

CREDITOR CLAIMS FOR POSTPETITION ATTORNEYS’  
FEES INCURRED IN BANKRUPTCY LITIGATION AND THE  
ROLE OF STATE LAW

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## INTRODUCTION

In *Travelers Casualty & Surety Co. v. Pacific Gas & Electric Co.*,<sup>1</sup> the Supreme Court admonished the Ninth Circuit Court of Appeals for judicially amending the Bankruptcy Code.<sup>2</sup> The Ninth Circuit had held that an attorneys' fee provision in a contract did not permit an unsecured creditor<sup>3</sup> to recover attorneys' fees from a bankrupt debtor if the fees were incurred litigating bankruptcy issues that did not involve a dispute regarding the contract.<sup>4</sup> In doing so, the Ninth Circuit cited *In re Fobian*<sup>5</sup> for the proposition that litigation of federal bankruptcy law must be distinguished from litigation of state law when determining the availability of postpetition<sup>6</sup> attorneys' fees in a bankruptcy proceeding<sup>7</sup>—a distinction the Supreme Court subsequently termed the *Fobian* rule.<sup>8</sup> The Supreme Court perceived this distinction as amending § 502(b) of the Bankruptcy Code<sup>9</sup> by implying a doctrine into the Code to preempt state law authorization of attorneys' fees related to bankruptcy litigation expenses.<sup>10</sup> The Court purported to overrule the Ninth Circuit's *Fobian* decision on the basis that the distinction drawn by the Ninth Circuit was not supported by the Bankruptcy Code.<sup>11</sup> In

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<sup>1</sup> *Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co.*, 549 U.S. 443 (2007). This Note will refer to the *Travelers* case at the District, Circuit, and Supreme Court level. For clarity, the short form citations for each will be as follows: *Travelers* will refer to the Supreme Court decision; *Travelers v. Pacific Gas* will refer to the Ninth Circuit decision; and *In re Pacific Gas* will refer to the district court decision.

<sup>2</sup> Throughout this Note, any reference to the "Bankruptcy Code," or simply to the "Code," is intended to refer to title 11 of the United States Code. 11 U.S.C. §§ 101–1532 (2012).

<sup>3</sup> An unsecured debt is one in which a creditor has no property interest in any of the debtor's property that can serve as collateral if the debtor fails to pay the debt. *Unsecured Creditor*, BLACK'S LAW DICTIONARY (10th ed. 2014).

<sup>4</sup> See *Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co.*, 167 F. App'x 593 (9th Cir. 2006).

<sup>5</sup> *Fobian v. W. Farm Credit Bank (In re Fobian)*, 951 F.2d 1149, 1150 (9th Cir. 1991).

<sup>6</sup> The word "postpetition" refers to events occurring after the bankrupt party has filed a petition for bankruptcy relief—as opposed to the word "prepetition," which refers to events occurring prior to a petition for bankruptcy relief. See Stephanie Wickouski, *Business Bankruptcy: Survival in a Turkish Bazaar*, LITIGATION, Spring 1987, at 38, 39. For a discussion of some of the effects of classifying an event as prepetition or postpetition, see Mark S. Scarberry, *Interpreting Bankruptcy Code Sections 502 and 506: Post-Petition Attorneys' Fees in a Post-Travelers World*, 15 AM. BANKR. INST. L. REV. 611, 617–24 (2007).

<sup>7</sup> *Travelers v. Pacific Gas*, 167 F. App'x at 594.

<sup>8</sup> See *Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co.*, 549 U.S. 443, 448 (2007). This Note will refer to the *Fobian* rule merely as a shorthand expression for the proposition that an attorneys' fee provision in a contract creates an unsecured claim for postpetition fees in bankruptcy for litigation of state law issues, but not for bankruptcy law issues. The same expression will be used without regard to the underlying justification for that legal proposition.

<sup>9</sup> § 502(b) lists the types of creditor claims that are not allowed in a bankruptcy proceeding. 11 U.S.C. § 502(b) (2012).

<sup>10</sup> See *Travelers*, 549 U.S. at 450–51.

<sup>11</sup> *Id.* at 452–53.

doing so, and by construing the *Fobian* decision itself as representing an illegitimate federal common law doctrine, the Court may have created some potential for confusion regarding the legitimacy of the *Fobian* rule as a general proposition—as opposed to a federal common law doctrine.<sup>12</sup>

This Note will provide an analysis of the history and development of the *Fobian* rule in order to assess the viability of the distinction it represents after the Supreme Court's *Travelers* decision. This Note will argue that the *Fobian* decision was originally based on the application of state law—not federal law—though the doctrine began to lose touch with its state law foundation as it developed. As a result, to the extent that the distinction embodied by the *Fobian* rule is consistent with applicable state law, this Note suggests that the distinction is not precluded by *Travelers*.

This Note will proceed in three Parts. Part I will provide a brief overview of how awards of attorneys' fees are treated generally, explore some of the interests at stake when attorneys' fees are sought within a bankruptcy context, and introduce the outlines of an ongoing debate concerning unsecured claims for postpetition attorneys' fees in bankruptcy proceedings. Part II will provide an account of the *Travelers* decision, followed by an analysis of *Fobian* and its progeny, arguing that the *Fobian* decision was originally based in California state law, and subsequently lost touch with that basis as the doctrine developed in the Ninth Circuit and in other courts. This Note will conclude, in Part III, that the distinction embodied by the *Fobian* rule should not be disregarded as an overruled doctrine because the principle could still be invoked if consistent with relevant state law. This Note suggests that there are significant reasons for preferring such an analysis to the alternatives, in light of the *Travelers* decision.

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<sup>12</sup> Commentators have concluded that the bankruptcy law–state law distinction, for the purposes of determining the availability of attorneys' fees, was completely foreclosed by *Travelers*. See, e.g., 1 RICHARD I. AARON, BANKRUPTCY LAW FUNDAMENTALS § 15:48 (perm. ed., rev. vol. June 2015) (determining that the Supreme Court rejected limiting attorneys' fee claims to substantively state law issues); Brian L. Holman & Melanie Scott, *Supreme Court Rules that Federal Bankruptcy Law Does Not Prohibit an Unsecured Creditor from Recovering Postpetition Attorney's Fees Authorized by an Enforceable Prepetition Contract*, 125 BANKING L.J. 79, 81 (2008) (suggesting that the Code would need to be amended before attorneys' fees covered by *Fobian* could be excluded); “Erik” Weiting Hsu & David W. Elmquist, *Can an Unsecured Creditor Recover Post-Petition Attorneys Fees? The Question Not Answered in Travelers*, AM. BANKR. INST. J., May 2007, at 10 (concluding that another theory would be necessary to deny claims for postpetition attorneys' fees); Scarberry, *supra* note 6, at 633–36 (determining that arguments based on *Fobian* were foreclosed by *Travelers*). After *Travelers*, courts have similarly begun to disregard the argument as foreclosed. See, e.g., *SNTL Corp. v. Ctr. Ins. (In re SNTL Corp.)*, 571 F.3d 826, 838–40 (9th Cir. 2009) (stating that *Fobian* has been overruled and moving on to other arguments without further discussion, ultimately holding that attorneys' fees must be allowed).

## I. ATTORNEYS' FEES IN BANKRUPTCY PROCEEDINGS

A. *General Overview*

It is a well-known principle of American jurisprudence, often referred to as the “American Rule,”<sup>13</sup> that each party to a litigation is ordinarily responsible for their own attorneys’ fees.<sup>14</sup> However, the American Rule is merely the default rule, and is subject to various exceptions.<sup>15</sup> The American Rule in federal jurisprudence is essentially derived by implication from a federal statute—the language of which was originally enacted in the nineteenth century—that limits an award of litigation costs to a nominal amount—between five and twenty dollars in civil litigation.<sup>16</sup> Because the American Rule developed as a common law doctrine based on a statutory implication, the legislature retains the power to enact other statutes that provide for an award of attorneys’ fees under particular circumstances, overriding the general implication raised by the nominal fee statute.<sup>17</sup> Additionally, courts may employ their inherent power in order to award attorneys’ fees when a party has litigated in bad faith or has abused the judicial system.<sup>18</sup> Federal courts will also recognize a contractual agreement, between the parties to a litigation, that allocates attorneys’ fees between them.<sup>19</sup> Such

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<sup>13</sup> See John Leubsdorf, *Toward a History of the American Rule on Attorney Fee Recovery*, LAW & CONTEMP. PROBS., Winter 1984, at 9, 27, 28 & n.130 (attributing the origin of the phrase to Arthur L. Goodhart, *Costs*, 38 YALE L.J. 849 (1929)).

<sup>14</sup> See *Alyeska Pipeline Serv. Co. v. Wilderness Soc’y*, 421 U.S. 240, 247 (1975); 1 MARY FRANCES DERFNER & ARTHUR D. WOLF, COURT AWARDED ATTORNEY FEES ¶ 1.01[1] (2015). See generally Leubsdorf, *supra* note 13 (outlining the history of attorneys’ fees recovery in the United States); John F. Vargo, *The American Rule on Attorney Fee Allocation: The Injured Person’s Access to Justice*, 42 AM. U. L. REV. 1567, 1570–90 (1993) (discussing the American Rule and its various exceptions).

<sup>15</sup> See DERFNER & WOLF, *supra* note 14, ¶ 1.02[2]; Vargo, *supra* note 14, at 1578–90.

<sup>16</sup> 28 U.S.C. §§ 1920(5), 1923 (2012); see also DERFNER & WOLF, *supra* note 14, ¶ 1.02[1]; Vargo, *supra* note 14, at 1578.

<sup>17</sup> DERFNER & WOLF, *supra* note 14, ¶ 6.02. Of course, the legislature also retains the power to repeal the statute, in whole or in part, expressly or implicitly. See, e.g., *Posadas v. Nat’l City Bank of N.Y.*, 296 U.S. 497, 503 (1936) (explaining that when two federal statutes are in irreconcilable conflict, the more recent statute constitutes a repeal of the earlier statute, to the extent of the conflict).

<sup>18</sup> Scholars have attributed the courts’ power to impose a bad faith exception to the American Rule to somewhat different sources. Compare DERFNER & WOLF, *supra* note 14, ¶ 4.01[1][a] (linking the bad faith exception to the federal courts’ inherent power to manage their own proceedings and control the conduct of those who appear before them), with Vargo, *supra* note 14, at 1584–87 (linking the bad faith exception to the courts’ inherent power in equity).

<sup>19</sup> DERFNER & WOLF, *supra* note 14, ¶ 6.01.

an agreement must be valid and enforceable under governing state law.<sup>20</sup>

The Bankruptcy Code specifically authorizes attorneys' fee awards in several situations. If a court dismisses an involuntary bankruptcy proceeding,<sup>21</sup> the debtor is presumptively entitled to an award of attorneys' fees<sup>22</sup> from creditors who have petitioned for the proceeding against it, unless the dismissal is consensual.<sup>23</sup> When a consumer debt is discharged, a debtor is also entitled to attorneys' fees from a creditor for the expense of defending the dischargeability of that debt, unless the creditor's argument for nondischargeability was substantially justified or special circumstances would not make the award unjust.<sup>24</sup> A debtor<sup>25</sup> may also recover attorneys' fees from a creditor as damages when it is injured by a creditor's willful violation of the automatic stay.<sup>26</sup>

A trustee, or debtor in possession,<sup>27</sup> may recover attorneys' fees against a creditor for the expense of successfully challenging a sale of estate property on the grounds that the price obtained was the result of collusion among the bidders.<sup>28</sup> However, attorneys' fees are not

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<sup>20</sup> See *Luce v. First Equip. Leasing Corp.* (*In re Luce*), 960 F.2d 1277, 1286 (5th Cir. 1992) (“[A] creditor can only recover postpetition attorney’s fees when that right arises from a contract between the creditor and the debtor that is enforceable under state law.”); *Martin v. Bank of Germantown* (*In re Martin*), 761 F.2d 1163, 1168 (6th Cir. 1985) (“[C]reditors are entitled to recover attorney’s fees in bankruptcy claims if they have a contractual right to them valid under state law.”).

<sup>21</sup> Although the vast majority of bankruptcy proceedings are the result of a voluntary petition by a debtor, see, e.g., Joseph Mullin, Comment, *Bridging the Gap: Defining the Debtor’s Status During the Involuntary Gap Period*, 61 U. CHI. L. REV. 1091, 1102 (1994), creditors may sometimes also commence bankruptcy proceedings against a debtor. See 11 U.S.C. § 303 (2012).

<sup>22</sup> The presumption may be rebutted by the creditor, and the court may exercise some discretion in determining whether to award fees based on the totality of the circumstances. *Higgins v. Vortex Fishing Sys., Inc.*, 379 F.3d 701, 706–07 (9th Cir. 2004); DERFNER & WOLF, *supra* note 14, ¶ 41.01[3].

<sup>23</sup> 11 U.S.C. § 303(i).

<sup>24</sup> *Id.* § 523(d).

