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**A Majority of Courts Reject the Application of the Rules for Disallowance of Claims under Section 502(d) to Administrative Expense Claims**

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**INTRODUCTION**

Since the adoption of title 11 of the United States Code (the “Bankruptcy Code”), courts have struggled with the application of administrative expense claims.<sup>1</sup> Administrative expenses include the actual costs and expenses of preserving the estate after the commencement of a bankruptcy case.<sup>2</sup> Allowance of an administrative expense claim is governed by section 503 of the Bankruptcy Code.<sup>3</sup> A question arises, however, whether the rules of governing the allowance of claims, under section 502, also applies to administrative expense claims.<sup>4</sup>

Under section 502(d), a court may “disallow any claim of any entity from which property is recoverable . . . or that is a transferee of a transfer avoidable . . . unless such entity or transferee has paid the amount or turned over any such property, for which such entity or transferee is liable.”<sup>5</sup> Although administrative expense claims are not mentioned within section

<sup>1</sup> See, e.g., *Matter of Georgia Steel, Inc.*, 38 B.R. 829 (Bankr. M.D. Ga. 1984).

<sup>2</sup> 11 U.S.C. § 503.

<sup>3</sup> *Id.*

<sup>4</sup> See, e.g., *Matter of Georgia Steel, Inc.*, 38 B.R. at 829; *In re MicroAge, Inc.*, 291 B.R. 503 (B.A.P. 9th Cir. 2002); *In re Cir. City Stores, Inc.*, 426 B.R. 560 (Bankr. E.D. Va. 2010).

<sup>5</sup> 11 U.S.C. § 502(d).

502(d), some courts determined this section applies to these claims.<sup>6</sup> However, most courts disagree with that interpretation.

This article discusses whether the rules for disallowance of claims, under section 502(d), applies to administrative expense claims. Part I analyzes the majority opinions within the courts, establishing that section 502(d) does not apply to administrative expense claims. Part II discusses the minority view that section 502(d) applies to disallow administrative expense claims.

## **I. The Majority of Courts do not Extend Section 502(d) to Administrative Expense Claims.**

Most courts that decided whether administrative expense claims may be disallowed under section 502(d) have answered that question negatively.<sup>7</sup> There are two principle reasons that section 502(d) does not apply to administrative expense claims. First, the language of section 502(d) prevents the disallowance of administrative expense claims under the statute.<sup>8</sup> Second, the Bankruptcy Code provides an independent statute, section 503, to govern the disallowance of administrative expense claims, which indicates Congress' intent to separate administrative expense claims from section 502(d).<sup>9</sup>

### *A. Section 502(d) Specifically Prevents Administrative Expense Claims Because of the Statutory Language*

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<sup>6</sup> See, e.g., *In re Cir. City Stores, Inc.*, 426 B.R. at 560; *In re MicroAge, Inc.*, 291 B.R. at 503; *Matter of Georgia Steel, Inc.*, 38 B.R. at 829.

<sup>7</sup> See, e.g., *ASM Capital v. Ames Department Stores, Inc. (In re Ames Dep't Stores, Inc.)*, 582 F.3d 422 (2d Cir. 2009); *In re CM Holdings, Inc.*, 264 B.R. 141, 150 (Bankr. D. Del. 2000); *In re Lids Corp.*, 260 B.R. 680 (Bankr. D. Del. 2001).

<sup>8</sup> See *In re Ames Dep't Stores, Inc.*, 582 F.3d at 422.

<sup>9</sup> See, e.g., *In re Rand Energy Co.*, 256 B.R. 712 (Bankr. N.D. Tex. 2000); 11 U.S.C. § 503(b) (“After notice and a hearing, there shall be allowed administrative expenses.”).

The majority opinion is that section 502(d) is not applicable to administrative expense claims because of the language within the statute.<sup>10</sup> Section 502(d) provides:

Notwithstanding subsections (a) and (b) of this section, the court shall disallow any claim of any entity from which property is recoverable under section 542, 543, 550, or 553 of this title or that is a transferee of a transfer avoidable under section 522(f), 522(h), 544, 545, 547, 548, 549, or 734(a) of this title, unless such entity or transferee has paid the amount, or turned over any such property, for which such entity or transferee is liable under section 522(i), 542, 543, 550, 553 of this title.<sup>11</sup>

The first part of section 502(d), “notwithstanding subsections (a) and (b) of this section,” signifies that section 502(d) only applies to claims included in section (a) and (b) of the statute.<sup>12</sup>

Since administrative expense claims are not within section (a) or (b), by including the introductory phrase under section 502(d), the majority opinion is that it is superfluous and contrary to statutory interpretation to apply section 502(d) to administrative claims.<sup>13</sup>

