

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE WESTERN DISTRICT OF VIRGINIA  
ROANOKE DIVISION**

<b>IN RE:</b>	)	<b>CHAPTER 11</b>
	)	
<b>HARMAN MINING CORP.</b>	)	
	)	
<b>Debtor.</b>	)	<b>Case No. 98-01988</b>

---

<b>HARMAN MINING CORP.</b>	)	
	)	
<b>Objecting Party</b>	)	
<b>v.</b>	)	<b>DEBTOR’S OBJECTION TO</b>
	)	<b>CLAIMS # 21, 46, 62, 63 and 69</b>
<b>TREASURER, BUCHANAN COUNTY</b>	)	
	)	
<b>Respondent.</b>	)	

---

**MEMORANDUM OPINION**

The question before the Court is the proper rate of interest to be applied to the Treasurer of Buchanan County’s administrative claim for unpaid personal property taxes for the years 1999 and 2000. The issue is whether interest should be awarded at the rate provided by Virginia law or upon some equitable basis under bankruptcy law taking into account the impact upon other claimants against the estate. The parties have fully briefed the issue and this matter is ready for decision. For the reasons set out below, the Court concludes that the proper rate of interest to be applied to the claim of the Treasurer of Buchanan County is the rate provided by applicable nonbankruptcy Virginia law.

**FINDINGS OF FACT**

The Debtor filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code on May 22, 1998. The Treasurer of Buchanan County filed several proofs of

claim in this case in varying amounts for taxes. The Debtor filed Objections to Claims # 21, 46, 62 and 63 of the Treasurer of Buchanan County on December 4, 2006 on the ground that these claims are duplicative of Claim # 69 of the Treasurer of Buchanan County. The Debtor also filed an objection to claim # 69 of the Treasurer of Buchanan County on several grounds, including that the claim appears to be an estimated claim which is not based upon actual returns filed by the Debtor. According to the Stipulation filed by the parties, the specific tax liability upon which interest is sought is for personal property taxes for the years 1999 and 2000. The parties have conferred regarding these claims and have reached an agreement regarding the amount of the obligation and that interest must be paid, but disagree over two issues, only one of which is currently before the Court: the rate of interest to be applied to the post-petition administrative tax claims held by the Treasurer of Buchanan County. The parties filed initial briefs on June 29, 2007 and reply briefs on July 10, 2007.<sup>1</sup>

The Debtor asserts that the Court should apply the rationale of *Till v. SCS Credit Corp. (In re Till)*, 541 U.S. 465, 124 S. Ct. 1951, 158 L. Ed 2d 787 (2004) and apply either the federal judgment rate or prime rate without addition as there is no risk of nonpayment. The Debtor asserts that the Court should consider all of the competing interests in the bankruptcy case “because every dollar paid to Buchanan County would be one less dollar available to another creditor. No one creditor should be permitted to receive an artificially high interest rate”. (Debtor’s Reply Memorandum.) The Treasurer of Buchanan County asserts that the proper rate of interest for its tax claim should be the interest rate set by § 58.1-3916 of the Code

---

<sup>1</sup> Counsel for the Treasurer of Buchanan County filed his reply brief on July 10, 2007, however the incorrect document was attached to the docket entry. Therefore, counsel re-filed this reply brief on July 11, 2007.

of Virginia, which is 10%, as the interest on said taxes is part and parcel of the same tax claim.

### CONCLUSIONS OF LAW

This Court has jurisdiction of this proceeding by virtue of the provisions of 28 U.S.C. §§ 1334(a) and 157(a) and the delegation made to this Court by Order from the District Court on July 24, 1984. Objections to claims are “core” bankruptcy matters pursuant to 28 U.S.C. § 157(b)(2)(B).

This case was filed on May 22, 1998. Therefore, this case is controlled by the law in effect prior to the adoption of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA). 11 U.S.C. § 503(b)(1)(B) provides that taxes incurred post-petition by the estate are administrative expenses entitled to priority. § 503(b)(1)(C) also provides an administrative priority for any “fine, penalty, or reduction in credit relating to a tax of a kind specified in subparagraph (B) of this paragraph”. 11 U.S.C. § 511, enacted as part of BAPCPA, establishes a rate of interest on tax claims, whether the tax claim is a pre-petition claim or an administrative expense claim. This section provides that the rate of interest on such claims shall be the rate determined under applicable nonbankruptcy law. However, prior to the enactment of BAPCPA, there was no specific code section which addressed the applicable rate of interest on tax claims when interest was allowed.

