" administrative expense claims under section 503(b) generally, based upon the inclusion of the word "including" in the prefatory sentence of subsection (b). *See id.* However, the *N.P. Mining* court did not find that the claim at issue could be allowed as a "nonlisted" administrative expense claim under section 503(b) in general. Rather, the *N.P.*

Mining court only found a "nonlisted" administrative expense claim under section 503(b)(1)(A) for the "actual, necessary costs and expenses of preserving the estate." *Id.* at 1459.

17. As the Claimant points out, the Eleventh Circuit finding that a "nonlisted" administrative expense claim may arise under section 503(b)(1)(A) is based upon policies the Supreme Court enunciated in *Reading*. *Id.* at 1459. However, *N.P. Mining* only applies to section 503(b)(1)(A) and only addresses situations where administrative expense claims may be allowed as "actual, necessary costs and expenses of preserving the estate" even though the costs did not benefit the estate.[3] *See id.* at 1454-55, 1459. Similarly, *Reading* involved the allowance of a claim pursuant to section 64a of the Bankruptcy Act, the Bankruptcy Act cognate of section 503(b)(1)(A) of the Bankruptcy Code. Specifically, the issue before the Supreme Court was whether the negligence of a receiver administering an estate gave rise to an "actual and necessary" cost of operating the debtor's business even though the transaction at issue gave rise to a tort claim, not a sale on credit that actually enhanced the estate. *See Reading*, 391 U.S. at 475-76. Accordingly, like *N.P. Mining*, *Reading* only supports the allowance of a non-listed administrative expense claim under the current equivalent of section 64a of the Bankruptcy Act, section 503(b)(1)(A) of the Bankruptcy Code, for the "actual, necessary costs and expenses of preserving the estate . . . ." *See N.P. Mining*, 963 F.2d at 1453 (recognizing that "*Reading* and a line of cases employing its reasoning . . . have created categories of costs that are entitled to administrative-expense status as 'actual, necessary' costs of preserving the estate even though these costs do not confer an actual benefit on the estate").

[3] In fact, *N.P. Mining* is even more limited because it only applies to state civil penalties assessed as a consequence of operating a bankruptcy estate. *See N.P. Mining*, 963 F.2d at 1459. The Eleventh Circuit relied on the policy of 28 U.S.C. § 959(b) to reach its conclusion. *Id.* As the Court has already ruled, 28 U.S.C. § 959 does not apply in chapter 9 cases. *See In re Jefferson County, Ala.*, 484 B.R. 427 (Bankr. N.D. Ala. 2012).

18. Neither *N.P. Mining* nor *Reading* provide any support for the notion that an administrative claim may be allowed for anything other than the "actual, necessary costs and expenses of preserving the estate" or in a case where there is no estate. Courts within the Eleventh Circuit only have referenced or applied *Reading* to claims under section 503(b)(1)(A), not to an otherwise nonlisted administrative expense under section 503(b) in general. *See N.P. Mining*, 963 F.2d at 1453-62 (applying *Reading* to claim under section 503(b)(1)(A)); *Matter of Younger*, 165 B.R. 965 (S.D. Ga. 1994) (applying *Reading* and *N.P. Mining* to claim under section 503(b)(1)(A)); *In re Urgent Care Holdings, Inc.*, 474 B.R. 298 (Bankr. S.D. Fla. 2012) (same); *In re Growth Development Corp.*, 168 B.R. 1009 (Bankr. N.D. Ga. 1994) (same); *In re Motel Invs., Inc.*, 172 B.R. 105 (Bankr. M.D. Fla. 1994) (same); *Matter of Younger*, 163 B.R. 609 (Bankr. S.D. Ga. 1993) (same); *In re G.I.C. Gov't Sec., Inc.*, 121 B.R. 647 (Bankr. M.D. Fla. 1990) (applying *Reading* to claim under 503(b)(1)(A)); *Park Nat'l Bank v. Univ. Centre Hotel, Inc.*, No. A:06-cv-00077-MP-AK, 2007 WL 604936 (N.D. Fla. Feb. 22, 2007) (same); *In re Concrete Products, Inc.*, No. 88-20240, 1994 WL 16860114 (Bankr. S.D. Ga. June 8, 1994) (applying *Reading* and *N.P. Mining* to claim under section 503(b)(1)(A)).

19. The Claimant specifically has conceded that section 503(b)(1)(A) does not apply to the County's chapter 9 case because a municipal debtor does not have an estate under chapter 9. *See* Memorandum at p. 3; *see also In re New York City Off-Track Betting Corp.*, 434 B.R. 131, 141-42 (Bankr. S.D.N.Y. 2010). It follows, therefore, that administrative expense claims under section 503 in chapter 9 are limited to expenses incurred in connection with the chapter 9 case itself, such as professional fees and expenses and creditor costs otherwise allowable outside section 503(b)(1)(A). *See Off-Track Betting*, 434 B.R. at 142. Claims allegedly arising from the "operation" of the County's "business" (to the extent those concepts even apply to municipal governments) simply do not qualify for administrative expense priority.

20. Accordingly, the Claimant cannot rely on *Reading* – a case that only applies to bankruptcy estates, or *N.P. Mining*, which similarly only applies to section 503(b)(1)(A) – to support its entitlement to an administrative expense claim. *See Hackney*, 351 B.R. at 196 (cases cited by administrative claim applicant not relevant to request because applicant conceded section at issue in those cases did not apply).[4] To the extent the *Reading* case provides an expansion or gloss on section 503(b)(1)(A), it simply relieves a claimant of having to prove an "actual, necessary" cost of preserving the estate conferred an "actual benefit" on the estate. *See N.P. Mining*, 963 F.2d at 1453. *Reading* and its progeny, therefore, do not address the issue critical to the Claimant's argument, which is the lack of an estate in chapter 9 and the inapplicability of section 503(b)(1)(A) as a whole. *Reading* and the cases that have applied *Reading* to section 503(b)(1)(A) provide no authority for adding a new subsection of section 503(b) that confers administrative expense priority on postpetition costs and expenses where no estate exists.

