IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF ALABAMA

In Re:

HARPER & ASSOCIATES, INC., Case No. 15-03160

Debtor.

ORDER ON OBJECTION TO CLAIM

This case is before the Court on the debtor's objection (doc. 160) to claim no. 7 filed by creditor Ashland General Agency, Inc. ("Ashland"). The Court has jurisdiction to hear this matter pursuant to 28 U.S.C. §§ 1334 and 157 and the order of reference of the district court. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(B), and the Court has authority to enter a final order.

Debtor Harper & Associates Insurance, Inc. ("Harper") is an independent insurance agency located in Mobile, Alabama. Ashland is an insurance brokerage agency in Mobile. Harper and Ashland have been doing business together for over 20 years. Harper as independent agent represents the insured in the procurement of insurance; Ashland as broker represents the insurer. Ashland represents ten or eleven insurance insurers and solicits business from 80 or 90 agents, one of which is Harper.

The two parties are relatively consistent in their description of the business arrangement as it existed prior to the bankruptcy. Harper as soliciting agent would request a quote from Ashland on behalf of an insured. If the quote was acceptable, Harper would ask Ashland on behalf of the insurer to bind coverage, which it had the power to do. [Ashland Exhib. 18, ¶ 1.1(b).] Harper would collect the total amount of the premium plus any applicable taxes from the insured. Ashland billed Harper on a monthly basis for the premiums and taxes, net the 10%

commission earned by Harper, for all policies sold during that month, with credit being given for any cancelled policies. Further up the line, the insurer would bill Ashland on a monthly basis for the premiums due it on all policies sold, net Ashland's commission. Ashland was obligated to pay the insurer once it bound coverage regardless of whether Harper paid.

If there were a return of unearned premiums because of a policy cancellation, the procedure would work in reverse. The insurer would apply a credit on its account with Ashland, Ashland would apply a credit on its monthly statement with Harper, and then Harper would be responsible for return of the unearned premium to the insured or premium financing company, whichever was the case. Although some other brokers work differently so that the insurer deals directly with the insured after the policy is placed, that was not the case with Ashland. Ashland dealt only through Harper and not directly with the insured. Any credits or returns of premium were applied on Ashland's monthly statements to Harper, with the exception of some small refunds which were made payable directly to insureds and delivered to Harper upon instruction of counsel after the filing of the bankruptcy case.

The brokerage contract between Harper and Ashland dates back to 1994 and does not provide for a security interest in favor of Ashland in any return of unearned premiums. [Harper Exhib. 1.]

Although Alabama Code § 27-7-36 required Harper to receive premiums from its insureds as trust funds in a fiduciary capacity and pay them over to the broker/insurer, at some point Harper started getting behind on its account with Ashland. By 2013, it owed about $60,000 on its account with Ashland. The parties discussed a possible sale of Harper from

which Ashland would be paid. There is some finger pointing between the parties as to why a sale never occurred, but the reasons are not relevant to the issues at hand.

Ashland's Exhibit 6 consists of the monthly statements from Ashland to Harper for the period of September 2012 through August 2015. The balance owed as of September 2012 was $69,968.04; by August 2015, the balance had grown to $368,567.93. Harper did not pay the net amount due in any given month during that period and instead usually paid even amounts such as $10,000, $15,000 or $20,000. Ashland credited Harper's payments to the oldest balance. However, it would use the funds received from Harper in any given month, along with funds collected from other agents, to pay the net amounts it owed to the various insurers on a current basis. Ashland would make up any shortfall by drawing on a line of credit. Ashland kept its collected premiums in an account separate from its operating account. Harper did not keep a separate account for collected premiums and instead used one operating account.

Ashland had the power on behalf of insurers to cancel policies on 10 days' notice for non-payment of premiums and on 30 days' notice for any other reason. [Ashland Exhib. 16, ¶ A.] The standard policy language called for any premium refunds to be paid to the "Named Insured." [Id.] However, as a matter of practice Ashland always credited the premium refunds to its account with Harper and Harper was responsible for making any refunds to the insured or premium finance company (with the exception of the postpetition refunds discussed above).

Harper filed this Chapter 11 case on September 25, 2015. On September 28, 2015, Ashland issued notices to about 20 policyholders that were insured clients of Harper cancelling their policies on 10 day notice for nonpayment of premiums. Harper quickly filed an adversary proceeding, AP No. 15-00157, seeking a temporary restraining order, preliminary injunction, and

damages against Ashland for alleged violation of the automatic stay. Harper contended that the premiums were in fact current on the policies which Ashland sought to cancel; that Ashland was violating the automatic stay; and that Harper was being damaged because it would lose business from insureds whose policies were being cancelled. When the motion for temporary restraining order came to be heard, the parties entered into a stipulation that Ashland would rescind its cancellations and the matter would be set for a later hearing on Harper's motion for preliminary injunction.

