

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEBRASKA

IN RE:)
 SOL LEWIS APPLIANCES, INC.,)
 Debtor.)
 MEYERSON DISTRIBUTING CO.,)
 Plaintiff,)
 vs.)
 SOL LEWIS APPLIANCES, INC.,)
 Defendant.)

AMERICAN DISTRIBUTORS, INC.,)
 Plaintiff,)
 vs.)
 SOL LEWIS APPLIANCES, INC.,)
 Defendant.)

BK 80-229
A 81-446

CV 84-0-55 FILED
DISTRICT OF NEBRASKA
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William L. Olson, Clerk
Deputy

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ORDER

These matters are before the Court on appeal from a judgment entered by the United States Bankruptcy Court for the District of Nebraska. Plaintiffs Meyerson Distributing Company ("Meyerson") and American Distributors, Inc. ("American") originally filed separate actions against defendant Sol Lewis Appliances, Inc. ("Sol Lewis") to reclaim merchandise from defendant's estate in bankruptcy. The parties subsequently stipulated that the merchandise would be returned to Meyerson and American for liquidation, reserving for trial the question of the parties' entitlement to the proceeds of such liquidation.

The cases were consolidated and tried on stipulated facts. The two cases involve almost identical factual and legal issues. The Bankruptcy Court ruled against Meyerson in the sum of

\$31,841.98 and against American in the sum of \$12,825.71. The Bankruptcy Court also ruled against Sol Lewis' claim for prejudgment interest. Meyerson and American appeal the Bankruptcy Court's entry of judgment against them. Sol Lewis also appeals the denial of prejudgment interest.

Sol Lewis Appliance, Inc. was a retail appliance dealer which filed for relief under Chapter 11 of the Bankruptcy Code on or about February 8, 1980. Thereafter, Sol Lewis continued operating its business in Omaha, Nebraska, as a debtor-in-possession through July 9, 1981.

In the course of operating its business, both before and after it filed the Chapter 11 petition, Sol Lewis obtained merchandise, property, and inventory from distributors on a "floor plan" arrangement. Under such an arrangement Sol Lewis gave the distributor a purchase money security interest in the merchandise supplied, and agreed to pay the distributor the cost of the respective items as they were sold at retail. Prior to filing the Chapter 11 petition, Sol Lewis had obtained merchandise on a floor plan from Meyerson, but not from American.

On or about February 27, 1980, Sol Lewis entered into a floor plan agreement with American. American supplied certain inventory to Sol Lewis, who executed and delivered to American a security agreement and financing statement covering that inventory. On or about October 23, 1980, Sol Lewis executed and delivered to American a second security agreement and financing statement covering additional inventory. The financing statements for both floor plans were filed promptly by American with the

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Douglas County Clerk. Neither American nor Sol Lewis sought the advice of counsel or court authorization or approval of these agreements.

On or about April 2, 1980, Sol Lewis and Meyerson entered into a new floor plan agreement. Meyerson supplied inventory to Sol Lewis, who executed and delivered to Meyerson a security agreement and financing statement. Meyerson promptly filed the financing statement with the Douglas County Clerk.

On July 12, 1980, Sol Lewis and Meyerson entered into another agreement under which Meyerson supplied Sol Lewis with new merchandise. The parties agreed that an "overseer" would supervise the handling of the merchandise supplied and would receive and disburse the proceeds from the sale of the merchandise. This arrangement substantially incorporated a Bankruptcy Court order of March 5, 1980, in a prior adversary proceeding involving Sol Lewis and various creditors, including Meyerson.

Neither Sol Lewis nor Meyerson sought the advice of counsel or court authorization or approval for either the April 2 or the July 12 agreements.

Sol Lewis thereafter sold or otherwise disposed of some of the inventory merchandise supplied by plaintiffs and failed to pay them the proceeds. Plaintiffs then brought adversary proceedings, seeking reclamation of the remaining merchandise supplied to Sol Lewis. The parties entered into a stipulation which allowed Meyerson and American to take immediate possession of the merchandise in which they claimed an interest. The parties stipulated that the value of the merchandise reclaimed by

American was \$12,825.17, and the value of that reclaimed by
by Meyerson was \$31,841.98. They agreed that the Bankruptcy
Court would determine who was entitled to these goods.

The Bankruptcy Court held that Sol Lewis was entitled to
the return of the stipulated amounts. The Bankruptcy Court
refused to award Sol Lewis prejudgment interest.

DISCUSSION

On appeal, plaintiffs argue that the Bankruptcy Court
improperly applied Section 364 of the Bankruptcy Code in determining
that plaintiffs were not entitled to the status of secured creditors
for failing to get court approval of their post-petition extensions
of credit to Sol Lewis. Plaintiffs contend that Section 364 does
not apply to the transactions at issue here. Alternatively, they
argue that even if court approval should have been obtained prior
to supplying Sol Lewis with the merchandise, the Bankruptcy Court
abused its discretion in not approving the transactions nunc pro
tunc. Finally, they argue that Sol Lewis and its other creditors
would be unjustly enriched if they received the value of the
merchandise plaintiffs supplied.

Under Section 364(c) of the Bankruptcy Code the trustee or
debtor-in-possession may request that the bankruptcy court
authorize the obtaining of secured credit. The Court, after
notice and a hearing, may authorize the credit with priority over
any and all administrative expenses. If the trustee or debtor-in-
possession obtains credit without the court's permission, the
creditor will be treated simply as an unsecured creditor, without
any priority.

The Bankruptcy Court held that Section 364(c) applied to the transactions between Sol Lewis and Meyerson and American. The parties did not get prior court permission. Therefore, the creditors were deemed to be unsecured creditors.

