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CHARACTERIZATION OF HEALTHCARE RECEIVABLES:

ARE POST−PETITION HEALTHCARE RECEIVABLES SUBJECT TO PRE−PETITION LIENS AS "PROCEEDS" OR "RENTS" UNDER THE BANKRUPTCY CODE, OR ARE THEY EXCLUDED AS AFTER−ACQUIRED PROPERTY?

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I. Introduction

Hospitals and healthcare providers are under increasing public pressure to contain or lower healthcare costs. [1] As a result of this pressure, which has been applied directly

by insurance companies [2] and the government, [3] hospitals as well as other healthcare providers are facing serious financial difficulties. [4] This, in turn, has precipitated a surge in healthcare related chapter 11 filings.

This Article addresses one issue relating to hospital chapter 11 filings. Specifically, this Article examines whether accounts receivable that are both generated and collected post−petition are prevented from being cash collateral pursuant to Bankruptcy Code section 552, [5] notwithstanding the existence of a secured lender holding a validly attached and properly perfected pre−petition comprehensive lien in all of a hospital debtor's assets. [6] While this issue was hotly contested in hotel bankruptcy cases during the 1980s and early 1990s, a debate which ultimately resulted in an amendment to section 552 specifically addressing hotels, [7] this issue has not been tackled in any published opinions involving hospital bankruptcies. As such, this Article relies upon the general principles of section 552 as addressed in non−hospital cases, including hotel cases.

Consideration of this issue requires close examination of section 552. [8] On the one hand, section 552(a) states that all pre−petition liens are automatically inapplicable to property acquired by the estate post−petition, even those liens with after−acquired property clauses. [9] On the other hand, section 552(b) provides an exception for "proceeds" and "rent," both of which remain covered by pre−petition liens. [10] The Code omits any specific guidance as to how a hospital's receivables should be treated within this framework. [11]

Of course, senior secured creditors contend that post−petition hospital receivables, unlike most others, are an amalgamation of "rent" and "proceeds" from the hospital facilities. Therefore, senior secured creditors posit that these receivables should fall within the section 552(b) exception, remaining subject to pre−petition liens. Debtor hospitals argue, or at least they should argue, that their receivables are an indistinguishable mixture of services and other assets. As such, they are property acquired post−petition by the debtor and, pursuant to section 552(a), are not subject to any pre−petition liens.

This Article will utilize a multistep analytical process. First, the Article will address the four predominant criteria for characterizing post−petition property: the *Local Loan* [12] framework, the U.C.C. non−bankruptcy law analysis, [13] the "fresh−start" policy analysis, [14] and an analysis of the relevant legislative history. [15] Second, to buttress the conclusions reached via these four methods, this Article will examine cases involving industries in which the treatment of post−petition receivables has been under consideration, drawing comparisons where appropriate. [16]

This Article takes the position that hospital receivables are generated either primarily by service work or an indistinguishable mix of services and other assets; are mere after−acquired property; and, pursuant to section 552(a), are not be subject to pre−petition liens of any kind. [17] This Article further contends that post−petition hospital receivables are not the proceeds of an interest in real property nor are they merely transmogrified collateral. Consequently, post−petition receivables do not fall within the ambit of the section 552(b) exception to section 552(a).

To substantiate these conclusions and present the analytical framework necessary to reach them, this Article is organized as follows: Part II places the aforementioned issue in context with a brief explanation of the healthcare industry as it relates to this issue; Part III presents the underlying legal principles associated with this issue; Part IV presents the existing tests for the examination of the character of property acquired by the estate and applies these tests, including considering cases where similar problems have been encountered, most notably in the hotel industry with hotel post−petition revenues, and highlighting instructive parallels to the present situation.

II. Background

Unlike most industries, a three−party market model prevails in the healthcare arena. The parties in this market model are patients, providers and purchasers. "Patients" are those people who select and receive services. "Providers" are the doctors or hospitals that provide services. Finally, "purchasers" are the employers, insurance companies, or organizations that pay for the services. [18] The distinctive feature of this market model is that the patient or consumer is typically not the party paying for the service. [19] Within each of these categories, there are multiple subgroups, only a few of which are particularly important for the instant discussion: hospitals, insurance companies, managed care organizations, as well as federal and state health insurance programs. [20] Hospitals are the most easily defined of the above entities. A hospital is a facility that normally employs or contracts with numerous physicians, nurses, and other professionals to perform healthcare services on−site for patients. [21] A general acute care hospital provides a wide variety of services through its staff. [22] The list of available services typically includes: internal medicine, general surgery, cardiology, oncology, neurosurgery, orthopedics, emergency medicine, rehabilitation, pediatrics, and a number of other medical services. [23] A hospital's revenue is heavily dependent upon several factors, primarily the volume of physician services provided on an inpatient basis, the ancillary services and therapy programs ordered by physicians and provided to patients, and the outpatient procedures and charges or negotiated payment rates associated with such services. [24]

The next group of market participants is composed of "purchasers." There are three relevant categories of "purchasers:" fee−for−service insurers, managed care organizations, and governmental insurance programs. [25] The first, fee−for−service insurance companies, are the oldest members of this group. Fee−for−service insurance companies generate revenue by charging their customers (the patients) a set monthly fee. [26] In exchange, the insurers cover some or all of the medical expenses incurred by the customer−patient, depending upon the insurance contract between them. [27] As its customers incur medical expenses, the insurance company pays them, typically without any substantial inquiry into the necessity for given procedures or medical services. [28] This model is notable for its minimal restraint on the desires of the patient/insurance customer in obtaining medical services and on the lack of negotiation between the insurer and the provider for cost containment. [29]

Managed care organizations are a somewhat newer form of "purchaser." There are two primary types: health maintenance organizations ("HMOs") [30] and preferred provider organizations ("PPOs"). [31] Managed care organizations are characterized by their negotiation with healthcare providers for low, fixed fees for the services provided to their members. [32] The rise of managed care over the past ten years has had a tremendous impact on the revenues of hospitals, which have been forced to continually revise their cost structures to keep prices in line with the demands of managed care organizations. [33]

In addition to the rise of managed care, hospital bottom lines everywhere have been seriously impacted by changes made by the third type of "purchaser." In the governmental sector, there are two types of health insurance, Medicare and Medicaid. [34] Medicare is a federal program containing three parts. Under Medicare Part A, the federal government provides hospital insurance benefits to people who are either over the age of 65 or who are disabled. [35] Under Medicare Part B, anyone eligible for Part A may voluntarily join for additional medical insurance benefits. [36] Under Medicare Part C, also known as Medicare + Choice, patients may enroll in an HMO, PPO or other managed care entity in conjunction with Medicare. [37]

The Medicaid program is a joint state and federal program providing healthcare services to impoverished and medically−needy individuals. [38] State funds are matched by federal funds on an approximately dollar for dollar basis. [39] The programs vary from state to state.

The Healthcare Financing Administration ("HCFA") administers the Medicare program and the federal government's role in Medicaid. [40] Unlike any of the preceding "purchasers," HCFA does not engage in much negotiation over price and does not pay fees as they are generated. Rather, HCFA utilizes a complex and arcane reimbursement system, the details of which may be found in the Medicare/Medicaid statutes and HCFA regulations. [41] HCFA's overly complex and bureaucratic payment system, combined with recent payment reductions by the government, is a further cause of the de−stabilization of hospitals, and one of the many reasons that more and more of them will be seeking reorganization over the years to come. [42]

Because hospitals may view HMOs, PPOs, and HCFA as the root of their financial woes, it is important to have a generalized understanding of the underlying relationship between hospitals, insurance companies, HMO's, PPO's, and HCFA. It is important to fully grasp that while concentrated receivables exist and are payable to hospitals, they are payable in exchange for medical services and products provided to *patients*. Thus, even though a hospital's receivables may be concentrated in a few payees, such as insurance companies, HMO's, PPO's, and HCFA, to properly evaluate the application of section 552, [43] it is the hospital−patient relationship that must be closely scrutinized, not the hospital−purchaser relationship. If a receivable is the "proceed, product, offspring or profit" [44] of something provided by the hospital, that something must necessarily have been provided to the patient, not to the purchaser.

III. The Legal Background

In determining the character of hospital services, it is necessary not only to provide the factual context outlined above, but also to put forth a basic description of the pertinent law and a brief explanation of its relevance. The Bankruptcy Code states that the determination of a creditor's interest in goods or real property is determined by state law. [45] With this in mind, the following pages contain an abbreviated discussion of state law generally applicable to the secured lending process as well as the post−petition effect of pre−petition liens in bankruptcy.

A. Secured Lending Under State Law

When a creditor wishes to secure his loan to a debtor with that debtor's collateral, a two−step process typically ensues. First, the parties enter into an agreement stipulating the terms of the transaction. Second, the creditor files a record of the transaction with the state to notify all others of the encumbrance on the debtor's collateral. If the collateral is not real property, these steps are typically governed by a state's enactment of Article 9 of the Uniform Commercial Code ("U.C.C."), as are all secured transactions. [46] If the collateral is real property, then the steps are governed by state real property law. [47]

Many hospital financiers take as their collateral all possessions of the hospital. These types of broad−based liens are known as omnibus liens and cover numerous forms of collateral. The law applicable to these forms of collateral varies. The important types covered by the U.C.C. are accounts, [48] inventory, [49] after−acquired property, and proceeds.