<sup>25</sup> There is some ambiguity as to whether § 362(k)(1) applies to all debtors in bankruptcy. The Code uses the term “individual” rather than “debtor.” As a result, some circuit courts have held that only natural persons, as opposed to corporations or other entities, are eligible for the award. See 11 U.S.C. § 362(k)(1) (originally codified in § 362(h)); *Chateaugay Corp. v. LTV Steel Co.* (*In re Chateaugay Corp.*), 920 F.2d 183, 186–87 (2d Cir. 1990). *But see* *Budget Serv. Co. v. Better Homes of Va., Inc.*, 804 F.2d 289, 292 (4th Cir. 1986).

<sup>26</sup> 11 U.S.C. § 362(k)(1). The automatic stay is a feature of a bankruptcy proceeding whereby creditors must cease, inter alia, all debt collection activities against the debtor. See *id.* § 362(a).

<sup>27</sup> A debtor in possession is “[a] Chapter 11 or 12 debtor that continues to operate its business as a fiduciary to the bankruptcy estate.” See *Debtor-in-Possession*, BLACK’S LAW DICTIONARY (10th ed. 2014). A debtor in possession has many of the same rights as a bankruptcy trustee. See 11 U.S.C. § 1107(a).

<sup>28</sup> 11 U.S.C. § 363(n).

commonly awarded under this statute, primarily because of the difficulty in proving collusion among bidders.<sup>29</sup>

The Bankruptcy Code mentions the availability of attorneys' fee awards to creditors—as opposed to debtors or trustees—in two instances. First, any creditor<sup>30</sup> may request attorneys' fees as administrative expenses<sup>31</sup> if the creditor can show that it has substantially benefited the bankruptcy estate, thereby ultimately benefiting other creditors who are also seeking distribution from the estate.<sup>32</sup> Second, an oversecured creditor<sup>33</sup> may extend its secured claim to include reasonable attorneys' fees pursuant to an agreement or state law under which its claim arose, but only to the extent that it is oversecured.<sup>34</sup> In no other section does the Code affirmatively or expressly provide for attorneys' fees to be awarded to creditors.<sup>35</sup> Because the second provision applies only to secured creditors, the Code expressly provides for attorneys' fee awards to unsecured creditors only where the creditor has benefited the estate itself. The reason for this is likely—at least in part—due to some of the policy considerations discussed below.

### B. Policy Concerns

One of the central tenets of bankruptcy law is “equality of distribution among similarly situated creditors.”<sup>36</sup> In most bankruptcy cases, there will not be enough assets in the bankruptcy estate to fully compensate all unsecured creditors, so some creditors' recoveries will be

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<sup>29</sup> DERFNER & WOLF, *supra* note 14, ¶ 41.01[3].

<sup>30</sup> Creditors are not the only parties who may be entitled to attorneys' fees under § 503(b). See 11 U.S.C. § 503(b).

<sup>31</sup> Administrative expenses are given higher priority than other types of debts when the bankruptcy estate is distributed. See *id.* § 507(a)(2).

<sup>32</sup> See *id.* § 503(b); see also, e.g., *In re Psychiatric Hosps. of Hernando Cty., Inc.*, 228 B.R. 764 (Bankr. M.D. Fla. 1998) (holding that creditor's attorneys' fees were allowed under § 503(b)(3) where attorneys' pursuit of the equitable subordination of a million dollar secured claim was not duplicative of services rendered by other parties and resulted in increasing the amount of the estate available to unsecured creditors by \$700,000).

<sup>33</sup> An oversecured debt is one in which a creditor's collateral is worth more than the debt owed. See *infra* note 55 and accompanying text.

<sup>34</sup> 11 U.S.C. § 506(b). For further discussion of this section of the Code, see *infra* Section I.C.

<sup>35</sup> See generally 11 U.S.C. §§ 101–1532.

<sup>36</sup> *In re Elec. Mach. Enters.*, 371 B.R. 549, 551 (Bankr. M.D. Fla. 2007); cf. *Qmect, Inc. v. Burlingame Capital Partners II, L.P. (In re Qmect, Inc.)*, 368 B.R. 882, 886 (Bankr. N.D. Cal. 2007) (suggesting that the fundamental policy of equality must also be balanced against the policy to preserve nonbankruptcy legal rights except to the extent necessary to facilitate the purpose of the bankruptcy proceeding).

limited to a percentage of their claims on a pro rata<sup>37</sup> basis.<sup>38</sup> As a result, the amount of one creditor's claim may significantly affect the amount that another creditor may recover from the pool of limited assets of the debtor.<sup>39</sup> Allowing some creditors who have filed a claim for a debt in a bankruptcy proceeding to tack on additional claims for postpetition attorneys' fees, incurred while litigating issues before the bankruptcy court, creates the potential for those creditors to increase the amount of their claims, relative to other similarly situated creditors, thus increasing the amount of their pro rata share over the course of the proceeding.<sup>40</sup>

This can be especially unfair for certain types of creditors, such as tort claimants, who will never have the benefit of a contract providing for attorneys' fees. To illustrate this point, assume that an individual, *D*, files a Chapter 7 bankruptcy petition. *D*'s only creditors are *A* and *B*, both unsecured. *A* was injured in a car accident and has received a money judgment against *D* for \$20,000. *B* is a credit card company that has extended \$20,000 in credit to *D*. Like many credit card contracts, *D*'s contract with *B* contains an attorneys' fee clause providing that *B* is entitled to reimbursement of fees incurred in enforcing the credit agreement. The amount in the bankruptcy estate available for distribution to creditors is \$20,000. All things being equal, *A* and *B* should receive \$10,000 each from the bankruptcy estate. Both creditors will have received half of what they are owed. However, assume that it was necessary for both parties to litigate issues in the bankruptcy proceeding to protect their interests, and each has incurred \$5,000 in attorneys' fees. *B*'s claim now totals \$25,000 while *A*'s claim is still \$20,000. *B* will now receive over \$11,000 while *A* will receive less than \$9,000. Although *A* and *B* are both unsecured creditors and are owed the same amounts, *B* has the ability to increase its claim and recover more of *D*'s assets at *A*'s expense. As the parties' litigation costs rise, so will the disparities in their ultimate recoveries.

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<sup>37</sup> Pro rata means proportionately. See *Pro Rata*, BLACK'S LAW DICTIONARY (10th ed. 2014). In the context of a bankruptcy proceeding, this means that each creditor must receive the same percentage of their claim as every other similarly situated creditor. 11 U.S.C. § 726(b). For example, if a debtor has enough assets to pay fifty percent of all his debts, each individual creditor will recover only fifty percent of their claim.

<sup>38</sup> See, e.g., Lynn M. LoPucki, *A General Theory of the Dynamics of the State Remedies/Bankruptcy System*, 1982 WIS. L. REV. 311, 311 & n.3 (discussing 1977 statistics showing that eighty percent of straight bankruptcy cases provided no distribution to general creditors, and the other twenty percent provided distributions of about 4.5% of creditors' claims); see also STANDARD & POOR'S GLOB. RATINGS CREDIT RESEARCH, U.S. RECOVERY STUDY: RECENT POST-BANKRUPTCY RECOVERY LEVELS DISAPPOINT SENIOR UNSECURED BONDHOLDERS 3 (2012) (showing some unsecured creditors in reorganization proceedings as recovering five percent of their claims).

<sup>39</sup> See Scarberry, *supra* note 6, at 613 & n.15.

<sup>40</sup> Although "[t]his result would harm the other creditors," it would typically leave the debtor unaffected. See *id.* at 613 & n.16.

Some courts and commentators have claimed that this is a good reason to deny unsecured creditors' the right to claim postpetition attorneys' fees in bankruptcy, regardless of the character of the underlying claim. For example, a Texas bankruptcy court, presenting its position as the majority view,<sup>41</sup> has stated that it would be unfair to allow some unsecured creditors to increase their recoveries postpetition at the expense of other creditors.<sup>42</sup> The court expressed concern that, as in the example above, allowing postpetition attorneys' fee claims to unsecured creditors would allow some creditors to unfairly increase the amount of their claims—and, therefore, their pro rata share of the estate's distribution—at the expense of other creditors, who would receive a smaller percentage of the total estate as a result.<sup>43</sup>

Courts have also expressed concern that allowing unsecured claims for postpetition attorneys' fees would negatively impact the administration of a bankruptcy case.<sup>44</sup> One court worried that if creditors' claims could continuously increase as the bankruptcy case proceeded, administration of the proceeding would become unbearable.<sup>45</sup> Another concern is that allowing general creditors to claim postpetition attorneys' fees could incentivize creditors to be more litigious in bankruptcy proceedings.<sup>46</sup> In addition to diminishing the pro rata share of unsecured creditors without attorneys' fee contracts, increased bankruptcy litigation could also force them to incur additional litigation expenses in order to protect their own interests. Increased

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<sup>41</sup> *Pride Cos. v. Johnson (In re Pride Cos.)*, 285 B.R. 366, 373 (Bankr. N.D. Tex. 2002) (stating that “the majority cases present [the] policy argument” that it ultimately relied on).

<sup>42</sup> *Id.* (“Allowing unsecured creditors to recover postpetition fees is inequitable to other unsecured creditors and may, in some cases, consume the estate.”).

<sup>43</sup> *Id.* at 373–74.

<sup>44</sup> *In re Elec. Mach. Enters.*, 371 B.R. 549, 553 (Bankr. M.D. Fla. 2007).

<sup>45</sup> *Id.* (“[B]ankruptcy courts would constantly have to revisit the issue of the amount of claims to include ever-accruing attorneys' fees.”).

<sup>46</sup> See, e.g., Michelle Campbell, Carriane Basler & Kerri Lyman, *The Travelers Effect: Case Administration and Creditor Recoveries*, AM. BANKR. INST. J., May 2007, at 28, 29; William P. Weintraub, *Fobian Rule Is a Casualty of Travelers: The Supreme Court's Decision Raises New Questions for Bankruptcy Attorneys*, BUS. L. TODAY, July–Aug. 2007, at 61, 64; see also *Ctr. Ins. v. SNTL Corp. (In re SNTL Corp.)*, 380 B.R. 204, 222 (B.A.P. 9th Cir. 2007) (emphasizing that barring creditors from claiming postpetition attorneys' fees “would prevent individual creditors from utilizing scorched-earth litigation tactics,” but deciding that such policy determinations should be left to Congress). *SNTL Corp.* was the first case within the Ninth Circuit addressing postpetition attorneys' fees since the Ninth Circuit was admonished for not following the text of the Bankruptcy Code by the Supreme Court in *Travelers*, perhaps making the court more hesitant to incorporate policy considerations into its decision. See *id.* at 207. On appeal, the Ninth Circuit later adopted the Bankruptcy Appellate Panel's opinion in full. See *SNTL Corp. v. Ctr. Ins. (In re SNTL Corp.)*, 571 F.3d 826, 829 (9th Cir. 2009) (per curiam).



creditor litigation would also likely result in additional litigation by the estate, which depletes the estate to the detriment of all creditors.<sup>47</sup>

Other courts have posited that allowing postpetition attorneys' fees would not be inequitable.<sup>48</sup> One court has noted that if a party has contracted for a right to attorneys' fees, the party presumably gave value for that right.<sup>49</sup> In the court's view, rather than an undeserved bonus, the right to attorneys' fees is just another property interest of which it would be unfair for the court to dispossess the claimant.<sup>50</sup> Another court has stated that, at least where the bankruptcy estate is permitted to recover contractual postpetition attorneys' fees against a creditor, it would be inequitable to deny the same right to the creditor when it would otherwise be entitled to it.<sup>51</sup> In addition to issues of fairness, it has also been argued that denying postpetition attorneys' fees could have economic repercussions.<sup>52</sup> For example, if lenders knew that they could not recover their attorneys' fees in bankruptcy litigation pursuant to an agreement, they may attempt to recoup the lost value of an attorneys' fee provision in some other way, such as increasing interest rates on loans.<sup>53</sup>

### C. Collateral Debate

One section of the Bankruptcy Code in particular has provided a focal point for debate regarding the availability of postpetition attorneys' fees to unsecured creditors in bankruptcy litigation. § 506(b) of the Bankruptcy Code provides that if a creditor, bringing an

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<sup>47</sup> Bankruptcy trustees can recover their attorneys' fees from the bankruptcy estate as administrative claims, which take priority over other claims by creditors. 11 U.S.C. §§ 330, 507(a)(1)(C) (2012).

<sup>48</sup> See, e.g., *United Merchs. & Mfrs., Inc. v. Equitable Life Assurance Soc'y of the U.S.* (*In re United Merchs. & Mfrs., Inc.*), 674 F.2d 134, 137 (2d Cir. 1982).

<sup>49</sup> *Id.*

<sup>50</sup> *Id.* ("When equally sophisticated parties negotiate a loan agreement that provides for recovery of collection costs upon default, courts should presume, absent a clear showing to the contrary, that the creditor gave value, in the form of a contract term favorable to the debtor or otherwise, in exchange for the collection costs provision. Such a creditor should recover more in the division of the debtor's estate because it gave more to the debtor at the time it made the loan. Rather than providing an undeserved bonus for one creditor at the expense of others, allowing a claim under a collection costs provision merely effectuates the bargained-for terms of the loan contract.").

