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ADEQUATE ASSURANCE UNDER SECTION 366: IN RE CALDOR, A STEP IN THE RIGHT DIRECTION

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I. INTRODUCTION

When a company decides to file a petition under chapter 11 of the Bankruptcy Code, the relationship between that company and its creditors is automatically redefined. [1] One such relationship is that between the company and its utility suppliers. While continuing electricity, gas, water and telephone service are essential to the company's reorganization and ultimate survival, [2] the resources to pay for those services may no longer be available. The utility company, however, does not want to continue providing service without some sort of payment from its customer.

The precarious nature of this relationship receives special consideration under the Code in section 366. [3] Under subsection (a) the debtor is protected from the discontinuance of future service by utility companies once the debtor files for bankruptcy. [4] Subsection (b), [5] the focus of this paper, offers protection to the utility. Specifically, the trustee or debtor−in−possession must, within twenty days of filing, give the utility adequate assurance of payment. [6] The question becomes, however, what exactly constitutes adequate assurance of payment? [7] Does it have to be in the form of a cash deposit or will something other than cash suffice?

The most recent decision in this area was a Second Circuit decision, *Virginia Electric & Power Co. v. Caldor, Inc*. [8] In this case of first impression, [9] the court of appeals held that "adequate assurance" under section 366(b) [10] does not require a debtor to post a security deposit with its utility suppliers. [11]

II. THE AMBIGUITY OF SECTION 366

Under section 366(b), a utility company can "alter, refuse, or discontinue service" if the company does not receive adequate assurance of payment for post−petition services from the debtor. [12] This provision of the Code does not necessarily require that there be a judicial determination of what constitutes adequate assurance of payment prior to any alteration, refusal or discontinuance of service. The utility may instead determine what is necessary from the debtor in terms of adequate assurance. [13] If the debtor does not agree with the utility's demand, in kind or amount, a request for judicial intervention can be submitted. [14] The court must then decide what assurances by the debtor will be adequate. [15]

Despite its apparently clear purpose, section 366 has been subjected to much interpretation. [16] The legislative history does not furnish clear guidance. The language concerning adequate assurance of payment was not initially agreed upon by the House and the Senate. The House Report on its draft version of section 366 states, in part, "[i]f an estate is sufficiently liquid, the guarantee of an administrative expense priority may constitute adequate assurance of payment for future services. It will not be necessary to have a deposit in every case." [17] The Senate Report is similar, but does not refer to the possibility of treating an administrative expense priority as adequate assurance to the utility company. [18] Furthermore, the provisions of section 366, as it appeared in the Senate bill, specifically stated that adequate assurance of payment should be furnished "in the form of a deposit or other security." [19] The Senate's language that "more than a mere administrative priority be

furnished," [20] indicates a significantly different position as to what is required of a debtor in terms of adequate assurance of payment. Some courts argued that because this language from the Senate bill became part of the final version of section 366, [21] the House Report is of little value in determining the meaning of adequate assurance. [22]

III. SECTION 366 AND ITS INTERACTION WITH OTHER PROVISIONS OF THE BANKRUPTCY CODE

This "administrative expense" that seemed to be a point of contention between the House and the Senate interacts with section 366 through two other sections of the Code: sections 503 and 507. Under section 503 of the Code, an "entity" is permitted certain administrative expenses. [23] An administrative expense allowed under section 503(b)(1)(A) [24] will receive first priority under section 507 of the Code. [25] It should be noted, however, that the granting of an administrative expense priority decreases the amount of the estate available to other unsecured creditors. [26] Permitting administrative expenses "encourages the necessary parties to undertake the collection and distribution of the assets of the estate so as to be able to generate proceeds to distribute to pre−existing creditors." [27]

The administrative expense is usually charged to the estate and not to the property of secured creditors. [28] If, however, the administrative expense is being applied for some type of service that will "preserve the property securing creditors' interests" and ultimately benefit the creditors, the secured creditors will be held accountable for the expense. [29] In order for a secured creditor to be deemed responsible for an administrative expense priority, the debtor is required to prove that "the expenditure was necessary, the amounts expended were reasonable and the creditors benefited from the expenses." [30]

IV. THE PROBLEM OF DEFINING "ADEQUATE ASSURANCE"

The clarity of the other Code provisions that interact with section 366 is contrasted by the section's imprecise requirement of "adequate assurance." [31] While section 366 appears to be "creditor−oriented," courts have applied the provision to protect the debtor. [32] As the courts attempt to help the debtor in the rehabilitation process, [33] the utility companies voice their concern that they will be subjected to an unreasonable risk of future loss. [34] The utilities, however, often fail to realize that "adequate assurance" of payment does not mean a guarantee of payment from the debtor. [35] As the courts continually struggle to maintain the balance between the interests of the debtor and the utility company, they also avoid delivering a clear definition of "adequate assurance." [36]

The United States Court of Appeals for the Second Circuit, however, recognizing the difficulty in determining what constitutes adequate assurance under section 366, [37] delivered a decision in *Virginia Electric & Power Co. v. Caldor* that maintains the principles of section 366 [38] and effectively tackles the problems associated with "adequate assurance."

