

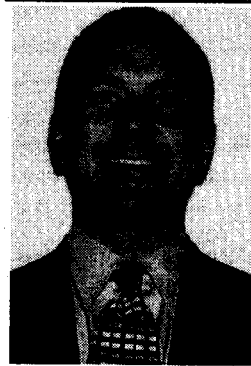
OBA Bankruptcy & Reorganization Section:  
 The 10th Circuit Rules That Post Petition  
 Attorneys' Fees Are Not Allowed under 11 U.S.C.  
 § 506(b) for Oversecured Nonconsensual Liens

By Gary D. Hammond and Jeffrey E. Tate

On January 20, 1999, the 10th Circuit Court of Appeals held in *In re Gledhill*, 164 F.3d 1338 (10th Cir. 1999), that a nonconsensual oversecured creditor is not entitled to recover attorneys' fees, costs, or other charges under 11 U.S.C. § 506(b). Previously, the issue had not been addressed in the 10th Circuit, although other districts and courts had ruled on the issue.<sup>1</sup>

In 1978, State Bank of Southern Utah ("Bank") loaned John Gledhill and Gloria Gledhill \$120,000.00 for construction of a service station. The loan was secured by a note and trust deed on the property. Both the note and deed provided for attorneys' fees and costs to cover collection expenses if the debtors defaulted. The Gledhills defaulted and Bank sued to foreclose the deed and collect the unpaid balance. The state court entered judgment in favor of Bank in the amount of \$172,448.55 and awarded Bank its attorney fees and costs.<sup>2</sup> Thereafter, Bank sold the service station, applied the proceeds to the debt, and the state court entered a judgment for the deficiency balance.

Bank enforced its judgment lien arising from the deficiency judgment by foreclosing on other property owned by the Gledhills. The Gledhills filed a chapter 7 bankruptcy petition shortly before the property was scheduled to be sold. During the course of the bankruptcy proceedings the property was sold for \$299,000.00. Bank filed a proof of claim in the bankruptcy, seeking to recover the remaining principal and interest under the deficiency



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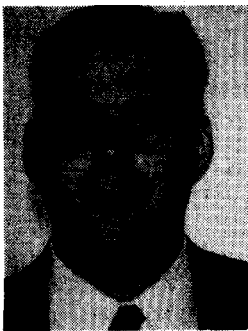
judgment, plus \$64,245.03 in post-petition attorneys' fees and costs to the extent recoverable under 11 U.S.C. § 506(b).<sup>3</sup>

The chapter 7 trustee objected to Bank's proof of claim on the ground that Bank was not entitled to any fees or costs under section 506(b). The bankruptcy court agreed. The district court affirmed. Bank appealed to the 10th Circuit Court of Appeals.

Arguing that the district court's decision was contrary to the plain language of section 506(b) and to the holding of *United States v. Ron Pair Enters., Inc.*, 489 U.S. 235 (1989), Bank asserted that section 506(b) does not distinguish between consensual and nonconsensual liens, but allows recovery of "fees, costs, or other charges" if "provided for under the agreement under which such claim arose." Bank then contended that the "agreement" in question was

the note, trust deed, and state court judgment. Not surprisingly, the note, trust deed and state court judgment each granted Bank its fees and costs.

The 10th Circuit Court began its analysis by recognizing that the amount of a creditor's bankruptcy claim is measured "as of the date of the filing of the petition." See, 11 U.S.C. § 502(b). According to the court, holders of an oversecured, consensual claim or an oversecured, nonconsensual claim are entitled to interest, penalties, attorney fees, and costs that accrue **before** the debtor's petition is filed. See, *In re Brentwood Outpatient, Ltd.*, 43 F.3d 256, 263 (6th Cir. 1994). The court further reasoned that interest, fees, costs and charges that accrue **after** the petition is filed, or post-petition, are permitted only if authorized by 11 U.S.C. § 506(b).



