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U.S. BKCY. APP. PANEL
OF THE NINTH CIRCUIT

NOT FOR PUBLICATION

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UNITED STATES BANKRUPTCY APPELLATE PANEL
OF THE NINTH CIRCUIT

In re:)	BAP No.	CC-13-1494-KiTad
)		
MERUELO MADDUX PROPERTIES,)	Bk. No.	1:09-13356-VK
INC.,)		
)		
Debtor.)		
_____)		
)		
RICHARD MERUELO,)		
)		
Appellant,)		
)		
v.)	MEMORANDUM¹	
)		
REORGANIZED MERUELO MADDUX)		
PROPERTIES, INC.,)		
)		
Appellee.)		
_____)		

Argued and Submitted on June 26, 2014,
at Pasadena, California

Filed - August 20, 2014

Appeal from the United States Bankruptcy Court
for the Central District of California

Honorable Victoria S. Kaufman, Bankruptcy Judge, Presiding

Appearances: _____
Aimee Dominguez, Esq. of Dominguez Alejo LLP argued
for appellant Richard Meruelo; Christopher E.
Prince, Esq. of Lesnick Prince & Pappas LLP argued
for appellee Reorganized Meruelo Maddux Properties,
Inc.

Before: KIRSCHER, TAYLOR and DUNN, Bankruptcy Judges.

¹ This disposition is not appropriate for publication.
Although it may be cited for whatever persuasive value it may have
(see Fed. R. App. P. 32.1), it has no precedential value. See 9th
Cir. BAP Rule 8013-1.

1 Richard Meruelo ("Meruelo") appeals an order denying his
2 request for severance pay in connection with his postpetition
3 termination from chapter 11² debtor, Meruelo Maddux Properties,
4 Inc. ("Debtor"). Because the bankruptcy court applied an
5 incorrect standard of law to Meruelo's severance claim, we VACATE
6 and REMAND, in part.

7 **I. FACTUAL BACKGROUND AND PROCEDURAL HISTORY**

8 **A. Prepetition events**

9 Meruelo, former CEO and Chairman of the Board of Directors
10 for Debtor, entered into an Executive Employment Agreement with
11 Debtor on January 30, 2007. It provided, among other things, a
12 base salary of \$450,000 and a mandatory annual bonus equal to
13 fifty percent of the base (\$225,000). The Employment Agreement
14 had an initial three-year term, but would automatically renew for
15 successive one-year terms, unless either party gave the required
16 notice of non-renewal.

17 If Meruelo's employment terminated "without cause," he would
18 receive a single lump-sum severance payment equal to three times
19 the sum of (i) his base salary and (ii) the greater of (a) the
20 bonus actually paid to him for the most recent completed fiscal
21 year and (b) the minimum bonus that would have been paid during
22 the fiscal year in which his employment was terminated. In short,
23 Meruelo would receive at least \$2,025,000.³

24 _____
25 ² Unless specified otherwise, all chapter, code and rule
26 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and
the Federal Rules of Bankruptcy Procedure, Rules 1001-9037.

27 ³ An identical employment agreement for Debtor's President
28 and COO, John Maddux ("Maddux"), was executed on the same day.

continue...

1 **B. Postpetition events**

2 Debtor and its affiliated entities filed chapter 11
3 bankruptcy cases in March 2009, before the end of the initial term
4 in Meruelo's Employment Agreement. The cases were consolidated
5 and jointly administered. Debtor continued its usual operations,
6 and Meruelo continued to serve as CEO. Meruelo filed a proof of
7 claim on September 23, 2009, and another one on March 7, 2012.

8 The initial term of Meruelo's Employment Agreement expired on
9 January 30, 2010. The Employment Agreement was not assumed, but
10 Meruelo continued to work for Debtor.

11 **1. The notice of non-renewal**

12 After the appointment of the Official Committee of Equity
13 Holders ("OEC") and during the time that competing plans were
14 being offered by Debtor and entities known as Charlestown Capital
15 Advisors, LLC and Hartland Asset Management Corporation
16 (collectively "Charlestown"), it became apparent to Debtor that if
17 the Charlestown plan were approved, Meruelo would no longer be
18 employed with the reorganized debtor and would hold a substantial
19 claim as a result of his termination. In particular, Meruelo
20 would be entitled to a significant severance package if he were
21 terminated during the Employment Agreement's term.