<sup>51</sup> *Qmect, Inc. v. Burlingame Capital Partners II, L.P.* (*In re Qmect, Inc.*), 368 B.R. 882, 885 (Bankr. N.D. Cal. 2007) ("It would seem highly inequitable to permit the estate to recover fees incurred in post-petition [litigation] with a creditor while at the same time denying the creditor the right even to include its post-petition fees in its unsecured claim.").

<sup>52</sup> See Ray Geoffroy, Comment, *Show Me the Money: The Debate over Creditors' Postpetition Attorneys' Fees*, 14 BANKR. DEV. J. 425, 457 (1998).

<sup>53</sup> *Id.*

allowable claim<sup>54</sup> against the bankruptcy estate, has a secured interest in estate property that is worth more than the amount of the creditor's claim,<sup>55</sup> the creditor's secured claim may include reasonable attorneys' fees—to the extent of the value of the security—if provided for by contractual agreement or state law.<sup>56</sup> Debate among courts and commentators has developed regarding the effect of § 506(b) on unsecured and undersecured—as opposed to oversecured—creditors' claims for postpetition attorneys' fees, which has been referred to as the *United Merchants*<sup>57</sup> issue.<sup>58</sup> This debate began before the Supreme Court's decision in *Travelers*,<sup>59</sup> and has continued with renewed force since *Travelers* was decided.<sup>60</sup>

On one side of the debate are those who take the position that § 506(b) precludes awarding postpetition attorneys' fees to unsecured and undersecured creditors. There have been relatively few cases supporting this position since *Travelers* was decided, but of those that have, *In re Electric Machinery*<sup>61</sup> is most often cited.<sup>62</sup> There have been several arguments advanced in support of the *Electric Machinery* position, including appeals to all of the policy concerns noted above regarding the equal treatment of creditors and case administration concerns.<sup>63</sup> The major legal argument asserted in support of the *Electric Machinery* position is the principle of *expressio unius est exclusio alterius*—one expression is the exclusion of the others.<sup>64</sup> The argument

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<sup>54</sup> Allowance of a claim in bankruptcy is governed by 11 U.S.C. § 502 (2012).

<sup>55</sup> Such a creditor will hereinafter be referred to as an “oversecured creditor.”

<sup>56</sup> 11 U.S.C. § 506(b) provides:

To the extent that an allowed secured claim is secured by property the value of which . . . 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.

<sup>57</sup> *United Merchs. & Mfrs., Inc. v. Equitable Life Assurance Soc'y of the U.S. (In re United Merchs. & Mfrs., Inc.)*, 674 F.2d 134 (2d Cir. 1982).

<sup>58</sup> Compare Geoffroy, *supra* note 52 (arguing that § 506(b) does not preclude unsecured creditors from claiming postpetition attorneys' fees, relying heavily on *United Merchants*), with Scarberry, *supra* note 6, at 614 (arguing that § 506(b), in conjunction with other sections of the Code, does preclude unsecured creditors from claiming postpetition attorneys' fees, and referring to the problem as the *United Merchants* issue).

<sup>59</sup> See Geoffroy, *supra* note 52 (discussing the debate in 1998).

<sup>60</sup> For a summary of recent court decisions demonstrating continued disagreement on the issue, see MARGARET A. MAHONEY, AM. LAW INST., POSTPETITION ATTORNEYS' FEES TO UNSECURED CREDITORS (2014); see also Scarberry, *supra* note 6; Jennifer M. Taylor & Christopher J. Mertens, *Travelers and the Implications on the Allowability of Unsecured Creditors' Claims for Post-Petition Attorneys' Fees Against the Bankruptcy Estate*, 81 AM. BANKR. L.J. 123 (2007).

<sup>61</sup> *In re Elec. Mach. Enters.*, 371 B.R. 549, 553 (Bankr. M.D. Fla. 2007).

<sup>62</sup> MAHONEY, *supra* note 60.

<sup>63</sup> See *supra* notes 36–47 and accompanying text.

<sup>64</sup> See *Pride Cos. v. Johnson (In re Pride Cos.)*, 285 B.R. 366, 372 (Bankr. N.D. Tex. 2002).

is that § 506(b) permits contractually provided attorneys' fees to be awarded with regard to oversecured claims, but does not mention unsecured claims.<sup>65</sup> Therefore, the negative pregnant<sup>66</sup> of § 506(b) is that contractually authorized attorneys' fees may not be awarded to those who do not have oversecured claims—that is, unsecured and undersecured creditors.<sup>67</sup> Commentators have also offered more subtle arguments suggesting that attorneys' fees should be precluded based on § 506(b) in conjunction with other sections of the Bankruptcy Code.<sup>68</sup>

On the other side of the debate are those who take the position that § 506(b) cannot be understood to preclude attorneys' fee awards to unsecured and undersecured creditors. *United Merchants*<sup>69</sup> is credited as the origin of this position.<sup>70</sup> In *United Merchants*, the court explained that neither § 506(b) nor the legislative history surrounding its enactment had anything to say about unsecured creditors' contractual claims for attorneys' fees.<sup>71</sup> Although the argument was originally stated in dicta,<sup>72</sup> other cases have subsequently followed the example set by *United Merchants*.<sup>73</sup> The basic argument is that § 502 (entitled "allowance of claims or interests") addresses whether a claim should be allowed, while § 506 (entitled "determination of secured status") addresses only whether a claim should be given secured status or not.<sup>74</sup> Therefore, courts must look only to § 502 to determine whether claims for attorneys' fees are allowed, without making inferences based on other sections, such as § 506(b), that are not relevant to the allowability of claims.<sup>75</sup> Proponents of the *United Merchants* position have also invoked the considerations of economic freedom, noted above, that favor general allowance of contractual attorneys' fee claims.<sup>76</sup> The

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<sup>65</sup> *Id.*

<sup>66</sup> The "negative pregnant" is a rule of construction, articulated by the Supreme Court. *Field v. Mans*, 516 U.S. 59, 67 (1995) ("[U]nder that rule[,] . . . an express statutory requirement in one [section of a statute], contrasted with statutory silence in another [section], shows an intent to confine the requirement to the specified instance.").

<sup>67</sup> See *In re Pride Cos.*, 285 B.R. at 372.

<sup>68</sup> See generally Scarberry, *supra* note 6 (summarizing many of the arguments made by others and proposing his own textual argument for precluding attorneys' fees based on §§ 502(b), 506(a), and 506(b) of the Code).

<sup>69</sup> *United Merchs. & Mfrs., Inc. v. Equitable Life Assurance Soc'y of the U.S. (In re United Merchs. & Mfrs., Inc.)*, 674 F.2d 134 (2d Cir. 1982).

<sup>70</sup> See Geoffroy, *supra* note 52, at 427.

<sup>71</sup> *United Merchs. & Mfrs.*, 674 F.2d at 138.

<sup>72</sup> *Id.* at 138 n.6 (acknowledging that § 506(b) took effect after the petition was filed and, therefore, did not govern the case).

<sup>73</sup> See, e.g., *Ogle v. Fid. & Deposit Co. of Md.*, 586 F.3d 143, 146 (2d Cir. 2009); *Qmect, Inc. v. Burlingame Capital Partners II, L.P. (In re Qmect, Inc.)*, 368 B.R. 882, 885–86 (Bankr. N.D. Cal. 2007).

<sup>74</sup> See *Qmect*, 368 B.R. at 884–85.

<sup>75</sup> See *id.*

<sup>76</sup> See *supra* notes 48–53 and accompanying text.

*Fobian* line of cases, and its subsequent rejection by the Supreme Court in *Travelers*, raises important implications for the policy concerns raised by both sides of this debate.

## II. CASE ANALYSIS

### A. *The Travelers Case*

#### 1. Background Facts

The *Fobian* rule was the central focus in the Supreme Court's *Travelers* opinion. The *Travelers* case arose from the bankruptcy of the Pacific Gas & Electric Company (PG&E), a privately owned San Francisco-based utility company.<sup>77</sup> Prior to PG&E's bankruptcy, Travelers Casualty and Surety Company of America (Travelers) had issued a \$100 million surety bond (the Bond) on PG&E's behalf, which guaranteed PG&E's payment of workers' compensation benefits as required by California state law.<sup>78</sup> The Bond made Travelers liable for workers' compensation benefits if PG&E defaulted on its obligation to make payments.<sup>79</sup> In consideration for Travelers' agreement to post the Bond on its behalf, PG&E agreed to indemnify Travelers<sup>80</sup> if Travelers was required to make any payments under the Bond. The agreements provided that PG&E would indemnify Travelers against any loss incurred in connection with the Bond, including any attorneys' fees incurred in enforcing its contractual rights.<sup>81</sup>

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<sup>77</sup> PG&E is one of the largest utility companies of its kind in the United States, currently supplying natural gas and electricity to approximately sixteen million people throughout northern and central California and employing approximately 20,000 workers. See *Company Profile*, PG&E, <http://www.pge.com/en/about/company/profile/index.page> (last visited Feb. 23, 2016).

<sup>78</sup> *Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co.*, 549 U.S. 443, 446 (2007). PG&E was required by the State of California to assure the payment of workers' compensation benefits to its employees either by purchasing workers' compensation insurance or by obtaining consent from the Director of Industrial Relations to self-insure. See CAL. LAB. CODE § 3700 (West 2011); Brief for Petitioner at 6, *Travelers*, 549 U.S. 443 (No. 05-1429), 2006 WL 3387940. PG&E chose the latter option, and in order to obtain the Director's consent, PG&E was required to post adequate security to the California Department of Industrial Relations by posting a bond. See CAL. LAB. CODE § 3701(e); Brief for Petitioner, *supra*, at 6.

<sup>79</sup> *Travelers*, 549 U.S. at 446 n.1.

<sup>80</sup> *Id.* at 446.

<sup>81</sup> The contract provision, as provided by Travelers' attorneys, reads:

NOW, THEREFORE, in consideration of the execution of any [of the surety bonds] . . . we, the Undersigned [PG&E], agree and bind ourselves . . . as follows . . . [to] indemnify, and keep indemnified, and hold and save harmless the Surety [Travelers] against all demands, claims, loss, costs, damages, expenses and

The litigation between Travelers and PG&E began after PG&E filed a voluntary Chapter 11<sup>82</sup> bankruptcy petition.<sup>83</sup> PG&E was to continue to operate its business as a debtor in possession,<sup>84</sup> and, on the same day that the bankruptcy petition was filed, obtained an order from the bankruptcy court authorizing it to continue to pay workers' compensation benefits in accordance with its prepetition obligations.<sup>85</sup> As noted by Travelers, that order did not itself order PG&E to make the payments,<sup>86</sup> but only permitted PG&E, as a debtor in possession, to make the payments without breaching its duties to the bankruptcy estate.<sup>87</sup>

In response to PG&E's Chapter 11 petition, Travelers filed a proof of claim to protect its rights to indemnification and subrogation<sup>88</sup> in the event that PG&E stopped making the workers' compensation payments

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attorney's fees whatever and all liability therefor, sustained or incurred by the Surety [Travelers] by reason of executing . . . [the Bonds] . . . or sustained or incurred by reason of making any investigation on account thereof, prosecuting or defending any action brought in connection therewith, . . . recovering or attempting to recover any salvage in connection therewith or enforcing by litigation or otherwise any of the agreements herein contained.

Brief for Petitioner, *supra* note 78, at 7 (alterations in original). The Supreme Court described the agreements as providing for "any attorney's fees incurred in pursuing, *protecting*, or litigating Travelers' rights in connection with th[e] bonds." *Travelers*, 549 U.S. at 446 (emphasis added). The contract provision itself, however, does not mention the *protection* of rights. It appears that the Court borrowed this wording from Travelers' summary of the provision supplied in its brief and petition for a writ of certiorari. See Brief for Petitioner, *supra* note 78, at 6; Petition for a Writ of Certiorari at \*i, *Travelers*, 549 U.S. 443 (No. 05-1429), 2006 WL 1272597.

<sup>82</sup> 11 U.S.C. §§ 1101–1174 (2012).

<sup>83</sup> *Travelers*, 549 U.S. at 445–46.

<sup>84</sup> A debtor in possession is a Chapter 11 or 12 debtor that continues to operate its business as a fiduciary to the bankruptcy estate. See *Debtor-in-Possession*, BLACK'S LAW DICTIONARY (10th ed. 2014); see also 11 U.S.C. § 1101(1) (defining a debtor in possession for the purposes of Chapter 11); § 1107(a) (describing the rights, powers, and duties of a debtor in possession); § 1108 (authorizing a debtor in possession to operate its business).

<sup>85</sup> See *Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co. (In re Pac. Gas & Elec. Co.)*, No. C-03-3499 PJH, 2004 WL 5167592, at \*1 (N.D. Cal. Feb. 18, 2004). The Bankruptcy Court order can be found at Joint Appendix at \*24A, *Travelers*, 549 U.S. 443 (No. 05-1429), 2006 WL 3404627.