V. *IN RE CALDOR*−FROM THE BANKRUPTCY COURT TO THE COURT OF APPEALS

Caldor, Inc. filed a petition under chapter 11 of the Code on September 18, 1995. [39] The corporation operates approximately 160 retail stores in the northeastern portion of the United States. [40] As of 1994, Caldor's annual sales exceeded $2.7 billion. [41] At the time of filing the chapter 11 petition in 1995, Caldor was receiving service from 425 utility companies, totaling $3.5 million in services each month. [42]

The United States Bankruptcy Court for the Southern District of New York entered an order preventing the utility companies from "refusing, altering, or terminating service ... pending the approval of Caldor's plan for reorganization." [43] A number of Caldor's utility suppliers (including Virginia Electric) appealed the district court's decision. Affirming, the district court determined that the utilities received adequate assurance of payment because the court interpreted the term "other security" to encompass the safeguards that the bankruptcy court had provided. [44] The basis for this determination rested upon Caldor's pre−petition payment history and its post−petition liquidity. [45] In addition, an administrative expense priority, an expedited

procedure for relief if Caldor was to default in payment and an order requiring Caldor to convey its monthly statements directly to the utility companies were other safeguards in place to protect the utilities. [46]

According to the utility companies, however, those safeguards *did not* constitute "adequate assurance of payment" because the protections were available to the utilities "in the normal course" and could not properly fall under the definition of "deposit or other security" in section 366. [47] The district court, disagreed with this interpretation of adequate assurance under section 366(b), [48] and supported the notion that a certain flexibility accompanied section 366; thereby contradicting any narrow interpretation of the section and its provisions. [49] As stated in the district court's decision, "[t]he interpretation proffered by the Utilities leads to the illogical result that a bankruptcy court would be required to impose a deposit or similar financial instrument, in at least a nominal amount, in every situation even when other security already created 'adequate assurance' of payment." [50] Furthermore, the court clarified that section 366(b) only required "adequate assurance" of payment, not an "absolute guarantee of payment." [51]

The narrow interpretation of "adequate assurance" presented by the utility companies was rejected, once again, by the United States Court of Appeals for the Second Circuit. [52] Like the district and bankruptcy courts, the circuit court did not clarify the terms "security or other deposit" and "adequate assurance" as prescribed by section 366(b). [53] In avoiding this opportunity to clearly define the terms within section 366, the court relied upon the bankruptcy court's authority under this provision of the Code:

> [w]e conclude that−whether because the phrase 'other security' is read to include safeguards that are otherwise available to a utility supplier under the Bankruptcy Code, or because a bankruptcy court has the authority to require no 'deposit or other security' at all−the bankruptcy court need not require some additional safeguard where it determines that safeguards otherwise available under the Code provide the 'adequate assurance of payment' with which section 366(b) is ultimately concerned. [54]

The court reasoned that if the bankruptcy court had the authority to modify the amount of deposit or other security, the court could also decide that such deposit or other security may not be required at all. [55]

The Second Circuit's decision in *Caldor* focused on exercising judicial flexibility and evaluating the facts and circumstances of this case, rather than adhering to a strict statutory standard. [56] Striking a balance between the "competing needs of a debtor and utility companies" was a fair and effective way for the court to implement the intended purposes of both section 366, and the Code in its entirety. [57]

VI. CASE LAW REJECTING THE ADMINISTRATIVE EXPENSE PRIORITY: *IN RE BEST PRODUCTS CO.*

In re Best Products Co. [58] is an example of an interpretation of "adequate assurance" that runs contrary to the interpretation in *Caldor*. Best Products, like Caldor, operated retail stores, but filed a petition under chapter 11 of the Code in 1996. [59] The debtor wanted to provide adequate assurance solely in the form of classifying any post−petition debt for utility services as an administrative expense. [60] This classification was approved, but the court also provided that any utility could seek further assurance under section 366. [61] Many of the utilities objected, claiming that because an expense priority was already guaranteed by the Code, [62] they had not received adequate assurance as required by section 366. The utilities also claimed that section 366 mandates that such adequate assurance be furnished in the form of deposit or other security. [63]

The bankruptcy court agreed with the utilities that under section 366, the utility company can demand a deposit from the debtor. [64] According to the court, the legislative history and the language of the statute clearly indicated that "adequate assurance" requires more than an administrative expense priority. [65]

A. Legislative History

The congressional purpose behind section 366 was "to strike a balance between the general right of a creditor to refuse to do business with a debtor post−petition and the coercive nature of such a move by a debtor's utility." [66] The court agreed with previous decisions, recognizing the post−petition utility service as an "actual and necessary cost of preserving the estate" that must be deemed an administrative expense. [67] The court then reasoned that if the utilities were not permitted to refuse post−petition service under section 366(b), then the debtor must provide some additional assurance of payment in consideration for this treatment. [68] Therefore, the court concluded that "[i]f Congress believed that the administrative priority already bestowed upon the utilities would suffice, then it had no need to carve out the exception in subsection (b) of section 366 to the general rule of non−discrimination in subsection (a)." [69]

B. Plain Meaning of Section 366

The lack of a clear statutory definition of "adequate assurance" led the court to examine the ordinary meaning of the term. [70] The court acknowledged that in other cases the term "other security," of section 366, had been construed to encompass pre−paid bills, shorter payment deadlines, letters of credit, surety bonds and other financial devices. [71] The court, giving great deference to the interpretations of those other courts, concluded that an administrative priority is not sufficient assurance under section 366. [72]

VII. WHY *VIRGINIA ELEC. & POWER CO. V. CALDOR* IS A CORRECT APPLICATION AND INTERPRETATION OF SECTION 366

The decision in *Best Products* is really no more than a cursory glance at section 366 and its implications. In determining that the administrative expense did not constitute adequate assurance of payment on its own, the court failed to develop an analysis that properly applied section 366. [73] As acknowledged in *Caldor*, the proper application of section 366 involves judicial flexibility and an evaluation of more than just the legislative history and statutory construction of the provision. [74] The decision in *Caldor* is also a more pervasive analysis, inasmuch as the bankruptcy and district courts incorporated the evaluation of a variety of factors, both monetary and non−monetary, into their respective interpretation of section 366. [75]