Because accounts and inventory are constantly fluctuating or churning, a static interest in the accounts or inventory existing at the time of the security agreement would be worthless. [50] To alleviate this problem, creditors take a floating lien on these types of collateral, thereby encumbering accounts and inventory both in the debtor's possession at the time of the agreement and thereafter acquired. [51] This is accomplished through the inclusion of an after−acquired property clause in the security agreement. [52]

In addition to their interest in after−acquired property under an appropriate contractual provision, creditors also may enjoy a qualified security interest in the proceeds of collateral. Under section 9−203 of the U.C.C., a creditor with a security agreement has rights to the proceeds of collateral as outlined in section 9−306. [53]

B. The Continuity of Security Interests in the Bankruptcy Context

A creditor's security interest in after−acquired property and proceeds is affected by a bankruptcy filing. In bankruptcy, section 552(a) of the Bankruptcy Code provides that "property acquired by the estate or by the debtor after commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case." [54] In other words, with respect to post−petition property, section 552 automatically cuts off any after−acquired property clauses in the debtor's pre−petition security agreements. [55]

However, section 552(b) contains several exceptions to this rule. Subsection (b)(1) states that if any security agreement entered into before the commencement of the case "extends to property of the debtor acquired before the commencement of the case and to proceeds, product, offspring, or profits of such property, then such security interest extends to such proceeds, product, offspring, or profits acquired by the estate after commencement of the case." [56] In addition, subsection (b)(2) of section 552 provides that if a pre−petition security agreement applies to property acquired "before the commencement of the case and to amounts paid as rents of such property or the fees, charges, accounts, or other payments for the use or occupancy of rooms and other public facilities in hotels, motels, or other lodging properties," then "such security interest extends to such rents and such fees, charges, accounts or other payments acquired by the estate after the commencement of the case." [57]

Thus under section 552 if property obtained by the estate is considered to be merely after−acquired property, it becomes an unencumbered asset of the estate. [58] Accounts and inventory classified as after−acquired property inuring to the estate after commencement may be liquidated by the estate and the cash thereof used to expedite a successful reorganization.

On the other hand, property received by the estate post−petition that is characterized as either proceeds of pre−petition collateral or rent, profit, or some other form of product or offspring of pre−petition collateral remains subject to the original collateral's pre−petition liens. [59] This property, once liquidated, becomes cash collateral of the estate. [60] Cash collateral, defined in section 363 of the Bankruptcy Code, means "cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents whenever acquired in which the estate and an entity other than the estate have an interest." [61] Cash collateral comprises all liquidated section 552(b) property.

The significance of characterizing money as cash collateral is that a debtor may not spend it without either the permission of the other interested parties or the authorization of the bankruptcy court. [62] Herein lie the seeds of the debtor−creditor controversies regarding characterization of post−petition property. As noted in Section II, the prevailing hospital business model exhibits high levels of accounts receivable as well as poor short term liquidity. [63] Thus, in a hospital bankruptcy, a substantial volume of receivables is generated post−petition. The characterization of these accounts as either rents of the hospital, proceeds of the hospital facility or proceeds of hospital inventory, or mere after−acquired property could determine which party in the bankruptcy proceeding takes control of these accounts, and, with it, a substantial level of control over the reorganization.

IV. The Characterization of Post−petition Receivables in Hospital Reorganizations and Their Concomitant Treatment under Bankruptcy Law

Hospital receivables generated post−petition are best characterized as revenues generated from a mix of services and other products. Thus they are not subject to pre−petition omnibus liens of creditors on hospital buildings, equipment, inventory, receivables, and their proceeds. Several analytical constructs and a number of case lines dictate this conclusion. This section begins by describing and then applying the four prevalent considerations used by courts to distinguish after−acquired property from proceeds: the *Local Loan* approach, [64] the fresh−start policy, [65] the definition of proceeds in the U.C.C., [66] and the legislative history of section 552 of the Bankruptcy Code. [67] This four−pronged analysis is followed by a presentation of three case lines involving service industries in which courts have differentiated proceeds, profits and rents from mere after−acquired property. [68]

A. Characterizing Hospital Receivables Using Court−Created Analytical Factors

1. The Factors

In analyzing the character of post−petition property, courts have used one or more of four different tests. The first, known as the *Local Loan* test, derives from a pre−Code principle. [69] This principle is that property received by the debtor and produced by the debtor's labor after the commencement of a bankruptcy case is free from all pre−bankruptcy liens. [70]

While initially only applied to personal bankruptcies and wage assignments, use of the principle has expanded to other areas over the years. [71] The United States Supreme Court introduced this principle in the 1934 case of *Local Loan v. Hunt*. [72] There, the Court evaluated a dispute between a discharged bankrupt, William Hunt, and one of his creditors. Mr. Hunt had secured a loan with his creditor by assigning the creditor a right to his future wages. [73] Upon his discharge from bankruptcy, the lender brought suit in municipal court to enforce the garnishment of Mr. Hunt's wages and protect its interest in his after−acquired property. [74] Mr. Hunt sought to have the creditor enjoined from its collection activity. [75] The Court, deciding the case for Mr. Hunt, stated:

[I]t logically cannot be supposed that the act nevertheless intended to keep such debts alive for the purpose of permitting the creation of an enforceable lien upon a subject not existent when the bankruptcy became effective or even arising from, or connected with, preexisting property, but brought into being solely as the fruit of the subsequent labor of the bankrupt. [76]

Thus in *Local Loan* the idea was born that post−petition revenues generated primarily by service work are not susceptible to pre−petition security interests. But it was not until later that this principle emerged from the personal bankruptcy context and was utilized in corporate scenarios. During the late 1980s and early 1990s, courts dealing with the characterization of post−petition hotel revenues extended the *Local Loan* logic to encompass the idea that property acquired by any post−petition service labor should not be subject to pre−bankruptcy liens. [77] In the 1991 case of *In re Corpus Christi Hotel Partners, Ltd.*, [78] the bankruptcy court determined that hotel revenues arising post−petition could not be proceeds or rents because they were generated by services. [79] The court cited to *Local Loan* in reaching this conclusion. [80] The *Local Loan* Court's reasoning permeated several other similar contemporary opinions and occupies the first step in the forthcoming analysis of hospital receivables. [81] The *Local Loan* case also produced a second consideration for bankruptcy courts to use when characterizing post−petition property. In *Local Loan*, the Supreme Court emphasized the fresh start and rehabilitative aspects of federal bankruptcy law, and this policy emphasis has been reiterated in modern cases. [82] The Court noted that allowing liens to encumber post−petition estate assets would subvert the efforts of the law to encourage bankrupt entities to re−enter the economy in a fiscally productive and efficient manner. [83] A debtor would have little incentive to work if still burdened with pre−petition liens. [84]

Specifically, the Court wrote that "[o]ne of the primary purposes of [bankruptcy] is to 'relieve the honest debtor from the weight of oppressive indebtedness, and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes.'" [85] And, "the power of the individual to earn a living for himself and those dependent upon him is in the nature of a personal liberty quite much if not more than it is a property right. To preserve its free exercise is of the utmost importance, not only because it is a fundamental private necessity, but because it is a matter of great public concern." [86] The Court decided this power to earn was of public concern because "[t]he new opportunity in life and the clear field for future effort, which it is the purpose of the [law] to afford the emancipated debtor, would be of little value [otherwise]." [87]

As with the first *Local Loan* principle, lower courts have expanded the application of the Court's policy analysis to encompass corporate reorganization. [88] In this latter sense, courts have decided that section 552 was designed to provide a debtor with a "fresh start" by freeing post−petition inventory and accounts receivable for collateralization. [89] One prominent decision sanctioning this factor is the Fourth Circuit's 1986 opinion, *In re Slab Fork Coal Company*. [90] The *Slab Fork* court had to resolve a dispute concerning the characterization of a debtor's accounts. [91] What is noteworthy about the case is not the court's holding, but the tenor of its opinion. [92] In its analysis, the court focused closely on the relative interests of the parties and the implementation of the aforementioned Bankruptcy Code policy. [93] In particular, the court said "[i]t appears clear from the legislative history related to section 552 that Congress undertook in that section to find an appropriate balance between the rights of secured creditors and the rehabilitative purposes of the Bankruptcy Code." [94] In the instant situation, then, the second step in evaluating the nature of post−petition hospital receivables is to determine what characterization would best effectuate the Code's goal of rehabilitating debtors.

The third analytical step used by many courts is a comparison of the subject post−petition property to the state law definition of "proceeds." This step derives from the language in the Bankruptcy Code, section 552(b), limiting security interests "to the extent provided by . . . applicable nonbankruptcy law." [95] Thus, courts look primarily to the relevant state commercial code definitions, which are modeled or wholly copied from the U.C.C. [96]

Looking through the U.C.C. rubric, courts typically focus their analysis on section 9−306(a). [97] Subsection (a) of section 9−306 defines "proceeds" as that which is received upon "sale, exchange, collection or other disposition of collateral or proceeds." [98] Courts using this analytical tool have applied the definition quite strictly and literally. [99] They have quantified post−petition property as collateral only when the property is in the hands of the debtor as direct compensation for the sale of collateral held pre−petition. [100] Thus, most courts have looked askance at attempts to characterize as proceeds such post−petition property as: forfeited deposit on the aborted sale of encumbered machinery; [101] partnership distributions, when the partnership interest was encumbered; [102] cash dividends on stock held as collateral; [103] and government agricultural deficiency payments, when the creditor held a lien on crops. [104]

Similarly, when the property is generated by the debtor merely through *use* of pre−petition collateral, courts have been very reluctant to characterize this property as proceeds under the U.C.C. definition. [105] For example, in many of the previously−referenced hotel bankruptcy cases, courts held that most revenues derived from hotel rooms were not proceeds under the U.C.C. because "the law construes proceeds to involve some permanent disposition of the collateral, more than the mere use of the property to provide hospitality to guests." [106] In a second situation, a court held that revenue generated by coin−operated video game machines was not proceeds. [107] The court reasoned "the cash which is generated through that equipment is not received from sale of the collateral, but rather, through use of it. It is more analogous to income [than to proceeds]." [108] Therefore, the third step of analysis should involve a comparison of the U.C.C. § 9−306(a) definition of "proceeds" to hospital receivables, with specific care given to the nature of the transaction creating the receivables.