22 In a formal written demand sent to Debtor on September 21,
23 2010, the OEC's counsel noted that Meruelo's Employment Agreement
24 would automatically renew for another one-year term (from
25 January 31, 2011 to January 30, 2012) absent the delivery of a

26 _____
27 ³...continue

28 Maddux sought the same severance claim as Meruelo. He is not a party to this appeal, but we discuss him where necessary.

1 non-renewal notice by November 29, 2010. To avoid Meruelo's
2 severance claim, the OEC demanded that Debtor issue a notice of
3 non-renewal by September 29, 2010.

4 When Debtor, still under the control of Meruelo and Maddux,
5 failed to issue the notice of non-renewal, the OEC sought standing
6 to issue it. The OEC noted that if the Charlestown plan were
7 confirmed, Meruelo would be terminated and such termination would
8 be "without cause" per the terms of his Employment Agreement. In
9 that case, Meruelo would hold a claim for severance. The OEC
10 contended that if the non-renewal notice were timely issued,
11 Meruelo's severance claim would be avoided because his employment
12 would not be terminated during the employment term under the
13 Employment Agreement. Failing to issue it, however, would result
14 in Debtor being saddled with a substantial administrative expense
15 for Meruelo's severance claim.

16 Debtor opposed the OEC's motion, contending that issuing the
17 notice of non-renewal to Meruelo would qualify as a "good reason"
18 for him to resign, thereby triggering a severance payment equal to
19 "one times the sum" of his base salary plus the amount equal to
20 the bonus he was paid the previous year. Likewise, a termination
21 "without cause" would trigger a severance payment equal to "three
22 times the sum" of his base salary plus the greater of the amount
23 equal to the bonus he was paid the previous year or what he would
24 have received in the year of his termination. Debtor contended
25 the notice of non-renewal clause in the Employment Agreement
26 permitted Debtor to terminate Meruelo's employment or at least to
27 transition him to an "at will" employee, without such termination
28 qualifying as one "without cause." However, argued Debtor, to

1 invoke this beneficial clause the executory Employment Agreement
2 would first have to be assumed, a decision within Debtor's
3 business judgment, not the OEC's, and which would require Debtor
4 to cure all existing defaults, currently about \$1 million in
5 unpaid bonuses.

6 After two hearings on the matter, the bankruptcy court
7 granted the OEC standing to issue the notice of non-renewal. The
8 order expressly provided that the issuance of the non-renewal
9 notice would not expand or restrict any party's right to dispute a
10 claim asserted by Meruelo under the Employment Agreement including
11 (a) any party's right to assert that his employment may be
12 terminated for "cause" or (b) Meruelo's right to assert a claim
13 under the Employment Agreement against the estate.

14 The OEC issued the notice of non-renewal to Meruelo on
15 November 24, 2010. Despite the notice, Meruelo continued to work
16 for Debtor until August 5, 2011, when he was officially
17 terminated.

18 **2. The Charlestown Plan and Meruelo's termination**

19 The bankruptcy court confirmed the Charlestown Plan. Per the
20 Charlestown Plan and by operation of law, on July 25, 2011,
21 Meruelo ceased to be employed by the reorganized debtor, EVOQ
22 Properties, Inc. ("EVOQ"). On August 5, 2011, EVOQ issued to
23 Meruelo a notice of termination, effective July 25, 2011.
24 Enclosed was a check for the amount EVOQ maintained was Meruelo's
25 accrued unpaid salary through August 5, as well as his unused
26 vacation time through July 25. The termination notice advised
27 Meruelo to file an administrative claim for any unpaid bonus
28 compensation he felt he was entitled to.

