

A QUESTION FOR LAWYERS REPRESENTING MINERAL CONTRACTORS TO ASK

by DEBORAH D. WILLIAMSON

The oil and gas industry once again is experiencing the consequences of the bust, which inevitably seems to follow each oil and gas boom. While the technology in the oil patch has changed dramatically and the plays are different, many of the questions for Texas attorneys representing creditors in a bankruptcy case remain the same. Do royalty owners have properly recorded assignments? Has the operator segregated all royalty payments? Have the secured lenders perfected liens on all collateral, including leases earned by a borrower after the mortgage? Have providers of goods and services to oil and gas properties perfected their mechanic's and materialmen's liens?

For attorneys representing mineral contractors, there is a new question: Does the contractor have an administrative claim in addition to any lien rights? A mineral contractor may have a right to a secured claim based on a mechanic's and materialmen's lien. Texas Property Code §56.002 creates a lien in favor of a mineral contractor or subcontractor "for labor or services related to the mineral activities." Although the date on which the entity first furnishes materials or performs services marks the inception date of the lien for purposes of relative priority as to other encumbrances, such as a deed of trust, Texas Property Code §56.004 provides that all mineral lien claimants with properly perfected liens are equal in rank — without regard to the date of filing or the date on which the labor or materials were furnished.

In bankruptcy, a claim is secured only to the extent of the value of the underlying collateral. Thus, the bankruptcy court will compare the total amount of all equal mineral lien claims plus any senior deed of trust liens to the value of the underlying collateral to determine whether a lien claimant is secured. Mechanic's and materialmen's lien claimants holding secured claims generally are entitled to payment pursuant to a

plan of reorganization over a specified period with an appropriate rate of interest. But there is no statutory requirement that the debtor pay such claimants in cash at confirmation or shortly thereafter. In fact, §1123(b)(4) specifically permits a plan to "modify the rights of holders of secured claims."

The 2005 amendments to the Bankruptcy Code added §503(b)(9), which created a new administrative claim in an amount equal to the "value of any goods received by the debtor within twenty (20) days of the date of the commencement of the case in which the goods have been sold to the debtor in the ordinary course of the debtor's business." Much has been written about the effect of this new administrative claim on bankruptcy cases involving retailers, such as clothing stores, and the

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potential for administrative insolvency due to the size of administrative claims; attorneys representing creditors in the energy industry should not overlook it.

Unlike retail cases that are driven by the imprecision of consumer confidence and vagaries of fashion trends, energy cases are more likely to actually confirm a plan of reorganization, depending in large part on the amount and priority of debt. The holder of a §503(b)(9) administrative claim is entitled to payment in full as a condition to confirmation of any reorganization plan. Bankruptcy Code §507(a)(2) provides that certain administrative claims have a priority over all unsecured claims. Section 1129(a)(9)(A) requires the debtor to pay §507(a)(2) administrative claims in cash in full as a condition of confirmation of a reorganization plan unless the holder of that claim agrees to different treatment.

Section 503(b)(9) became effective Oct. 17, 2005. There have been few bankruptcy cases involving a filed and confirmed reorganization plan since then. As a result, there has been little discussion and no reported decisions on the impact of §503(b)(9) on the plan confirmation process.

The U.S. Bankruptcy Appellate Panel of the 9th U.S. Circuit Court of Appeals, the only appellate court that has addressed the issue, held in *In Re: Brown & Cole Stores LLC* (2007) that a creditor can have both a secured claim and an administrative claim under §503(b)(9). Thus, attorneys for mineral contractors and subcontractors need to add another item to the bankruptcy to-do list: Take steps to protect any administrative claim. While the filing of the bankruptcy petition automatically creates the administrative claim, a creditor easily can lose such a claim. There is no statutory date by which a creditor needs to assert an administrative claim. A court order early in a bankruptcy case or a confirmed plan of reorganization may set a date beyond which creditors cannot file administrative claims. A failure to timely file an administrative claim will generally result in forfeiture of administrative claim status. Even if a creditor timely files

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an administrative claim, litigation could ensue regarding what exactly is the value of the goods (as opposed to the services) provided to the debtor. Separate pricing for goods (as opposed to services) in the relevant contract or invoice could help eliminate any controversy over the value of such goods.

Other than payment in full as a condition to confirmation, other benefits of an administrative claim are less clear. A number of cases have addressed whether the holders of §503(b)(9) administrative claims are entitled to payment during the case or whether they must wait until confirmation. To date, the courts uniformly have held that debtors do not have to pay these claims prior to plan confirmation. Also, unlike secured claims, administrative claim holders generally are not entitled to interest or to recover the attorney's fees.

Creditors that delivered goods in the 20 days prior to the filing of a bankruptcy petition have the option to object to confirmation of a plan of reorganization if at least that portion of the claim is not paid in full. This leverage is without regard to lien priority and, at least with regard to mechanic's and materialmen's liens, gives a new option for the holders of those claims if they proactively protect their administrative claim rights. **INB**

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