UNITED STATES BANKRUPTCY APPELLATE PANEL FOR THE FIRST CIRCUIT

BAP NO. EB 16-015

Bankruptcy Case No. 13-10670-PGC

MONTREAL, MAINE & ATLANTIC RAILWAY, LTD.,
Debtor.

ROBERT J. KEACH, Chapter 11 Trustee,
Appellant,

v.

NEW BRUNSWICK SOUTHERN RAILWAY COMPANY LIMITED,
and MAINE NORTHERN RAILWAY COMPANY,
Appellees.

Deasy, U.S. Bankruptcy Appellate Panel Judge.

ORDER GRANTING MOTION FOR LEAVE TO APPEAL

Robert J. Keach, the former chapter 11 trustee[1] (the "Appellant"), seeks leave to appeal the bankruptcy court's February 26, 2016 order (the "Order") sustaining in part and overruling in part his objections to certain proofs of claim filed by New Brunswick Southern Railway Company Limited ("NBSR") and Maine Northern Railway Company ("MNR" and, collectively with NBSR, the "Appellees"). The Appellees filed a response to the motion for leave to appeal,

[1] The Appellant asserts that in accordance with the Trustee's Chapter 11 Plan of Liquidation dated July 15, 2015 (As Amended on October 8, 2015) (the "Plan"), upon the Effective Date of the Plan (which occurred on December 22, 2015), he is no longer the chapter 11 trustee of the Debtor's estate, but is the Estate Representative of the Post-Effective Date Estate (as defined in the Plan).

stating they do not oppose the motion because they agree the resolution of the pending appeal may potentially advance the final disposition of litigation with the Appellant in several matters pending before the bankruptcy court.

For the reasons discussed below, the motion for leave to appeal is **GRANTED**.

BACKGROUND

From January 2003 until May 2014, Montreal, Maine & Atlantic Railway, Ltd. (the "Debtor") operated an integrated international shortline freight railroad system (the "System") with its wholly owned Canadian subsidiary, Montreal, Maine & Atlantic Canada Co. ("MMAC"). On July 6, 2013, an unmanned train operated by the Debtor containing 72 tank cars filled with crude oil derailed in Lac-Mégantic, Quebec, causing several large explosions, the death of 47 people, damage to or destruction of several nearby structures, and significant environmental damage.

On August 7, 2013, the Debtor filed a chapter 11 petition in the U.S. Bankruptcy Court for the District of Maine, and the Appellant was subsequently appointed chapter 11 trustee. Shortly thereafter, MMAC commenced a parallel proceeding under Canada's Companies' Creditors Arrangement Act, and Richter Advisory Group was appointed as the monitor in MMAC's case.

On June 13, 2014, MNR filed Proofs of Claim Nos. 242-1 (the "MNR Duplicate Claim") and 257-1 ("Claim 257") and NBSR filed Proofs of Claim Nos. 243-1 (the "NBSR Duplicate Claim") and 259-1 ("Claim 259"). The MNR Duplicate Claim was identical to Claim 257 and the NBSR Duplicate Claim was identical to Claim 259. Together, the MNR Duplicate Claim and the NBSR Duplicate Claim are referred to as the "Duplicate Claims."

In Claim 259, NBSR asserted claims in the aggregate amount of $2,164,471.30 arising from "[f]reight services provided to the Debtor in connection with interline rail shipments." Of the total amount claimed, NBSR asserted that not less than $1,971,834.67 was "secured by equitable liens against all property of the Debtor under the Six Month Rule applicable in federal court receiverships, and [we]re entitled to priority pursuant to 11 U.S.C. § 1171(b)," because such claims: (1) related to current operating expenses incurred by the Debtor that were necessary for the on-going operation of the Debtor's railroad; (2) were incurred within six months prior to the commencement of the Debtor's reorganization case; and (3) were for services that were provided by NBSR with the expectation that they would be paid out of current operating revenue and not in reliance on the Debtor's general credit.

In Claim 257, MNR asserted claims in the aggregate amount of $355,101.19 arising from "[f]reight services provided to the Debtor in connection with interline rail shipments." Of the total amount claimed, MNR asserted that approximately $167,228.89 was entitled to priority under § 1171(b)[2] for the same reasons advanced by NBSR in Claim 259. Together, Claim 259 and Claim 257 are referred to as the "Asserted 1171(b) Claims."