<sup>86</sup> Travelers emphasized this point in its brief. See Brief for Petitioner, *supra* note 78, at 8.

<sup>87</sup> See Joint Appendix, *supra* note 85, at \*24A. "First-day motions," of the type employed by PG&E, are a common and important part of transitioning into the reorganization process. See George W. Kuney, *Hijacking Chapter 11*, 21 EMORY BANKR. DEV. J. 19, 74–75 (2004). A debtor in possession will almost always require employees to continue to operate the business. *Id.* at 75. However, because employees are considered creditors of the bankrupt debtor, the debtor must obtain authorization from the court in order to pay wages or honor employee benefits. *Id.* Courts usually approve first-day motions because they are essential to retain employees. *Id.*

<sup>88</sup> Travelers' subrogation right entitled it to stand in the shoes of the injured employees whose payments it may have had to cover, and assert their claims against PG&E. Brief for Respondent at 3, *Travelers*, 549 U.S. 443 (No. 05-1429), 2006 WL 3825666; see also *Subrogation*, BLACK'S LAW DICTIONARY (10th ed. 2014).

in the future; in which case Travelers would then have been required to make payments under the Bond.<sup>89</sup> At the time the claim was filed, however, Travelers had not had to assume any liability pursuant to the Bond.<sup>90</sup> It was undisputed that PG&E had not defaulted on its obligations to make payments, and there was no suggestion that, at the time of the filing, PG&E was in breach of its agreement with Travelers.<sup>91</sup>

Nevertheless, when PG&E filed its first plan of reorganization<sup>92</sup> and disclosure statement,<sup>93</sup> Travelers objected.<sup>94</sup> Travelers claimed that the disclosure statement did not provide adequate information regarding how the plan would affect PG&E's obligations to make the workers' compensation payments or how it would affect Travelers' rights with respect to the Bond.<sup>95</sup> As a result, the parties, with the approval of the bankruptcy court, agreed to insert language into the plan of reorganization and disclosure statement to address Travelers' concerns.<sup>96</sup>

A second dispute arose concerning the final language that was ultimately added to the plan of reorganization and disclosure statement, and the significance of PG&E's subsequent objection to allowing Travelers' claim,<sup>97</sup> resulting in further litigation between the parties.<sup>98</sup> The dispute was ultimately resolved by an agreed stipulation that Travelers' claims would be disallowed under § 502(e)(1)(B) of the

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<sup>89</sup> *In re Pacific Gas*, 2004 WL 5167592, at \*1.

<sup>90</sup> *Id.*

<sup>91</sup> *See Travelers*, 549 U.S. at 446; *In re Pacific Gas*, 2004 WL 5167592, at \*1.

<sup>92</sup> A plan of reorganization is a detailed program which governs the debtor's reorganization in a Chapter 11 bankruptcy proceeding. *See Bankruptcy Plan*, BLACK'S LAW DICTIONARY (10th ed. 2014). A plan of reorganization will specify the treatment of creditors' claims, and the means by which the debtor will satisfy the terms of the plan. *See* 11 U.S.C. § 1123 (2012) (describing the contents of a plan of reorganization).

<sup>93</sup> A disclosure statement is intended to provide creditors with the information necessary to determine whether they ought to accept the plan. *See Prudential Ins. Co. of Am. v. Monnier Bros. (In re Monnier Bros.)*, 755 F.2d 1336, 1342 (8th Cir. 1985); *see also* 11 U.S.C. § 1125.

<sup>94</sup> *In re Pacific Gas*, 2004 WL 5167592, at \*1.

<sup>95</sup> *Id.*; Brief for Petitioner, *supra* note 78, at 12–13.

<sup>96</sup> *Travelers*, 549 U.S. at 446; *In re Pacific Gas*, 2004 WL 5167592, at \*1. At the hearing, the parties agreed that the added language would create a new creditor class consisting of the workers who may be entitled to benefits—and also Travelers, to the extent that it would take over those workers' claims by subrogation—and that class's contingent claims would not be impaired by the reorganization. *See* Joint Appendix, *supra* note 85, at \*42a–45a; Brief for Petitioner, *supra* note 78, at 13–15.

<sup>97</sup> *Compare* Brief for Petitioner, *supra* note 78, at 15–16 (asserting that PG&E unilaterally modified the negotiated language and that PG&E's objection to Travelers' claim was an attempt to impair its rights), *with* Brief for Respondent, *supra* note 88, at 5–7 (asserting that the negotiated “comfort language” was consistently accompanied by PG&E's reservation of its right to object to subrogation claims, and arguing that subrogation was never a valid claim).

<sup>98</sup> *Travelers*, 549 U.S. at 446–47; *In re Pacific Gas*, 2004 WL 5167592, at \*1.

Code.<sup>99</sup> It was agreed that Travelers would not be prejudiced if Traveler's sought reconsideration of the disallowance in the event that PG&E did, in fact, default on its obligations to pay workers' compensation benefits in the future and Travelers was then required to make payments on the Bond.<sup>100</sup> Neither would the disallowance affect Travelers' subrogation rights under applicable law.<sup>101</sup> It was also agreed that PG&E would retain the right to oppose reconsideration of Travelers' claim or any asserted subrogation right.<sup>102</sup>

Pursuant to the stipulation, Travelers' withdrew its original claims against the estate.<sup>103</sup> Travelers then filed an amended proof of claim requesting attorneys' fees and costs, pursuant to the indemnity agreement, for its expenses in litigating the original claims—totaling over \$167,000—to which PG&E objected.<sup>104</sup>

## 2. Court Decisions

The bankruptcy court sustained PG&E's objection and disallowed Travelers' claim for attorneys' fees and costs.<sup>105</sup> Citing *Fobian*, the bankruptcy court stated that Travelers' state law rights did not appear to be implicated such that they could invoke the attorneys' fee provision in the indemnity agreement.<sup>106</sup> The court stated that “[a]s a matter of bankruptcy law,” the attorneys' fees could not be assessed against PG&E.<sup>107</sup>

On appeal, the district court framed the issue in terms of “[w]hether the bankruptcy court erred when it sustained PG&E's objection to Travelers' claim for attorney's fees *as a matter of bankruptcy law*.”<sup>108</sup> The court first noted that the attorneys' fee claim did not arise from any prepetition collection efforts or litigation related

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<sup>99</sup> *Travelers*, 549 U.S. at 447; *In re Pacific Gas*, 2004 WL 5167592, at \*1. 11 U.S.C. § 502(e)(1)(B) (2012), which deals with indemnity claims, provides in relevant part that:

[T]he court shall disallow any claim for reimbursement or contribution of an entity that is liable with the debtor on or has secured the claim of a creditor, to the extent that . . . such claim for reimbursement or contribution is contingent as of the time of allowance or disallowance of such claim for reimbursement or contribution . . . .

<sup>100</sup> *In re Pacific Gas*, 2004 WL 5167592, at \*1.

<sup>101</sup> *Id.*

<sup>102</sup> *Id.*

<sup>103</sup> *Id.*

<sup>104</sup> *Travelers*, 549 U.S. at 447; *In re Pacific Gas*, 2004 WL 5167592, at \*2.

<sup>105</sup> *In re Pacific Gas*, 2004 WL 5167592, at \*2; Joint Appendix, *supra* note 85, at \*143a.

<sup>106</sup> Joint Appendix, *supra* note 85, at \*142a.

<sup>107</sup> *Id.* at \*142a–143a (“[A]s a matter of bankruptcy law, [the attorneys' fees] cannot be assessed against the Debtor . . .”).

<sup>108</sup> *In re Pacific Gas*, 2004 WL 5167592, at \*2 (emphasis added).

to the bond or indemnity agreements because PG&E had not breached its obligations under the contract, which may have entitled Travelers to attorneys' fees.<sup>109</sup> The district court then affirmed the bankruptcy court's ruling,<sup>110</sup> expressing its concern that it would be inappropriate to allow a bankruptcy creditor to import state law into an exclusively federal setting.<sup>111</sup>

The Ninth Circuit's discussion of this issue was brief.<sup>112</sup> The court affirmed the district court with very little analysis other than reference to *Fobian* and another of its own prior opinions discussing *Fobian*.<sup>113</sup>

The Supreme Court granted Travelers' petition for certiorari, noting a perceived conflict among the Courts of Appeals regarding whether federal bankruptcy law precluded an unsecured creditor from recovering attorneys' fees authorized by a prepetition contract and incurred in postpetition litigation.<sup>114</sup> The Court began its analysis by observing that the Bankruptcy Code requires a bankruptcy court to allow a claim, except to the extent that the claim implicates one of the nine exceptions enumerated in § 502(b), the only one of which that could reasonably have applied to the case at issue being § 502(b)(1).<sup>115</sup> The Court determined that the lower courts did not conclude that Travelers' claim for attorneys' fees was unenforceable under § 502(b)(1)

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<sup>109</sup> *Id.* at \*3–4.

<sup>110</sup> The court did not hear oral argument on the issue, determining that the facts and legal arguments were adequately provided by the briefs and record. *See id.* at \*6.

<sup>111</sup> *Id.*

<sup>112</sup> The entire opinion consisted of five relatively short paragraphs. *See Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co.*, 167 F. App'x 593 (9th Cir. 2006).

<sup>113</sup> *See id.* The Ninth Circuit affirmed the bankruptcy and district court “[f]or the reasons set forth in [*DeRoche v. Ariz. Indus. Comm’n (In re DeRoche)*, 434 F.3d 1188 (9th Cir. 2006)].” *Travelers v. Pacific Gas*, 167 F. App'x at 593. In *DeRoche*, the bankrupt debtors incurred over \$30,000 in attorneys' fees successfully litigating the dischargeability of a debt in a Chapter 7 proceeding. *DeRoche*, 434 F.3d at 1190. The debt consisted of sums paid to an injured employee of the debtors by an Arizona state entity. *Id.* After the debt was discharged, the debtor requested an award of attorneys' fees against the state entity pursuant to an Arizona state statute that provided for such fees in order to protect individual citizens against unwarranted litigation pursued by the state. *Id.* at 1191–92. The *DeRoche* court denied the fee request, stating “that no fees are available under state law for litigation of substantive federal bankruptcy issues” and that the “state statute is irrelevant to this analysis.” *Id.*

<sup>114</sup> *Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co.*, 549 U.S. 443, 448 (2007). The Court cited a Fourth Circuit case, *Three Sisters Partners, L.L.C. v. Harden (In re Shangra-La, Inc.)*, 167 F.3d 843 (4th Cir. 1999), as evidencing a circuit split on the issue. *Travelers*, 549 U.S. at 448. For an interesting discussion explaining that no circuit split existed on the particular issues involved in either *Travelers* or *DeRoche* when *Travelers* filed its petition for certiorari, see Scarberry, *supra* note 6, at 629–30 (arguing that a Sixth Circuit case, decided the day after the last brief was filed on *Travelers*' petition, both created a true circuit split on the issue involved in *Travelers* and demonstrated that there was not previously a circuit split on that issue).

<sup>115</sup> *Travelers*, 549 U.S. at 449. § 502(b)(1) disallows any “claim [that] is unenforceable against the debtor and property of the debtor, under any agreement or applicable law for a reason other than because such claim is contingent or unmatured.” 11 U.S.C. § 502(b)(1) (2012).



as a matter of applicable nonbankruptcy law or under any provision of the Bankruptcy Code.<sup>116</sup> As a result, the Court vacated the lower court's judgment and remanded the case.<sup>117</sup>

In its opinion, the Court noted that PG&E did not defend the *Fobian* rule in its brief or at oral argument,<sup>118</sup> but argued instead that § 506(b) of the Code categorically disallows unsecured claims for attorneys' fees.<sup>119</sup> The Court, however, declined to express any opinion on that issue.<sup>120</sup> Additionally, the Court noted that its decision did not address whether "other principles of bankruptcy law might provide an independent basis for disallowing Travelers' claim for attorney's fees."<sup>121</sup> Similarly, the Court declined to address the validity of Travelers' claim on the basis of contract interpretation or enforceability.<sup>122</sup> As noted above, the Ninth Circuit had affirmed the denial of postpetition attorneys' fees by curtly relying on its earlier opinion in *Fobian*.<sup>123</sup> As a result, the Supreme Court felt compelled to reverse, taking the undefended *Fobian* rule to be a piece of federal judicial legislation.<sup>124</sup> The following Section analyzes whether the Supreme Court accurately assessed the status of *Fobian*.

## B. *The Fobian Decision*

### 1. Background Facts

In *Fobian*, the creditor, Western Farm Credit Bank (Western), was seeking attorneys' fees and costs against two solvent debtors in bankruptcy, Elmer and Elsie Fobian.<sup>125</sup> The Fobians were rice farmers who owned a 70.5 acre plot of land in Glenn County, California.<sup>126</sup> Western was the holder of a promissory note, secured by a deed of trust to the Fobians' land.<sup>127</sup> When the Fobians filed a petition for relief under

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<sup>116</sup> *Travelers*, 549 U.S. at 451.