The fourth and final analytical consideration is to inquire whether the post−petition property falls within the definition of "proceeds" found in the legislative history of section 552. [109] The House Reports contain the statement that "[t]he term 'proceeds' is not limited to the technical definition of that term in the U.C.C., but covers any property into which property subject to the security interest is converted." [110] Some courts have used this to formulate a broader definition of proceeds, one that includes any post−petition property transmogrified from pre−petition collateral, not just that arising from the sale, exchange, collection or disposition of the collateral. [111]

Even with this broader interpretation, courts approaching the characterization issue via this avenue have reasoned that labeling post−petition property as "proceeds" must "be limited to those instances where the nature of the creditor's collateral is altered so substantially that the collateral is transformed into a new property." [112] Under this last consideration, proceeds clearly do not include "by−products" or mere "fruits of the principal collateral held by the debtor."

2. Applying the Factors

Summarizing and compiling the above factors yields the following four−step test for evaluating the character of post−petition hospital receivables: First, whether the debtor's service labor generated or contributed most heavily to the production of receivables; [113] second, whether characterizing the receivables as proceeds or rents would comport with the fresh−start policy goals of the Bankruptcy Code; [114] third, whether the receivable or cash was generated by the sale, exchange, collection or other disposition of collateral or proceeds; [115] and fourth, if the receivables do not fit within the narrow state law definition of proceeds, whether they were in any way converted from pre−petition collateral. [116]

Applying the four foregoing factors to the instant problem results in the conclusion that post−petition hospital receivables are not subject to pre−petition liens. With regard to the first factor, *Local Loan*, service labor produces almost all of the revenue of a typical hospital. A hospital's revenues are derived almost exclusively from the services of medical staff and other professionals. Hospital patients do not pay simply to occupy rooms. Rather, they pay for professional medical care and the safety and convenience of being within close proximity to medical facilities and personnel. Therefore, even more so than with hotel revenues, hospital accounts are neither rents derived from hospital premises nor proceeds of those premises and the equipment located thereon. Instead, hospital receivables are property generated primarily "as the fruit of the subsequent labor of the bankrupt." [117] As such, they are after−acquired property and should not be subject to pre−petition liens.

Moreover, the service revenue of a hospital cannot be readily segregated and quantified. The Ninth Circuit, in the hotel case of *Days Inns,* [118] pointed out that hotel methods of accounting allow for separate itemization of room receipts from restaurants, phones, and other items that are typically broken out in hotel accounting. This simply does not work for hospitals, however. The service component of revenues cannot be separately accounted for on hospital bills. While it is true that bills may include separate charges for doctors' services, laboratory tests, or other separately itemized services, the room charge also includes certain charges for providing the availability of services. For example, a heart patient paying $300 per day for a hospital room is not simply paying for a room and a bed. Among other things, that patient pays for having a defibrillator down the hall, a professional staff standing by that can operate the defibrillator if needed, and an operating room in close proximity in the event emergency by−pass surgery is needed. In fact it is likely that patients believe hospital fees are paid primarily as consideration for medical care rather than merely for room rental. In short, while the patient's bill may simply state "room charge," there is considerably more to this "room charge" than just supplying a room.

Looking to the second factor, the rehabilitative policy of the Code, leads to the same answer as the *Local Loan* analysis. [119] Characterizing hospital accounts as proceeds or rents contradicts the Code's rehabilitative and fresh start policies. In simple terms, giving the corporate debtor a chance at rehabilitation translates to supplying it with sufficient liquidity to emerge from the bankruptcy. Normally, this means allowing the debtor access to as much of its cash, near−cash, and readily disposable assets as is possible. In the hospital arena, however, the complexity of the reimbursement system, with its annual reviews and irregular payment schedule, coupled with the push for cost containment, has altered the typical work−out variables. [120] For hospitals, post−petition liquidity may only be accomplished if the hospital has full access to its new accounts receivables. [121]

To elaborate, characterizing these accounts as after−acquired property would alleviate a hospital's cash needs in two ways. First, it would permit the hospital to collateralize the accounts. Second, it would enable the hospital to utilize the cash freely upon receipt because it would not be cash collateral. The hospital's enhanced liquidity position could allow an otherwise ill−fated restructuring to succeed. Thus, characterizing post−petition hospital accounts as after−acquired property would further the policy of the Bankruptcy Code.

Under the third consideration, the U.C.C. analysis, hospital accounts do not qualify as "proceeds." The relevant U.C.C. provision, section 9−306(a), defines proceeds to mean only property that is gained by the "sale, exchange, collection or other disposition of collateral or proceeds." [122] As demonstrated above in section IV.A.1., courts have construed this definition narrowly, blocking creditors' attempts to avoid the section 552(a) rule via an expanded reading of section 552(b). [123] By way of these attempts, courts have taken the opportunity to clearly voice their opinion that neither property generated by "use" of collateral nor produced by a right held through collateral (such as cash dividends) is sufficient to be proceeds. [124] Like the examples provided, hospitals produce their accounts receivable by use of their personal property and through the services of their staff. [125] This revenue is not the product of a sale, exchange, or other disposition of the hospital building or any other collateralized assets. Consequently, hospital revenues are not proceeds under the U.C.C.

Nor are hospital revenues proceeds as this term is used in the legislative history of section 552. This fourth consideration states that, at a minimum, proceeds are new property transformed or converted from a creditor's pre−petition collateral. [126] Typical examples of this type of proceed might include refreshed inventory or the cash generated by paid accounts receivable. Having been generated almost entirely by services and the use of personal property, hospital receivables cannot fall within this definition.

In sum, post−petition hospital receivables do not qualify as proceeds, product, rent or derivatives of pre−petition collateral. They are the product of the hospital debtor's labor or a mixture of labor and other assets, and they are not proceeds under the U.C.C. or legislative history of the Bankruptcy Code. Furthermore, classifying hospital receivables as proceeds would defeat the fresh start and rehabilitative policies underpinning the Bankruptcy Code. Therefore, post−petition hospital receivables are merely after−acquired property and are thus not subject to the pre−petition liens of creditors.

B. Relevant Case Law

Three lines of cases, each dealing with somewhat similar fact patterns, support the conclusion that post−petition hospital receivables are not subject to pre−petition liens. The following discussion provides a brief explanation of each line of cases and their relevance to the instant discussion.

The first and most analogous line comprises the hotel cases of the late 1980s and early 1990s. Prior to 1994, Bankruptcy Code section 552(b) did not contain a section dealing specifically with hotels and post−petition receivables and income. [127] Rather, the courts were left to determine whether hotel receivables and income were to be classified on the one hand as proceeds, rent, or cash collateral, or, on the other hand, as mere after−acquired property, pursuant to the *Local Loan* logic and other applicable factors. In making their determination, many courts distinguished between post−petition property produced by the secured property (i.e., the hotel) and that which was generated by services. [128] Hotel revenues, which were considered a product of the hotel, were classified as "rents" or "proceeds" and subjected to pre−petition liens on the hotel or other revenue−generating property. [129] The post−petition service income, however, was removed from the other revenue and deemed exempt from any pre−petition liens. [130] As stated by the Ninth Circuit, there is a "distinction between income that is derivative from the secured property and income that is derived from services . . . . The revenues derived from the sale of food and drink and from other services provided by [a] hotel generate 'accounts' that cannot be classified as rent." [131]

This logic, setting aside service revenues as non−proceeds or rents and enabling the debtor to use this money in its discretion, migrated from hotel cases to a second group of cases, those involving landfill tipping fees. [132] Landfills collect tipping fees for allowing customers to deposit waste material on their property. [133] Creditors secured pre−petition with interests in the landfill property contended that post−petition tipping fees were subject to their liens. [134] In the only case to date dealing with the characterization of these fees, the Bankruptcy Court for the Eastern District of Pennsylvania held tipping fees were free from pre−petition liens on the landfill sites. [135] The court, using logic similar to that in the hotel cases, cast tipping fees as business receipts, at least some part of which were attributable to the "labor and incidental services provided by the Debtor." [136] Therefore, tipping fees were neither rent nor profits of the land. As largely service revenues, tipping fees were merely after−acquired property of the debtor.

The last line of conceptually similar cases to employ the services/proceeds distinction deals with creditor liens on golf and racquet clubs. In the case of *In re Everett Home Town Limited Partnership*, [137] the court decided that all service−related revenue generated post−petition by a club, including green fees, cart fees, restaurant revenues, tennis fees, and pro shop revenue, could not be "proceeds, products, offspring or rents." [138] The court reasoned that services provided by a debtor post−petition were merely after−acquired property of the club, free from pre−petition liens on the property of the debtor. [139]

In light of these cases, hospital proceeds, as primarily service revenues, should be characterized as merely after−acquired property when generated post−petition. Each of the discussed case lines characterized a debtor's post−petition on−site revenues as after−acquired property to the extent that those revenues were acquired through service efforts. Hospitals derive all or most of their income from the provision of services. Hospital patients do not take rooms simply for occupancy purposes. Patients use the rooms because of a desire or necessity to be close to hospital staff and equipment. Were it not for the services available to them in the hospital, patients would not be in the hospital in the first place. To attempt to characterize the majority of hospital revenue as anything other than service revenue would be simply inaccurate. Thus, to characterize post−petition receivables as anything other than mere after−acquired property would likewise be inaccurate. As with room service at a hotel, post−petition hospital receivables are neither subject to pre−petition liens nor later classifiable as cash collateral.

