

# Can I Recover Attorneys' Fees in Bankruptcy?

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**The United States Court of Appeals for the Fourth Circuit – which covers federal courts in North Carolina – recently handed a big victory to lenders whose borrowers file for bankruptcy protection.**

In SummitBridge National Investments III, LLC v. Faison, the Fourth Circuit held that if a lender's loan documents contain an attorneys' fees provision, then the lender may file a claim for post-petition fees incurred during the bankruptcy. Since all standard loan documents should have an attorneys' fees clause, and because bankruptcy cases can last for years, this is a win for lenders. Although the claim will be "unsecured," it should entitle the lender to recover at least a portion of its fees.

## The Facts

Over nine years, BB&T loaned \$2.1 million to Mr. Ollie Faison's farm operations under three promissory notes. The loans were secured by farmland. BB&T's loan documents contained a standard attorneys' fees provision providing that if Faison defaulted and BB&T retained an attorney to collect, Faison would pay "all costs of collection, including but not limited to reasonable attorneys' fees." Faison filed a Chapter 11 bankruptcy petition in 2014. A year later, with the bankruptcy still pending, BB&T sold its loans to SummitBridge. The bankruptcy case continued until 2016 when the bankruptcy court confirmed Faison's reorganization plan.

Faison's plan treated SummitBridge's claims as one aggregate secured claim for \$1,715,000 – the value of the farmland securing the three notes. That amount covered the outstanding principal and pre-petition interest on the notes, and a portion of SummitBridge's post-petition interest and attorneys' fees.

## Secured Claims and Unsecured Claims

In any bankruptcy proceeding, creditors are generally classified as having either a "secured" or "unsecured" claim. A secured claim is supported by the value of collateral securing repayment of the claim, while an unsecured claim is not supported by collateral. An unsecured claim is combined with the unsecured claims of other creditors, and often a percentage of the total is repaid pro rata.

Section 506(b) of the Bankruptcy Code specifically provides that if a creditor has an over-secured claim (i.e.,

the value of the creditor's collateral exceeds the loan balance on the date the debtor filed bankruptcy), then the creditor is allowed a claim for post-petition interest and any reasonable fees, costs, or charges provided under the loan documents. The collateral value sets the ceiling on the recovery of post-petition interest and fees. For SummitBridge, that amount was \$1,715,000. This was the full extent of SummitBridge's *secured* claim.

But SummitBridge sought to recover all its attorneys' fees, so it filed an *unsecured* claim for the fees it could not include in the \$1,715,000 secured claim. Faison argued that the Bankruptcy Code allows no unsecured claim for post-petition attorneys' fees or costs. The Bankruptcy Court and District Court agreed with Faison, but the Fourth Circuit reversed.

### **The Power of the Attorneys' Fees Clause**

As a general rule, a creditor's claims in bankruptcy are fixed as of the petition date – the day the debtor files bankruptcy. By definition, SummitBridge could not have incurred any post-petition fees on the petition date. So how could SummitBridge have a claim for post-petition attorneys' fees? The Fourth Circuit held that for a lender to have a valid unsecured claim for post-petition attorneys' fees, the *right* to those fees must arise pre-petition, even though the fees had not yet been incurred. If a lender's loan documents contain an attorneys' fees clause, it satisfies this requirement. The fees are a contingent pre-petition obligation that becomes fixed post-petition when the creditor incurs the fees.

The Fourth Circuit rejected Faison's arguments that specific Bankruptcy Code provisions prohibited an unsecured claim for post-petition fees. The Fourth Circuit also rejected equity arguments. Faison argued it would be unfair to allow SummitBridge – which already had a \$1,715,000 secured claim – also to have an unsecured claim for attorneys' fees, because that claim would reduce the pool of assets available to wholly unsecured creditors who have yet to recover any principal, let alone fees.

The Fourth Circuit highlighted a basic tenet of bankruptcy law – secured creditors are privileged over unsecured creditors. Faison's argument reversed this privilege. By allowing unsecured but not under-secured creditors to assert claims for post-petition attorneys' fees, it would put unsecured creditors in a *more* protected position than secured creditors.

The Fourth Circuit also held that Faison's policy argument upset another basic tenet of bankruptcy law – that state law governs the substance of claims. Allowing creditors like SummitBridge, who have bargained specifically for attorneys' fees under state law, to enforce those rights in bankruptcy upholds that tenet, even if it reduces the pool of assets otherwise available. The result does not provide an "undeserved bonus for one creditor at the expense of others," as Faison argued. Rather, it enforces the bargained-for loan terms.

### **Conclusion**

This decision will have an immediate impact on creditors and debtors in bankruptcy. Debtors may attempt to move their cases towards confirmation faster and with less litigation, now knowing the meter is running on legal fees for some creditors. Creditors will need to file – and amend as necessary – proofs of claim addressing not only their underlying loan balances but also their post-petition fees.

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