Meyerson and American assert that Section 364(c) does not apply to their dealings with Sol Lewis. Their first argument is that Section 363(c)(1), rather than 364(c), controls. Section 363(c)(1) provides that the trustee or debtor-in-possession may "enter into transactions, including the sale or lease of property of the estate, in the ordinary course of business . . . and may use property of the estate in the ordinary course of business" without prior court approval. They argue that because the transactions were in the ordinary course of Sol Lewis' business, court approval under Section 364(c) was not required.

Meyerson and American argue secondly that the merchandise supplied did not become property of Sol Lewis' estate. Sol Lewis, they say, had only legal title, and an interest in the value of the merchandise in excess of the value of the equitable interest retained by plaintiffs. Thirdly, they contend that the transactions were not extensions of credit as contemplated by Section 364(c). Court approval is required to protect the interests of the estate and of other creditors. They argue that Section 364(c) is concerned with liens being placed on existing property of the estate. Where, as here, the property subject to the security interest is being supplied to the debtor by the creditor, there is no risk to other creditors. This, they say, is not an "extension of credit" under

Section 364(c). Rather, the plaintiffs retained their own interest in the merchandise. Finally, Meyerson argues that the July 12, 1980, agreement created an express or constructive trust and was not, therefore, an extension of credit.

Plaintiffs' first argument is not without merit. The concerns to which Section 364(c) are addressed are not significantly raised by a purchase money security interest. Court approval for the obtaining of secured credit is required to ensure that the trustee or debtor-in-possession does not harm the estate or the interests of already existing creditors. A purchase money security interest risks neither. If the goods are sold, the creditor gets its money and the estate is enriched by the amount of the purchase price in excess of that amount. If the goods are not sold, the creditor merely reclaims the goods and the estate is in the same position as it was prior to the transaction.

There is a good argument, then, for exempting purchase money security interests, like those at issue here, from Section 364(c)'s requirements. However, that is not a proper function of this Court, and Congress does not seem to have done so. Section 363 speaks generally of transactions in the ordinary course of business. Section 364(c) is much more specific, referring to obtaining credit. It is an established principle of construction that a specific statute or clause takes precedence over a general one. Bulova Watch Co. v. United States, 365 U.S. 753, 761 (1961). Therefore, a trustee or debtor-in-possession seeking to obtain secured credit, even in the ordinary course of business, must apply to the Bankruptcy Court. Any

other reading of the statute would exempt all credit transactions in the ordinary course of business from Section 364(c), whether or not they were purchase money security interests. Congress gave no indication of such an intent.

Furthermore, the transactions between Sol Lewis and Meyerson and American were extensions of credit that brought merchandise into the estate. Plaintiffs transferred the merchandise to defendant. They retained, not title, but a security interest. Ownership of the merchandise passed to defendant and, therefore, it became property of the estate under Section 541 of the Bankruptcy Code. Plaintiffs' security interest was to secure the money defendant owed to them. This was clearly an extension of credit.

The Court also finds no reason to disturb the Bankruptcy Code's finding that the July 12, 1980, agreement between Meyerson and Sol Lewis did not create an express or constructive trust. There is no language in the agreement supporting Meyerson's claim. In addition, the overseer was not holding the merchandise, but rather was to protect Meyerson's interest while Sol Lewis retained the merchandise. There was no trust.

The Bankruptcy Court correctly ruled that the agreements between plaintiffs and defendant were subject to Section 364(c). Court approval should have been obtained.

Justice requires, however, that the Court carefully review plaintiffs' claim for nunc pro tunc relief. Prior cases establish that an unauthorized loan may, by an order nunc pro tunc, be afforded priority as an expense of administration when the circumstances justify such equitable relief. This

doctrine has arisen from the Second Circuit's opinion in the case of In Re American Cooler Co., Inc., 125 F.2d 496 (2nd Cir. 1942). That case involved an unauthorized post-petition loan of operating funds to a debtor-in-possession. The Court held that nunc pro tunc relief is appropriate where the judge "is confident that he would have authorized [the agreement] if a timely application had been made, and . . . he is reasonably persuaded that the creditors have not been harmed by a continuation of the business made possible by the loan." 125 F.2d at 497. The court also held that the good faith of the parties was important and emphasized that the particular facts of each case were to be considered carefully. 125 F.2d at 497.

The facts of this case meet both elements of the American Cooler test. It seems certain that had the parties presented their agreements to the Bankruptcy Court, they would have been approved. In fact, the Bankruptcy Court had previously approved virtually identical agreements between Sol Lewis and various creditors. Approval would have been proper, perhaps even necessary, because the agreements were essential for the continuation of the debtor's business and posed no risk to the estate or its creditors. As explained previously, the only risk to the estate was that the goods supplied by Meyerson and American would be repossessed, leaving Sol Lewis no worse off than if the agreements had never been made. This also meets the second part of the American Cooler test. There was no risk of harm to other creditors.

In addition, there is no evidence of bad faith on the part of the parties. They entered into agreements essential to Sol Lewis' business, agreements that were in the ordinary course of business. These agreements could have only helped the debtor. The parties were mistaken in not consulting with counsel, but this was an honest error, not one of deceit.

In American Cooler the loan which was approved nunc pro tunc was secured by already existing property of the estate. Thus the transaction was clearly within the intent of Section 364(c). Here, where the security interest was in the goods supplied as part of the agreement, the equities are even more strongly in favor of plaintiffs. Plaintiffs are entitled to nunc pro tunc approval of their agreements with Sol Lewis and the amounts in question should be given priority as an expense of administration.

IT IS THEREFORE ORDERED that the judgment of the Bankruptcy Court is reversed and remanded for action consistent with this opinion.

DATED this 6th day of November, 1984.

BY THE COURT:



C. ARLEN BEAM
UNITED STATES DISTRICT JUDGE