V. Conclusion

Having examined post−petition hospital receivables both by considering the four existing court−created tests and by looking at rulings in factually similar situations, it is evident that hospital receivables are neither proceeds nor rents under Bankruptcy Code section 552(b). These receivables are almost entirely the product of the debtor's services and do not conform to prevailing state law definitions of "proceeds." Furthermore, characterizing post−petition hospital receivables as proceeds or rents would be contrary to the purpose of the Bankruptcy Code. Thus, any receivables of a hospital that are generated post−petition may only be characterized as mere after−acquired property. As such, these receivables are not subject to the pre−petition liens of creditors, and the cash produced through their realization is not cash collateral.

FOOTNOTES:

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[1] *See* Patrick A. Guida, *Financing Healthcare Providers*, SD71 ALI−ABA 401, 403 (May 6, 1999) (stating that healthcare industry has been under pressure to contain healthcare costs). Over the past thirty years, the percentage of the gross domestic product ("GDP") expended on healthcare has almost doubled, from 7.4% in 1970 to 13.6% in 1996. *See id*. By 2006, this figure is expected to reach 16.2%. *See id*. In aggregate dollar amounts, healthcare purchasers in the United States are expected to spend over $4,500 per citizen in 2000. *See id.* This is up from only $700 billion dollars or $2,691 per citizen in 1970. *See id.* By 2008, this amount is expected to reach $2.2 trillion, having grown by 6.8% per annum. *See* Department of Health and Human Services, *National Health Expenditures Projections 1998−2000* (last modified Jan. 10, 2000) <http://www.hcfa.gov/stats/NHE−Proj/proj1998/hilites.htm>. Almost all of the above costs are paid under Medicare/Medicaid, managed care contracts or by fee−for−service insurance companies. *See Plunkett's Healthcare Industry Almanac* (last modified Feb. 9, 2000) <http://www.plunkettresearch.com/ Plunkett/book_titles/ HCIA/5−trends.htm> (describing healthcare industry's structure and major participants). At present, federal and state expenditures under Medicare/Medicaid and other public programs account for approximately 46% of the total amount spent, and estimates show that they will surpass 50% by the year 2005, with managed care organizations and fee−for−service insurance companies making up the bulk of the remainder. *See* Department of Health and Human Services, *The Nation's Health Dollar: 1998* (last modified Jan. 10, 2000) <http://www.hcfa.gov/stats/nhe−oact/tables/chart.htm>. Over the last 10 years each of these groups has taken substantial steps toward reducing the escalation of healthcare costs. *See Plunkett's Healthcare Industry Almanac*, *supra*. Back To Text

[2] *See* Michael D. Belsley, Comment, *The Vatican Merger Defense—Should Two Catholic Hospitals Seeking to Merge be Considered a Single Entity for Purposes of Antitrust Merger Analysis?*, 90 Nw. U. L. Rev. 720, 722 n.5, 724 (1996) (noting that pressure to merge stems from insurance company pressure to cut healthcare costs); Rex O'Neal, Note, *Safe Harbor for Healthcare Cost Containment*, 45 Stan. L. Rev. 399, 399−401, 408 (1991) (opining that private healthcare insurance pressure to cut healthcare costs will continue to grow). In the private sector, fee−for−service programs have been largely phased out and massive managed care organizations have arisen in their place. *See* Plunkett's Healthcare Industry Almanac, supra note 1 (describing healthcare industry's structure and major participants). These new groups are utilizing their substantial bargaining power to force providers to lower prices for their services. *See* id. In addition, they are becoming more involved with the decision−making process at hospitals and other healthcare facilities, encouraging increased outpatient care and reducing unnecessary testing and ancillary work that was once ordered by physicians. *See* id. To date, the managed care system has reduced cost growth. For example, while during the late 1980's and early 1990's expenses increased at annual rates typically in the double digits (13.6% average from 1988−1992), the 1990's growth has been reduced, coming in at roughly 2.9% per annum for the private sector. *See* id. Back To Text

[3] In the public sector three important cost−cutting changes have taken place. First, Congress implemented the prospective payment system ("PPS") in 1983 to add greater oversight to the system of billing that had previously been in place. *See* 42 U.S.C. § 1395ww(g) (1994). While this legislation had the effect of reducing fraudulent claims, it still did not prevent legitimate cost increases, as evidenced by the 1980's hyper−growth. *See* Plunkett's Healthcare Industry

Almanac, supra note 1. In 1987, Congress took a second step to reduce costs by altering the Periodic Interim Payment system, which had been used to supply all participating hospitals with biweekly cash infusions based on estimated future costs of non−discharged Medicare/Medicaid payments. *See* Sarah B. Foster & Shalom L. Kohn, *When the Healthcare Provider Gets Sick −Healthcare Issues in Bankruptcy*, 1998 Nat'l Conference of Bankr. Judges 1−37; Guida, supra note 1, at 403. In 1997, Congress took a third step when it passed the Balanced Budget Act containing large across−the−board reductions in amounts paid to hospitals for services rendered. *See* Balanced Budget Act of 1997, Pub. L. No. 105−33, 111 Stat. 397−403 (1997). Back To Text

[4] All of the steps discussed in this section−−the increased scrutiny by private organizations, the removal of interim payments by the federal government, and the overall reductions in expenditures−−have had a negative impact on the healthcare industry. Once very stable and profitable enterprises, many hospitals now have significant liquidity problems. *See* Gregory R. Salathe, Reducing Healthcare Costs Through Hospital Accounts Receivable Securitization, 80 Va. L. Rev. 549, 549−50 (1994) (noting that hospitals must bear most of burden of increasing healthcare costs). While their accounts receivable have remained considerable or in certain cases even grown, their cash flow has become unpredictable. *See* id. at 553−54; *see also The Business Bankruptcy Reform Act − Preserving the Quality of Patient Care in Healthcare Bankruptcies: Hearing on S.1914, 104th Cong.(1998) (statement of Keith J. Shapiro on behalf of American Bankruptcy Institute), also found at www.abiworld.org/legis/testimony/98junshapiro.html. These liquidity pressures have both increased the demand for loans and reduced the creditworthiness of many hospitals, elevating the cost of loans and the security required for them. See Guida, supra note 1, at 405. Indeed, the recent spate of instability has spurred many creditors to take the additional step of securing their lending with omnibus liens on hospitals, encumbering their buildings and accounts, as well as other property. See Salathe, supra, at 551. Back To Text*

[5] § 552 of the Bankruptcy Code states:

Except as provided in subsection (b) of this section, property acquired by the estate or by the debtor after the commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case.

(b)(1) Except as provided [elsewhere in] this title, if the debtor and an entity entered into a security agreement before the commencement of the case and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement of the case and to proceeds, product, offspring, or profits of such property, then such security interest extends to such proceeds, product, offspring, or profits acquired by the estate after the commencement of the case to the extent provided by such security agreement and by applicable nonbankruptcy law, except to any extent that the court, after notice and a hearing and based on the equities of the case, orders otherwise.

(b)(2) Except as [otherwise] provided . . . if the debtor and an entity entered into a security agreement before the commencement of the case, and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement of the case and to amounts paid as rents of such property or the fees, charges, accounts or other payments for the use or occupancy of rooms and other public facilities in hotels, motels, or other lodging properties, then such security interest extends to such rents and such fees, charges, accounts, or other payments acquired by the estate after the commencement of the case to the extent provided in such security agreement, except to any extent that the court, after notice and a hearing and based on the equities of the case, orders otherwise. 11 U.S.C. § 552 (1994); *see also* Brever v. State Bank of Young Am. (In re Kohls), 94 B.R. 1006, 1010 (Bankr. D. Minn. 1987) (finding that where creditor has perfected interest, lien attaches to future proceeds); Salathe, supra note 4, at 566−67 (explaining problems with non−mortgage asset based securities, such as receivables). Back To Text

[6] This Article assumes that a lender can obtain a validly attached and properly perfected security interest in healthcare receivables, including Medicaid and Medicare receivables. This Article should not be construed as support for or against the proposition that valid liens can be attached and perfected on Medicaid and Medicare receivables; the Article simply takes no position on this topic. Other writers have addressed this issue. *See* U.C.C. § 9−203 (1998) (setting forth requirements of attachment for creditors);

In re American Care Corp., 69 B.R. 66, 67 (Bankr. N.D. Ill. 1986) (allowing creditor security interest in debtor's Medicare accounts receivable); Salathe, supra note 4, at 558−61. Back To Text

[7] *See* Chequers Inv. Assocs. v. Hotel Sierra Vista Ltd. Partnership (*In re* Hotel Sierra Vista Ltd. Partnership), 112 F.3d 429, 430 (9th Cir. 1997) (requiring hearing to determine amount of creditor's interest in cash collateral in conformity with *Days California* decision); Financial Sec. Assurance v. Days Cal. Riverside Ltd. Partnership (In re Days Cal. Riverside Ltd. Partnership), 27 F.3d 374, 376−77 (9th Cir. 1994) (stating that portion of hotel revenues were "rent" under old § 552(b)). Congress resolved the issue of whether hotel receivables were "rent" with an amendment to the section in late 1994.

See Bankruptcy Code, Rules and Forms, 11 U.S.C. § 552(b), Historical and Revision Notes (West 1999). Back To Text

[8] Bankruptcy Code § 552 provides merely that pre−petition liens do not cover property acquired post−petition by the debtor. *See* 11 U.S.C. § 552(a) (1994). The section also outlines certain exceptions, notably for proceeds and rents, but does not elaborate on the definitions of any of the terms. *See* 11 U.S.C. § 552(b) (1994). Nor are these definitions found elsewhere in the Code. Back To Text

[9] 1 U.S.C. § 552 (a) (1994). Specifically, § 552 (a) states:

(a) Except as provided in subsection (b) of this section, property acquired by the estate or by the debtor after the commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case.