1 **3. Meruelo's motion to compel payment of wages and**
2 **severance**

3 In response to his termination, Meruelo filed a Motion for
4 Order Compelling Debtors to Pay Administrative Expense and
5 Prepetition Unsecured Wage Claims ("Motion to Compel Payment").
6 In short, Meruelo argued that EVOQ, per the Charlestown Plan,
7 failed to pay his administrative expense and prepetition unsecured
8 claim on the Effective Date, July 25, 2011. Meruelo argued he was
9 entitled to no less than \$450,000 in bonus wages for 2009 and 2010
10 (\$225,000 for each year), a prorated bonus of \$133,767 for 2011
11 (from January 31, 2011 to August 5, 2011, after the non-renewal
12 notice and up to the termination date), at least \$2,025,000 in
13 severance pay, accrued and unused vacation wages, and other
14 penalties and attorney's fees.⁴ The Motion to Compel Payment did
15 not distinguish whether the severance payment was considered a
16 prepetition unsecured claim or an administrative expense. Nowhere
17 in the motion were relevant Code sections referenced or discussed.

18 EVOQ opposed Meruelo's Motion to Compel Payment, arguing that
19 Meruelo was not entitled to an administrative claim for his 2011
20 base salary, bonus and severance benefits under the Employment
21 Agreement. The Employment Agreement no longer existed because it
22 expired on January 30, 2011. As for Meruelo's prepetition claims,
23 EVOQ argued that it had 180 days from the Effective Date of the
24

25 ⁴ Upon objection by several creditors to Meruelo's bonus
26 wages for 2009, Judge Thompson issued a Memorandum Decision on
27 July 6, 2009, determining that the issue of bonus wages to Meruelo
28 and other Debtor executives was to be decided at a later date
"upon further notice to creditors." All objections to payment of
his salary were overruled. The 2009 bonus wages were later
granted by Judge Kaufman on November 23, 2011.

1 Charlestown Plan to object to prepetition claims. Thus, Meruelo's
2 request was premature.

3 In November 2011, the bankruptcy court granted the Motion to
4 Compel Payment, in part, as to Meruelo's 2009 bonus claim. He was
5 ultimately also awarded his 2010 bonus claim. In its arguments
6 against Meruelo's remaining employment claims, EVOQ conceded that
7 Meruelo was entitled to reasonable compensation for his services
8 after the Employment Agreement expired, but argued he was not
9 entitled to severance because once the Employment Agreement
10 expired, the Term of Employment ended and the company was no
11 longer liable for severance pay.

12 In June 2012, the bankruptcy court issued a scheduling order
13 for Meruelo's remaining disputed employment claims: (1) his 2011
14 bonus claim for \$133,767; and (2) his claim for severance pay.⁵
15 The court ordered briefing and scheduled an evidentiary hearing.

16 Meruelo, pro se, filed his brief, which incorporated the
17 arguments made in Maddux's brief on the same issue. Meruelo (as
18 argued by Maddux) contended he was entitled to severance if he was
19 terminated without cause during the "Term of Employment," which
20 was defined in paragraph 3 of the Employment Agreement. While the
21 "Term of Employment" included the three-year initial term and any
22 one-year extended term, the Employment Agreement did not address
23 when the "Term of Employment" technically ended. Meruelo argued
24 that issue was answered in the last sentence of paragraph 3, which
25 provided, "but the Term of Employment shall end upon any

26
27 ⁵ The bankruptcy court's ruling respecting the 2011 bonus
28 claim is not at issue in this appeal, but we discuss it where
necessary since it was decided with the severance claim.

1 termination of Executive's employment with Employer as herein
2 provided." Arguably, the language did not say the Term of
3 Employment ended when the initial term or extended term expired.
4 Instead, argued Meruelo, the Term of Employment ended when the
5 employment terminated, which implied that the Term of Employment
6 was effective until he was officially terminated on August 5,
7 2011, not when the notice of non-renewal was sent in November
8 2010. Thus, the terms of the Employment Agreement were
9 enforceable at the time he was terminated, and he was entitled to
10 full severance.

11 Meruelo argued that he should get the severance he bargained
12 for and not be in a worse position because he remained on the job,
13 when he could have resigned upon the non-renewal notice and
14 received the severance payment. Alternatively, if the court
15 determined that the terms of the Employment Agreement were not
16 contractually binding at the time of his termination, Meruelo
17 argued he was entitled to a "reasonable" severance on a "quantum
18 meruit" basis.