The analysis at the bankruptcy court, district court and circuit court levels outlined several factors that were relevant in determining adequate assurance. [76] The seven factors were:

> [p]re−petition security required of the debtor by the utility, the debtor's payment history, the debtor's present and future ability to pay its current expenses, the debtor's net worth, the debtor's cash requirements, the probability of payment through distribution under the bankruptcy laws, and, since some degree of risk is calculated as part of the rate charged for utility services, the degree by which the risks of nonpayment from the debtor exceed the risks of nonpayment from the utility's other customers. [77]

Implementing these factors into an analysis of "adequate assurance" under section 366, fosters the rehabilitative purpose of chapter 11 and maintains the balance between debtor and utility provider as sought by section 366. [78] Caldor argued that its excellent pre−petition payment history, financial condition, access to $500 million under its court−approved debtor−in−possession financing facility, and the freeze on all of its pre−petition debt demonstrated that a security deposit was not necessary for adequate assurance of payment. [79] The courts agreed. [80] Furthermore, the bankruptcy court gave special attention to the $500 million post−petition financing facility; according to the bankruptcy court, this indicated a high probability of payment by Caldor, for both present and future expenses. [81]

In respecting the decisions of the bankruptcy and district courts, the Court of Appeals for the Second Circuit was setting an example for other tribunals dealing with this uncertain area of bankruptcy law. The Second Circuit acknowledged that the bankruptcy court's authority under section 366 includes the authority not to require a deposit from the debtor to the utility. [82] This deference to the bankruptcy court will allow future courts to properly exercise judicial flexibility in applying section 366, as intended by the provision. [83] Accordingly, the bankruptcy court is free to evaluate and apply section 366 on a case−by−case basis so that

adequate assurance of payment can be determined according to the specific circumstances of the case, not by a restrictive, rigid statutory standard. [84]

The opinion from the Second Circuit also affirmed the notion that deciding what constitutes "adequate assurance," in a particular case, requires a "focus upon the need of the utility for assurance, and to require that the debtor supply no more than that, since the debtor almost perforce has a conflicting need to conserve scarce financial resources." [85] In order to place Caldor in the best possible position for successful rehabilitation, the Second Circuit also affirmed the determination of the bankruptcy and district courts that what was provided to the utility company as "adequate assurance" was, in fact, adequate assurance in these circumstances. [86] The Second Circuit did not rely upon confusing legislative history and strict statutory construction, [87] but rather, by considering several factors in its determination of whether "adequate assurance" was provided, the Second Circuit offered a workable solution to the problems that have plagued section 366 since its inception.

VIII. CONCLUSION

While it appears that the Second Circuit's decision in *Caldor* has set down important guidelines, only time will tell if these guidelines will solve the problems associated with interpreting and applying section 366(b). The Second Circuit obviously valued the careful consideration and evaluation of the bankruptcy and district courts. Furthermore, the Second Circuit acknowledged that the most effective implementation of section 366 requires flexibility and understanding of all relevant circumstances. Most importantly, the United States Court of Appeals for the Second Circuit recognized the importance of maintaining and fostering the rehabilitative principles of section 366 and the Code.

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FOOTNOTES:

[1] *See* Michael J. Crames et al., *Utility Deposits and § 366: A Delicate Balancing Act, Second Circuit Court Weighs In On Issue*, N.Y. L.J., Sept. 29, 1997, at 7 (discussing complex issue of whether utility suppliers should automatically receive security deposit in order to ensure future service to debtor or if administrative expense priority will be sufficient for utility supplier).Back To Text

[2] *See* David M. Reeder, *The Administrative Expense Priority in Bankruptcy: A Survey*, 36 Drake L. Rev. 135, 151 (1986−87) (stating utility service is essential to chapter 11 business reorganization); Cheryl F. Anderson, Comment, *Providing Adequate Assurance for Utilities Under Section 366*, 9 Bankr. Dev. J. 199, 200 (1992) (commenting that loss of utility service can foil reorganization attempt); Amy L. Banse, Note, *Bankruptcy Law−Bankruptcy Code Section 366 Balancing A Utility's Right To Terminate Against A Debtor's Fresh Start−Begley v. Philadelphia Electric Co. 760 F.2d 46 (3d. Cir. 1985)*, 59 Temp. L.Q. 1011, 1042 (1986) (stating that as matter of public policy debtors should not be deprived of utility service).Back To Text

[3] 11 U.S.C. § 366 (1994):

> (a) Except as provided in subsection (b) of this section, a utility may not alter, refuse, or discontinue service to, or discriminate against, the trustee or the debtor solely on the basis of the commencement of a case under this title or that a debt owed by the debtor to such utility for service rendered before the order for relief was not paid when due.
>
> (b) Such utility may alter, refuse, or discontinue service if neither the trustee nor the debtor, within 20 days after the date of the order for relief, furnishes adequate assurance of payment, in the form of a deposit or other security, for service after such date. On request of a party in interest and after notice and a hearing, the court may order reasonable modification of the amount of the deposit or other security necessary to provide adequate assurance of payment.