Id.*; see also* Kucera v. Bank of Brainard (In re Kucera), 123 B.R. 852, 854 (Bankr. D. Neb. 1990) (stating that § 552 makes pre−petition liens inapplicable to after−acquired property regardless of after−acquired property clause); In re Wallman, 71 B.R. 125, 127 (Bankr. D.S.D. 1987) (recognizing that § 552 (a) states that property acquired post−petition is not subject to after−acquired property clause). Back To Text

[10] *See* supra note 5 and accompanying text (setting forth text of U.S.C. § 552 (b)); *see also* In re T−H New Orleans Ltd., 10 F.3d 1099, 1104 (5th Cir. 1993) (adopting broader interpretation of FSA's revenues and defining them as "rent" within the meaning of 11 USC § 552 (b)); United Virginia Bank v. Slab Fork Coal Co. (In re Slab Fork Coal Co.), 784 F.2d 1188, 1191 (4th Cir. 1986) (discussing Congressional intent to include "cash collateral" in scope of § 552(b)). Back To Text

[11] There is no mention of hospital receivables in any relevant section of the Bankruptcy Code. *See generally* 11 U.S.C. § 101 (1994) (omitting definition for term "hospital receivables"); 11 U.S.C. § 363 (1994) (providing detailed definition of "cash collateral"); 11 U.S.C. § 552 (1994) (discussing post−petition treatment of pre−petition liens). Back To Text

[12] Local Loan Co. v. Hunt, 292 U.S. 234, 243 (1934) (considering propriety of garnishing debtor's wages after filing of petition); *see also* In re Corpus Christi Hotel Partners, 133 B.R. 850, 857 (Bankr. S.D. Tex. 1991) (applying *Local Loan* methodology to hotel industry); In re Cooley, 87 B.R. 432, 438 (Bankr. S.D. Tex. 1988) (reaffirming that post−petition service earnings are not proceeds of estate). Back To Text

[13] *See, e.g.*, Unsecured Creditors Comm. v. Marepcon Fin. Corp. (*In re* Bumper Sales, Inc.), 907 F.2d 1430, 1436 (4th Cir. 1990) (looking to definition of proceeds and discussion of after−acquired property in Article 9 of U.C.C. for guidance in determining whether post−petition inventory was subject to pre−petition lien); Covey v. Ipava State Bank (In re Ladd), 106 B.R. 174, 176 (Bankr. C.D. Ill. 1989) (reviewing U.C.C. definition of property as it applies to property acquired through pre−petition collateral); In re Wiegmann, 95 B.R. 90, 93 (Bankr. S.D. Ill. 1989) (applying U.C.C. to definition of post−petition farm revenue). Back To Text

[14] *See* In re Slab Fork Coal Co., 784 F.2d at 1190 (evaluating post−petition proceeds of pre−petition contract, with consideration of fresh−start policy underlying Code); In re Transportation Design and Tech., Inc., 48 B.R. 635, 640

(Bankr. S.D. Cal. 1985) (considering importance of debtor's ability to enjoy fresh start relating to post−petition patent); In re Lawrence, 41 B.R. 36, 38 (Bankr. D. Minn. 1984) (emphasizing that courts should interpret Code in manner consistent with fresh start policy of bankruptcy law). Back To Text

[15] *See* Brever v. State Bank of Young Am. (In re Kohls), 94 B.R. 1006, 1010 (Bankr. D. Minn. 1987) (using broader definition of "proceeds" as set forth in legislative history of § 552 to analyze security interest with respect to dairy farm revenues generated post−petition); Pigeon v. Production Credit Assoc. of Minot (In re Pigeon), 49 B.R. 657, 659 (Bankr. D.N.D. 1985) (utilizing legislative history to determine that broad definition of "proceeds" did not qualify post−petition milk products as subject to pre−petition lien); In re Cupp, 38 B.R. 953, 958 (Bankr. N.D. Ohio 1984) (holding that goods received in governmental payment−in−kind were considered "proceeds"). Back To Text

[16] *See* Calmark Motel Holding Corp. v. Official Unsecured Creditors Comm. (*In re* Northview), 130 B.R. 543, 548 (9th Cir. B.A.P. 1991) (applying *Local Loan* logic in determining that hotel revenues are not "proceeds"); In re West Chestnut Realty of Haverford, Inc., 166 B.R. 53, 57 (Bankr E.D. Pa. 1993) (utilizing analysis set forth in hotel cases to determine that post−petition tipping fees for landfills are not proceeds of land); In re Everett Home Town Ltd., 146 B.R. 453, 460 (Bankr. D. Ariz. 1992) (delineating between services and proceeds in regard to golf and racquet clubs); *see also* infra Section IV (comparing hotel, landfill and golf/racquetball club industries to healthcare industry in order to establish methodology for evaluating post−petition receivables). Back To Text

[17] *See* infra Section IV (presenting arguments based upon legislative history and court decisions from other industries that revenue from services is after−acquired property); s*ee also* 11 U.S.C. § 552(a) (1994) (stating that after−acquired property is not subject to lien resulting from security agreement entered into before commencement of case). Back To Text

[18] *See* Plunkett's Healthcare Industry Almanac, supra note 1 (describing healthcare industry). S*ee generally* 29 U.S.C. § 1161 (1994) (discussing mandated coverage by group health plans); Shea v. Esensten, 107 F.3d 625, 629 (8th Cir. 1997) (examining financial and fiduciary relationship between patient, provider and insurer). Back To Text

[19] *See* Plunkett's Healthcare Industry Almanac, supra note 1 (describing healthcare industry); *see also* Joseph A. Snoe, American Healthcare Delivery Systems 308 (1998) (stating that "[t]he users of services usually are not the payors of services"); Herman Miles Somers & Anne Ramsay Somers, *Doctors, Patients and Health Insurance: The Organization and Financing of Medical Care*, Healthcare L. and Ethics 13, 13−15 (1998). *See generally* 29 U.S.C. § 1161 (1994) (describing mandated coverage by group health plans); Shea, 107 F.3d at 629 (describing financial and fiduciary relationship between patient, provider and insurer). Back To Text

[20] These industry players are particularly important because the cost containment pressures placed on hospitals by managed care organizations and the governmental insurers have decreased the stability of the sector, leading to a heightened need for clear bankruptcy guidelines for hospitals. *See* Plunkett's Healthcare Industry Almanac, supra note 1 (stating that "[a]ccording to Zimmerman and Associates, hospitals could write off a massive $20 billion in bad debt in the year 2000 [alone]"). The decreased stability in this market is further exemplified by the rapid decrease in the Moody's and S&P bond ratings for hospitals. *See* Richard Haugh, *The Ratings Slide*, Hospital and Health Networks, August 1999, at 42. It is anticipated that with the enactment of the balanced budget act and increased managed care penetration, "hospitals" total profit margins will drop from a median of 4% to minus 4% by 2002. *See* Kristin Hallan, *Managed Care Linked to Financial Strain*, Mod. Healthcare, October 4, 1999, at 3. Back To Text

[21] *See* Plunkett's Healthcare Industry Almanac, supra note 1 (describing healthcare industry); *see also* Black's Law Dictionary 737 (6th ed. 1990) (defining "hospital" as "[a]n institution for the treatment and care of sick, wounded, or aged persons"). Back To Text

[22] *See* Form 10−Q, Columbia/HCA Healthcare Corporation, (June 30, 1999), <http://www.sec.gov/Archives/edgar/data/860730/0000950144−99−009792.txt> (stating Columbia/HCA's primary objective is to provide communities it serves with comprehensive array of quality healthcare services); Form 10−K, Tenet Healthcare Corporation, <http://www.sec.gov/Archives/edgar/data/ 70318/0000912057−97−029143.txt> (noting each of Tenet's general hospitals offers acute care services); *see also* 29 C.F.R. § 103.30 (f)(2) (1999)

(defining acute care hospitals as hospitals in which stay is less than thirty days, or short term care hospital in which 50% of patients are admitted to units in which stay is less than 30 days). Back To Text

[23] *See* Form 10−Q, Columbia/HCA HealthCare Corporation, supra note 22 (listing services provided by company); *see also* Advocacy Org. for Patients and Providers v. Mercy Health Servs., 987 F.Supp. 967, 973 n.9 (E.D. Mich. 1997) (listing services generally available at acute care facilities as gynecology, pediatrics, general medicine, and general surgical services); City of Smithville v. St. Luke's Northland Hosp. Corp., 972 S.W.2d 416, 418 (Mo. Ct. App. 1998) (identifying hospital as acute care facility and listing its services as including 24−hour emergency room, radiological services and intensive care unit). Back To Text

[24] *See* Form 10−Q, Columbia/HCA HealthCare Corporation, supra note 22 (identifying sources of revenue); *see also* County Board of Equalization of Utah County v. Intermountain Healthcare, Inc., 709 P.2d 265, 273 (Utah 1985) (noting revenue of defendant hospital was derived primarily from patient charges, third parties (i.e., Blue Cross, Blue Shield, Medicare, Medicaid) and gifts); McMahon v. Baroness Erlanger Hosp., 306 S.W.2d 41, 43 (Tenn. Ct. App. 1957) (showing that sources of revenue of defendant hospital included patient charges, taxes, gifts, and blood bank sales). Back To Text

[25] *See* Plunkett's Healthcare Industry Almanac, supra note 1 (describing categories of purchasers within healthcare industry). Back To Text

[26] *See* Plunkett's Healthcare Industry Almanac, supra note 1 (listing key attributes of largely−defunct fee−for−service plans). Those attributes are as follows:

[A][p]atients could choose any medical provider and insurance company and ask for any treatment they wanted.