21. The reason the Claimant cannot extend *Reading* beyond section 503(b)(1)(A) claims is that the policy underlying *Reading* does not apply in chapter 9 cases. The equitable consideration central to *Reading* is forcing creditors to bear the costs of the court allowing a bankruptcy estate to operate for creditors' benefit:

> At the moment when an arrangement is sought, the debtor is insolvent. Its existing creditors hope that by partial or complete postponement of their claims they will, through successful rehabilitation, eventually recover from the debtor either in full or in larger proportion than they would in immediate bankruptcy. Hence the present petitioner did not merely suffer injury at the hands of an insolvent business: it had an insolvent business thrust upon it by operation of law. That business will, in any event, be unable to pay its [tort] debts in full. ***But the question is whether the [tort]***

[4] To the extent the Claimant still asserts that it has provided a benefit to the County, it has failed to address the issue raised in the Objection regarding the amount of the taxes actually retained by the County. *See* Objection at ¶ 3.

> ***claimants should be subordinated to, should share equally with, or should collect ahead of those creditors for whose benefit the continued operation of the business . . . was allowed.***

Reading, 391 U.S. at 478 (emphasis added). The Supreme Court emphasized that in a commercial bankruptcy a business continues to operate with the hope of paying creditors:

> The 'master,' liable for the negligence of the 'servant' in this case was the business operating under a Chapter XI arrangement ***for the benefit of creditors and with the hope of rehabilitation***. That benefit and that rehabilitation are worthy objectives. But it would be inconsistent both with the principle of respondeat superior and with the rule of fairness in bankruptcy to seek these objectives ***at the cost of excluding tort creditors of the arrangement from its assets, or totally subordinating the claims of those on whom the arrangement is imposed to the claims of those for whose benefit it is instituted.***

Id. at 479 (emphasis added); *see also id.* at 482-83 ("Existing creditors are, to be sure, in a dilemma not of their own making, but there is no obvious reason why they should be allowed to attempt to escape that dilemma at the risk of imposing it on others equally innocent."). In chapter 9, of course, there is no "business" operating for the benefit of creditors and no estate. The purpose and effect of chapter 9 is different and the Claimant's efforts to force chapter 11 concepts into the County's case are unavailing. *See Off-Track Betting*, 434 B.R. at 142.

22. Many principles that apply in other chapters of the Bankruptcy Code are of limited assistance in construing provisions within chapter 9. *In re Richmond Unified Sch. Dist.*, 133 B.R. 221, 224-25 (Bankr. N.D. Cal. 1991); *see also Newhouse v. Corcoran Irr. Dist.*, 114 F.2d 690, 690-91 (9th Cir. 1940). The Claimant's argument is based on effectively analogizing the payment of taxes to a municipality to the operational transactions of a chapter 11 estate. The Claimant provides no basis for the proposition that the relationship between a taxing authority and a taxpayer should be governed by principles of commercial transactions. For example, tax obligations and refunds are not debts that give rise to rights of setoff under state law. *See Jefferson County v. City of Birmingham*, 129 So. 48 (Ala. 1930) (share of road tax collected by

county not subject to reduction by setoff for overpayments in previous years); *Enterprise v. Rawls,* 86 So. 374, 374 (Ala. 1920) (absent specific statutory authority, taxes may only be satisfied in money, and are not subject to setoff against a municipality); *Shelton v. Blount County*, 81 So. 562, 564 (Ala. 1919) ("a tax debtor can never be allowed to set off against his taxes a claim against the state or municipality"). Similarly, the primary purpose of chapter 9 is to allow the provision of public services rather than preservation of enterprise value through a bankruptcy estate. *See In re Mt. Carbon Metro. Dist.*, 242 B.R. 18, 34 (Bankr. D. Colo. 1999); *see also* H.R. REP. 95-595, 263, 1978 U.S.C.C.A.N. 5963, 6221. Because chapter 9 does not share the policy underpinning chapter 11 (to preserve value for creditors and shareholders), the parallels the Claimant attempts to draw between its situation and the *Reading* case are not valid. *See Off-Track Betting*, 434 B.R. at 142-43.

23. The Claimant relies solely on the Supreme Court's *Reading* decision to support its purported entitlement to an administrative expense claim. *Reading* is inapplicable to the County's chapter 9 case and does not support an administrative expense claim. *Reading* provides at most a gloss on the concept of actual benefit to the estate in section 503(b)(1)(A). *Reading* does not make section 503(b)(1)(A) apply where there is no estate, and does not create a new, unenumerated vehicle to force section 503(b)(1)(A) concepts of "preserving the estate" into chapter 9. Accordingly, the Motion is due to be denied.

WHEREFORE, the County respectfully requests that the Court deny the Motion requesting allowance of an administrative expense claim pursuant to section 503 of the Bankruptcy Code.

Respectfully submitted this 8th day of October, 2014.

By: /s/ Patrick Darby

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CERTIFICATE OF SERVICE

I hereby certify that on October 08, 2014, I electronically filed the foregoing with the Clerk of the Court using the CM/ECF system which will send notification of such filing to the following:

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