19 EVOQ argued that expiration of the Employment Agreement
20 precluded any severance, and it disputed Meruelo's contention that
21 the notice of non-renewal served no purpose, particularly when he
22 and Maddux decided to not renew every other executive whose
23 initial term was set to expire in January 2009 in order to avoid
24 severance claims. EVOQ also disputed Meruelo's quantum meruit
25 theory; it argued that quantum meruit applied only to the 2011
26 bonus because the parties had disputed what was the "reasonable
27 value" of Meruelo's services. EVOQ distinguished the cases
28 Meruelo claimed supported his quantum meruit theory for severance.

1 **4. The evidentiary hearing and the bankruptcy court's**
2 **ruling on the 2011 bonus and severance claims**

3 At the start of the evidentiary hearing on the 2011 bonus and
4 severance claims, the bankruptcy court confirmed with counsel for
5 EVOQ that both claims were administrative expense claims. The
6 court went on to say that such claims were "supposed to be
7 necessary and beneficial," and that the burden was on the claimant
8 to demonstrate the bonus and severance package was necessary to
9 "keep them there." Hr'g Tr. (April 22, 2013) 12:1-4. The court
10 then stated that the burden was on the claimant to "show the
11 reasonableness of the compensation," particularly when the
12 Employment Agreement was not controlling as it was not renewed.
13 Id. at 12:13-13:1. It later ruled that the 2011 bonus and
14 severance claims were not subject to the terms of the Employment
15 Agreement because it had not been renewed; Meruelo was working
16 without a contract during the period of January 31, 2011 through
17 August 5, 2011.

18 Counsel for EVOQ then argued that because the Employment
19 Agreement was not controlling, the court had to look at what was
20 "reasonable," and Meruelo and Maddux had not presented any
21 evidence as to what amount was reasonable. After further argument
22 by EVOQ, counsel for Maddux argued:

23 MR. SHEMANO: The Court mentioned that these claims are
24 being asserted as administrative expense claims and
25 really were these reasonable and necessary benefits to
26 the estate. Let's just remember, we can call these -- we
27 don't have to call these administrative expense claims;
28 we can call these general unsecured claims.

27 Id. at 18:15-20. The bankruptcy court then noted again that the
28 2011 bonus and severance claims were brought as administrative

1 expense claims, but opined that even if they were considered
2 unsecured claims, the burden was still on the claimant to show the
3 amount requested was "reasonable" given that no contract was in
4 effect. Id. at 22:11-23:5. In response, Maddux's counsel stated
5 that the court did not need to get "fixated" on "whether these are
6 administrative expense claims or not." Id. at 23:7-9. His
7 client's case did "not stand or fall on whether we demonstrate
8 benefit to the estate." Id. at 23:19-20.

9 After further argument from counsel, the bankruptcy court
10 expressed its view about the severance claim:

11 The agreements were not renewed. They waived their right
12 to severance. They could have collected it and left and
13 said, you know what, go ahead with that other plan. But
14 instead, they decided, we're going to shoot for keeping
15 the company in our control.

16 . . .

17 I don't have any evidence that this is reasonable. I
18 don't think it is reasonable. I don't understand why
19 that would be reasonable

20 . . .

21 They -- I don't think its reasonable. I think it's their
22 burden to show it's reasonable.

23 . . .

24 No, it is not reasonable for people who stayed on after
25 the agreements were not renewed to simply assume in the
26 absence of an approved -- court-approved employment
27 agreement -- they didn't ask for severance in their
28 insider comp forms.

29 . . .

30 Well, I don't think there's any record it's reasonable.
31 There's no record it's reasonable. None, zero. I mean,
32 you may say that, well, we have a record that since the
33 Court approved the 2009 bonuses and 2010 bonuses maybe
34 the Court should approve (indiscernible), but no court
35 ever approved the severance It was never
36 litigated.

1 . . .

2 Okay. So I just don't think it's reasonable to expect
3 you to collect severance pay when there was all this
4 litigation about the fact that you were going to get a
5 notice of non-renewal to cut off your right to severance
6 pay.