While interest is not specifically mentioned in § 503(b)(1)(C), the law in the Fourth Circuit is clear that interest relating to such taxes should be included as an allowed administrative expense under § 503(b)(1)(C). The Court in *United States v. Friendship College, Inc. (In re Friendship College, Inc.)*, 737 F.2d 430, 433 (4<sup>th</sup> Cir. 1984) held that the government

was “entitled as a first priority expense of the bankruptcy estate to full payment of the taxes claimed, the penalties for failure to pay them on time, and interest from the date that it accrued.”

In support of its holding, the Court noted:

The bankruptcy *Code* accords first priority treatment to penalties on taxes which are first priority administrative expenses, § 503(b)(1)(C). . . . Interest, on the other hand, is not mentioned by the *Code*, but we find no support anywhere for differentiation in the treatment of the tax and the interest thereon. . . . To treat interest inconsistently from the taxes and penalties, we would require proof that such different treatment was intended by the Code.

*Id.* The *Friendship College* Court, however, did not explicitly address the issue of the appropriate interest rate to be allowed on such claim.

Therefore, the question in this matter becomes the proper rate of interest to be allowed on these administrative tax claims. Neither the Court nor counsel for the parties have located any Fourth Circuit authority regarding the proper rate of interest to be allowed unless *Friendship College* is read to make the implicit assumption in using the language “the tax and the interest thereon” that “the interest thereon” is the interest which accrues pursuant to state law. Counsel for the Debtor contends that different interest rates have been applied by different courts (i.e., state statutory rate, federal judgment rate, state judgment rate, rate money is being invested) and suggests that the proper rate of interest is that provided by *Till*. The Debtor relies on two 5<sup>th</sup> Circuit cases, *In re Process Property Corp.*, 327 B.R. 603, 610 (Bankr. N.D. Tex. 2005) and *In re Jones*, 2007 Bankr. LEXIS 1436 (Bankr. S.D. Tex. 2007), for its position that the bankruptcy court has discretion to set an interest rate equitably appropriate to the circumstances of each case, even where there is an applicable state statutory rate. The Court in *In re Process Property* considered the proper interest rate for claims by over-secured,

nonconsensual lienholders for interest accrued post-petition under § 506(b) and held that the proper rate of interest is the prime rate adjusted upwards according to the risk of the debtor, not the statutory rate of 12% under Texas law for delinquent taxes. Accordingly, that decision does not deal with what interest would accrue upon a taxing authority's administrative claim for interest on post-petition taxes. The *Jones* Court also considered the issue of the proper rate of interest for an over-secured lender's claim under § 506(b). In *Jones*, a post BAPCPA case, the Court stated: "In the wake of the passage of BAPCPA, the Court lacks discretion to equitably determine the appropriate interest rate to be paid on a tax claim . . . Under § 511, the Court is bound to enforce the interest rate set forth in the applicable state law." *Id.* at \*12. Based on these cases, the Debtor asserts that the Court should apply the rationale of *Till* and apply either the federal judgment rate or prime rate without addition as there is no risk of nonpayment. In *Till*, the Court, in a plurality opinion, held that the formula approach, requiring adjustment of the national prime rate of interest based on the greater risk of nonpayment for debtors versus solvent commercial borrowers, was the appropriate method for determining the adequate rate of interest in a Chapter 13 cramdown under § 1325(a)(5)(B). *Till*, 541 U.S. at 479-480. *Collier on Bankruptcy* states that section 511

has the effect of circumscribing by statute the impact of the U.S. Supreme Court's decision in *Till v. SCS Credit Corp.*, in which the Court plurality suggested in *dictum* that rate of interest applicable to deferred payments under section 1129(a)(9)(C) should be set by using the national prime rate as the initial starting point with additional interest points added to account for nonpayment risk.

*Collier on Bankruptcy* ¶ 511.01 at p. 511-3 (Alan N. Resnick & Henry J. Sommer eds., 15th ed. rev.)

