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UNITED STATES BANKRUPTCY COURT

SOUTHERN DISTRICT OF CALIFORNIA

In re	Bankruptcy No. 01-10624-JM
LYON'S OF CALIFORNIA, INC.,	Memorandum Decision
Debtor.	

I. Overview

This dispute concerns the objection filed by Lyon's of California, Inc., as the reorganized debtor ("Debtor"), to the claim of the State Compensation Insurance Fund ("State Fund"), which concerns workers' compensation insurance provided to the Debtor. The Debtor filed its petition for relief under Chapter 11 of the Bankruptcy Code ("Code") on October 12, 2001.

There are two workers' compensation insurance policies involved in this case. The first policy ("First Policy") insured the Debtor from March 13, 2001 to November 27, 2001. The second policy ("Second Policy") covers the period from September 30, 2002 to November 24, 2003.

On March 14, 2002, the Debtor served all creditors with notice of a claims bar date. The bar date was May 3, 2002. In response, State Fund filed a proof of claim ("Claim No. 397") on May 1, 2002. It asserted a prepetition, unsecured, priority claim in the amount of $460,560.87 for the time period between March 13, 2001 to October 12, 2001. Claim No. 397 made no mention of any debt owed for the time period from October 12, 2001 (the date the petition was filed) and November 27, 2001 (when the First Policy expired). There were no documents attached to the proof of claim.

On August 15, 2002, the Debtor served creditors, including State Fund, with notice of the bar date for administrative claims ("First Administrative Claims Bar Date"). This bar date was September 30, 2002, and it applied to all administrative claims that might have arisen between the date of the filing of the petition date, October 12, 2001, and April 30, 2002.

On August 22, 2002, State Fund filed another proof of claim (Claim No. 456), again asserting an unsecured, priority claim. State Fund checked off on the form that Claim No. 456 amended the prior claim. The amended amount of the claim was $601,053.14. State Fund left blank the space provided for "Date debt was incurred" on Claim No. 456. Nothing on the face of Claim 456 indicated that State Fund was including an administrative claim along with its earlier asserted unsecured prepetition claim.

State Fund attached five pages of documents to Claim No. 456. On only one of those pages was there any indication that the claim might cover a period of time that included insurance coverage postpetition. That page listed a "Report/Audit Period" as October 1, 2001 to November 27, 2001, and indicated the amount for the total

premium was for "10/01/01 - 11/27/01."

An order setting a second administrative claims bar date ("Second Administrative Claims Bar Date") was entered on October 22, 2002. The order required the filing of administrative claims incurred from May 1, 2002, through October 15, 2002, to be filed by December 2, 2002. On October 24, 2002, the Debtor served creditors with its "Notice of Second Administrative Claims Bar Date." The address listed for State Fund in the proof of service did not match the address provided by State Fund in either Claim No. 397 or Claim No. 456.

The order confirming the Debtor's Second Amended Plan of Reorganization ("Plan") was entered on February 3, 2003. Pursuant to the Plan, the effective date was 60 days after the order confirming the Plan became final. That order became final on February 14, 2003, and therefore, the effective date was April 15, 2003.

The Debtor filed its objection to State Fund's claim on July 14, 2003. The Debtor objected to the accounting and to State Fund's assertion it was entitled to priority for a portion of its claim.

On August 7, 2003, State Fund filed two proofs of claim. One claim, no. 521 (Claim No. 521), changed the amount of the unsecured, priority claim to $426,815.49, and included a general, unsecured claim in the amount of $52,457.61. State Fund indicated that the debt was incurred between March 13, 2001 and October 12, 2001, which mirrored the dates provided in Claim No. 397, the first proof of claim.

In the other claim, No. 520 (Claim No. 520), State Fund asserted for the first time that it had an administrative claim for the period between October 12, 2001 and November 27, 2001. The amount of the claim was set at $106,780.04.

State Fund filed two more proofs of claim on January 12, 2004.

On Claim No. 525 ("Claim No. 525") State Fund apparently looked to amend its original unsecured claim. It stated that the pertinent debt had been incurred between March 13, 2001 and October 12, 2002. It is unclear whether the date of October 12, 2002 is a typographical error, intended to be October 12, 2001, the date of the petition. In any case, State Fund asserted a priority claim of $426,815.49, and an unsecured debt of $52,457.71, for a total claim of $479,273.10.