5 . . .

6 There's no . . . evidence that the severance amount is
7 reasonable, none. No evidence that it's reasonable. I
8 mean, you're saying based on a 2007 contract provided for
9 three times when he knew that there was a notice of non-
10 renewal and that this was the main focus of it and -- you
11 know, he -- there's just no evidence that it's -- in this
12 context that it's reasonable.

10 . . .

11 There's no evidence that somebody else would have
12 required three years of severance or they would have
13 agreed to pay three years of severance.

13 Id. at 38:1-5; 39:13-16; 39:20-22; 40:6-10; 40:21-41:3; 42:5-9;
14 51:5-13; 51:21-23. In response, counsel for Maddux argued:

15 MR. SHEMANO: Your Honor, we say under § 502(b)(4) this
16 Court can do what it wants as a court of equity of
17 reasonableness. If this Court thinks three times [the
18 base salary] is not reasonable, we live or die with that.
19 Like I said, we -- that's what our papers say.

18 Id. at 51:24-52:3. Upon further discussion, the following
19 colloquy ensued:

20 MR. SHEMANO: Your Honor, again, the point is, when they
21 negotiated it . . . this is a package. Okay. And if you
22 -- if the Court thinks the value is zero under quantum
23 meruit, I think the Court is making a mistake. I -- if
24 the Court said it's not two million dollars, I can't
25 argue with the Court. I think there's a number between
26 zero and two million that based upon the facts and
27 circumstances this Court should --

24 THE COURT: I'm not picking numbers out of the sky.

25 MR. SHEMANO: -- choose --

26 THE COURT: I mean, you know, I'm just -- it's not --

27 MR. SHEMANO: Well, all right, now, I will --
28

1 THE COURT: Three times is unreasonable. There's no
2 evidence it's reasonable. The fact that it's in a
contract that was negotiated three years before

3 Id. at 54:5-21.

4 After further argument from counsel, the bankruptcy court
5 announced its oral ruling denying the severance claim in its
6 entirety:

7 I don't think [the severance amount is] reasonable or
8 appropriate on quantum meruit grounds that that severance
amount in that contract, which was not renewed.

9 And I think whether it's administrative or unsecured,
10 it's the claimant's ultimate burden on showing it as
being reasonable and appropriate and payable and I don't
11 see it where an agreement wasn't renewed, and for all of
the reasons I've articulated. So I think the case is
12 [sic] that look at severance are distinguishable on the
specific facts of this case, and so no severance.

13 Id. at 75:18-76:2.

14 The bankruptcy court entered an order allowing Meruelo's 2011
15 bonus claim but denying his claim for severance ("Compel Order").
16 The Compel Order was silent as to what authority the bankruptcy
17 court relied upon for its decision. On September 24, 2013, the
18 court entered an order for attorney's fees in connection with
19 Meruelo's and Maddux's employment claims. Although they were
20 determined to be the prevailing parties, because Meruelo had no
21 attorney's fees or expenses, he was awarded nothing. This timely
22 appeal followed.

23 **II. JURISDICTION**

24 The bankruptcy court had jurisdiction under 28 U.S.C. §§ 1334
25 and 157(b) (2) (B). We have jurisdiction under 28 U.S.C. § 158.

26 **III. ISSUE**

27 Did the bankruptcy court abuse its discretion by applying an
28 incorrect standard of law to Meruelo's severance claim?

1 **IV. STANDARD OF REVIEW**

2 We review the bankruptcy court's order allowing or
3 disallowing an administrative claim for abuse of discretion.
4 Gonzales v. Gottlieb (In re Metro Fulfillment, Inc.), 294 B.R.
5 306, 309 (9th Cir. BAP 2003) (citing Teamsters Indus. Sec. Fund v.
6 World Sales, Inc. (In re World Sales, Inc.), 183 B.R. 872, 875
7 (9th Cir. BAP 1995)). A bankruptcy court abuses its discretion if
8 it applies an incorrect legal standard or its factual findings are
9 illogical, implausible or without support from evidence in the
10 record. TrafficSchool.com v. Edriver Inc., 653 F.3d 820, 832 (9th
11 Cir. 2011).