Expanding on the statutory interpretation, most courts note that there is a distinction between administrative expense claims and other expense claims because there are two separate statutory provisions.<sup>14</sup> Administrative expense claims are generally post-petition claims, covered under section 503, rather than prepetition claims.<sup>15</sup> However, there is an exception under section 503(b)(9), where an administrative expense is for a pre-petition debt.<sup>16</sup> Section 502(b) notes that section 502 focuses only on pre-petition claims.<sup>17</sup> Because the Bankruptcy Code treats post-

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<sup>10</sup> See, e.g., *In re Ames Dep't Stores, Inc.*, 582 F.3d at 422; *In re Momenta, Inc.*, 455 B.R. 353 (Bankr. D.N.H. 2011).

<sup>11</sup> 11 U.S.C. §502(d).

<sup>12</sup> *In re Momenta, Inc.*, 455 B.R. at 363; 11 U.S.C. § 502(a)–(b) (listing a group of claims that fall under section 502, notably excluding administrative expense claims).

<sup>13</sup> See, e.g., *In re Momenta Inc.*, 455 B.R. at 365.

<sup>14</sup> *In re Ames Dep't Stores, Inc.*, 582 F.3d at 428 (citing *In re Plastech Engineered Products, Inc.*, 394 B.R. 147 (Bankr. E.D. Mich. 2008); *In re Lids Corp.*, 260 B.R. 680 (Bankr. D. Del. 2001)).

<sup>15</sup> *In re Rand Energy Co.*, 256 B.R. 712, 718–19 (Bankr. N.D. Tex. 2000).

<sup>16</sup> *In re TI Acquisition, LLC*, 410 B.R. 742, 750 (Bankr. N.D. Ga. 2009); 11 U.S.C. § 503(b)(9) (providing goods received by the debtor before the date of the commencement of the case falls under this title).

<sup>17</sup> 11 U.S.C. § 502(b) (“[T]he court, after notice and a hearing, shall determine the amount of such claim . . . as of the date of the filing of the petition.”).

petition claims under section 503, and pre-petition claims under section 502, the majority of courts have held that section 502(d) should not apply to administrative expense claims.<sup>18</sup>

*B. Congress Intended to Exclude Administrative Expense Claims Under Section 502(d)*

In addition, courts have held that the legislature did not intend to include administrative expense claims under section 502(d).<sup>19</sup> Section 502(b), which is referenced in section 502(d), specifically states the types of claims that apply.<sup>20</sup> The textual language of section 502(b) includes five post-petition claims.<sup>21</sup> Since the statute mentions some post-petition claims and not others, the drafters did not intend to include any other post-petition claims under section 502(d).<sup>22</sup> As administrative expense claims are post-petition claims that are not included as an exception under section 502(b), it was likely Congress' intent to exclude these claims under section 502(d).<sup>23</sup>

**II. A Minority of Courts Apply Section 502(d) to Administrative Expense Claims**

Multiple lower courts and the Ninth Circuit apply section 502(d) to administrative expense claims.<sup>24</sup> There are two principal reasons these courts have found that section 502(d) can be used to disallow administrative expense claims. First, the statutory language of section 502(d) and Congress' intent in creating the statute permits the application of administrative expense

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<sup>18</sup> *In re Rand Energy Co.*, 256 B.R. at 719.

<sup>19</sup> *In re Lids Corp.*, 260 B.R. at 683; *In re CM Holdings, Inc.*, 264 B.R. 141, 150 (Bankr. D. Del. 2000).

<sup>20</sup> 11 U.S.C. §502(b).

<sup>21</sup> *In re Lids Corp.*, 260 B.R. at 683; 11 U.S.C. § 502(b) (noting post-petition claims that section 502 applies to are limited to (i) a claim for reimbursement; (ii) an involuntary claim arising out of the ordinary course of business; (iii) a claim from a rejection of an executory contract; (iv) a claim arising from the recovery of property; and (v) a claim arising for a tax entitled to priority after the commencement of the case).

<sup>22</sup> *In re CM Holdings, Inc.*, 264 B.R. at 150.

<sup>23</sup> *In re Lids Corp.*, 260 B.R. at 683–84.