[B]There was no practical limit on what physicians and hospitals could charge.

[C]Payers (insurance companies) paid the bills with few questions asked; therefore, patients never questioned the bills.

[D]The costs charged by providers soared unrestrained (For example, 13.6 percent average per year between 1988 and 1992).

Id.; *see also* Andrew Bindman, *Primary and Managed Care: Ingredients for Healthcare Reform, 161 W. J. of Med. 1, 78 (1994) (comparing high monthly premiums for "fee−for service" plans to lower managed care premiums). Back To Text*

[27] *See* supra note 26 and accompanying text (discussing fee−for−service system); *see also* Jerome J. Kornfeld, *Let's Not Forget the Oath; Hippocratic Oath*, Med. Economics, February 22, 1999, at 7 (describing one doctor's memories of fee−for−service system, where claims were submitted by providers and paid by insurance, and when insurance companies simply raised premiums rather than question services); Michael M. Weinstein, *Whiplash; In Healthcare, Be Careful What You Wish For*, NY Times, May 31, 1998, § 4, at 1 (describing fee−for−service as putting all choices in the hands of patients and providers). Back To Text

[28] *See* supra note 26 and accompanying text (discussing fee−for−service system); *see also* Andrew Rushkin, Note, Unbridled Managed Care: When Consumers Experience Anti−Trust Welfare Loss From Exclusionary Contracts Between HMO Insurers and Healthcare Providers, 6 Health Matrix 391, 393−94 (1996) (stating that fee−for−service insurers pay provider based on patient's costs, regardless of actual expenses). Back To Text

[29] *See* Plunkett's Healthcare Industry Almanac, supra note 1 (stating "[p]atients could demand almost any treatment they wanted with little or no concern for cost"); *see also* Rushkin, supra note 28, at 393 (noting that fee−for−services providers generally do not restrict patients' choice of provider). Back To Text

[30] *See* Plunkett's Healthcare Industry Almanac, supra note 1 (noting that HMOs are corporations that provide both health insurance and medical care)*; see also The Benefit Services Group, Inc*. (last modified November 3, 1999)

<http://www.bsg.com/ProdSrv/Medical/MngCre.htm> (showing that like fee−for−service insurance companies, HMOs have customers who pay set periodic fee in exchange for coverage of medical expenses incurred).

There are four principal HMO models: (1) the staff model, in which the HMO actually employs physicians and other professionals to provide medical care; (2) the group model, in which an HMO contracts with a large healthcare corporation that provides a comprehensive range of medical services; (3) the network model, in which an HMO contracts with a number of physicians who may also serve non−HMO patients; and (4) the IPA model, in which an HMO contracts with an Individual Practice Association, which in turn contracts with physicians who remain independent and provide services in their own offices. *See Managed Care Article, Continuing Learning Education, State Bar of Texas* [hereinafter *Managed Care Article*] (last modified July 19, 1999) <http.www.texasbarcle.com/articles/5admed/mccuee.html> (defining four HMO models); *see also* WNET New York Web Site (visited February 27, 2000) <http://www.wnet.org/archive/mhc/Overview/Sidebar1.html> (describing how HMO operates and listing four HMO models). Through these and other similar models and their emphasis on negotiating fixed, low rates for medical services, HMOs have been able to drive healthcare costs down, making them less expensive for members. Back To Text

[31] PPOs are very similar to HMOs, but provide subscribers with a greater range of flexibility in choosing their provider. In the PPO model, members may use any provider, but are given a financial incentive to use providers within the network. *See* Managed Care Article, supra note 30. When using so−called "preferred providers," members have higher levels of coverage, lower deductibles, and lower co−payments. *See* id. Like HMOs, PPOs negotiate fixed rates with various providers, forcing the providers to price competitively for placement on the preferred provider list. *See* id. PPOs also represent a lower−cost alternative to traditional fee−for−service insurance providers. *See* id; *see also The Benefit Services Group, Inc.* (visited February 4, 2000) <http://www.bsg.com/ProdSrv/Medical/MngCre.htm>. The Benefit Services Group Web Site contains the following succinct definition of managed care:

Healthcare systems that integrate the financing and delivery of appropriate healthcare services to covered individuals by arrangements with selected providers to furnish a comprehensive set of healthcare services, explicit standards for selection of selection of healthcare providers, formal programs for ongoing quality assurance and utilization review, and significant financial incentives for members to use providers and procedures associated with the plan.

Id. Back To Text

[32] *See Healthcare Law – HMO Regulation – Arkansas Requires HMOs To Accept Any Provider Willing To Join Their Networks. – Patient Protection Act, 1995 Ark. Acts 505, Amended by 1995* Ark. Acts 1193, 109 Harv. L. Rev. 2122, 2124 (June 1996) (observing act attempts to preserve patient's ability to choose her own doctor, hospital, or pharmacist). HMOs use their considerable number of subscribers as a bargaining tool by which they negotiate pre−arranged, fixed service fees with healthcare providers. *See* Gregory D. Jones, *Primum Non Nocere: The Expanding "Honest Services"* Mail Fraud Statute and the Physician−Patient Fiduciary Relationship, 51 Vand. L. Rev. 139, 167−68 (1998) (stating general structure of HMO – Provider fee arrangements). In exchange for these specially negotiated rates, HMOs typically stipulate that their members will use only or primarily the contracted−with healthcare providers' services. *See* id. Thus, unlike fee−for−service arrangements, HMO members are typically only insured to the extent that they utilize the services of physicians who have contracts with or are employed by the HMO. *See* id. However, like fee−for−service arrangements, HMOs pay for the incurred expenses as they come due. *See* Diana Joseph Bearden & Bryan J. Maedgen, *Emerging Theories of Liability in the Managed Healthcare Industry*, 47 Baylor L. Rev. 285, 293 (1995) (discussing IPA model where HMO pays IPA plan who, in turn, pays provider).

See generally Plunkett's Healthcare Industry Almanac, supra note 1 (describing practices of HMOs). Back To Text

[33] *See* Plunkett's Healthcare Industry Almanac, supra note 1 (stating that "hospitals have managed to maintain profit margins by cutting expenses, expanding outpatient services and diversifying into post−discharge care"). Back To Text

[34] Medicare is a federal healthcare insurance program established by the Comprehensive Social Security Act Amendments of 1965. See Comprehensive Social Security Act Amendments of 1965, Pub. L. No. 89−97, 79 Stat. 286 (1965) (codified as amended at 42 U.S.C. § 1395 (1994)). Medicaid is codified primarily at 42 U.S.C. § 1396 (1994).

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[35] *See* 42 U.S.C. § 1395c (1994) (stating that Medicare "provides basic protection against the costs of hospital, related post−hospital, home health services, and hospice care . . . for (1) individuals who are age 65 or over and are eligible for retirement benefits . . . (2) individuals under the age of 65 who have been entitled . . . to benefits . . . on the basis of disability"). Back To Text

[36] *See* 42 U.S.C. § 1395j (1994) (establishing voluntary insurance program to provide medical insurance benefits for aged and disabled individuals who elect to enroll in such program, which will be financed by premium payments by enrollees and contributions from funds appropriated by Federal Government). Back To Text

[37] *See* 42 U.S.C. § 1395w−21 (Supp. 1998) (providing that person entitled to receive Medicare may instead choose to receive care under "Medicare + Choice plan"). Medicare + Choice plans include "[c]oordinated care plans. . . including but not limited to health maintenance organization plans . . . , plans offered by provider−sponsored organizations . . . , and preferred provider organization plans." Id. at § 1395w−21(a)(2); *see also Financing Healthcare Providers*, SD71 ALI−ABA 401, 403 (May 6, 1999) (analyzing banker's ability to access receivable income deriving from government healthcare programs). Back To Text

[38] The purpose of Medicaid is to enable:

[E]ach State, as far as practicable under the conditions in such State, to furnish (1) medical assistance on behalf of families with dependent children and of aged, blind, or disabled individuals, whose income and resources are insufficient to meet the costs of necessary medical , and (2) rehabilitation and other services to help such families and individuals attain or retain capability for independence or self−care.

42 U.S.C. § 1396 (1994). Back To Text

[39] *See* 42 U.S.C. § 1396b (1994) (outlining plan whereby amount of federal funds are computed). Back To Text

[40] The Secretary of the Department of Health and Human Resources has administrative authority over both Medicare and Medicaid. See 42 U.S.C. § 1395hh (1994). However the Secretary has delegated most of this power to the Healthcare Financing Administration ("HCFA"). *See* 42 C.F.R. § 400 (1997). Back To Text

[41] *See* 42 U.S.C. § 1395 (1994) (describing reimbursement system); 42 C.F.R. § 400 (1998) (stating same). *See generally* West Virginia University Hosps., Inc. v. Casey, 898 F.2d 357, 360 (3d Cir. 1990) (noting particular reimbursement litigation involved "complex issues of state and federal Medicaid reimbursement law").

Since 1983, the government has paid general acute care hospitals under a prospective payment system ("PPS"). *See* 42 C.F.R. § 412 (1998). *See generally* Sarah B. Foster & Shalom L. Kohn, *When the Healthcare Provider Gets Sick −Healthcare Issues in Bankruptcy*, 1998 Nat'l Conference of Bankr. Judges 1 (discussing how government payments are made to hospitals). This means that hospitals receive standardized, predetermined fees for each discharged Medicare/Medicaid patient.