12 **V. DISCUSSION**

13 **The bankruptcy court abused its discretion by applying an**
14 **incorrect standard of law to the severance claim.**

15 We start by briefly recapping the pertinent facts of this
16 case. Meruelo's Employment Agreement, which no one disputes was
17 an executory contract, was executed in January 2007. It was still
18 in effect when Debtor filed its chapter 11 cases in 2009, as the
19 initial term of the Employment Agreement did not end until
20 January 30, 2010. The Employment Agreement was not assumed or
21 rejected prior to confirmation, but the parties apparently
22 believed that it renewed for one more year from January 31, 2010
23 to January 30, 2011. The OEC acted as though it had renewed,
24 which explained its belief that a notice of non-renewal was needed
25 by November 29, 2010, to satisfy the 60-day notice requirement.
26 The bankruptcy court also noted at the evidentiary hearing that
27 the Employment Agreement automatically renewed for one more year
28 in January 2010.

1 The bankruptcy court did not enter written findings and
2 conclusions, nor state its analysis with any particularity at the
3 evidentiary hearing. The court determined: that the Employment
4 Agreement had not been renewed after January 2011 and had expired
5 prior to Meruelo's termination in August 2011; and that the amount
6 of his severance claim was not reasonable. The court, however,
7 never stated any statutory or case law authority for its decision.

8 The bankruptcy court stated during its oral ruling that
9 whether the severance claim was an administrative expense or an
10 unsecured claim, the claimant had the burden to prove the amount
11 was "reasonable." The court also stated that it had distinguished
12 the "quantum meruit" cases cited by Maddux (and thus Meruelo), but
13 did not say on what basis. Adding to the confusion, Meruelo
14 argued in the Motion to Compel Payment that the severance claim
15 was an administrative expense, but later argued (through Maddux)
16 that such claim could be treated as either an administrative
17 expense or an unsecured claim under § 502(b)(4). Meruelo had
18 filed both a proof of claim and the Motion to Compel Payment,
19 which functioned as a motion to allow an administrative expense
20 claim. The Compel Order, drafted by counsel, does not state under
21 what authority the severance claim was being denied.

22 Section 502(b)(4) provides for the allowance of a claim over
23 objection "except to the extent that . . . if such claim is for
24 services of an insider . . . such claim exceeds the reasonable
25 value of such services." Thus, an insider's claim for services
26 under § 502(b)(4) is subject to a "reasonableness" standard. See
27 The Margulies Law Firm, APLC v. Placide (In re Placide), 459 B.R.
28 64, 72 (9th Cir. BAP 2011). However, such claims are only for the

1 insider's services rendered and unpaid at the time of the filing
2 of the petition. 4 COLLIER ON BANKRUPTCY ¶ 502.03[5][a] (Alan N.
3 Resnick & Henry J. Sommer eds., 16th ed. 2012). In other words,
4 § 502(b)(4) applies to prepetition claims. Since the claims at
5 issue here were for Meruelo's 2011 bonus, which was for services
6 rendered postpetition, and the severance claim, which accrued
7 postpetition, they were not for prepetition claims. Therefore, if
8 the bankruptcy court applied § 502(b)(4), it abused its
9 discretion.

10 Section 503(b)(1)(A)(i) provides that administrative expenses
11 include "the actual, necessary costs and expenses of preserving
12 the estate, including wages, salaries, and commissions for
13 services rendered after the commencement of the case[.]" The
14 burden of proving an administrative expense claim is on the
15 claimant. Einstein/Noah Bagel Corp. v. Smith (In re BCE West,
16 L.P.), 319 F.3d 1166, 1172 (9th Cir. 2003).