In the other claim filed on that date, claim no. 526 ("Claim No. 526"), State Fund stated that the claim was for a postpetition administrative claim. It stated that the debt represented in Claim No. 526 was incurred between October 12, 2001 and November 27, 2001 and between September 30, 2002 and November 25, 2003. This was the first proof of claim in which State Fund sought payment based on the Second Policy. The amount of the claim was $447,479.72.

Then, on May 28, 2004, State Fund filed its last two proofs of claim. It stated that claim no. 527 ("Claim No. 527") was for the period from March 13, 2001 to October 12, 2002. The claim was characterized as an unsecured claim, with $426,815.49 allegedly entitled to be treated as a priority claim and $52,457.61 as general unsecured claim.

In claim no. 528 ("Claim No. 528"), State Fund asserted a debt allegedly incurred between October 12, 2001 and November 27, 2001, and also between September 30, 2002 and November 24, 2003. The amount claimed was $483,906.93. Claim No. 528 increased the amount stated in Claim No. 526, and mirrored it in all other respects.

To summarize the various claims filed, Claim Nos. 397, 456, 521, 525 and 527 were all for prepetition unsecured claims. Claim Nos. 520, 526 and 528 specifically requested payment of an administrative

claim. Claim No. 520 only concerned the First Policy, while Claim Nos. 526 and 528 included claims for both policies.

II. Late Filed Administrative Claim under First Policy

The bar date for unsecured creditors was May 3, 2002. Claim No. 397, which was filed on May 1, 2002, was timely filed. The First Administrative Claims Bar Date was September 30, 2002. Claim No. 456, filed on August 22, 2002, was timely filed relative only to the First Administrative Claims Bar Date. All other proofs of claim were untimely filed.

The first issue concerns whether the late filed proofs of claim relate back to a timely filed proof of claim, and as such, can be treated as timely filed. Specifically, the question is whether Claim Nos. 520, 526 and/or 528, wherein State Fund asserted an administrative claim based on the First Policy, could be said to relate back in time to Claim No. 397 or Claim No. 456.

State Fund contends that the Debtor had to know of the workers' compensation insurance being provided postpetition and, given that knowledge, the timely proofs of claim put the Debtor on notice that it had a right to an administrative claim, even if the claims themselves failed to specifically use the term "administrative claim." In other words, according to State Fund, the Debtor and creditors should not have relied on how the State Fund itself characterized the claim, but should have done an independent analysis of the claim, which allegedly would have shown the debt, at least in part, was incurred postpetition.

The Debtor contends that the recharacterization of the claim from an unsecured claim with priority to an administrative claim amounts to the filing of a new claim. Consequently, it argues that the

proofs of claim for the administrative claim were not timely filed and should be denied on that basis. It also argues that allowing the amendment would be inequitable because the estate is administratively insolvent and administrative claimholders who filed timely claims would be prejudice if State Fund's claim is allowed. The Debtor asserts that State Fund knew of the bar date, that it filed a claim and could have filed a proper claim in the first instance. It also argues that the Debtor and creditors relied on the characterization of the claim as unsecured in proposing and voting on the confirmed plan and that creditors would be prejudiced now if the amendment were allowed. It also contends that State Fund has not provided any reason why the administrative claim was late filed.

Allowing an amendment to a claim is within the sound discretion of the Court. In re Roberts Farms Inc., 980 F.2d 1248 (9th Cir. 1992) and In re Wilson, 96 B.R. 257, 263 (9th Cir. BAP 1988). The Court considers whether the amendment would result in any undue prejudice and whether there is some justification for State Fund's failure to file a proper claim within the limitations period. In determining the prejudicial effect the Court will look to such elements as bad faith or unreasonable delay in filing the amendment, impact on other claimants, reliance by the debtor or other creditors and change of the debtor's position. Wilson, 96 B.R. at 262.

State Fund did not specifically assert an administrative claim until it filed Claim No. 520 on August 7, 2003. This was more than a year after the First Administrative Claims Bar Date. It was also six months after the plan of reorganization was confirmed. Additionally, State Fund did not raise the prospect of an administrative claim until the Debtor filed an objection to State

Fund's unsecured, priority claim. The Court finds that this was an unreasonable delay in filing Claim No. 520. Furthermore, State Fund has not offered any justification for the delay in filing that claim.