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Because section 506(b) refers to an "allowed secured claim," the court reasoned it first had to identify the "allowed secured claim" at issue. Defining an "allowed secured claim" as the "specific claim presented to the bankruptcy court for payment," the court rejected Bank's assertion that the note and trust deed comprised its "allowed secured claim." Instead, the court reasoned that when the service station was sold to satisfy Bank's foreclosure judgment, the underlying note and trust deed merged into the judgment pursuant to applicable state law. Thus, the court ruled that it was "the Bank's nonconsensual judgment lien on the Gledhills' remaining property...that is the 'allowed secured claim' at issue..."

Having identified the "allowed secured claim," the court was then ready to determine whether section 506(b) allows both creditors

having oversecured consensual claims and creditors having oversecured nonconsensual claims to recover post-petition attorney fees and costs. In *Ron Pair* the United States Supreme Court held that section 506(b) entitles a creditor to recover post-petition interest on oversecured nonconsensual claims. Bank contended that the United States Supreme Court's reasoning extended beyond interest to include attorneys' fees and costs as well.

The court, however, refused to interpret *Ron Pair* to include attorneys' fees and costs for oversecured nonconsensual liens. According to the court, the natural reading of section 506(b) entitles the holder of an oversecured claim to post-petition interest. The court also stated that section 506(b) additionally allows for reasonable fees, costs and other charges to a secured creditor under a security agreement authorizing such recovery. While it concluded that recovery of interest is unqualified under section 506(b), the court reasoned that recovery of attorneys' fees, costs, and charges, is allowed only if reasonable and authorized in the agreement under which the claim arose. Therefore, in the absence of a consensual agreement, post-petition interest is the only added recovery available to an oversecured creditor.

The court closely examined the language of *Ron Pair* to conclude that attorneys' fees and costs were not allowed. Parsing the structure of section 506(b), the *Ron Pair* court articulated that "[t]he phrase 'interest on such claim' is set aside by commas, and separated from the reference to fees, costs, and charges by the conjunctive words 'and any.' As a result, the phrase 'interest on such claim' stands independent of the language that follows. '[I]nterest on such claim' is not part of the list made up of 'fees, costs, or charges,' nor is it joined to the following clause so that the final 'provided for under the agreement' modifies it as well....The language and punctuation Congress used cannot be read in any other way. By the plain language of the statute, the two types of recovery are distinct."

In a decision squarely established on the foundation of *Ron Pair* and the plain language of section 506(b), the *Gledhill* court announced that in the 10th Circuit, nonconsensual creditors cannot recover attorneys' fees, costs or other charges after a debtor files bankruptcy,

even if they are oversecured. According to Gledhill, such creditors are entitled to post petition interest and nothing else.

1. See, *In re Brentwood Outpatient, Ltd.*, 43 F.3d 256 (6th Cir. 1994); *In re Pointer*, 952 F.2d 82, 89 (5th Cir. 1992) ("All creditors can recover interest on an oversecured claim, but only creditors who have voluntary secured claims can recover penalties, fees, and costs."); *In re Parr Meadows Racing Ass'n*, 880 F.2d 1540, 1549 (2d Cir. 1989); *In re Tricca*, 196 B.R. 214, 218 (Bankr. D. Mass. 1996) ("The overwhelming majority of cases have held that a secured creditor is not entitled to recover legal fees as part of its secured claim when the claim for fees and costs arises solely by operation of law."); *In re Vulpetti*, 182 B.R. 923, 927 (Bankr. S.D. Fla. 1995) ("Section 506(b) does not provide an avenue for recovery of post-petition attorneys' fees and costs for a creditor whose secured claim arises by operation of law rather than pursuant to a consensual security agreement.").

2. The judgment specifically provided: "The Defendants John Herbert Gledhill and Gloria Kay Gledhill are jointly and severally indebted to the Plaintiff, State Bank of Southern Utah, in the total amount of \$172,448.55 as of April 15, 1992, pursuant to those two notes dated July 22, 1976, and December 18, 1978, respectively, plus interest on the [principal] balance at the contract rate from and after this date until paid; and plus subsequently accruing costs and attorney's fees."

3. 11 U.S.C. § 506(b) states:

To the extent that an allowed secured claim 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 under which such claim arose.