17 The Ninth Circuit has afforded administrative expense
18 priority for certain types of severance pay for employees who
19 provided postpetition services. The rule is that "pay at
20 termination in lieu of notice" is considered an administrative
21 expense, but "pay at termination based upon length of employment"
22 is not. See Teamsters Local No. 310 v. Ingram (In re Tucson
23 Yellow Cab Co.), 789 F.2d 701, 703 (9th Cir. 1986); Lines v. Sys.
24 Bd. of Adjustment No. 94 Bhd. of Ry., Airline & S.S. Clerks
25 (In re Health Maint. Found.), 680 F.2d 619, 621 (9th Cir. 1982)
26 (applying § 64(a)(1) of the former Bankruptcy Act, now
27 § 503(b)(1)(A)(i)). However, the lump-sum severance payment at
28 issue here does not fall into either one of these categories. It

1 provided for severance on termination without cause, with no
2 mention of length of service or a notice period. We faced this
3 same issue in Dullanty v. Selectors, Inc. (In re Selectors, Inc.),
4 85 B.R. 843, 845-46 (9th Cir. BAP 1988):

5 Despite the apparent simplicity of the severance pay
6 rule, the result in the instant case is not obvious.
7 First, the parachute clause in the case at bar is not
8 like the provisions in the cases cited above. In those
9 cases, the severance pay clauses provided compensation
10 based upon what the employee would have earned during a
11 specified period prior to termination. See Tucson Yellow
12 Cab, 713 F.2d at 703 (two weeks notice or two weeks pay);
13 Health Maintenance, 680 F.2d at 620 (specified number of
14 days pay based on length of employment); Mammoth Mart,
15 536 F.2d at 952 (one [week's] salary per year of
16 employment); Straus-Duparquet, 386 F.2d at 650 (one or
17 two weeks pay); Public Ledger, 161 F.2d at 771 (specified
18 number of weeks pay depending on the length of
19 employment). (Footnote omitted).

20 The parachute clause in the instant case is unlike any of
21 these provisions: It does not provide compensation based
22 upon salary during employment; nor does it mention or
23 base compensation upon any notice period or length of
24 employment.

25 . . .

26 In our view, the parachute clause in the instant case is
27 so different from the severance pay provisions addressed
28 in the Ninth Circuit cases, that it should not be forced
into either category.

We held that in cases with severance or "parachute" clauses like
the one at issue here, the Ninth Circuit severance pay rules are
inapplicable, and instead such clauses should be subjected to
analysis under § 503(b)'s standards – does the severance clause
give rise to an actual and necessary expense of preserving the
estate? Id. at 846.

We recognize authority exists which dictates that employees
shall receive compensation on a quantum meruit basis for services
rendered postpetition for the time period before an executory

1 contract has been assumed or rejected:

2 If the debtor-in-possession elects to continue to receive
3 benefits from the other party to an executory contract
4 pending a decision to reject or assume the contract, the
5 debtor-in-possession is obligated to pay for the
reasonable value of those services, which depending on
the circumstances of a particular contract, may be what
is specified in the contract.

6 NLRB v. Bildisco & Bildisco, 465 U.S. 513, 531 (1984). This
7 "reasonable value of services" standard appears to be what the
8 bankruptcy court applied to both the 2011 bonus claim and the
9 severance claim. While this may be the proper standard to apply
10 for compensation consisting of wages or something akin to wages
11 when a contract has not yet been assumed or is non-existent, it
12 does not apply to severance claims.

13 A claimant's right to a lump-sum severance payment should be
14 analyzed under the general rules governing administrative expense
15 priority. In re Selectors, Inc., 85 B.R. at 846; Bachman v.
16 Commercial Fin. Servs., Inc (In re Commercial Fin. Servs., Inc.),
17 246 F.3d 1291, 1293-94 (10th Cir. 2001) (applying § 503(b)'s
18 "actual and necessary" test to executives' lump-sum severance
19 claims); Klemick v. Able Labs., Inc., 2007 WL 952030, at *5
20 (D.N.J. Mar. 28, 2007) (same); In re Big M, Inc., 2014 WL 2442940,
21 at *4 (Bankr. D. N.J. May 30, 2014) (same); In re Ellipso, Inc.,
22 2012 WL 827103, at *3 (Bankr. D.D.C. Mar. 9, 2012) (employment
23 contract not assumed; court applied "reasonable value" test to
24 executive's wage claim, but applied § 503(b)'s "actual and
25 necessary" test to executive's severance claim); In re M Group,
26 Inc., 268 B.R. 896, 902 (Bankr. D. Del. 2001) (applying "actual and
27 necessary" test under § 503(b) to executive's lump-sum severance
28 claim); In re Uly-Pack, Inc., 128 B.R. 763, 766-69 (Bankr. S.D.