<sup>117</sup> *Id.* at 456.

<sup>118</sup> *Id.* at 454.

<sup>119</sup> For a synopsis of the general argument, see *supra* Section I.C.

<sup>120</sup> *Travelers*, 549 U.S. at 455. The Court explained that it "granted certiorari to resolve a conflict among the lower courts regarding the *Fobian* rule" only, and that the § 506(b) issue was neither addressed by the lower courts nor presented in the parties' briefs concerning the petition for certiorari. *Id.*

<sup>121</sup> *Id.* at 456.

<sup>122</sup> See *id.* at 455 n.5.

<sup>123</sup> See *infra* Section II.B.2.c.

<sup>124</sup> See *infra* Section II.B.3.

<sup>125</sup> See *Fobian v. W. Farm Credit Bank (In re Fobian)*, 951 F.2d 1149, 1150 (9th Cir. 1991).

<sup>126</sup> *Id.*

<sup>127</sup> *Id.*

Chapter 12 of the Bankruptcy Code,<sup>128</sup> Western filed a proof of claim<sup>129</sup> for over \$191,000, to which the Fobians did not object.<sup>130</sup> However the land was estimated by the Fobians to be valued at \$70,500, rendering the debt undersecured.<sup>131</sup>

The Fobians submitted a plan for reorganization in which Western would be given a choice between two alternatives regarding its claim.<sup>132</sup> The first alternative allowed the Fobians to refinance their debt and write off any balance over \$70,500—that is, the estimated value of the land.<sup>133</sup> The second alternative allowed the Fobians to surrender the property under § 1225(a)(5)(C),<sup>134</sup> in full satisfaction of the debt.<sup>135</sup>

Western objected to confirmation of the plan on the grounds that it did not take into consideration the unsecured portion of its plan—that is, the difference between the amount of its claim and the value of the property.<sup>136</sup> Western also claimed that the plan did not meet the requirements of § 1225(a)(4) because the plan did not guarantee Western at least as much of its claim as a Chapter 7 liquidation would have yielded.<sup>137</sup> The plan was confirmed by the bankruptcy court, but

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<sup>128</sup> 11 U.S.C. §§ 1201–1231 (2012). At the time the *Fobian* case was decided, only farmers qualified for protection under Chapter 12 of the Bankruptcy Code. See Bankruptcy Judges, United States Trustees, and Family Farmer Bankruptcy Act of 1986, Pub. L. 99-554, sec. 253, § 109, 100 Stat. 3088, 3105 (codified as amended at 11 U.S.C. § 109 (2012)).

<sup>129</sup> A claim is defined broadly by the Code, in part, as a “right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured.” 11 U.S.C. § 101(5)(A). A proof of claim is a creditor’s written statement of the basis and amount of its claim. *Proof of Claim*, BLACK’S LAW DICTIONARY (10th ed. 2014). A creditor must file a proof of claim, under § 501(a), in order to enforce its claim against the bankruptcy estate. See 11 U.S.C. § 502(a).

<sup>130</sup> *Fobian*, 951 F.2d at 1150.

<sup>131</sup> *Id.*

<sup>132</sup> *Id.* at 1150–51.

<sup>133</sup> *Id.* at 1151.

<sup>134</sup> 11 U.S.C. § 1225(a)(5)(C) (“Except as provided in subsection (b), the court shall confirm a plan if . . . with respect to each allowed secured claim provided for by the plan . . . the debtor surrenders the property securing such claim to such holder . . .”). This is the same language that was in effect at that time. See Bankruptcy Judges, United States Trustees, and Family Farmer Bankruptcy Act of 1986, Pub. L. 99-554, sec. 255, 100 Stat. 3088, 3110–11 (codified as amended at 11 U.S.C. § 1225 (2012)).

<sup>135</sup> *Fobian*, 951 F.2d at 1151.

<sup>136</sup> *Id.*

<sup>137</sup> *Id.* § 1225(a)(4) currently provides:

Except as provided in subsection (b), the court shall confirm a plan if . . . the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under chapter 7 of this title on such date . . . .

11 U.S.C. § 1225(a)(4). This is the same language that was in effect at that time. See § 255, 100 Stat. at 3110–11. Because the Fobians were solvent, Western would have been paid in full in a Chapter 7 liquidation. *Fobian*, 951 F.2d at 1152.

that ruling was reversed on Western's appeal to a bankruptcy appellate panel (the BAP).<sup>138</sup> On the Fobians' appeal from that ruling, the Ninth Circuit affirmed the BAP's decision in favor of Western on the merits.<sup>139</sup>

In addition to asking the Ninth Circuit to uphold the reversal of the plan's confirmation, Western requested attorneys' fees incurred while litigating its claim.<sup>140</sup> Western asserted that an award of attorneys' fees was appropriate based on provisions in the promissory note and the deed of trust, "which provide[d] for the payment of fees . . . incurred in collection of amounts due or enforcement of rights."<sup>141</sup> It is the Ninth Circuit's denial of attorneys' fees—and, more particularly, its reasons for denial—for which the *Fobian* case has come to be known.<sup>142</sup>

The Ninth Circuit denied Western's request for attorneys' fees on the grounds that the litigation concerned only the proper application of § 506 and § 1225 of the Bankruptcy Code, rather than the enforcement of any contract obligation.<sup>143</sup> The court held that postpetition attorneys' fees are not available in a bankruptcy action pursuant to a contract when the issues litigated solely involve federal bankruptcy law.<sup>144</sup>

## 2. Analysis of the Ninth Circuit's Holding

### a. The Language

The *Fobian* court's analysis of the attorneys' fees issue spanned a whopping three paragraphs, the longest of which was four sentences long—excluding citations—and the shortest being a single sentence.<sup>145</sup> Because the court's analysis was so truncated, the reasoning behind the court's holding is not entirely apparent at first blush. Therefore, a careful inspection of the court's analysis is necessary in order to tease out the court's meaning.

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<sup>138</sup> *Fobian*, 951 F.2d at 1151. A bankruptcy appellate panel is a specialized appellate tribunal composed of bankruptcy judges sitting in three-judge panels. Thomas E. Carlson, *The Case for Bankruptcy Appellate Panels*, 1990 BYU L. REV. 545, 545. An appeal from a bankruptcy court's ruling in a circuit that has established a bankruptcy appellate panel may be heard by the panel instead of the district court. See Paul M. Baisier & David G. Epstein, *Resolving Still Unresolved Issues of Bankruptcy Law: A Fence or an Ambulance*, 69 AM. BANKR. L.J. 525, 528 (1995). For a brief discussion about the lack of precedential value of BAP decisions, see *id.* at 529–31.

<sup>139</sup> *Fobian*, 951 F.2d at 1153.

<sup>140</sup> *Id.*

<sup>141</sup> *Id.* Unfortunately, the precise language of the provisions was not provided by the court. The quoted language reflects the Ninth Circuit's apparent paraphrase of the provisions.

<sup>142</sup> See *infra* note 151 and accompanying text.

<sup>143</sup> *Fobian*, 951 F.2d at 1153.

<sup>144</sup> *Id.*

<sup>145</sup> See *id.*

The court began its analysis by articulating its understanding of the relevant law generally.<sup>146</sup> The first paragraph consisted of two sentences.<sup>147</sup> The first stated: “Where a contract or statute provides for an award of attorneys’ fees, a creditor *may be entitled* to such fees in bankruptcy proceedings.”<sup>148</sup> The second sentence stated: “Such an award *is governed* by state law.”<sup>149</sup> The first sentence does not commit the court to any particular position. If a creditor *may* be entitled to attorneys’ fees, it stands to reason that a creditor also *may not* be entitled to fees. The second sentence, however, is less equivocal. The second sentence clearly states that an award of attorneys’ fees, provided by a contract or statute, *is governed* by state law.<sup>150</sup> In contrast to the first sentence, the court does not qualify its statement. Therefore, in the court’s view, all such awards *are* governed by state law. This point is extremely important in order to understand the court’s holding.

The second paragraph represented the court’s statement of the law as applicable to the particular facts before it. This articulation of the law is what eventually came to be known as the *Fobian* rule.<sup>151</sup> The only sentence of that paragraph reads: “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.”<sup>152</sup> The court begins this statement with the word “however,” which indicates that the statement is contrary to what was stated before.<sup>153</sup> Determining what this statement contrasts with provides insight into what the statement means. As noted above, the court unequivocally acknowledged that attorneys’ fee awards, provided for by a contract, *are* governed by state

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<sup>146</sup> *See id.*

<sup>147</sup> *See id.*

<sup>148</sup> *Id.* (emphasis added).

<sup>149</sup> *Id.* (emphasis added).

<sup>150</sup> *See id.*

<sup>151</sup> *E.g.*, BankBoston, N.A. v. Sokolowski (*In re Sokolowski*), 205 F.3d 532, 535 (2d Cir. 2000) (per curiam) (“[W]here 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.” (quoting *Fobian*, 951 F.2d at 1153)); *see also* Official Comm. of Unsecured Creditors v. Dow Corning Corp. (*In re Dow Corning Corp.*), 456 F.3d 668, 684 (6th Cir. 2006) (same); Owens v. Bolger (*In re Bolger*), 351 B.R. 165, 170 (Bankr. N.D. Okla. 2006) (same); Nw. Corp. v. Magten Asset Mgmt. Corp. (*In re Nw. Corp.*), 326 B.R. 519, 524 (Bankr. D. Del. 2005) (same).

<sup>152</sup> *Fobian*, 951 F.2d at 1153. The exception for bad faith or harassment is external to the *Fobian* rule, as it is simply an articulation of the court’s inherent powers to award fees. *See supra* note 18.

<sup>153</sup> Oxford Dictionary defines “however” as an adverb “used to introduce a statement that contrasts with or seems to contradict something that has been said previously.” *However*, OXFORD DICTIONARIES, [http://www.oxforddictionaries.com/us/definition/american\\_english/however](http://www.oxforddictionaries.com/us/definition/american_english/however) (last visited Feb. 26, 2016).

law.<sup>154</sup> For that reason, it is unlikely that the court intended to directly contradict that proposition in the very next sentence. Rather, the court's statement should be understood to contrast with the first sentence of the first paragraph,<sup>155</sup> not the second.<sup>156</sup> The first sentence was stated in equivocal terms, making it reasonable to infer that the court intended to contrast that general language with the contrary, more specific counterstatement found in the second paragraph. In other words, the court was explaining that a creditor *may* be entitled to attorneys' fees, but not under the circumstances described. This statement is independent of, and does not contradict, the court's unqualified statement that such claims are "governed by state law."<sup>157</sup>

b. Prior Ninth Circuit Cases

In its articulation of the law, the Ninth Circuit distinguished litigation of "basic contract enforcement questions" from "issues peculiar to federal bankruptcy law," for the purpose of determining whether attorneys' fees were appropriate.<sup>158</sup> However, the court did not provide a separate explanation for why that particular distinction was proper. Rather, the court simply cited three of its own prior decisions as support.<sup>159</sup> Therefore, in order to put the *Fobian* court's holding in context, its language must be read not only with reference to the preceding paragraph, but also in light of a careful analysis of the cases the court cites to justify the *Fobian* rule.

i. *In re Coast Trading Co.*

*Coast Trading*,<sup>160</sup> the first case cited by the *Fobian* court, involved a debt between a grain wholesaler and a grain broker.<sup>161</sup> The bankrupt party was the broker, who had entered into two agreements to purchase grain, which the wholesaler was to deliver directly to the broker's clients.<sup>162</sup> When the broker filed a petition in bankruptcy, the wholesaler had not received payment for the grain because the broker's check had bounced.<sup>163</sup>

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<sup>154</sup> See *Fobian*, 951 F.2d at 1153.

<sup>155</sup> "Where a contract or statute provides for an award of attorneys' fees, a creditor may be entitled to such fees in bankruptcy proceedings." *Id.*

<sup>156</sup> "Such an award is governed by state law." *Id.*

<sup>157</sup> *Id.*

<sup>158</sup> See *id.*

<sup>159</sup> See *id.* (citing *Johnson v. Righetti (In re Johnson)*, 756 F.2d 738 (9th Cir. 1985); *Collingwood Grain, Inc. v. Coast Trading Co. (In re Coast Trading Co.)*, 744 F.2d 686 (9th Cir. 1984); *Grove v. Fulwiler (In re Fulwiler)*, 624 F.2d 908 (9th Cir. 1980) (per curiam)).

<sup>160</sup> *In re Coast Trading Co.*, 744 F.2d 686.

<sup>161</sup> See *id.* at 688.

<sup>162</sup> *Id.*

<sup>163</sup> *Id.* at 688–89.