Additionally, allowing Claim No. 520 to relate back to the timely filed claims would prejudice creditors. The Debtor provided an estimate of the amount of administrative claims prior to confirmation of the Plan. The $106,780.04 set forth in Claim No. 520 represents nearly a 10% increase in the administrative class. Administrative creditors were entitled to payment in full upon the effective date pursuant Code Section 1129(a)(9)(A). However, they consented to receiving payment over time under the Plan. Those payments are to be made on a pro rata basis from various sources. Allowing State Fund's late filed administrative claim will undoubtedly create delays in payment to other administrative creditors, and any delay could increase the risk on non-payment to such creditors.

State Fund contends that its timely claims provided adequate notice to the Debtor and any creditors of its right to assert an administrative claim, despite State Fund not characterizing it as such. However, a party in interest reviewing the claims registry would not have had any reason to know State Fund was entitled to an administrative claim based on Claim No. 397 or Claim No. 456.

On Claim No. 456, State Fund set forth that the debt was incurred prepetition. On its face there was nothing in the claim to indicate that State Fund sought payment on a postpetition debt. Additionally, State Fund failed to provide a date for when the debt was incurred on Claim No. 456. Also, State Fund did not attach any documents to Claim No. 397. Furthermore, the only page attached to Claim No. 456 that arguably suggested State Fund had a claim for postpetition insurance

coverage made reference to a period of time that was both prepetition as well as postpetition. Therefore, it was too ambiguous to stand as the only basis for State Fund's assertion that its proof of claim gave notice of its alleged administrative claim.

The Court rejects State Fund's contention that adequate notice was provided to the Debtor and the other creditors that it was entitled to an administrative claim. Claim No. 520, in which State Fund first explicitly sought payment for an administrative claim for the period from October 12, 2001 to November 27, 2001 was a new claim, and does not relate back to earlier filed claims. See Matter of Alliance Operating Corp., 60 F.3d 1174, 1175 (5th Cir. 1995)(amendment to a proof of claim, which changed the nature of the claim from unsecured to priority status, set forth a new claim and could not relate back to a previously filed claim); In re Metro Transportation Company, 117 B.R. 143, 148 (E.Pa. 1990)(attempt to reclassify claim is actually an attempt to file a new claim). Claim Nos. 526 and 528 did nothing more than amend Claim 520. Therefore, the Court will disallow State Fund's claim for an administrative claim based on the First Policy as set forth in Claim Nos. 520, 526 and 528.

III. Claim under Second Policy up to Date of Confirmation

The next issue concerns the extent to which State Fund is entitled to an administrative claim flowing from the Second Policy. The Second Policy did not become effective until September 30, 2002. There seems to be some confusion regarding the applicable bar date. In its pleadings, the Debtor contended that State Fund could have met the First Administrative Claims Bar Date of September 30, 2002. At the hearing, counsel for the Debtor reversed course and stated that State Fund should have an administrative claim for unpaid premiums

from the date of the inception of the Second Policy until the date the plan was confirmed, in other words, from September 30, 2002 until February 3, 2003, because the Second Policy became effective on the same day as the First Administrative Claims Bar Date. In other words, State Fund could hardly have filed its claim based on the Second Policy before the First Administrative Claims Bar Date when the Second Policy did not even become effective until the date of the First Administrative Claims Bar Date itself.

The Debtor never made any mention of the Second Administrative Claims Bar Date. That bar date applied to administrative claims incurred from May 1, 2002, through October 15, 2002. Such claims needed to be filed by December 2, 2002. Arguably State Fund should have filed its claim under the Second Policy by December 2, 2002. The Debtor had ample opportunity to raise this issue, but failed to do so. Therefore, the argument is waived. This may be just as well since it appears that the Debtor, by not using the address provided by State Fund on its initial proofs of claim, failed to properly serve State Fund with notice of the Second Administrative Claims Bar Date. Consequently, State Fund is allowed an administrative claim for premiums due from September 30, 2002, until February 3, 2003. The Court now turns to the question of whether State Fund is also allowed an administrative claim under the Second Policy after February 3, 2003.

IV. Post Confirmation Administrative Claim

The remaining issue is whether State Fund can seek compensation from the estate for premiums due after confirmation of the plan of reorganization. The Debtor contends that any further responsibility on behalf of the estate for the premiums due was barred once the plan

was confirmed. State Fund contends that it calculated the postpetition amounts due using the Debtor's own books and records, suggesting that this shows that the Debtor continued to benefit from the workers' compensation insurance being provided, either directly or indirectly. It specifically contends that "workers' compensation insurance was absolutely necessary for the operation of Debtor's restaurants throughout Chapter 11 reorganization and throughout the implementation of the Liquidating Plan over which this Court has continuing jurisdiction." State Fund's Response to Supplemental Brief of Debtor Re Objection to Claim, filed January 19, 2005.