On October 19, 2015, the Appellant filed an objection to the proofs of claim filed by the Appellees (the "Claim Objection"), asserting that the Duplicate Claims were duplicative of Claim 257 and Claim 259 and should be disallowed in their entirety, and that the Asserted 1171(b) Claims were improperly asserted as administrative and/or priority claims and should be allowed only as general unsecured claims. Specifically, with respect to the Asserted 1171(b) Claims, the Appellant argued that "as a matter of controlling law in this circuit," pre-petition

[2] Unless expressly stated otherwise, all references to "Bankruptcy Code" or to specific statutory sections shall be to the Bankruptcy Reform Act of 1978, as amended, 11 U.S.C. §§ 101, et seq.

interline freight claims of the type asserted by the Appellees do not qualify as "six-month" claims entitled to priority under § 1171(b), citing In re Boston & Maine Corp., 600 F.2d 307 (1st Cir. 1979) ("Boston & Maine I"). The Appellant also argued that the evidence established that, in furnishing services to the Debtor, the Appellees relied—not on the Debtor's operating revenues at the time the service was provided—but upon the Debtor's general credit and, as a consequence, their claims were not entitled to be treated as § 1171(b) claims, citing In re Boston & Maine Corp., 634 F.2d 1359, 1379-80, 1382 (1st Cir. 1980) ("Boston & Maine II").

On November 12, 2015, the Appellees filed a response to the Claim Objection ("Appellees' Response"). The Appellees argued that Boston & Maine I was not applicable controlling law on the issue because it did not decide or even address the issue of whether interline freight claims qualify as "six-month" claims entitled to priority in a railroad reorganization; rather, Boston & Maine I only addressed the question of the timing of the payment of such claims. The Appellees also argued that the question of whether the interline freight claims asserted in Boston & Maine I were entitled to treatment as priority claims under the debtor's plan of reorganization was addressed by the U.S. Court of Appeals for the First Circuit in the subsequent case of Boston & Maine II. According to the Appellees, in Boston & Maine II , the First Circuit reversed a decision of the district court that those claims should be treated as general unsecured claims. The First Circuit held instead that per diem claims, such as those asserted by the interlining railroads, constituted "six-month" claims entitled to priority, if such claims: (1) represented a current operating expense necessarily incurred; (2) were incurred within six months before the reorganization petition was filed; and (3) the goods or services were delivered in the expectation that they would be paid for out of current operating revenues of the

railroad, and not in reliance on the railroad's general credit. According to the Appellees, the evidence clearly established that their claims satisfied the test articulated in Boston & Maine II.

On November 19, 2015, the parties filed their Stipulations With Regard to Trustee's Objection to Proofs of Claim Filed by New Brunswick Southern Railway Company Limited and Maine Northern Railway Company Limited (the "Stipulations"). Pursuant to the Stipulations, the parties stipulated to certain facts, including the following: (a) at all relevant times, Wheeling & Lake Erie Railway Company held a valid security interest in the Debtor's accounts receivable and certain inventory to secure obligations due under a line of credit; (b) the Debtor was a participant in the Interline Settlement System ("ISS"),[3] but the Appellees were not participating railroads in the ISS; (c) by agreement, the Debtor acted as the billing railroad when either MNR or NBSR originated traffic and interchanged with the Debtor, as well as when the Debtor originated traffic and interchanged with either of the Appellees; and (d) the Debtor collected from the ISS freight revenue attributable to freight services provided by the Appellees in connection with shipments originated by other carriers that were interchanged by such carriers with the Debtor, and by the Debtor with the Appellees. The parties also agreed that the Appellees would withdraw the Duplicate Claims, and that the only issue to be addressed at the November 20, 2015 hearing on the Claim Objection was whether the claims asserted by the Appellees in Claim 257 and Claim 259 qualified as "six-month" claims entitled to priority under § 1171(b), and if so, the amount of such claims would be determined at a subsequent hearing, if required.

[3] According to the bankruptcy court, "[t]he ISS provides a certain central clearing house for participating railroads involved in the interchange of freight traffic among multiple rail carriers to settle accounts receivable and accounts payable arising from the interchange of such traffic."