<sup>24</sup> See, e.g., *In re MicroAge, Inc.*, 291 B.R. 503 (B.A.P. 9th Cir. 2002); *In re Cir. City Stores, Inc.*, 426 B.R. 560 (Bankr. E.D. Va. 2010); *Matter of Georgia Steel, Inc.*, 38 B.R. 829 (Bankr. M.D. Ga. 1984).

claims.<sup>25</sup> Second, there are public policy supports applying section 502 to administrative expense claims.<sup>26</sup>

*A. Congress Intended Section 502(d) to Apply to Administrative Expense Claims*

*Because of the Language of the Statute*

Relying on the language of section 502(d) of the Bankruptcy Code, some courts have held that there is nothing in the text of the statute that expressly limits its application to prepetition claims.<sup>27</sup> “Any claim” mentioned in section 502, should apply to all claims.<sup>28</sup> The definition of claim in section 101(5) of the Bankruptcy Code is sufficiently broad and includes payments of administration expense claims.<sup>29</sup> Furthermore, the predecessor of section 502(d), section 57g of the Bankruptcy Act of 1898, includes administrative expense claims. Therefore, section 502 should apply to administrative expense claims as well.<sup>30</sup>

If Congress intended to change the meaning of the statute, Congress would have made the intent specific.<sup>31</sup> Congress would have explicitly excluded administrative expense claims from the statute, as it has done in other statutes.<sup>32</sup> Congress did not create section 502 to punish creditors, but to give creditors an option to keep or surrender their transfers.<sup>33</sup> It does not matter if the creditors have administrative expense claims or pre-petition claims.<sup>34</sup> The evidence the

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<sup>25</sup> See, e.g., *In re MicroAge, Inc.*, 291 B.R. at 503, 508; *Matter of Georgia Steel, Inc.*, 38 B.R. at 839.

<sup>26</sup> *In re Triple Star Welding, Inc.*, 324 B.R. 778, 794 (B.A.P. 9th Cir. 2005); *In re MicroAge, Inc.*, 291 B.R. at 512.

<sup>27</sup> *In re MicroAge, Inc.*, 291 B.R. at 508.

<sup>28</sup> *Id.*

<sup>29</sup> *Id.*; 11 U.S.C. § 101(5)(A) (defining claim 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 . . .”).

<sup>30</sup> *In re MicroAge, Inc.*, 291 B.R. at 508; The Bankruptcy Act of 1898, Pub. L. No. 55-541, §57g, 30 Stat. 544, 560 (1898) (“The claims of creditors who have received preferences . . . shall not be allowed unless such creditors shall surrender such preferences.”).

<sup>31</sup> *In re MicroAge, Inc.*, 291 B.R. at 509 (citing *Midlantic Nat’l Bank v. New Jersey Dept. of Env’tl. Protection*, 474 U.S. 494, 501 (1986)).

<sup>32</sup> *Id.* at 508; see also 11 U.S.C. § 365(n)(1)(B)(i) (referring to any claim allowable under section 503(b)); 11 U.S.C. § 348(d) (excluding any claim allowable under section 503(b)).

<sup>33</sup> *Matter of Georgia Steel, Inc.*, 38 B.R. 829, 839 (Bankr. M.D. Ga. 1984).

<sup>34</sup> See *id.*

majority courts use to infer Congress's intent is ambiguous and not clear enough to overcome the presumption that Congress wanted to keep the law the same.<sup>35</sup>

*B. Applying Administrative Expense Claims to Section 502(d) is Beneficial for  
Repayments to the Estate*

The minority view also cites to public policy as a compelling reason for section 502(d) to apply to administrative expense claims.<sup>36</sup> “502(d) is designed to assure an equality of distribution of assets of the bankruptcy estate not create penalties for asserting a setoff right.”<sup>37</sup> Allowing administrative expense claims under section 502 would not increase risk but would rather provide another source of repayment for the estate.<sup>38</sup> The goals of equitable distribution and efficiency support a decision that section 502(d) should apply to administrative expense claims.<sup>39</sup> If the objective of section 502(d) was to encourage the return of avoidable transfers to the estate, then it would be best served to apply section 502(d) to transfers of both administrative expense claims and prepetition claims.<sup>40</sup>

## CONCLUSION

The way courts interpret section 502(d) changes the application of the statute to administrative expense claims. Most courts interpret the statute and the intent of Congress to prevent the disallowance of administrative expense claims. However, the minority of courts interpret the statute and Congress' intent in a different way to apply section 502(d) to administrative expense claims.

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<sup>35</sup> *In re MicroAge, Inc.*, 291 B.R. at 511.

<sup>36</sup> *In re Triple Star Welding, Inc.*, 324 B.R. 778, 794 (B.A.P. 9th Cir. 2005); *In re Cir. City Stores, Inc.*, 426 B.R. 560, 571 (Bankr. E.D. Va. 2010).

<sup>37</sup> *Campbell v. United States (In re Davis)*, 889 F.2d 658, 662 (5th Cir. 1989).

<sup>38</sup> *In re MicroAge, Inc.*, 291 B.R. at 512.

<sup>39</sup> *In re Cir. City Stores, Inc.*, 426 B.R. at 571.

<sup>40</sup> *In re MicroAge, Inc.*, 291 B.R. at 512.