Harper's motion for preliminary injunction in the adversary proceeding and Ashland's motion for relief from stay in the main case (to cancel the policies and retain the unearned premiums) were set for an evidentiary hearing on December 14, 2015. After encouragement from the Court, the parties entered into settlement discussions and reached a resolution that day which was ultimately incorporated in a court order. The order provided that Harper would pay Ashland a total of $90,000 -- $60,000 within 30 days and $30,000 in installments over 13 months -- and that the payments "shall be credited to the ultimate, allowed claim of Ashland, if any, and the nature of such credit shall be later determined by the Court." [Harper Exhib. 5.] In return, Ashland would forego any efforts to cancel the policies at issue.

Although Ashland thought at the time of the preliminary injunction hearing that the unearned premiums on the policies it sought to cancel were about $120,000 on the September 25, 2015 petition date and about $60,000 at the time of the December 14, 2015 hearing, after further research it determined that those amounts were $145,333.44 and $80,845.44, respectively. [Ashland Exhib. 14.]

Since approval of the settlement in January 2016, Harper has paid the $90,000 as agreed to Ashland. Ashland has filed a proof of claim no. 7 and a stipulation that, after application of the $90,000, it is currently owed $260,604.33 as a general unsecured claim. [Ashland Exhib. 15.] Harper disputes that calculation, contending that pursuant to the agreed order the $90,000 is to be credited toward whatever distribution Ashland is to receive under a Chapter 11 plan -- not the amount of the claim itself. Ashland contends that that was not the agreement incorporated into the order; alternatively, it says (a) a portion of its claim was secured from the outset pursuant to its right of setoff or recoupment under Bankruptcy Code § 553 or (b) that it should have an administrative expense claim pursuant to Bankruptcy Code §§ 503(b)(1) or 507(b) because it preserved the estate by giving up its alleged right to return of unearned premiums and because its interest in the unearned premiums was not adequately protected.

The first issue before the Court is interpretation of the agreed order entered January 6, 2016 on the Harper's motion for preliminary injunction in the adversary proceeding and Ashland's motion for relief from stay in the main case. As noted above, the order provided that Ashland would pay $60,000 within 30 days and then a stream of payments totaling $30,000 within 13 months. Both paragraphs contain the same language that the $60,000 and $30,000 "payment[s] shall be credited to the ultimate, allowed claim of Ashland, if any, and the character of such credit shall be later determined by the Court." The agreed order further provided in paragraph 6: "The above compromise does not reflect any agreement regarding the extent of or the allowance of any claim of Ashland or whether such claim is a secured, priority or unsecured claim. All rights are reserved."

The order in question was jointly drafted by the parties and submitted to the Court. The Court is not construing its terms against either party as drafter. After considering the evidence presented at trial regarding the settlement and reviewing the audiotape of the December 14, 2015 hearing, the Court finds that the provision in the order about application of the settlement funds means what it says -- that the $90,000 was to be credited to the "claim" of Ashland, not to the amount of any distribution Ashland may receive under a confirmed Chapter 11 plan. The term "claim" is a term of art in the bankruptcy world. Although we are here dealing with a court order rather than the Bankruptcy Code, "claim" is defined at 11 U.S.C. § 101(5) as a "right to payment," whether or not reduced to judgment, liquidated, fixed, contingent, etc. A claim is very different from a distribution resulting from a bankruptcy case; indeed, one of the primary purposes of the bankruptcy system is to determine what distribution is to be made on a given claim in the particular circumstances of a bankruptcy case. If the parties and the Court had intended for the $90,000 to be credited against Ashland's ultimate distribution pursuant to a confirmed plan of reorganization, the order would have contained words to that effect. The parenthetical phrase "and the nature of such credit shall be later determined by the Court" does not change the meaning.

This ruling is consistent with Harper's counsel's explanation of the settlement in open court on the date of the preliminary injunction hearing:[1]

Harper's counsel:	The [first payment of] $60,000 will be credited to the overall obligation to Ashland General Agency. However, no one is saying specifically what that amount.
Court:	[Unintelligible] old versus new?

1 The following rendition is based on the undersigned's review of the audiotape of the hearing and is not an official transcript.