*Id.**Back To Text*

[4] 11 U.S.C. § 366(a).Back To Text

[5] 11 U.S.C. § 366(b).Back To Text

[6] *See id*.Back To Text

[7] *See* Anderson, *supra* note 2, at 203−13 (1992) (recognizing that section 366 does not contain definition of adequate assurance); *see also* Marion Steel Co. v. Ohio Edison Co. (*In re* Marion Steel Co.), 35 B.R. 188, 197 (Bankr. N.D. Ohio 1983) (noting "adequate assurance of payment" is not defined in Bankruptcy Code); *In re* Santa Clara Circuits W., Inc., 27 B.R. 680, 685 (Bankr. D. Utah 1982) (noting Bankruptcy Code does not define adequate assurance of payment).Back To Text

[8] 117 F.3d 646 (2d Cir. 1997). The case arose out of Caldor's desire to maintain utility service from the time of filing the chapter 11 petition until the final approval of its reorganization plan.Back To Text

[9] *See* Crames, *supra* note 1, at 7 (noting that decision from Second Circuit affirmed that security deposit is not always required of debtor).Back To Text

[10] 11 U.S.C. § 366(b).Back To Text

[11] *See Caldor*, 117 F.3d at 647 (holding that forms of payment assurance that were ordered by bankruptcy court, even if otherwise available to utility companies, did satisfy requirement of section 366(b) for "adequate assurance of payment").Back To Text

[12] *See* 11 U.S.C. § 366(b).Back To Text

[13] *See id*.Back To Text

[14] *See In re* Robmac, Inc., 8 B.R. 1, 2 (Bankr. N.D. Ga. 1979) (noting that debtor objected to amount of security deposit demanded by power company and debtor's request for judicial intervention was granted); *In re* Stagecoach Enters., 1 B.R. 732, 734 (Bankr. M.D. Fla. 1979) (acknowledging that under section 366, utility possesses "initial right" to determine amount of payment and that upon application to court, "reasonable modification of whatever amount the utility deems necessary" can be ordered); *see also In re* Santa Clara Circuits W., Inc., 27 B.R. 680, 683 (Bankr. D. Utah 1982) (reminding that if debtor or other interested third party does not request hearing, service can be altered, refused or discontinued if utility believes that it has not received adequate assurance of payment).Back To Text

[15] The utility's request for adequate assurance, especially in the form of a security deposit, may appear to be an act to obtain property from the bankruptcy estate, thereby violating the automatic stay.
11 U.S.C. § 362(a)(3) states:

> (a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970, operates as a stay, applicable to all entities, of−(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate.

It must be recognized, however, that if the utility's demand is authorized under section 366(b), then Congress must have intended that the action under section 366 would not violate the stay. *See Santa Clara Circuits W.*, 27 B.R. at 683 (concluding that Congressional intention was for consistency between two provisions without any violation of automatic stay); Morton v. Mancari, 417 U.S. 535, 551 (1974) (stating "[t]he courts are at liberty to pick and choose among congressional enactments, and when two statutes are capable of coexistence, it is the duty of courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective").Back To Text

[16] *See* Vera Victoria Miles, *Adequate Assurance of Payment Under §366 of the Bankruptcy Code: A Term for Interpretive Flexibility or Judicial Confusion?*, 20 Akron L. Rev. 715, 726 (1987) (discussing that original purpose of section 366 was to "eliminate coercion by utilities against bankrupt debtors," but language of section was not as clear as that purpose); Daniel Keating, *Offensive Uses of the Bankruptcy Stay*, 45 Vand. L. Rev. 71, 98 (1992) (stating section 366 prevents utilities from using their powerful leverage to ensure payment of prepetition debts which could be discharged in bankruptcy); *see also In re* Woodland Corp., 48 B.R. 623, 624 (Bankr. D. N.M. 1985) (recognizing that section 366 was drafted to address problems debtors have in obtaining service from utilities to which they owe pre−petition debts).Back To Text

[17] H.R. Rep. No. 95−595, at 350 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6306. The House Report also states that subsection (b) will "prevent a utility from terminating service until there is a court hearing, if there is a dispute over what is adequate assurance." *Id*.Back To Text

[18] The Senate Report states:

> This section gives debtors protection from a cut−off of service by a utility because of the filing of a bankruptcy case. This section is intended to cover utilities that have some special position with respect to the debtor, such as an electric company, gas supplier, or telephone company that is a monopoly in the area so that the debtor cannot easily obtain comparable service from another utility. The utility may not alter, refuse, or discontinue service because of the nonpayment of a bill that would be discharged in the bankruptcy case. Subsection (b) protects the utility company by requiring the trustee or the debtor to provide within ten days, adequate assurance of payment for service provided after the date of the petition.

S. Rep. No. 95−989, at 60 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5846 (note: the time period has been changed to twenty days as of the 1984 amendments).Back To Text

[19] *Id*.Back To Text

[20] *In re* Best Products Co., 203 B.R. 51, 53 (Bankr. E.D. Va. 1996) (explaining significant difference between House Report which required only adequate assurance be furnished to utility and Senate bill that required assurance to be in form of deposit or other security).Back To Text

[21] 11 U.S.C. § 366 (1994).Back To Text

[22] *See Best Products*, 203 B.R. at 53 (concluding that House Report comment on adequate assurance "carries only negligible weight in interpreting the section" and that elimination of this language from final version of section is explicit rejection of House's interpretation of what is proper adequate assurance).Back To Text

[23] 11 U.S.C. § 503(b)(1)(A) states "[a]fter notice and a hearing, there shall be allowed administrative expenses, other than claims allowed under section 502(f) of this title, including the actual, necessary costs and expenses of preserving the estate, including−wages, salaries, or commissions for services rendered after the commencement of the case."Back To Text