See 42 U.S.C. § 1395ww(g) (1994); 42 C.F.R. § 412.2(a) (1998) (stating that "hospitals are paid a predetermined amount per discharge for inpatient hospital services furnished to Medicare beneficiaries."). Pursuant to the statute, HCFA determines the base standardized amount, and has provided guidelines for the modification of this amount to accurately reflect the cost to a hospital. *See* 42 U.S.C. § 1395ww (g) (1994); 42 C.F.R. § 412 (1998). The factors used to adjust the base amount for a service include the location of the hospital (urban or rural), the relative use of resources (adjusted by what is termed the "diagnosis related group"), labor cost differentials, the cost of medical education, and any unusual case−specific costs.

See 42 U.S.C. § 1395ww(c), (d) (adjusting for geographic differences); 42 C.F.R. §§ 412.1, 412.60, 412.230 (1998) (adjusting for number of residents employed, geography, and other factors).

As with the above pricing scheme, the payment procedure for Medicare/Medicaid also varies substantially from that of other purchasers. Instead of paying on a fee−for−services basis, the Medicare Act requires HCFA to make interim estimated payments to PPS hospitals on a monthly basis. *See* 42 U.S.C. § 1395g(e) (1994); *see also* 42 U.S.C. § 1395g(a) (1994) (stating that "Secretary shall periodically determine the amount which should be paid under this part to each provider of services with respect to the services furnished by it, and the provider of services shall be paid, at such time or times as the Secretary believes appropriate (but not less often than monthly)."); 42 C.F.R. § 412.116(b)(2) (1998) (implementing statute with biweekly payments). HCFA has generally paid treating hospitals on a biweekly basis. *See* 42 C.F.R. § 412.116 (b)(2) (1998). *See generally* Foster & Kohn, supra (discussing how government payments are made to hospitals). In addition, at the end of each fiscal year, Plan A hospitals must submit cost reports to their fiscal intermediary (then on to Medicare) for the year. *See* 42 U.S.C. § 1395g (1994) (providing "no such payments shall be made to any provider unless it has furnished such information as the Secretary may request."). These reports compare the total actual expense for the services rendered with the amount of reimbursement payments received. *See* 42 C.F.R. § 413.20(d) (1998). *See generally* Foster & Kohn, supra (discussing how government payments are made to hospitals). If the hospital has received an overpayment, it must refund the difference at the time of the report's submission. *See* 42 U.S.C. § 1395oo (1993). *See generally* Foster & Kohn, supra (discussing how government payments are made to hospitals). If the hospital has been underpaid, HCFA or an agent of HCFA conducts an investigation, normally paying a portion of the amount prior to settlement of the report. *See generally* Foster & Kohn, supra (discussing how government payments are made to hospitals). Once an investigation is completed and the report has been settled, HCFA issues a Notice of Amount of Medicare Program Reimbursement, closing the matter. *See* id. Services performed under the other Medicare plans, B or C, are submitted as claims to the insurance company or managed care company. *See* Charles E. Harrell & Mark D. Folk, Financing American Health Security: The Securitization of Healthcare Receivables, 50 Business Lawyer 47, 52−53 n.18 (1994) (stating that "[p]art B participants submit claims to, and receive reimbursements from, a 'carrier'"). Back To Text

[42] *See The Business Bankruptcy Reform Act: Business Bankruptcy Issues in Review: Hearings on S. 1914 Before the Subcomm. on Administrative Oversight and the Courts of the Sen. Comm. on the Judiciary, 105th Cong.* (statement of Keith J. Shapiro on behalf of the American Bankruptcy Institute) (available at <www.abiworld.org/legis/testimony/98junshapiro.html>).

As many states began reforming their healthcare systems and managed care became the norm in the healthcare industry, many healthcare businesses found themselves vulnerable to increased competition, decreasing profit margins and extinction. In addition, many leveraged healthcare businesses lacked the necessary cash flow to support the junk bond debt undertaken in the 1980s.

In addition, healthcare businesses failed or required financial restructuring with increasing frequency. For example, between 1994 and 1995 the total number of failures in the healthcare industry increased by 10.6%; between 1995 and 1996 the failures increased by 14.3%; and between 1996 and 1997, the failures increased by 15.5%. *See* Neil DiBernardo, Business Failure Record 1996 (Final) and 1997 (Preliminary) (The Dun & Bradstreet Corporation 1998); *see also* BNA's Health Reporter, *Roundup: Impact of STARK II Proposal Studied;* GAO To Review Path Audits of Hospitals, 7 BHLR 131, January 22, 1998 (observing that "many are predicting a flurry of healthcare business restructuring to ensure compliance with" HCFA's proposed STARK II regulations); James E. Eggleston, *Patient Advocacy and Consumer Protection Through Union Activism: Protecting Healthcare Consumers, Patients and Workers During an* Unprecedented Restructuring of the Healthcare Industry, 41 St. Louis U. L.J. 925, 930−31 (1997) (noting that in 1995, 735 of nation's hospitals were involved in mergers and acquisitions, and approximately one in five community hospitals changed hands within past two years. From 1994 to 1995, amount of hospitals that were either acquired or subject of merger talks increased by 47%. Additionally, in first quarter of 1996, 223 mergers were made public, which was increase of 34% over previous quarter) (citing Sandy Lutz, *1995: A Record Year for Hospital Deals*, MOD. HEALTHCARE, Dec. 18, 1995, at 43); Thomas Campbell & Daniel McDevitt, *Healthcare Merger Activity Sets Record Pace in First Quarter of 1996*, [1994] Healthcare Antitrust Manual (Thompson Publishing Group, June 8,1996)). Back To Text

[43] 11 U.S.C. § 552 (1994). Back To Text

[44] Id. § 552(b). Back To Text

[45] *See* Butner v. United States, 440 U.S. 48, 54−56 (1979) (holding property rights of parties in and affected by bankruptcy are determined under state law); Genesys Data Techs., Inc. v. Genesys Pacific Techs., Inc. (In re Genesys Data Techs., Inc.), 198 F.3d 128, 132 (4th Cir. 1999) (stating determination of creditors claim is question of state law); Mitsui Mfrs. Bank v. Unicom Computer Corp. (In re Unicom Computer Corp.), 13 F.3d 321, 324−25 (9th Cir. 1994) (noting state law determines whether property held by debtor in constructive trust is included in bankruptcy estate). Back To Text

[46] *See* U.C.C. § 9−102 (1998) (stating policy and subject matter of Article 9); *see also* Leasing Serv. Corp. v. First Tenn. Bank Nat. Ass'n, 826 F.2d 434, 437 (6th Cir. 1987) (stating Bankruptcy Code designates Article 9 of Uniform Commercial Code as governing authority regarding consensual liens over personal property); In re Allen, 123 B.R. 580, 580 (Bankr. S.D. Ohio 1991) (providing that "[t]he Bankruptcy Code makes it clear that Article 9 of the Uniform Commercial Code, as it is adopted by a state governs consensual liens in personal property and fixtures and any claims arising from default under such agreement.").

Under Article 9, the first step in secured lending, the agreement phase, is termed "attachment;" the second step, the filing or possession phase, is called "perfection." *See* U.C.C. §§ 9−203, 9−301 (1998). Attachment is defined in U.C.C. § 9−203, and is the step needed to make a security interest valid between the parties. This section provides generally that, for a creditor's interest in the property of a debtor to be valid, the transaction must comply with three requirements: first, the parties must complete and the debtor must sign a security agreement; second, value must be given in exchange for the security; and third, the debtor must have rights in the collateral. In addition, the section provides that a security agreement gives a creditor rights to proceeds of the collateral, as defined below.

Perfection, which takes place after attachment, is the process by which the creditor makes his security interest valid against other creditors of the debtor, both present and future. *See* U.C.C. §§ 9−301−19 (1994); *see also* U.C.C. § 9−302 (providing perfection must be accomplished by filing financing statement, with certain exceptions). For most forms of collateral, perfection occurs when a security interest has attached and the creditor has either filed a financing statement listing a brief description of the collateral with the State, or taken possession of the collateral. *See* U.C.C. § 9−302(a) (filing with financing statement is normally required, but certain exceptions exist; for instance, possession of collateral by secured party, (a)(1));

U.C.C. § 9−303(a) (stating security interest is perfected when it has "attached and when all of the applicable steps required for perfection have been taken"). Once perfected, a secured creditor has an interest in the subject collateral that is superior to any unperfected interest or interest filed or perfected at a later date. *See* U.C.C. § 9−301 (stating that unperfected security interest is subordinate to rights of persons entitled to priority under § 9−312); § 9−312(5)(a) (asserting that "[c]onflicting security interests rank according to priority in time of filing or perfection. Priority dates from the time a filing is first made covering the collateral or the time the security interest is first perfected, whichever is earlier"). Back To Text

[47] *See* Barnhill v. Johnson, 503 U.S. 393, 398 (1992) ("In the absence of any controlling federal law" property interests are determined by state law); Butner, 440 U.S. at 54−55 ("Property interests are created and defined by state law.") *See generally* Grant S. Nelson and Dale A. Whitman, Real Estate Transfer, Finance, and Development II (West 1994). The general principles of secured lending in this field provide that a lender may collateralize real property by first drafting and having the debtor sign one of several secured loan documents, for instance, a mortgage, deed of trust, an installment sales contract, or the like.

See id. at Chapters 3, 7. This agreement, whatever shape it may take, legally binds both the lender and the borrower, normally permitting the lender to foreclose the property of the buyer upon default. *See* id. at Appendix for Sample Agreements; *see also* id. at Chapter 6 (discussing foreclosure). Further, the lender must file a copy of this agreement with the local land records office to give notice to other present or future creditors of the instant creditor's interest. *See* id. at 182−187. This filing is needed to protect the lender against other creditors who attempt to collateralize the same real property. Back To Text

[48] Accounts are defined as "any right to payment for goods sold or leased or for services rendered which is not evidenced by an instrument or chattel paper, whether or not it has been earned by performance."