On November 20, 2015, the bankruptcy court held an evidentiary hearing during which testamentary evidence was submitted. Following the hearing, the bankruptcy court took the matter under advisement, and directed the parties to submit post-trial briefs. Both parties filed their post-trial briefs on December 10, 2015.

On February 5, 2016, the bankruptcy court issued oral findings of fact and conclusions of law, determining that the Asserted 1171(b) Claims were entitled to priority under § 1171(b). Specifically, the bankruptcy court found that the Appellees had met their burden of establishing that the Asserted 1171(b) Claims qualified as claims that are entitled to priority under § 1171(b) because: (1) the Asserted 1171(b) Claims represented current operating expenses that were necessarily incurred by the Debtor in connection with its on-going operations; (2) the Asserted 1171(b) Claims were incurred within six months prior to the commencement of this case; and (3) the services that were the subject of the Asserted 1171(b) Claims were provided to the Debtor with the expectation that they would be paid for out of the Debtor's current operating revenues, and not in reliance on its general creditworthiness.

Thereafter, on February 26, 2016, the bankruptcy court entered the Order which stated, in relevant part: "The Asserted 1171(b) Claims, to the extent allowed, are afforded priority status under § 1171(b). The amount of the Asserted 1171(b) Claims is not determined by this Order, and thus those Asserted 1171(b) Claims are not allowed in any amount at this time. The [Appellant]'s rights to object to the amount of the Asserted 1171(b) Claims are fully reserved."

The Appellant timely filed a notice of appeal of the Order. He also filed the subject motion for leave to appeal.

DISCUSSION

I. Interlocutory Orders

The Panel has jurisdiction to hear appeals from: (1) final judgments, orders and decrees; or (2) with leave of court, from certain interlocutory orders. 28 U.S.C. § 158(a); Fleet Data Processing Corp. v. Branch (In re Bank of New Eng. Corp.), 218 B.R. 643, 645 (B.A.P. 1st Cir. 1998). A decision is considered final if it "ends the litigation on the merits and leaves nothing for the court to do but execute the judgment." Id. at 646 (citations omitted). An interlocutory order, however, "only decides some intervening matter pertaining to the cause, and requires further steps to be taken in order to enable the court to adjudicate the cause on the merits." Id. (quoting In re American Colonial Broad. Corp., 758 F.2d 794, 801 (1st Cir. 1985)). Thus, "[t]o be final, 'a bankruptcy order need not resolve all of the issues in the proceeding, but it must finally dispose of all the issues pertaining to a discrete dispute within the larger proceeding.'" Morse v. Rudler (In re Rudler), 576 F.3d 37, 43 (1st Cir. 2009) (quoting Perry v. First Citizens Fed. Credit Union (In re Perry), 391 F.3d 282, 285 (1st Cir. 2004)). Here, the Order determined whether the Asserted 1171(b) Claims would be afforded priority status under § 1171(b), but it did not determine whether the Asserted 1171(b) Claims would be allowed and if so, in what amount. Moreover, the Order specifically reserved the Appellant's rights to object to the amount of the Asserted 1171(b) Claims. Thus, the Order did not resolve all of the issues relating to the Asserted 1171(b) Claims or the Claim Objection, and, therefore, it is interlocutory.

II. Motion for Leave to Appeal

The Panel has discretionary authority to grant leave to appeal from interlocutory orders pursuant to 28 U.S.C. § 158(a)(3). In determining whether to hear an interlocutory appeal from an order of a bankruptcy court under 28 U.S.C. § 158(a)(3), appellate courts in this circuit

typically apply the factors set forth in 28 U.S.C. § 1292(b), which defines the jurisdiction of courts of appeal to review interlocutory orders.[4] "Section 1292(b) permits appellate review of 'certain interlocutory orders, decrees and judgments . . . to allow appeals from orders other than final judgments when they have a final and irreparable effect on the rights of the parties.'" In re Bank of New Eng., 218 B.R. at 652 n.17.

To determine whether to exercise its discretion to review an interlocutory appeal, the Panel considers the following factors: (1) whether the order involved controlling questions of law; (2) whether there exists a substantial ground for difference of opinion; and (3) whether immediate appeal from the order might materially advance the ultimate termination of the litigation. See In re Advanced RISC Corp., 317 B.R. at 456; see also In re Bank of New Eng., 218 B.R. at 652. For an issue to rise to the level of difficulty and significance required under 28 U.S.C. § 1292(b), the case must involve "difficult and pivotal questions of law not settled by controlling authority." In re Bank of New Eng., 218 B.R. at 653. Dissatisfaction with the court's decision or a "garden variety legal argument" will not suffice. Id.