Case 15-03160 Doc 240 Filed 04/28/17 Entered 04/28/17 16:33:32 Desc Main
Document Page 6 of 9

Harper's counsel:	Well, no. No agreement as to the character of that claim or the amount of that claim. It will have to be an allowed claim ultimately. So no workout on, however, that claim, let's say for example, if it's $100,000, $60,000 will be credited to that claim such that the residual amount will be $40,000. Now whether that $40,000, that's just in the abstract.
Court:	Are you talking about overall claim or talking about secured claim?
Harper's counsel:	Overall claim. Now if the other side says the $40,000, the other side may argue that $40,000 is secured. We will argue $40,000, I'm sure we'll argue is unsecured, but that will have to be addressed at a later time, as part of the plan.
	. . . .
Harper's counsel:	Now, the residual amount, if any, which I know the other side will argue yes, there is a residual amount, the character of that, the nature of that, will be determined at a later time. So if it's all unsecured then it'll be put set forth in the plan as unsecured. The other side will retain the opportunity to say we don't agree that all of that is unsecured, but we think it should be more, that's something that'll have to get worked out down the road. The primary purpose of this compromise is to address what we're here for today. Although certainly the administrative expense claim, you know, carries beyond that.
	. . . .
Harper's counsel:	There is no agreement, as I think I have already stated on the allowance of Ashland's claim. Or on the character of the remainder of the claim. No claims are released except for those that we have discussed and all rights are reserved by the parties otherwise.

The undersigned's understanding both after the in-court description of the settlement and upon reviewing the draft order was that Harper would pay Ashland $90,000 in exchange for Ashland not cancelling the policies and that the parties would fight another day about whether Ashland had any remaining claim or whether any remaining claim was unsecured, secured, or administrative. Although the order was drafted by counsel, the Court is entitled to interpret its own order. "[A] bankruptcy court's interpretation of its own prior order is entitled to

substantial deference." In re Optical Technologies, Inc., 425 F.3d 1294, 1302-03 (11th Cir. 2005). "A court's order does not mean what a litigant, even a drafting litigant, subjectively and privately hopes it to mean; rather, the interpretation of a court's order triggers an objective examination." Taylor v. Teledyne Technologies, Inc., 338 F. Supp. 2d 1323, 1341-42 (N.D.Ga. 2004).

Harper's owner Robert Harper testified that he thought that the $90,000 was to be credited against Ashland's distribution under the plan. However, he testified his understanding was based upon his discussions with his own counsel, not discussions with Ashland or Ashland's counsel. His different understanding thus does not change the result. "It is elementary that it is the terms of the written contract, not the mental operations of one of the parties, that control its interpretation." Alabama Title Loans, Inc. v. White, 80 So. 3d 887, 893 (Ala. 2011) (quoting Kinmon v. J.P. King Auction Co., 276 So. 2d 569, 570 (1973)).

As noted above, Ashland has stipulated that, after credit for the $90,000 paid, its claim is unsecured in the amount of $260,604.33.

At the hearing of this matter conducted over the greater portions of two days, the parties presented evidence as to whether Ashland has an administrative expense claim under Bankruptcy Code §§ 503 or 507(b) for the unearned premiums which it contends it was entitled to receive after ten or thirty days' notice of cancellation or whether it should be entitled to a secured claim under Bankruptcy Code § 553 based upon a right of setoff or recoupment. The Court also informed the parties that it intended to rule on those issues. However, after further reflection since the hearing, the Court is going to defer any such ruling because those issues are not properly before the Court. Ashland has not filed an application or motion for approval of

administrative expense with notice to all creditors, so there is no actual motion before the Court and there has been no notice to other creditors whose treatment in the plan could be affected if an administrative expense claim were allowed. Similarly, at this point Ashland does not seek to have any part of its amended claim treated as secured; it would thus not be appropriate for the Court, on the debtor's objection to Ashland's unsecured claim, to consider whether to allow some portion of the claim as secured when the creditor is not asserting such a claim. Again, other creditors whose treatment might be affected have received no notice of such a potential ruling. Perhaps depending on whether debtor appeals the ruling on its objection to Ashland's claim, Ashland may take no further action with regard to seeking an administrative or secured claim; that has been its position thus far. If Ashland does file a motion for administrative claim or at point amend its claim to seek secured status, unless some party other than Ashland or Harper wishes to participate, the Court intends to take those matters under consideration without a further evidentiary hearing.

However, for the time being, for the reasons stated above, the Court overrules the debtor's objection to Ashland's claim no. 7 and allows the claim as unsecured in the amount of $260,604.33. The Court is not ruling upon whether Ashland is entitled to an administrative expense claim or secured claim. The Court resets Harper's disclosure statement (doc. 143) and Ashland's objection (doc. 154) for hearing at 8:30 a.m. on June 6, 2017.

Dated: April 28, 2017

HENRY A. CALLAWAY
CHIEF U.S. BANKRUPTCY JUDGE