[24] *Id*.Back To Text

[25] 11 U.S.C. § 507(a)(1) (stating that administrative expenses allowed under section 503(b), in addition to any fees and charges assessed against estate have first priority); *see also* 4 Collier on Bankruptcy ¶ 507.02[1], at 13 (Lawrence P. King et al. eds., 15th ed. rev. 1997) (stating that "[w]ere the principle of equality among creditors the only guiding principle in a bankruptcy case, the allocation of proceeds would be apportioned among all holders of claims in proportion to the amount of their claims. Yet there are other principles that govern the bankruptcy process and those principles have led to the establishment of a hierarchy by which some claims are entitled to payment before others").Back To Text

[26] *See In re* Stagecoach Enters., 1 B.R. 732, 734 (Bankr. M.D. Fla. 1979) (suggesting that to "generally" grant administrative expense priority to debtor for post−petition utility service would "unwarrantedly prejudice the rights of general creditors").Back To Text

[27] 4 Collier, *supra* note 25, ¶ 507.02[1][a], at 13. It must be noted that the claims with the highest priorities, such as utility expenses, gain such status because these claims have been incurred in relation to the administration of the estate.Back To Text

[28] *See* New Orleans Pub. Serv., Inc. v. Delta Towers, Ltd. (*In re* Delta Towers, Ltd.), 112 B.R. 811, 814 (E.D. La. 1990), *aff'd in part, rev'd in part,* 924 F.2d 74 (5th Cir. 1991) (explaining that "[g]enerally, administrative expenses must be charged to the bankruptcy estate and not to equity or assets belonging to secured creditors"); *In re* Trim−X, Inc., 695 F.2d 296, 301 (7th Cir. 1982) (stating that "[t]raditionally administrative expenses have not been charged against secured creditors"); *In re* Combined Crofts Corp., 54 B.R. 294, 297 (Bankr. W.D. Wis. 1985) (explaining that "administration expenses" cannot be recovered from bankruptcy estate because trustee or debtor in possession is acting for "interest of general creditors and not secured creditors").Back To Text

[29] *See* Anderson, *supra* note 2, at 208 (explaining that if property securing creditor's secured interests is going to be preserved by access to post−petition utility service, creditor would qualify for administrative expense priority for which other creditors will be responsible); *see also* New Orleans Pub. Serv., Inc. v. First Federal Sav. & Loan (*In re* Delta Towers, Ltd.), 924 F.2d 74, 76−77 (5th Cir. 1991) (discussing exception to general rule of section 506(c) that allows administrative expense to be charged to secured creditor); *Delta Towers*, 112 B.R. at 814 (defining exception to section 506(c) as liability for expenses "incurred to preserve or dispose of the property securing the creditor's interest").Back To Text

[30] *Delta Towers*, 112 B.R. at 815 (describing three−part test that must be satisfied before secured creditor can be charged with administrative expense); *see also In re* Woodland Corp., 48 B.R. 623, 625 (Bankr. D. N.M. 1985) (stating "[h]ad Congress intended that utilities be accorded an automatic administrative expense priority, it would have said so").Back To Text

[31] *See* Marion Steel Co. v. Ohio Edison Co. (*In re* Marion Steel Co.), 35 B.R. 188, 198 (Bankr. N.D. Ohio. 1983) (noting that "adequate assurance of payment" is not defined in Bankruptcy Code); Massachusetts Elec. Co. v. Keydata Corp. (*In re* Keydata Corp.), 12 B.R. 156, 158 (B.A.P. 1st Cir. 1981) (explaining that Code does not define "adequate assurance of payment"); *In re* Alipat, Inc., 36 B.R. 274, 276 (Bankr. E.D. Mo. 1984) (indicating that Bankruptcy Code does not provide definition of "adequate assurance of future performance").Back To Text

[32] *See* Anderson, *supra* note 2, at 211−12 (explaining that section 366 was "not intended to give utilities greater protection or assurance of payment than utilities normally receive"); *see also* Virginia Elec. & Power Co. v. Cunha (*In re* Cunha), 1 B.R. 330, 332−33 (Bankr. E.D. Va. 1979) (honoring debtor's request to "obtain a fresh start" after losing his job to serious illness); *Marion Steel Co.*, 35 B.R. at 196 (explaining that section 366 was intended to protect utility "while preventing discrimination against debtor").Back To Text

[33] *See In re* Robmac Inc., 8 B.R. 1, 4 (Bankr. N.D. Ga. 1979) (suggesting amount of adequate assurance should not be contrary to rehabilitative process); *In re* Santa Clara Circuits W., Inc., 27 B.R. 680, 685 (Bankr. D. Utah 1982) (indicating that "adequate assurance" must be interpreted in accordance with rehabilitation function of chapter 11); *In re* Frye Co., 7 B.R. 856, 858 (Bankr. D. Me. 1980) (finding administrative expense priority and requirement to pay telephone bills within ten days of receipt is adequate assurance during administration of debtor's chapter 11 case).Back To Text

[34] *See Cunha*, 1 B.R. at 331 (requesting from debtor cash deposit not less than $280.00 as adequate assurance of payment for future service); *Robmac, Inc.*, 8 B.R. at 2 (asking debtor for deposit that equaled two times average monthly bill in order to secure future service); *In re* Penn Jersey Corp., 72 B.R. 981, 983−84 (Bankr. E.D. Pa. 1987) (demanding sum of money from debtor without specifying how amount was determined is not

acceptable as adequate assurance of payment for future service).Back To Text

[35] *See Keydata Corp*., 12 B.R. at 158 (stating "[i]n our view, 'adequate assurance of payment' does not require an absolute guarantee of payment"); *Marion Steel Co*., 35 B.R. at 198 (interpreting adequate assurance of payment as not requiring "absolute guarantee of payment"); *see also Woodland Corp*., 48 B.R. at 624 (stating that in order to avoid extortionate demands "[s]ection 366 treats utilities differently from most post−petition creditors").Back To Text