1 Ill. 1991) (employment contract of chapter 11 debtor's former CEO
2 was terminated postpetition when case was converted to chapter 7
3 and assets were sold by trustee; court applied § 503(b) analysis
4 to severance claim but determined it was entitled only to the
5 status of a general unsecured claim under § 502(b)(7)).

6 In determining whether the claimant's severance claim is
7 entitled to priority as an administrative expense, the bankruptcy
8 court must consider: (1) was the severance provision the result
9 of a transaction with the debtor in possession; and (2) was the
10 consideration supporting the claimant's right to severance
11 beneficial to the debtor's operation of its business.

12 In re Selectors, Inc., 85 B.R. at 846; In re Commercial Fin.
13 Servs., Inc., 246 F.3d at 1294-95; Klemick, 2007 WL 952030, at *5;
14 In re Big M, Inc., 2014 WL 2442940, at *4-5; In re Ellipso, Inc.,
15 2012 WL 827103, at *3; In re M Group, Inc., 268 B.R. 896, 902
16 (Bankr. D. Del. 2001); In re Uly-Pack, Inc., 128 B.R. at 766. See
17 generally In re BCE West, L.P., 319 F.3d at 1172 (claimants
18 seeking payment of an administrative expense claim must show the
19 debt arose from a transaction with the debtor and directly and
20 substantially benefitted the estate).

21 One could argue that In re Tucson Yellow Cab Co., Inc.,
22 789 F.2d at 703-05, suggests that Meruelo's severance claim could
23 be analyzed under a "reasonableness" or "quantum meruit" theory.
24 In Tucson Yellow Cab, a collective bargaining agreement between
25 the taxi drivers and the company provided for two weeks notice
26 prior to termination or severance pay in lieu of notice. Id. at
27 703. The CBA was ultimately rejected by the estate; the taxi
28 drivers were terminated by the new owner several days thereafter.

1 The taxi drivers sought administrative priority for their
2 severance claims. Id. The Ninth Circuit held that severance pay
3 in lieu of notice was entitled to administrative priority under
4 § 503(b)(1)(A), as long as such pay was owed by contract or in
5 quantum meruit - i.e., when the contract no longer exists at the
6 time of termination. Id. Because the CBA at issue was no longer
7 in existence on the date of termination, the court allowed the
8 two-week pay severance claims as administrative claims on a
9 quantum meruit basis. Id. at 704.

10 We distinguish Tucson Yellow Cab, which was largely decided
11 on equitable grounds. First, Meruelo's severance payment is not
12 "pay in lieu of notice." Further, the clear intent of the CBA was
13 to compensate the taxi drivers for at least two weeks before
14 termination, either by giving them two weeks notice, after which
15 the drivers would presumably work two more weeks and be paid, or
16 to pay them two weeks severance pay and terminate them
17 immediately. Therefore, the "pay in lieu of notice" was clearly a
18 component of compensation - a payment akin to wages. See
19 In re Commercial Fin. Servs., Inc., 246 F.3d at 1296. The
20 severance claim at issue here is not a component of wages subject
21 to a "reasonable value" analysis. Meruelo was paid his normal
22 wages and, ultimately, his bonuses for the time he worked for
23 Debtor postpetition. The lump-sum severance payment is an
24 entirely separate claim and subject to the general rules governing
25 administrative expense priority under § 503(b).

26 From our review of the record, we conclude the bankruptcy
27 court abused its discretion by applying an incorrect standard of
28 law when analyzing Meruelo's severance claim. It was not subject

1 to a "reasonableness" standard, but rather the "actual and
2 necessary" standard set forth in § 503(b). Accordingly, we must
3 VACATE and REMAND.

4 **VI. CONCLUSION**

5 Because the bankruptcy court applied an incorrect standard of
6 law, we VACATE and REMAND the Compel Order, in part, so the court
7 can consider the severance claim under the proper legal standard.

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