The main issue litigated by the parties was whether the wholesaler had a right to reclaim the grain from the broker upon the broker's bankruptcy petition, under § 546(c) of the Bankruptcy Code.<sup>164</sup> If such was the case, the wholesaler would have been entitled to an administrative priority to the funds paid by the broker's clients into the estate because the wholesaler was prevented by that sale from asserting its right to reclaim the actual grain.<sup>165</sup> Both parties also requested an award of attorneys' fees.<sup>166</sup>

After resolving the disputed bankruptcy law issues, the Ninth Circuit<sup>167</sup> held that neither party was entitled to attorneys' fees.<sup>168</sup> The court noted that if either party had a right to attorneys' fees, that right must be premised on applicable state law.<sup>169</sup> Both parties had requested attorneys' fees pursuant to Oregon state statutes.<sup>170</sup> However, the court determined that the statutes were inapplicable, leaving neither party with a basis for their attorneys' fee claims.<sup>171</sup>

One of the statutes provided for an award of attorneys' fees to the prevailing party on an action to enforce a contract, if the contract specifically provides for attorneys' fees to be awarded to one of the parties.<sup>172</sup> The contracts at issue did provide for attorneys' fees to be awarded,<sup>173</sup> however the court held that litigation concerning the wholesaler's entitlement to priority on its contract claim was not an action to enforce a contract, so the statute was inapplicable and an award of attorneys' fees was not authorized.<sup>174</sup> The court explained that determining the applicability of bankruptcy law to a particular contract is not a question regarding the enforcement of contract rights, but is

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<sup>164</sup> *Id.*

<sup>165</sup> *Id.*

<sup>166</sup> *Id.* at 693.

<sup>167</sup> Interestingly, the opinion was written by Justice Kennedy, then a judge on the Ninth Circuit, who later signed on to the Supreme Court's unanimous decision in *Travelers*. See *id.* at 688; see also *Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co.*, 549 U.S. 443 (2007).

<sup>168</sup> *Coast Trading*, 744 F.2d at 693.

<sup>169</sup> *Id.*

<sup>170</sup> *Id.*

<sup>171</sup> *Id.*

<sup>172</sup> *Id.* The statute, which has since been amended, stated that:

In any action or suit on a contract, where such contract specifically provides that attorney[s'] fees and costs incurred to enforce the provisions of the contract shall be awarded to one of the parties, the prevailing party, whether that party is the party specified in the contract or not, at trial or on appeal, shall be entitled to reasonable attorney[s'] fees in addition to costs and disbursements.

OR. REV. STAT. § 20.096(1), quoted in *Carlson v. Blumenstein*, 651 P.2d 710, 711 (Or. 1982).

<sup>173</sup> Unfortunately, the court did not provide the exact language of the parties' contracts.

<sup>174</sup> *Coast Trading*, 744 F.2d at 693 (“[T]he applicability of the bankruptcy laws to particular contracts is not a question of the enforceability of a contract but rather involves a unique, separate area of federal law.”).

rather a question regarding the enforcement of unique and separate federal rights.<sup>175</sup>

ii. *In re Fulwiler*

*Fulwiler*<sup>176</sup>—which was not only cited as authority by the *Fobian* court, but also invoked by the *Coast Trading* court<sup>177</sup>—involved a nondischargeability action in which a creditor attempted to set aside the discharge of a bankrupt debtor's \$26,000 loan debt, which the creditor alleged was procured by producing a false financial statement.<sup>178</sup> The debtor prevailed on the merits, but its request for attorneys' fees was denied by the bankruptcy court.<sup>179</sup> The only issue on appeal before the Ninth Circuit was whether the debtor should have been awarded attorneys' fees.<sup>180</sup>

The loan instrument provided for the creditor to be awarded attorneys' fees incurred in the collection of the note.<sup>181</sup> The debtor's claim for attorneys' fees was based on the same Oregon statute at issue in *Coast Trading*,<sup>182</sup> which made attorneys' fee clauses reciprocally binding.<sup>183</sup> As a result, the validity of the debtor's attorneys' fee claim depended on whether the creditor's attorneys' fee clause in the loan instrument was applicable to the litigation.<sup>184</sup>

The applicability of the attorneys' fee clause itself required that the relevant litigation must have been in enforcement of the loan agreement, or an "action on the contract."<sup>185</sup> The debtor took the position that the creditor's nondischargeability action was a claim to enforce the loan agreement.<sup>186</sup> The creditor argued that the action was more akin to a tort claim, with the amount of the contract obligation claimed as fraud damages.<sup>187</sup> The court disagreed with both

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<sup>175</sup> See *id.* The court also held that the parties' litigation of nonbankruptcy issues involving the parties' rights on rescission of the contract could not be considered contract enforcement. *Id.* The other Oregon statute, which has since been repealed, provided for an award of attorneys' fees to the prevailing party in an action on a dishonored check. See *id.* The court held that the litigation was not an action on a dishonored check because the broker's obligation to pay the debt was not in dispute; therefore, the statute was not applicable. *Id.*

<sup>176</sup> *Grove v. Fulwiler (In re Fulwiler)*, 624 F.2d 908 (9th Cir. 1980) (per curiam).

<sup>177</sup> *Coast Trading*, 744 F.2d at 693.

<sup>178</sup> *Fulwiler*, 624 F.2d at 909.

<sup>179</sup> *Id.*

<sup>180</sup> *Id.*

<sup>181</sup> *Id.* Again, the court unfortunately did not see fit to provide the precise language of the agreement.

<sup>182</sup> *Coast Trading*, 744 F.2d at 693 (citing OR. REV. STAT. § 20.096).

<sup>183</sup> *Fulwiler*, 624 F.2d at 909.

<sup>184</sup> *Id.*

<sup>185</sup> *Id.*

<sup>186</sup> *Id.*

<sup>187</sup> *Id.*

characterizations, holding that the creditor's claim constituted a purely federal cause of action, which could not be characterized as a contract or a tort claim.<sup>188</sup> As such, attorneys' fees could not be claimed pursuant to the Oregon statute.

The court further noted that in the absence of specific authorization, the court could only use its "inherent power . . . [in] equity to award [attorneys'] fees where the losing party ha[d] acted in bad faith, vexatiously, wantonly, or for oppressive reasons."<sup>189</sup> Because there was no finding of bad faith, and no other authorization for the attorneys' fee award applied, the court held that the debtor was not entitled to have its attorneys' fees paid by the creditor.<sup>190</sup>

iii. *In re Johnson*

*Johnson*,<sup>191</sup> also cited by the *Fobian* court, involved a request for relief from an automatic stay.<sup>192</sup> The debtors had previously filed a petition for reorganization under Chapter 11 of the Bankruptcy Code.<sup>193</sup> The creditors, who had not been receiving payments on a promissory note from the debtors, which was secured by a deed of trust, filed their request for relief from stay under § 362(d)<sup>194</sup> in order to foreclose on their collateral.<sup>195</sup> The debtors succeeded in resisting the creditors' motion in the bankruptcy court and on appeal to the district court.<sup>196</sup> The only issue before the Ninth Circuit on appeal was whether the debtors were entitled to attorneys' fees for the costs of opposing the creditors' motion for relief from stay.<sup>197</sup>

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<sup>188</sup> *Id.* at 910.

<sup>189</sup> *Id.*

<sup>190</sup> *Id.*

<sup>191</sup> *Johnson v. Righetti (In re Johnson)*, 756 F.2d 738 (9th Cir. 1985).

<sup>192</sup> *Id.* at 739.

<sup>193</sup> *Id.*

<sup>194</sup> The statute in effect at that time stated that:

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay—

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest; or

(2) with respect to a stay of an act against property, if—

(A) the debtor does not have an equity in such property; and

(B) such property is not necessary to an effective reorganization.

See *Johnson*, 756 F.2d at 740 (quoting 11 U.S.C. § 362(d) (1982)). The current statute includes all of the language quoted above, with the addition of two more causes for granting relief. See 11 U.S.C. § 362(d) (2012).

<sup>195</sup> *Johnson*, 756 F.2d at 739.

<sup>196</sup> *Id.*

<sup>197</sup> *Id.*



Both the deed of trust and the promissory note, held by the creditors, contained attorneys' fee provisions.<sup>198</sup> Those provisions provided that the debtors were obligated to pay any attorneys' fees that the creditors incurred in enforcing those documents.<sup>199</sup> The debtors' claim for attorneys' fees was made pursuant to section 1717 of the California Civil Code.<sup>200</sup> Similarly to the Oregon statute at issue in *Coast Trading* and *Fulwiler*,<sup>201</sup> section 1717 provided that an attorneys' fee clause in a contract should be treated as reciprocally binding on both parties.<sup>202</sup>

The Ninth Circuit held that, because a motion for relief from an automatic stay could not be considered an "action on a contract," the state statute was inapplicable, leaving the debtors with no basis for their claim.<sup>203</sup> The court observed that the stay litigation did not involve the validity of a claim on a contract, so state law governing contractual relationships was not considered during the litigation.<sup>204</sup> Because state contract law was not relevant to the creditors' motion, the state statute was not relevant to the issue of attorneys' fees incurred defending against that motion.<sup>205</sup>

#### iv. Synthesis of Prior Ninth Circuit Cases

*Johnson*, *Fulwiler*, and *Coast Trading* (together, the pre-*Fobian* cases or the pre-*Fobian* courts) each dealt with the issue of postpetition attorneys' fee claims arising out of bankruptcy litigation.<sup>206</sup> Each court addressed the issue by determining that the relevant state law could not support the attorneys' fee claim under the circumstances.<sup>207</sup>

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<sup>198</sup> *Id.*

<sup>199</sup> *Id.*

<sup>200</sup> *Id.*; CAL. CIV. CODE § 1717(a) (West 2009).

<sup>201</sup> See *supra* notes 182–83 and accompanying text.

<sup>202</sup> As quoted by the court, the statute in effect at that time stated:

In any action on a contract, where the contract specifically provides that attorney's fees and costs, which are incurred to enforce the provisions of that contract, shall be awarded either to one of the parties or to the prevailing party, then the party who is determined to be the prevailing party, whether he or she is the party specified in the contract or not, shall be entitled to reasonable attorney's fees in addition to costs and necessary disbursements.

*Johnson*, 756 F.2d at 739 (emphasis omitted) (quoting CAL. CIV. CODE § 1717(a)). The current language of the statute remains substantially similar to that quoted above. See § 1717(a).

<sup>203</sup> *Johnson*, 756 F.2d at 740.

<sup>204</sup> *Id.*

<sup>205</sup> *Id.* at 741.

<sup>206</sup> See *id.* at 739; *Collingwood Grain, Inc. v. Coast Trading Co. (In re Coast Trading Co.)*, 744 F.2d 686, 693 (9th Cir. 1984); *Grove v. Fulwiler (In re Fulwiler)*, 624 F.2d 908, 908 (9th Cir. 1980).

<sup>207</sup> *Johnson*, 756 F.2d at 740 (stating that the attorneys' fee award was not appropriate because state statute did not apply); *Coast Trading*, 744 F.2d at 693 (same); *Fulwiler*, 624 F.2d at

Accordingly, each case analyzed the scope of the state law at issue to determine whether it could support the claim, rather than analyzing the scope of federal law to determine whether it precluded the claim.<sup>208</sup>

Unlike *Fobian*, where a successful creditor was seeking attorneys' fees, in each of the pre-*Fobian* cases, debtors had requested attorneys' fees pursuant to a state reciprocal fee statute in conjunction with a contractual attorneys' fee provision in favor of their creditor.<sup>209</sup> As a result, the pre-*Fobian* courts discussed the applicability of the relevant statutes.<sup>210</sup> However, by holding that the attorneys' fees in those cases were not within the scope of the reciprocal fee statutes, those cases also implicitly held that the attorneys' fees did not fall within the scope of the parties' contracts.

The primary purpose of the reciprocal fee statutes at issue in the pre-*Fobian* cases was to insure the mutuality of remedy where contractual provisions make attorneys' fees available to one party, and the state courts have applied the statutes to effectuate that purpose.<sup>211</sup> Therefore, the pre-*Fobian* courts' conclusions that the debtors had no right to attorneys' fees by virtue of the reciprocal fee statutes implied that the creditors in those cases also had no right; otherwise the right to attorneys' fees would not have been reciprocal, despite the purpose of

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910 (stating that the attorneys' fee award was not appropriate because no state-law basis for the award applied).

<sup>208</sup> *Johnson*, 756 F.2d at 740; *Coast Trading*, 744 F.2d at 693; *Fulwiler*, 624 F.2d at 909.

<sup>209</sup> See *Johnson*, 756 F.2d at 739 (citing CAL. CIV. CODE § 1717); *Coast Trading*, 744 F.2d at 693 (citing OR. REV. STAT. § 20.096); *Fulwiler*, 624 F.2d at 909 (same). Additionally, the court in *Coast Trading* also discussed the applicability of a dishonored check statute. See *Coast Trading*, 744 F.2d at 693.

<sup>210</sup> *Johnson*, 756 F.2d at 740 (affirming district court, which originally held that automatic stay action was not an "action on a contract" within the meaning of the state statute); *Coast Trading*, 744 F.2d at 693 (stating that state statutes were not applicable to the action); *Fulwiler*, 624 F.2d at 909-10 (rejecting the argument that a dischargeability proceeding fell within the letter of that state statute).