[36] *See* Miles, *supra* note 16, at 717 (recognizing "merits of judicial flexibility in determining what constitutes adequate assurance of payment" but also realizing that variety of interpretations has caused problems of "very little consistency or certainty"); Larry T. Garvin, *Adequate Assurance of Performance*: *Of Risk, Duress and Cognition*, 69 U. Colo. L. Rev. 71, 154 (1998) (indicating that legal standard for defining "adequate assurance" lacks bright lines and relies on fact driven inquiries).Back To Text

[37] *See* Virginia Elec. & Power Co. v. Caldor, Inc., 117 F.3d 646, 650 (2d Cir. 1997) (declaring that "[w]e need not decide whether this, or some other, strict definition of 'other security' is most appropriate, or whether the term is best read more broadly, as the district court did, to encompass any form of safeguard that a bankruptcy court determines would help to assure a utility supplier of continued payment").Back To Text

[38] *See* Begley v. Philadelphia Elec. Co., 760 F.2d 46, 49 (3d Cir. 1985) (stating that purpose of section 366 is to prevent threat of termination from being used to collect debts, while protecting utility from providing services without payment).Back To Text

[39] *Caldor*, 117 F.3d at 647.Back To Text

[40] *See* Crames, *supra* note 1, at 7.Back To Text

[41] *See id*.Back To Text

[42] *See id.Back To Text*

[43] *Caldor*, 117 F. 3d at 647.Back To Text

[44] *See id*. at 649. The court of appeals realized that in affirming the order of the bankruptcy court, the district court did not adopt the exact reasoning behind the order−that Caldor was not required to produce a security or other form of deposit. The safeguards included a streamlined default procedure if Caldor was to default in payment and the delivery of monthly operational reports to the utility companies.Back To Text

[45] *See In re* Caldor, 199 B.R. 1, 2 (S.D.N.Y. 1996) (affirming Bankruptcy Court's conclusion that combination of numerous factors, including pre−petition payment history, "cash on hand", access to financing, solvency and operation from "proceeds of their operation" and lack of any past requirement for deposit amounted to adequate assurance).Back To Text

[46] *Id*.Back To Text

[47] *See id*. at 3 (acknowledging that utilities' argument concerning language of section 366 "places undue emphasis on semantics").Back To Text

[48] *See id*. at 2.Back To Text

[49] *See id*; 3 Collier, *supra* note 25, ¶ 366.03, at 4 (stating "[t]he intent of § 366, as elsewhere, is to leave some judicial flexibility while protecting the utility from unreasonable risk of future losses"); Consumer News and Bus. Channel Partnership v. Financial News Network (*In re* Financial News Network, Inc.), 980 F.2d 165, 169 (2d Cir. 1992) (citing *In re* Lionel Corp., 722 F.2d 1063, 1069 (2d Cir. 1983) (stating, "[f]irst and

foremost is the notion that a bankruptcy judge must not be shackled with unnecessarily rigid rules when exercising the undoubtedly broad administrative power granted him under the Bankruptcy Code.")); *In re* Utica Floor Maintenance, Inc., 25 B.R. 1010, 1013 (Bankr. N.D.N.Y. 1982) (explaining that courts have used "flexibility" and "sensitivity" in applying section 366).Back To Text

[50] *Caldor*, 199 B.R. at 3.Back To Text

[51] *See id*. (explaining that "adequate assurance" of payment differs from "absolute guarantee of payment"); *see also Utica Floor Maintenance*, 25 B.R. at 1014 (citing *In re* Keydata Corp., 12 B.R. 156, 158 (B.A.P. D. Mass. 1981) (stating that adequate assurance of payment only provides utility company with protection from "unreasonable risk of nonpayment," but does not provide absolute guarantee of payment)); Hennen v. Dayton Power & Light Co., 17 B.R. 720, 724 (Bankr. S.D. Ohio 1982) (stating "[a]dequate assurance does not require an absolute guarantee of payment").Back To Text

[52] *See* Virginia Elec. & Power Co. v. Caldor, Inc., 117 F.3d 646, 647 (2d Cir. 1997).Back To Text

[53] *See id.* at 650 (stating that court need not decide on strict definition of "other security"). The pattern among both bankruptcy and district courts has been to avoid providing a clear definition of the imprecise language in section 366(b); *see generally In re* Penn Jersey Corp., 72 B.R. 981, 982 (Bankr. E.D. Pa. 1987) (holding that section 366 "contemplates" that utility should only receive assurance of payment that will be "sufficient to protect its interests given the facts of the debtor's financial circumstances" which, in some cases, may forego requirement of payment or security deposit); *In re* George Frye, Co., 7 B.R. 856, 858 (Bankr. E.D. Me. 1980) (concluding that "adequate assurance" does not mean guarantee of payment); *Keydata Corp*., 12 B.R. at 158 (stating that "'adequate assurance of payment' does not require an absolute guarantee of payment" from debtor to utility company); *In re* Robmac, Inc., 8 B.R. 1, 4 (Bankr. N.D. Ga. 1979) (recognizing that "other methods" can be offered to utility as adequate assurance).Back To Text