The Appellant asserts that the Order involved a controlling issue of law as it determined that the Asserted 1171(b) Claims were entitled to priority under § 1171(b), and that statute—as construed by applicable case law—is the only basis on which the Appellees can claim priority status. The Appellant also contends that substantial grounds for difference of opinion exist, as evidenced by the differing views of the parties in the proceedings below. The Appellant points out that, throughout the proceedings below, he consistently maintained that controlling authority

[4] See, e.g., Rodriguez-Borges v. Lugo-Mender, 938 F. Supp. 2d 202, 212 (D.P.R. 2013); Nickless v. Merrill Lynch, Pierce, Fenner & Smith, Inc. (In re Advanced RISC Corp.), 317 B.R. 455, 456 (D. Mass. 2004) (considering 28 U.S.C. § 1292(b) factors); Viburnum, Inc. v. The Directors and Officers of JBI (In re Jackson Brook Inst., Inc.), 280 B.R. 1, 4 (D. Me. 2002) (same); In re Bank of New Eng., 218 B.R. at 652 (same); Northeast Savings, F.A. v. Geremia (In re Kalian), 191 B.R. 275 (D.R.I. 1996) (same).

in the First Circuit—Boston & Maine I—explicitly mandates against priority treatment of the Asserted 1171(b) Claims. At the same time, the Appellees consistently argued that controlling authority in the First Circuit—Boston & Maine II—clearly weighs in favor of priority treatment. Moreover, the Appellant contends, the bankruptcy court's comments, commentary on the statute, case law construing the statute, and the findings and conclusions contained in the Order, are all evidence that substantial grounds for differing opinions exist with respect to this issue. Finally, the Appellant asserts that an immediate appeal of the Order will materially advance the ultimate termination of the claims adjudication process. The Appellant points out that the Appellees are seeking payment on the Asserted 1171(b) Claims at the same time they are defending against preference claims in various proceedings pending before the bankruptcy court and, if the Asserted 1171(b) Claims are determined to be general unsecured claims, they may be disallowed as a result of the pending preference litigation under § 502(d). If, however, those claims have priority status under § 1171(b), it is possible that § 502(d) may not be used to disallow the claims. Thus, the Appellant contends, the issue of basic claim allowance cannot continue until the issue on appeal is resolved.

In their response to the motion for leave to appeal, the Appellees agree that the sole issue on appeal is whether the bankruptcy court erred, as a matter of law, in failing to hold that interline freight charges of the type asserted by the Appellees as per se general unsecured claims not entitled to priority as "six-month" claims under § 1171(b). They disagree, however, with Appellant's assertion that the bankruptcy court's holding that the Asserted 1171(b) Claims are entitled to priority under § 1171(b) is in direct conflict with First Circuit precedent as set forth in Boston & Maine I. To the contrary, the Appellees contend, this legal issue has been resolved by controlling authority in the First Circuit as set forth in Boston & Maine II, and, therefore,

there are no grounds for a difference of opinion. Nonetheless, the Appellees do not oppose the motion for leave to appeal because they agree that resolution of this appeal may advance the ultimate termination of litigation with the Appellant and may effectively decide the preference litigation.

As the Order involves a controlling issue of law, and because both parties agree that resolution of this appeal will materially advance the ultimate termination of the claims adjudication process and the preference litigation pending in the bankruptcy court, the Panel will exercise its discretion under 28 U.S.C. § 158(a)(3) to hear this interlocutory appeal.

CONCLUSION

For the reasons set forth above, the motion for leave to appeal is hereby **GRANTED**.

FOR THE PANEL:

Dated: March 29, 2016

By: /s/ Mary P. Sharon
Mary P. Sharon, Clerk

[cc: Hon. Peter G. Cary, Clerk, U.S. Bankruptcy Court, District of Maine; and
D. Sam Anderson, Esq., Lindsay Zahradka, Esq., Alan Lepene, Esq., Keith Cunningham, Esq., Ryan Kelley, Esq., Eric Bradford, Esq., Stephen Morrell, Esq.]