<sup>211</sup> *Reynolds Metals Co. v. Alperson*, 599 P.2d 83, 85-86 (Cal. 1979) (en banc) (holding that the attorneys' fee provision in a contract entitled nonsignatories who were sued on the contract to recover attorneys' fees under section 1717 of the California Civil Code in order to effectuate the statute's purpose, noting that "[s]ince [the defendants] would have been liable for attorney's fees pursuant to the fees provision had plaintiff prevailed, [the defendants] may recover attorney's fees"); *Leach v. Home Sav. & Loan Ass'n*, 230 Cal. Rptr. 553, 560 (Ct. App. 1986) ("[U]nder section 1717, if [the plaintiff] would have been able to recover attorney's fees from the [defendants] had she prevailed, [the defendants] may recover fees from [the plaintiff] when they prevail."); *Jewell v. Triple B. Enters.*, 626 P.2d 1383, 1388 (Or. 1981) (en banc) ("[Section 20.096 of the Oregon Revised Statutes] must be construed with one pervasive principle in mind: the purpose of the statute is to achieve reciprocity and mutuality."); *McMillan v. Golden*, 497 P.2d 1166, 1168 (Or. 1972) (en banc) (discussing the legislative history of section 20.096 of the Oregon Revised Statutes and holding that "the intention of the legislature was to provide that '(when a) contract specifically provides that attorney fees . . . shall be awarded to one of the parties,' such attorney fees shall be awarded to the prevailing party" (alterations in original) (quoting OR. REV. STAT. § 20.096)).

the statute.<sup>212</sup> Thus, it appears that, according to the pre-*Fobian* cases, the state reciprocal fee statutes limited authorization of litigants' contractual claims for attorneys' fees to those incurred in an action to enforce the contract, thereby excluding authorization for fees unrelated to contract enforcement, such as fees incurred in litigating purely bankruptcy-related rights. Limiting parties' ability to reallocate litigation costs would not have been an unreasonable implication of the statutes in light of their purpose and the general policy, embodied in the American Rule, that parties should ordinarily bear their own attorneys' fees.<sup>213</sup>

The holding in *Coast Trading* further supports the conclusion that the pre-*Fobian* courts' holdings were not limited to attorneys' fee requests pursuant to reciprocal fee statutes.<sup>214</sup> Although the *Coast Trading* court analyzed the issue with reference to the Oregon reciprocal fee statute, it denied fees to the creditor as well as the debtor,<sup>215</sup> despite the fact that the both parties had obtained some of the relief that they requested.<sup>216</sup> If the *Coast Trading* holding were limited to application of the reciprocal fee statute, then the holder of the fee provision would have been entitled to attorneys' fees if it had prevailed, even if the reciprocal fee statute was irrelevant. The court did not engage in any analysis of whether either party had prevailed, and simply denied fees to both.<sup>217</sup> Therefore, the court's holding could not have rested on the mere inapplicability of the reciprocity statute, but must have regarded the applicability, under state law, of contractual attorneys' fee provision itself.

### c. Scope of the *Fobian* Holding

As noted above,<sup>218</sup> the *Fobian* court held that an unsecured creditor may not recover contractually authorized postpetition attorneys' fees when the issues litigated concern only federal bankruptcy law.<sup>219</sup> Although the court's basis for its holding was less clear, due to the brevity of its analysis of the issue, a close reading reveals that the

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<sup>212</sup> This argument can be understood as a *modus tollens* type syllogism: If A, then B. Not B. Therefore, not A. Under the statutes, if the creditors had a right to attorneys' fees, then the debtors did. The debtors did not have a right to attorneys' fees. Therefore, the creditors had no right. See, e.g., Lincoln Davis Wilson, Comment, *Judgmental Neutrality: When the Supreme Court Inevitably Implies that Your Religion Is Just Plain Wrong*, 38 SETON HALL L. REV. 715, 723-24 (2008).

<sup>213</sup> See *Alyeska Pipeline Serv. Co. v. Wilderness Soc'y*, 421 U.S. 240, 247 (1975).

<sup>214</sup> See *Coast Trading*, 744 F.2d at 693.

<sup>215</sup> *Id.*

<sup>216</sup> The creditor was granted administrative priority for the amount of one if its claims. *Id.* The debtor's estate prevailed with respect to the creditor's other claims. *Id.*

<sup>217</sup> See *id.*

<sup>218</sup> See *supra* text accompanying note 144 and Introduction.

<sup>219</sup> *Fobian v. W. Farm Credit Bank (In re Fobian)*, 951 F.2d 1149, 1153 (9th Cir. 1991).

decision was premised on the applicability of state law.<sup>220</sup> The court acknowledged, without qualification, that state law governs a contract-based attorneys' fee claim in a bankruptcy proceeding.<sup>221</sup> Furthermore, the court regarded the three pre-*Fobian* cases, which had each based their decisions on the application of state law, as supportive authority for its own position.<sup>222</sup> In fact, as noted above, the *Fobian* court's application of the pre-*Fobian* courts' holdings to an unsecured creditor—rather than a debtor—was hardly an extension of those decisions.<sup>223</sup> In light of these facts, this Note suggests that, under *Fobian*, the reason that an unsecured creditor may not recover contractually provided attorneys' fees in a bankruptcy proceeding when the issues litigated concern only federal bankruptcy law is because, in such a situation, state law does not authorize the contractual fee shifting and, therefore, provides no basis for an award of fees.

At the time that *Fobian* was decided, the court's interpretation of California law appears to have been sound. The California Supreme Court had not ruled on whether California's reciprocal fee statute, section 1717,<sup>224</sup> precluded awarding contractual attorneys' fees when the fees were not incurred enforcing a contract.<sup>225</sup> The policy determination underlying section 1717 strongly suggested that contractual attorneys' fee provisions should be interpreted to exclude fees not involving an action on a contract, in order to prevent provisions from being enforced nonreciprocally.<sup>226</sup> As a result, it was reasonable for the *Fobian* court to infer that the California legislature intended to limit authorization of contractual fee shifting to contract enforcement costs, which did not include bankruptcy litigation.

### 3. Subsequent Development of the *Fobian* Rule

The later Ninth Circuit cases applying the analysis articulated in *Fobian* were equally unclear regarding the state-law basis of the *Fobian*

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<sup>220</sup> See David Gray Carlson, *Postdefault Interest Rates in Bankruptcy*, 2015 U. ILL. L. REV. 617, 640–41.

<sup>221</sup> See *supra* Section II.B.2.a.

<sup>222</sup> See *supra* Section II.B.2.b.

<sup>223</sup> The *Fobian* holding was implied in the previous cases. See *supra* notes 209–12 and accompanying text.

<sup>224</sup> See *supra* note 202.

<sup>225</sup> One California appellate court had stated, in dicta, that section 1717 would not have invalidated a contractual attorneys' fee provision with respect to fees incurred in litigating tort claims. *Malibou Lake Mountain Club, Ltd. v. Smith*, 95 Cal. Rptr. 553, 556 n.2 (Ct. App. 1971) (finding that section 1717 did not have any effect on the contract at issue because it was executed prior to the statute becoming effective).

<sup>226</sup> See *supra* note 211.

rule.<sup>227</sup> In *Hashemi*, the court denied a credit card company's request for postpetition attorneys' fees incurred successfully avoiding a debtor's discharge of certain credit card debts.<sup>228</sup> The court did not mention section 1717, but invoked the "on the contract" language found in the statute and the pre-*Fobian* cases.<sup>229</sup> In *Baroff*, the court held that the debtor was entitled to postpetition attorneys' fees that were incurred defending against a nondischargeability action.<sup>230</sup> The court undertook an analysis of section 1717, and articulated its understanding that California state law did not authorize contractual fee shifting to give one party a right to attorneys' fees incurred in noncontract actions.<sup>231</sup> Because the debtor litigated state contract law issues in defending against the action, the court held that the action was "on the contract," within the meaning of the statute.<sup>232</sup> However, before addressing the section 1717 issue, the court seemed to have applied *Fobian* as a separate and distinct analysis.<sup>233</sup> The *Baroff* court's reasons for engaging in a separate *Fobian* analysis are unclear because both analyses involved that same considerations, and lead to the same conclusions.<sup>234</sup> Nonetheless, the *Hashemi* and *Baroff* courts' ultimate holdings both remained consistent with the *Fobian* court's interpretation of California law.

However, in 1998, the California Supreme Court declared that section 1717 did not preclude contractual fee shifting with regard to at least one type of noncontract claim.<sup>235</sup> In *Santisas v. Goodin*, the California Supreme Court determined that a contract clause, which authorized a claim for attorneys' fees incurred litigating tort claims, was unaffected by section 1717, even if the statute would have governed the

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<sup>227</sup> See *Am. Express Travel Related Servs. Co. v. Hashemi (In re Hashemi)*, 104 F.3d 1122, 1126 (9th Cir. 1997); *Ford v. Baroff (In re Baroff)*, 105 F.3d 439 (9th Cir. 1997).

<sup>228</sup> *Hashemi*, 104 F.3d at 1126–27.

<sup>229</sup> *Id.* ("American Express' dischargeability claim is not an *action on the contract*. American Express is therefore not entitled to fees incurred pursuing this part of its claim." (emphasis added)).

<sup>230</sup> *Baroff*, 105 F.3d at 443.

<sup>231</sup> *Id.* at 442 ("Section 1717 limits the court's ability to enforce an attorney fees clause to 'any action on the contract' . . ." (quoting CAL. CIV. CODE § 1717(a) (West 1996))).

<sup>232</sup> *Id.* at 443.

<sup>233</sup> *Id.* at 442.

<sup>234</sup> The court first held that the litigation involved "an action on the contract" because "the document containing the attorney fees clause . . . played an integral role in the proceedings." *Id.* The court then proceeded to analyze, in a separate section of the opinion, whether California law authorized the fees, holding that "for the reasons discussed above, the nondischargeability proceeding was an *action on the contract*." *Id.* at 443 (emphasis added). Although the court essentially engaged in the same analysis—even employing the same language—in both sections, the court seems to have understood itself to have been engaged in separate analyses, one federal and one state.

<sup>235</sup> *Santisas v. Goodin*, 951 P.2d 399, 411 (Cal. 1998).

availability of fees in a contract claim.<sup>236</sup> That holding would seem to have called the *Fobian* holding into question because if section 1717 did not preclude awarding attorneys' fees incurred in tort litigation—which is not contract enforcement—it might also not preclude awarding fees incurred in bankruptcy litigation. At least one federal court has held, based on the *Santisas* decision, that contractual attorneys' fee claims in noncontract actions are not precluded by section 1717, and may be enforced under section 1021 of the California Code of Civil Procedure.<sup>237</sup>

Despite the California Supreme Court decision in *Santisas*, the Ninth Circuit continued to apply the *Fobian* rule without addressing the potential inconsistency raised by that decision.<sup>238</sup> In *Thrifty Oil v. Bank of America*, the court held that a creditor was entitled to postpetition contractually provided attorneys' fees incurred litigating California law, but not for litigating the allowability of the creditor's claim under § 502(b) of the Bankruptcy Code.<sup>239</sup> The court based its holding entirely on the *Fobian* line of cases, and did not mention either section 1717 or *Santisas*.<sup>240</sup> The Ninth Circuit also began to apply the *Fobian* analysis to attorneys' fee claims that were clearly authorized under state law.<sup>241</sup> In *Renfrow*, the court applied the *Fobian* analysis to a claim for postpetition attorneys' fees provided by a divorce decree that was governed and authorized by Washington state law.<sup>242</sup> The Ninth Circuit holdings in cases like *Thrifty Oil* and *Renfrow* thus appear to mark the beginning of the Ninth Circuit's clear departure from the state-law basis of *Fobian*.

Courts in other circuits have also applied the *Fobian* analysis in cases involving the law of states other than those involved in the *Fobian* line of cases.<sup>243</sup> In *Best Products*, a New York case, the bankruptcy court denied postpetition attorneys' fees to a creditor pursuant to a lease agreement.<sup>244</sup> The court cited *Fobian* for the proposition that contractual fee shifting is not appropriate with regard to litigation of

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<sup>236</sup> *Id.* (holding that section 1717 would have barred fee shifting if the contract action was voluntarily dismissed, but the statute did not affect availability of fees when the tort action was voluntarily dismissed).

<sup>237</sup> *MRW, Inc. v. Big-O Tires, LLC*, 684 F. Supp. 2d 1197, 1201–02 (E.D. Cal. 2010).

<sup>238</sup> *See, e.g., Thrifty Oil Co. v. Bank of Am. Nat'l Tr. & Sav. Ass'n*, 322 F.3d 1039 (9th Cir. 2003).

<sup>239</sup> *Thrifty Oil*, 322 F.3d at 1060.

<sup>240</sup> *Id.* at 1059–60.

<sup>241</sup> *See, e.g., Renfrow v. Draper*, 232 F.3d 688 (9th Cir. 2000).

<sup>242</sup> *Id.* at 694.