[54] *Caldor*, 117 F.3d at 651. *See* 3 Collier, *supra* note 25, ¶ 366.03, at 4 (stating that "the intent, as elsewhere, is to leave some judicial flexibility while protecting the utility from unreasonable risk of future losses").Back To Text

[55] *See Caldor*, 117 F.3d at 650 (discussing that even if "deposit or other security" is interpreted narrowly, authority of bankruptcy court permits conclusion that no deposit or other security is required to provide utility supplier with adequate assurance of payment). Back To Text

[56] *See id*. (explaining that in bankruptcy proceedings, substance should not give way to form).Back To Text

[57] *See* Miles, *supra* note 16, at 718 (discussing importance that section 366 "plays in the success of the bankruptcy process"). According to Miles, section 366 eliminates the imposition of unfair pressure by utilities against bankrupt debtors, preserves the bankrupt estate with continued utility service, and secures the interest and cooperation of the utility creditor in this process with an adequate assurance of payment for future services. *See also* Heard v. City Water Bd. (*In re* Heard), 84 B.R. 454, 457 (Bankr. W.D. Tex. 1987) (stating that intent of section 366 is to balance competing interests of utility and debtor on case by case basis); *In re* Sweetwater, 40 B.R. 733, 743 (Bankr. D. Utah 1984) (indicating Bankruptcy Code is Congress' effort to balance competing interests).Back To Text

[58] 203 B.R. 51 (Bankr. E.D. Va. 1996).Back To Text

[59] *See id*. at 52.Back To Text

[60] *See id*.Back To Text

[61] *See id*.Back To Text

[62] *See Best Products,* 203 B.R. at 53 (explaining that section 507 of Bankruptcy Code provides first priority to administrative expenses allowed under section 503(b) of Code). According to section 503(b), those "expenses" include costs that are essential to maintaining the estate. The court reasoned, therefore, that the costs associated with the post−petition utility service of a retail debtor were "actual and necessary" and must be treated as an administrative expense. The court then concluded that, "[e]ven if § 366 did not exist, the utilities would be entitled to this priority under the Code." *Id.*Back To Text

[63] *See id.**Back To Text*

[64] *See id*; *see also In re* Norsal Indus., 147 B.R. 85, 89 (Bankr. E.D.N.Y. 1992) (holding that section 366(b) permits utility to receive adequate assurance of payment in form of deposit or other security, which meant that debtor in this case had to provide utility company with amount totaling two months of "winter peak" service); *cf. In re* George C. Frye Co., 7 B.R. 856, 858 (Bankr. D. Me. 1980) (concluding that debtor's grant of administrative expense priority constituted adequate assurance of payment when coupled with procedure to facilitate payment of telephone bills within 10 days of receipt).Back To Text

[65] *See Best Products,* 203 B.R. at 52−54; *see also In re* Santa Clara Circuits W., Inc., 27 B.R. 680, 685 (Bankr. D. Utah 1982) (observing that cash deposit was necessary component of adequate assurance of payment under circumstances of case). Back To Text

[66] *Best Products,* 203 B.R. at 53; *see also* Hanratty v. Philadelphia Elec. Co. (*In re* Hanratty), 907 F.2d 1418, 1424 (3d Cir. 1988) (discussing that Congress' intent in creating § 366 was to provide protection to debtors under subsection (a) while protecting utility companies under subsection (b) in light of competing concerns of debtor and its creditor utility suppliers); Brown v. Pennsylvania State Employees Credit Union, 851 F.2d 81, 85 (3d Cir. 1990) (acknowledging right of creditor to refuse to conduct business with debtor).Back To Text

[67] *Best Products,* 203 B.R. at 53; *see also In re* Finevest Foods, Inc., 140 B.R. 581, 584 (Bankr. M.D. Fla. 1992) (granting administrative priority to electricity that benefited bankruptcy estate); *In re* Statmore, 177 B.R. 312, 314−15 (Bankr. D. Neb. 1995) (explaining that creditor supplying post−petition services to debtor "in ordinary course of business" is entitled to administrative expense claim as long as service benefits debtor in operation of business).Back To Text

[68] *Best Products,* 203 B.R. at 53; *cf. Santa Clara Circuits W.*, 27 B.R. at 685 (concluding that cash deposit was required in consideration for continued service by utility).Back To Text

[69] *Best Products,* 203 B.R. at 53. The court also stated "[t]herefore, even if § 366 did not exist, the utilities would be entitled to this priority under the Code." *Id.*Back To Text

[70] *See id.*; *see also* Federal Deposit Ins. Corp. v. Meyer, 510 U.S. 471, 476−78 (1994) (discussing that courts cannot take liberty to pick and choose among congressional enactments, and when two statutes are capable of co−existence it is duty of courts, absent clearly expressed congressional intention to contrary to regard each as effective).Back To Text

[71] *See Best Products* 203 B.R. at 53−54; *see also In re* Smith Richardson & Conroy, 50 B.R. 5, 6 (Bankr. S.D. Fla. 1985) (holding that offer to prepay utility bill does not provide adequate assurance to utility and therefore, utility's demand for security deposit was reasonable); *In re* Utica Floor Maintenance Inc., 25 B.R. 1010, 1017 (Bankr. N.D.N.Y. 1982) (stating that existing security deposit securing past due bills cannot serve "double duty" as deposit for post petition services); *In re* Cunha, 1 B.R. 330, 333 (Bankr. E.D. Va. 1979) (acknowledging that in previous decisions, payment of "adequate, pre−estimated sum, in cash and in advance" was required of commercial debtors); *In re* Stagecoach Enters., 1 B.R. 732, 734 (Bankr. M.D. Fla. 1979) (stating "[i]n the opinion of this Court, it is not generally appropriate to give administrative expense priority to debts incurred by debtor for utility service...as 'adequate assurance of payment'...").Back To Text