Counsel for the Treasurer of Buchanan County contends that the proper rate of

interest is 10%, the rate of interest provided under Virginia law. As noted by counsel, the Nebraska bankruptcy court has determined that the appropriate rate of interest to be allowed on post-petition administrative claims is the applicable rate under nonbankruptcy law. Citing *Friendship College*, the court in *In re Cooper*, 124 B.R. 797 (Bankr. D. Neb. 1990), held that the county's administrative claim for post-petition interest on its post-petition property tax claim was to be calculated at the rate under the applicable Nebraska statute. "If it is appropriate to give administrative claim status to penalties provided by statute at the statutory rate and if interest provided by statute is to be treated similar to penalties, then the appropriate interest rate is the statutory rate." *Id.* at 799. The Court in *In re Isley*, 104 B.R. 673 (Bankr. D. N.J. 1989) also held that the interest accruing on the administrative priority tax claims under § 503(b) is the statutory rate under New Jersey law. *See also In re Venable*, 48 B.R. 853 (Bankr. S. D. N.Y. 1985) where the Court held that the proper rate of interest for taxes due the City from the debtors for post-petition taxes is the statutory rate under the City's Charter. Counsel for the Treasurer also relies on a Tennessee case where the Court applied the Tennessee statutory interest rate to a tax claim under § 506. *In re D.M. White Construction Co., Inc.*, 2007 Bankr. LEXIS 1308 (Bankr. E.D. Tenn. 2007).

This Court agrees with the Treasurer of Buchanan County that the proper rate of interest to be applied to the claim at issue is that provided under Virginia law. It would be illogical to give administrative priority to the 5% penalty assessed by the Treasurer of Buchanan County and allowed under Virginia law for failure to make a timely payment of taxes but not to the full interest provided by state law until such time as payment might be made. To give an example, it wouldn't make much sense to accord administrative expense priority to a statutorily

proclaimed “penalty” of 20% per year upon delinquent taxes, prorated to the date of payment, but deny it for some far lesser rate characterized as “interest.” With specific reference to the 10% statutory interest rate applicable to the tax at issue in this proceeding, it might be reasonably observed that such rate exceeds Virginia’s “legal rate of interest” (6%) (Va. Code Ann. §6.1-330.53) and the current judgment rate of interest (6%)(Va. Code Ann. §6.1-330.54). To the extent of that difference, then, one could reasonably surmise that the General Assembly of Virginia intended the 10% rate to include both a compensation component for the late receipt of payment and a punitive component to recognize the harm to the Commonwealth, its political subdivisions and its citizens, indeed truly the common weal, resulting from taxpayers who fail to pay their tax obligations when due. In summary, the administrative expense priority accorded to the taxing authorities’ normal claims arising from untimely payment of taxes should not vary depending upon whether the applicable statute characterizes such claims as penalties or interest. Furthermore, *Till* involved the proper rate of interest to be charged with regard to a cramdown under § 1325, not interest on a post-petition administrative tax claim.

The Court finds further support for its position in the Fifth Circuit case of *In Re Al Copeland Enterprises, Inc.*, 991 F.2d 233 (5<sup>th</sup> Cir. 1993). The Fifth Circuit Court considered whether the statutory award of interest under Texas law constituted an administrative expense under § 503. In that case, the debtor had collected nearly two million dollars in sales tax revenues for the State of Texas prior to its bankruptcy filing. The taxes became due ten days after the debtor filed its petition. The Court allowed an administrative priority for statutory interest under Texas law which accrued post-petition on the state sales tax receipts. While *Copeland Enterprises* dealt with the statutory award of post-petition interest based upon the

post-petition actions of a debtor in possession, namely, its failure to turn over to the State its tax money which the debtor had collected pre-petition, rather than a tax incurred during post-petition reorganization efforts under § 503(b)(1)(C), the underlying reasoning behind the decision is relevant to the issue at hand.

The Court further believes that its holding is consistent with the general principle that bankruptcy debtors attempting to reorganize under chapter 11 are protected after filing from the enforcement of their creditors' pre-bankruptcy claims, but not from the normal liabilities they incur subsequent to their filing. Reorganizing debtors, generally speaking, are expected to meet their post-filing responsibilities to the same extent as their non-filing competitors. Accordingly, for example, they must comply with applicable environmental legal requirements<sup>2</sup> and fulfill all of their obligations under new contracts which they enter into post-petition or under pre-bankruptcy leases and other executory contracts which they assume. In *CIT Communications Fin. Corp. v. Midway Airlines Corp. (In re Midway Airlines Corp.)*, 406 F.3d 229, 237 (4<sup>th</sup> Cir. 2005), the Fourth Circuit Court of Appeals considered the administrative expense claim under 11 U.S.C. § 365(d)(10) of a lessor of personal property for all payments due under the lease for the thirteen-month period beginning sixty-one days after the order for relief and ending when the debtor rejected the lease. The Court noted as a preliminary matter that the "term 'administrative expense' is not defined in the Code, but courts agree that an administrative expense has two defining characteristics: (1) the expense and right to payment arise after the filing of bankruptcy,

---

<sup>2</sup> See *Collier, supra*, at ¶ 503.06[4] and 28 U.S.C. § 959(b).

and (2) the consideration supporting the right to payment provides some benefit to the estate.”<sup>3</sup>