State Fund has not made it clear under what Code Section it seeks payment as an administrative claim for coverage under the Second Policy. Presumably it seeks payment pursuant to Section 503(b)(1). Under that Section, "any claim for administrative expenses and costs must be the actual and necessary costs of preserving the estate for the benefit of its creditors." In re Dant & Russell, Inc., 853 F.2d 700, 706 (9th Cir. 1988). The court in Dant & Russell further stated:

> two factors must be weighed: maintaining the estate in as healthy a form as possible for the benefit of creditors while allowing essential costs of administering an ongoing business venture to be paid up front, thereby giving the debtor its best shot at emerging as a vital concern. Baldwin-United Corp., 43 B.R. at 452. Although a claim may meet the implicit requirement of section 503(b)(1)(A), namely that any claims under the section must have a distinct postpetition character, bankruptcy courts have broad discretion in determining whether to award administrative expense priority. Baldwin-United Corp., 43 B.R. at 453; Matter of Hearth & Hinge, Inc., 28 B.R. 595 (Bankr.S.D.Ohio 1983) (administrative expense priority granted where storage and appraisal of the debtor's property protected and preserved the major portion of the estate's assets and thus conferred a benefit upon the debtor and its creditors). That discretion is limited by the clear intent of section 503(b)(1)(A): the actual and necessary costs of preserving the estate. See Matter of Jartran, Inc., 732 F.2d 584 at 586 (7th Cir. 1984).

In making its argument that the estate should not be liable to State Fund post-confirmation, the Debtor pointed out that under paragraph 12.1 of the Plan, the property of the estate vested in the Reorganized Debtor on the effective date of the Plan. The Debtor asserts that State Fund could proceed against the Reorganized Debtor for post-confirmation premiums.

However, the Court finds that paragraph 12.1 justifies awarding State Fund a portion of its claim post-confirmation because until the property vested in the Reorganized Debtor the estate had an interest in maintaining workers' compensation insurance. The Court is satisfied that the workers' compensation insurance provided by State Fund was an actual and necessary expense of preserving the estate for the benefit of creditors up until the effective date of the Plan. The effective date under the Plan was April 15, 2003. Therefore, State Fund is allowed an administrative claim under the Second Policy from September 30, 2002, until April 15, 2003.

V. Summary

State Fund asserted an administrative claim in Claim Nos. 520, 526 and 528. The Court rejects State Fund's argument that those claims should relate back in time to a timely filed claim. Therefore, the Court denies State Fund's administrative claim based on the First Policy as late filed.

Claims No. 526 and 528 also included a request for the payment of an administrative claim based on the Second Policy. The Debtor conceded that State Fund was entitled to an administrative claim from the time the policy started, September 30, 2002, until the confirmation date. Additionally, the Court determines that since the property of the estate did not vest in the Reorganized Debtor until

the effective date of April 15, 2003, that the estate benefitted from the Second Policy until that date. Therefore, State Fund is allowed an administrative claim based on the Second Policy from September 30, 2002, until April 15, 2003. Counsel for the parties shall meet and confer to determine if they can agree on a dollar amount for this portion of State Fund's administrative claim. The remainder of State Fund's claim under the Second Policy (from April 16, 2003 until November 24, 2003) is disallowed as against the bankruptcy estate.

Counsel for the Reorganized Debtor shall file an order consistent with this Memorandum Decision within 21 days of the entry of this Decision.

Date: JUL 26 2005

Hon. James W. Meyers
UNITED STATES BANKRUPTCY JUDGE

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF CALIFORNIA
325 West F Street, San Diego, California 92101-6991

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BY 104 DEPUTY

In re Bankruptcy Case No(s). 01-10624-M11
Adversary No(s).

CERTIFICATE OF MAILING AND FACSIMILE

The undersigned, a regularly appointed and qualified clerk in the office of the United States Bankruptcy Court for the Southern District of California, at San Diego, hereby certifies that a true copy of the attached document, to wit:

Memorandum Decision

was enclosed in a sealed envelope bearing the lawful frank of the bankruptcy judges and mailed to each of the parties at their respective addresses listed below:

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Said envelope(s) containing such document was deposited by me in a regular United States Mail Box in the City of San Diego, in said District on July 26, 2005.

Molly Dishman
Judicial Assistant to the Honorable James W. Meyers