[72] *See Best Products*, 203 B.R. at 54 (holding that "adequate assurance under § 366 requires more than administrative priority").Back To Text

[73] *See id.* at 53 (analyzing section 366 in light of legislative discussions predating enactment of statute); *see also Stagecoach Enters*., 1 B.R. at 734 (Bankr. M.D. Fla. 1979) (discussing adequate assurance with respect to legislative history surrounding statute); *cf.* Marion Steel Co. v. Ohio Edison Co. (*In re* Marion Steel Co.), 35 B.R. 188, 196 (Bankr. N.D. Ohio 1983) (analyzing section 366 from perspective of legislative intervention).Back To Text

[74] *See* Virginia Elec. & Power Co. v. Caldor, Inc., 117 F.3d 646, 650 (2d Cir. 1997) (reminding that bankruptcy courts "must be afforded reasonable discretion" in order to determine what is adequate assurance of payment under section 366); *see also Utica Floor Maintenance*, 25 B.R. at 1014 (stating "[i]n the four years since the enactment of the new Code, bankruptcy courts have exhibited a marked flexibility and sensitivity in applying § 366 that, in our view, is laudable").Back To Text

[75] *See Caldor*, 117 F.3d at 648−49 (including debtor's pre−petition payment history, its post−petition financial condition and administrative expense priorities afforded to creditor utility under section 503(b) and section 507(a)); *cf. In re* Santa Clara Circuits W., Inc., 27 B.R. 680, 684−85 (Bankr. D. Utah 1982) (noting that courts could include level of debtor's use of utility services in its analysis).Back To Text

[76] *See In re* Caldor, 199 B.R. 1, 2 (Bankr. S.D.N.Y. 1996); *Caldor*, 117 F.3d at 648−49; *see also Santa Clara Circuits W*., 27 B.R. at 680. This case involved the chapter 11 petition of an electronic circuits board manufacturer and seller. The debtor's natural gas supplier, Mountain Fuel Supply Company, demanded a security deposit in order for the debtor to receive post−petition service. In evaluating the utility's demand for payment, the court determined that what constitutes adequate assurance is "dependent upon the circumstances of each case." Depending upon the case, the factors taken into consideration and the weight applied to those factors will differ. *Id*. at 685.Back To Text

[77] *Santa Clara Circuits W*., 27 B.R. at 685.Back To Text

[78] *See In re* Robmac, Inc., 8 B.R. 1, 4 (Bankr. N.D. Ga. 1979) (advising that amount of adequate assurance "should not be contrary to the rehabilitation process" and that refusal of "other methods" as adequate assurance might "thwart or deter rehabilitation potential" of debtor).Back To Text

[79] *See Caldor*, 117 F.3d at 648−49.Back To Text

[80] *See Caldor*, 199 B.R. at 3 (concluding that utility companies were not seeking additional security for adequate assurance for future payment but "solely because their monopoly position permits them to capitalize on the Debtor's bankruptcy filing"); *Caldor*, 117 F.3d at 647 (holding "that, even assuming that the forms of payment assurance ordered by the bankruptcy court were otherwise available to the Utilities, they do not fail as a matter of law to satisfy § 366(b)'s requirement that utility suppliers receive 'adequate assurance of payment' from debtors in bankruptcy").Back To Text

[81] *See* Transcript of Hearing at 125−26, *In re* Caldor, 199 B.R. 1, 2−3 (Bankr. S.D.N.Y. 1995) (No. 95 B 44080) (providing that creditors received adequate assurance of payment).Back To Text

[82] *See Caldor*, 117 F.3d at 650 (agreeing with debtor that if bankruptcy court has authority to "modify" amount of deposit, bankruptcy court could excuse debtor from such requirement).Back To Text

[83] *See* 3 Collier, *supra* note 25, ¶ 366.03, at 4 (recognizing intent of § 366 is to provide some judicial flexibility); *see also In re* Utica Floor Maintenance, Inc., 25 B.R. 1010, 1013 (Bankr. N.D.N.Y. 1982) (stating that "bankruptcy courts must be afforded reasonable discretion in determining what constitutes 'adequate assurance' of payment for continuing utility services").Back To Text

[84] *See Caldor*, 117 F.3d at 650−51 (declining to "adopt" interpretation of section 366 that would "so raise form over substance and 'shackle' the bankruptcy courts with 'unnecessarily rigid rules'").Back To Text

[85] *Id*. at 650 (citing *In re* Penn Jersey Corp., 72 B.R. 981, 985 (Bankr. E.D. Pa. 1987)).Back To Text

[86] *See Caldor*, 117 F.3d at 651 (concluding that safeguards provided to utility by debtor were adequate assurance and additional safeguards were not necessary); *see also Caldor*, 199 B.R. at 2. The district court affirmed the determination of the bankruptcy court that the only necessary security was:

> (1) granting the Utilities an administrative priority, (2) creating a streamlined procedure for the Utilities to obtain immediate relief and future security if the Debtors were late on a single payment, and (3) requiring the Debtors to provide certain financial reports on a monthly basis to the Utilities.

*Id.**Back To Text*

[87] *See Caldor*, 199 B.R. at 2 (deciding to afford greater reliance to findings of bankruptcy and district courts and refusing to adopt reading of statute which would "raise form over substance and 'shackle' bankruptcy courts with 'unnecessarily rigid rules'").Back To Text