*Id.* at 237<sup>4</sup>. The Court agreed with the conclusion that

a lessor is entitled to recover all payments due under the lease (including rent, taxes, interest, late fees, and attorney’s fees) as an administrative expense if (1) the trustee fails to perform its obligations under § 365(d)(10), and (2) the court has not previously modified the trustee’s obligations pursuant to § 365(d)(10). The provision makes clear that a lessor is entitled to the trustee’s

---

<sup>3</sup> In the case before this Court the tax liabilities in question unquestionably were incurred after the Debtor’s 1998 bankruptcy filing and the Debtor obtained the benefit of the use of its personal property in its post-filing reorganization efforts, a fact which cannot be separated from the tax liability associated with it.

<sup>4</sup> To be sure the general principle perceived by this Court, that bankruptcy debtors are obliged to satisfy in full liabilities resulting from their post-petition operations, is not without exception. The *Midway Airlines* opinion itself notes that the Bankruptcy Code in section 365(d)(10) does expressly authorize a procedure whereby the Bankruptcy Court may equitably adjust on a prospective basis and after notice and a hearing a reorganizing debtor’s liabilities on a lease which it can no longer afford to meet. The Court noted as follows:

Section 365(d)(10) requires that the trustee timely perform all obligations under a personal property lease unless the court, ‘based on the equities of the case, orders otherwise with respect to the obligations or timely performance thereof.’ . . . By its terms the statute allows a bankruptcy court to modify only the trustee’s actual performance under § 365(d)(10), including his ongoing obligation to make full payments under the lease on a timely basis. . . . The provision does not, however, authorize a bankruptcy court to make an equitable adjustment of the amount recoverable as an administrative expense under § 503(b) should the trustee fail to make payments as they come due under § 365(d)(10). In short, we read the equitable modification provision as authorizing a bankruptcy court to modify, based on the equities, a trustee’s responsibilities on a prospective basis only. A trustee cannot remain idle after the sixty-day grace period, neither seeking modification of nor fulfilling his obligations under the lease, and then ask for a retroactive modification of his obligations when the lessor seeks an administrative expense.

*Id.* at 240.

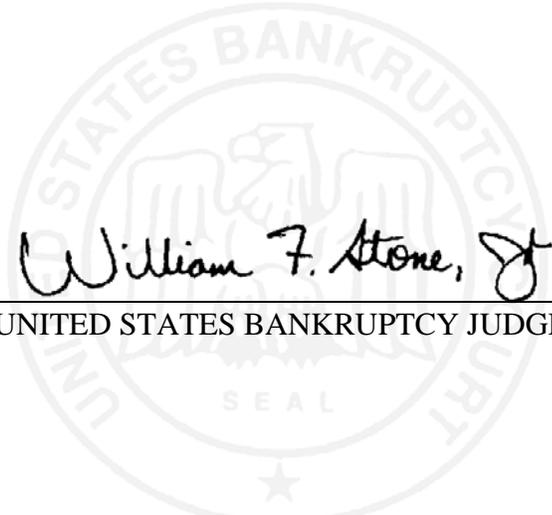
performance of all obligations under the lease.

*Id.* at 236. Similarly, if post-filing operations result in a casualty loss injurious to the rights of others, such injured other parties must be fairly compensated before the pre-petition creditors can be paid. *Reading Co. v. Brown*, 391 U.S. 471 (1968)(decided under Bankruptcy Act). The very sensible rationale of this decision and the general principle perceived by the Court is that, at least in theory, the reorganization is being attempted in substantial part to provide greater value and return to the debtor's creditors, so they should not benefit from post-filing operations at the expense of innocent third parties. Therefore, it is right, proper and in harmony with applicable precedent that a reorganizing debtor face exactly the same monetary consequences resulting from its late payment of tax liabilities incurred as a result of its post-filing operations as do all other taxpayers incurring similar liabilities.

#### CONCLUSION

For the foregoing reasons, the Court holds that the proper rate of interest to be applied to the administrative tax claim of the Treasurer of Buchanan County is the rate provided by applicable nonbankruptcy Virginia law under § 58.1-3916 of the Code of Virginia. An order to such effect will be entered contemporaneously with the signing of this Memorandum Opinion.

This 23rd day of July, 2007.

The seal of the United States Bankruptcy Court is visible in the background, featuring a central figure holding scales and a sword, surrounded by the text "UNITED STATES BANKRUPTCY COURT" and "SEAL" with a star below.

William F. Stone, Jr.  
UNITED STATES BANKRUPTCY JUDGE