<sup>243</sup> *BankBoston, N.A. v. Sokolowski (In re Sokolowski)*, 205 F.3d 532 (2d Cir. 2000) (per curiam); *Agassi v. Planet Hollywood Int'l, Inc.*, 269 B.R. 543 (D. Del. 2001); *In re Child World, Inc.*, 161 B.R. 349 (Bankr. S.D.N.Y. 1993); *In re Best Prods. Co.*, 148 B.R. 413 (Bankr. S.D.N.Y. 1992).

<sup>244</sup> *Best Prods. Co.*, 148 B.R. at 415.

bankruptcy law issues.<sup>245</sup> However, the court also explained that the “contract must be construed to determine the latitude and scope of the contractual right to such fees.”<sup>246</sup> The court went on to analyze the relevant contract clause, which provided for attorneys’ fees incurred in enforcing contract rights, and held that the fees were incurred litigating bankruptcy rights rather than contract rights, noting that the litigation was not related to any default on the lease.<sup>247</sup>

In *Child World*, another New York case, the bankruptcy court allowed postpetition attorneys’ fees related to rent collection, maintenance, and taxes for property under a lease, but denied fees incurred while preparing for and attending a bankruptcy claims hearing.<sup>248</sup> As in *Best Products*, the court cited *Fobian*, but also analyzed the relevant contract clause and determined that the contract was intended to provide only for attorneys’ fees incurred in enforcement of the contract.<sup>249</sup> The court held that attorneys’ fees related to the claims hearing were not in enforcement of the contract, noting that the hearing was not the result of a breach.<sup>250</sup>

Although both courts invoked *Fobian* to support their conclusions, they looked to the scope of the relevant contracts and distinguished bankruptcy litigation from contract enforcement as a matter of contract interpretation, rather than as a matter of federal law under the Bankruptcy Code.<sup>251</sup> A Delaware court, which also cited *Fobian*, more directly construed the rule as a contract interpretation issue, rather than an application of federal common law.<sup>252</sup> In *Agassi v. Planet Hollywood*, the court denied creditors’ claims for postpetition attorneys’ fees incurred while successfully arguing that a contract was deemed rejected by the debtor under § 365(g) of the Bankruptcy Code, which constituted a breach of the contract.<sup>253</sup> The court rejected the creditors’ argument that the contract provided for attorneys’ fees that were “in any way” related to the debtor’s breach of the contract, holding instead that the recovery of attorneys’ fees was logically limited to expenses incurred “to

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<sup>245</sup> *Id.* at 414.

<sup>246</sup> *Id.* (citing *In re Westview 74th St. Drug Corp.*, 59 B.R. 747, 757 (Bankr. S.D.N.Y. 1986)).

<sup>247</sup> *Id.* at 414–15.

<sup>248</sup> *In re Child World, Inc.*, 161 B.R. at 355.

<sup>249</sup> *Id.* at 353–55.

<sup>250</sup> *Id.* at 354–55. The Second Circuit also held a Connecticut reciprocal fee statute—similar to those involved in the pre-*Fobian* cases—inapplicable where litigation involved a bankrupt debtor’s right to retain a loan-secured automobile under § 521 of the Code after a discharge in bankruptcy. See *BankBoston, N.A. v. Sokolowski (In re Sokolowski)*, 205 F.3d 532, 535 (2d Cir. 2000) (per curiam).

<sup>251</sup> *In re Child World, Inc.*, 161 B.R. at 354–55; *Best Prods. Co.*, 148 B.R. at 414–15.

<sup>252</sup> See *Agassi v. Planet Hollywood Int’l, Inc.*, 269 B.R. 543 (D. Del. 2001).

<sup>253</sup> *Id.* at 552–54.

address the breach.”<sup>254</sup> Because litigation was not designed to address the breach of contract, but to resolve issues of federal bankruptcy law, the court determined that attorneys’ fees were not available.<sup>255</sup> Although the court cited *Fobian* and drew the same distinction between state and bankruptcy law, the court clearly confined its inquiry to whether the scope of the particular contract encompassed the attorneys’ fees requested, as opposed to whether all attorneys’ fees were precluded by federal law generally.<sup>256</sup>

### III. POSTPETITION ATTORNEYS’ FEES AFTER *TRAVELERS*, AND THE ROLE OF STATE LAW

The *Travelers* decision did not say very much about whether postpetition attorneys’ fees are actually available to unsecured creditors.<sup>257</sup> As noted above, the holding of the case was simply that the *Fobian* rule, as a federal common law doctrine, was not supported by federal bankruptcy law.<sup>258</sup> The *Travelers* opinion did, however, express the Court’s concerns about affording due respect to state law and states’ interests in governing the contractual rights of their citizens.<sup>259</sup> The Supreme Court explained that it was the intention of Congress generally to allow state law to govern property rights in the assets of a bankrupt’s estate.<sup>260</sup> Despite the Supreme Court’s concern for preserving the application of state law in bankruptcy, the case may—ironically—ultimately result in the complete preemption by § 506(b) of creditors’ state law rights to attorneys’ fees.

The competing concerns, on the one hand, for parties to have the freedom to govern their own contractual interests with minimal federal interference, and on the other hand, for federal courts to maintain equitable and efficient administration of bankruptcy proceedings, were the primary concerns involved in the § 506(b) debate discussed above.<sup>261</sup> As noted, however, allowing unsecured claims for postpetition attorneys’ fees could result in significant administrative issues, increased litigation, unnecessary depletion of estate assets, and unfairness to other similarly situated creditors.<sup>262</sup> Federal bankruptcy courts may be slightly

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<sup>254</sup> *Id.* at 552–53 (quoting *In re Exch. Res., Inc.*, 214 B.R. 366, 370 (Bankr. D. Minn. 1997)).

<sup>255</sup> *Id.* at 553.

<sup>256</sup> *Id.* at 554.

<sup>257</sup> See Weintraub, *supra* note 46, at 62 (describing *Travelers* as a very narrow holding).

<sup>258</sup> *Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co.*, 549 U.S. 443, 452 (2007).

<sup>259</sup> *Id.* at 450–51.

<sup>260</sup> *Id.*

<sup>261</sup> See *supra* Section I.C.

<sup>262</sup> See *supra* notes 36–47 and accompanying text.



more sensitive to the administrative considerations concretely affecting their own dockets, than the relatively more abstract state interests in governing contractual fee shifting. As a result, if bankruptcy courts believe that, after *Travelers*, the only alternatives are to allow all postpetition attorneys' fee claims or to hold that all such claims are precluded by negative implication of § 506(b), there may be a strong incentive for courts to rule that state law has been preempted by § 506(b)<sup>263</sup>—which would ultimately deny states the power to govern an important area of law.

In practical terms, if not in principle, the distinction embodied by the *Fobian* rule established a sort of compromise between the two positions, which may have been the reason for the rule's popularity prior to the *Travelers* decision.<sup>264</sup> The rule assumed that § 506 did not preclude unsecured claims for postpetition fees, but stopped short of opening the flood gates for any and all attorneys' fee claims. Under the rule, unsecured creditors were permitted to recover postpetition attorneys' fees when the litigated issues involved state law, in which instances, states would have the strongest interest in governing the availability of attorneys' fees. However, postpetition fees were precluded with regard to bankruptcy litigation, which is a common and administratively intensive part of many bankruptcy proceedings, and does not otherwise implicate state law interests.

One possible interpretation of the *Travelers* decision is that courts must decide whether unsecured claims for postpetition attorneys' fees are allowable in wholesale fashion—either denying all claims or allowing them all, along the lines articulated in the § 506(b) debate.<sup>265</sup> This is the conclusion that many courts and commentators have drawn from the decision.<sup>266</sup> However, bankruptcy courts should not feel constrained by the *Travelers* decision to allow or deny postpetition attorneys' fees on an all-or-nothing basis; the *Travelers* decision does not require that result. *Travelers* explicitly left open the possibility that bankruptcy courts could

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<sup>263</sup> See *supra* notes 57–68 and accompanying text.

<sup>264</sup> Before *Travelers* was decided, *Fobian* had been approvingly cited by courts in the Ninth, Third, and Second Circuits, and no court had yet disagreed with that line of jurisprudence. See *supra* notes 114 and 243.

<sup>265</sup> See *supra* Section I.C.

<sup>266</sup> See generally *Ogle v. Fid. & Deposit Co. of Md.*, 586 F.3d 143, 146 (2d Cir. 2009) (holding that unsecured claims for postpetition attorneys' fees are allowed); *Ctr. Ins. v. SNTL Corp. (In re SNTL Corp.)*, 380 B.R. 204, 222 (B.A.P. 9th Cir. 2007) (same); *Qmect, Inc. v. Burlingame Capital Partners II, L.P. (In re Qmect, Inc.)*, 368 B.R. 882, 886 (Bankr. N.D. Cal. 2007) (same); see also *In re Elec. Mach. Enters.*, 371 B.R. 549, 551, 554 (Bankr. M.D. Fla. 2007) (holding that unsecured claims for postpetition attorneys' fees are disallowed); Michael E. Foreman, *What Happens to a Creditor's Post-Petition Litigation Costs?*, AM. BANKR. INST. J., Oct. 2015, at 26 (“[W]e are at least clear that the Supreme Court in *Travelers* disposed of any distinction between post-petition attorneys' fees incurred in connection with bankruptcy and nonbankruptcy issues.”).

look to state law, under § 502(b)(1) of the Code, for a basis to deny some claims for attorneys' fees.<sup>267</sup> As the origin of the *Fobian* rule demonstrates, there may be justification in state law itself for denying postpetition fees related to bankruptcy law litigation, while allowing creditors to claim the same fees they would have been entitled to had their underlying, state-law based claims been litigated in state court rather than a bankruptcy proceeding. For example, a bankruptcy court could analyze whether a state reciprocal fee statute was intended to limit the authorization of contractual fee shifting clauses to contract enforcement actions only, as the early *Fobian* cases did.<sup>268</sup> Such a decision would greatly lessen some of the administrative burdens that accompany allowing postpetition attorneys' fees in bankruptcy, such as the need to reassess fees after routine bankruptcy related motions or hearings, while also allowing creditors the same rights to fees they would have been entitled to outside of bankruptcy.<sup>269</sup>

A bankruptcy court could also determine that, as a matter of contract interpretation under state law, fee-shifting clauses should not be interpreted so broadly as to include fees incurred in bankruptcy litigation, unless the contract expressly provides otherwise, as the New York and Delaware courts mentioned above appeared to do.<sup>270</sup> Such a rule of contract interpretation would make abundant sense. In the absence of specific language, there is little reason to think that the parties to a contract contemplated shifting the costs that may be incurred in a bankruptcy proceeding. A claim to such fees from an insolvent debtor will often be worth very little to the creditor, and some commentators would argue that it is often not sensible for creditors to draft contractual attorneys' fee clauses to include costs incurred in bankruptcy proceedings.<sup>271</sup> Especially in jurisdictions with reciprocal fee statutes—such as section 1717 in California—attorneys' fee shifting in bankruptcy proceedings is often more likely to harm the creditor than help them. In one exceptional case, for example, a solvent creditor, who had unsuccessfully asserted a \$7000 claim against a bankrupt debtor, was required to pay \$245,000 to the debtor as a result of a reciprocally imposed attorneys' fee clause.<sup>272</sup> Therefore, it is not unreasonable to presume that parties did not intend for their contractual attorneys' fee

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<sup>267</sup> *Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co.*, 549 U.S. 443, 450 (2007).

<sup>268</sup> See *supra* Section II.B.

<sup>269</sup> See Scarberry, *supra* note 6, at 635.

<sup>270</sup> See *supra* notes 243–56 and accompanying text.

<sup>271</sup> Dan Schechter, *Chapter 13 Debtor Recovers \$245,000 in Fees from Lender After Defeating \$7000 Portion of Lender's Claim. [In re Penrod (9th Cir.)]*, COM. FIN. NEWSL., Oct. 5, 2015, at 81.

<sup>272</sup> *Id.*

provisions to apply to bankruptcy proceedings, unless the contract expressly so provides.

Deciding the issue on grounds such as these, rather than categorically denying unsecured claims for postpetition attorneys' fees on § 506(b) grounds, allows courts to more adequately balance the relevant interests involved, by awarding unsecured creditors many of the same fees they would have been entitled to in a state court action, while also maintaining a greater potential for fair and efficient bankruptcy case administration than would be possible if all unsecured claims for postpetition attorneys' fees were indiscriminately allowed.

#### CONCLUSION

In conclusion, this Note aims simply to bring to the attention of the legal community an additional option for determining the availability of postpetition attorneys' fees in bankruptcy proceedings. As the courts and scholars weighing in on the § 506(b) debate have expressed, there are important policy reasons for allowing—and for denying—unsecured claims to postpetition attorneys' fees. Therefore, a legal framework that permits courts to adopt a more compromising approach may be able to better balance some of those interests than an absolute allowance or prohibition of postpetition fees. Although *Travelers* expressly denied the existence of any federal basis for the *Fobian* rule, the distinction remains viable to the extent that it can be supported by state law. This Note suggests that before deciding this issue on broader § 506(b) grounds, courts should consider whether relevant state law could support deciding the issue under an analysis similar to that underlying the *Fobian* decision.