U.C.C. § 9−106 (1998). To perfect an interest in a debtor's accounts, the creditor must file a financing statement with the office of the secretary of state. *See* U.C.C. § 9−401; *see also* Butts v. Bendix Forest Prods. Corp. (In re Summit Creek Plywood Co.), 27 B.R. 209, 213 (Bankr. D. Or. 1982) (positing that "UCC §§ 9−106 and 9−109 provide for six major categories of collateral, these being accounts, general intangibles, consumer goods, equipment, farm products, and inventory.")

U.C.C. § 9−401states:

The proper place to file in order to perfect a security interest is as follows:

(1) when the collateral is consumer goods, . . .

(2) when the collateral is timber . . .

(3) in all other cases, in the office of the Secretary of State.

U.C.C. § 9−401(a). Because accounts fall within the "other cases" language, financing statements for them are filed with the office of the Secretary of State. Note, however, that this Article does not address the issue of whether or how a security interest in Medicare and Medicaid receivables can be attached or perfected under applicable federal law and regulations. Back To Text

[49] Inventory is defined as goods that are "held by a person who holds them for sale or lease or to be furnished under contracts of service or if he has so furnished them, or if they are . . . materials used or consumed in a business." U.C.C. § 9−109. A creditor may perfect an interest in inventory by filing or by taking possession of the inventory. *See* U.C.C. §§ 9−302 and 9−401(a). Section 9−302 states that a financing statement need not be filed if the secured creditor has possession of the collateral. *See* U.C.C. § 9−302(a)(1); *see also* In re Summit Creek, 27 B.R. at 213 (noting that inventory is included under UCC § 9−109). Back To Text

[50] Once the specific secured collateral has been sold, the creditor will have nothing securing his loan.

See generally Brian A. Blum, Bankruptcy and Debtor/Creditor 14 (1993); David Gray Carlson, Security Interests In The Crucible of Voidable Preference Law, 1995 U. Ill. L. Rev. 211, 316−17 (1995) (noting Congress was concerned for retention of security interests in fluctuating inventories and accounts when it enacted 11 U.S.C. § 547(c) (1988)); D. Benjamin Beard, *The Purchase Money Security Interest In Inventory: If It Does Not Float, It Must Be Dead!*, 57 Tenn. L. Rev. 437, 442−43 (1990) (stating that "[u]nless a lender's security interest can float over the fluctuating pool of inventory, the lender's ability to conduct on going inventory financing is severely restricted"). Back To Text

[51] *See* Paulman v. Gateway Venture Partners III, L.P. (In re Filtercorp), 163 F.3d 570, 580 (9th Cir. 1998) (observing majority of courts reason that presumption of floating loan on inventory and accounts receivable is not created by particular language but rather springs from cyclical nature of collateral itself); Stoumbos v. Kilimnik, 988 F.2d 949, 956 (9th Cir. 1993) (noting after−acquired property clauses apply to accounts receivable and inventory because both are cyclically depleted and replenished assets); *see also* Blum, *supra* note 50, at 14 (discussing after−acquired property clauses and their utility). Back To Text

[52] *See* U.C.C. § 9−204(1) (1998). The section provides as follows:

(a) Except as provided in subsection (b), a security agreement may provide that any or all obligations covered by the security agreement are to be secured by after−acquired collateral.

(b) No security interest attaches under an after−acquired property clause to consumer goods other than accessions (§ 9−314) when given as additional security unless the debtor acquires rights in them within ten days after the secured party gives value.

(c) Obligations covered by a security agreement may include future advances or other value whether or not the advances or value are given pursuant to commitment (Subsection (a) of § 9−105).

Id. Back To Text

[53] *See* U.C.C. § 9−203(3) (1994) (stating "security agreement gives the secured party the rights to proceeds provided by § 9−306"). U.C.C. § 9−306(a) defines proceeds as "whatever is received upon the sale, exchange, collection or other disposition of collateral or proceeds . . . Money, checks, deposit accounts, and the like are 'cash proceeds.' All other proceeds are 'non−cash proceeds." U.C.C. § 9−306(a); *see also* id. § 9−306 (b) & (c) (stating "security interest continues in collateral notwithstanding sale, exchange or other disposition thereof . . . and also continues in any identifiable proceeds including collections received by the debtor and providing for the continuance of perfection, automatically for ten days, and thereafter upon fulfillment of certain qualifications"). Back To Text

[54] 11 U.S.C. § 552(a) (1994). Back To Text

[55] *See* Fed. Deposit Ins. Corp. and Acquisition Mgmt., Inc. v. Hastie (*In re* Hastie), 2 F.3d 1042, 1043 (10th Cir. 1993) (noting property acquired after commencement of bankruptcy proceeding is not subject to any security agreement lien entered into prior to bankruptcy petition); Casco N. Bank v. Green Corp. (In re Green Corp.), 154 B.R. 819, 821 (Bankr. D. Me. 1993) (observing floating and after−acquired liens do not extend to property received by debtor after bankruptcy filing); Executive Assocs. v. Southern Nat'l Bank (In re Executive Assocs., Inc.), 24 B.R. 171, 172 (Bankr. S.D. Tex. 1982) (stating property acquired by debtor after filing of petition is not subject to pre−petition lien resulting from any security agreement entered into prior to commencement of case). Back To Text

[56] 11 U.S.C. § 552(b)(1); *see also* Charleston Nat'l Bank v. Slab Fork Coal Co. (*In re* Slab Fork), 784 F.2d 1188, 1191 (4th Cir. 1986) (noting "§ 552(b) gives the bankruptcy court considerable latitude in applying pre−petition security interests to post−petition proceeds"); *In re* Patio & Porch Sys., Inc., 194 B.R. 569, 574 (Bankr. D. Md. 1996) (finding that payments made under contracts subject to perfected security agreement were proceeds of accounts receivable for purposes of § 552(b) exception). Back To Text

[57] 11 U.S.C. § 552(b)(2). Back To Text

[58] *See* id. § 552(a) (stating that property acquired by debtor post−bankruptcy is not subject to liens created by security agreement before bankruptcy); *see also* Financial Sec. Assurance v. Days Cal. Riverside Ltd. Partnership (In re Days Cal. Riverside Ltd. Partnership), 27 F.3d 374, 376−77 (9th Cir. 1994) (observing that "purpose of § 552 is to permit a debtor 'to gather into the estate as much money as possible to satisfy the claims of all creditors'") (quoting Philip Morris Capital Corp. v. Bering Trader, Inc. (In re Bering Trader, Inc.), 944 F.2d 500,502 (9th Cir. 1991)). *But cf.* T−H New Orleans Limited Partnership v. Financial Sec. Assurance, Inc. (In re T−H New Orleans Ltd. Partnership), 10 F.3d 1099, 1104 (5th Cir. 1993) (noting that § 552(b) creates significant exception to § 552(a)). Back To Text

[59] *See* 11 U.S.C. § 552(b) (noting how pre−petition security agreement covering proceeds of property acquired before commencement of case covers proceeds acquired after commencement); *see also* In re Wabash Valley Power Ass'n., 72 F.3d 1305, 1322 (7th Cir. 1995) (discussing that secured creditors are not entitled to after−acquired property unless security agreement specifically provides that security interest created extends to proceeds of collateral or rents paid on it); *In re Bering Trader, Inc.*, 944 F.2d at 501 (stating that § 552(b) exception applies where valid pre−petition security agreement is present and it covers pre−petition property of debtor and to proceeds, offspring, rents or profits of such property). Back To Text

[60] *See* 11 U.S.C. § 363(a) (1994) (noting that "cash collateral" includes "proceeds, products, offspring, rents, or profits of property…subject to a security interest as provided in § 552(b)"); *see also* New York State Electric and Gas Company v. McMahon a/k/a McRich Foods (In re McMahon), 129 F.3d 93, 98 (2d Cir. 1997) (finding utility may exercise equitable doctrine and apply pre−petition deposit to its post−petition application); Liberty Nat'l Enter. v. Anbanc La Mesa Ltd. Partnership (In re Anbanc La Mesa Ltd. Partnership), 115 F.3d 650, 652 (9th Cir. 1997) (noting Bankruptcy Court found that RTC had properly perfected interest entitling them to rents and revenue, "cash collateral", as defined under § 363). Back To Text

[61] 11 U.S.C. § 363; *see also* Watson Pacific Ventures v. Valley Federal Savings and Loan (In re Safeguard Self−Storage Trust), 2 F.3d 967, 973−74 (9th Cir. 1993) (finding revenue under lease agreements protected "cash collateral"); *But cf.* First National Bank of Lafayette v. Texas Tri−Collar, Inc. (In re Texas Tri−Collar, Inc.), 29 B.R. 724, 726 (Bankr. W.D. La. 1983) (finding "accounts receivable" do not fit within § 552(b) definition by which secured interest may make claim). Back To Text

[62] *See* In re McMahon, 129 F.3d at 98 (observing use of term "cash collateral" defined in § 363)*; see also* In re Perroncello, 170 B.R. 189, 192 (Bankr. D. Mass. 1994) (holding that debtor must show (1) that sale would not result in unfair discrimination to lienholder in order to sell property free and clear of liens and (2) that trustee acted in good faith); United States v. Wabash Valley Power Ass'n, Inc. (In re Wabash Valley Power Ass'n, Inc.), 167 B.R. 885, 889 (Bankr. S.D. Ind. 1994) (finding promissory notes to be cash collateral and debtor needing court authorization); Titusville Country Club v. Pennbank (In re Titusville Country Club), 128 B.R. 396, 399 (Bankr. W.D. Pa. 1991) (noting that debtor must show "sound business purpose" to sell property prior to confirming plan). Back To Text

[63] *See* supra Section II. Back To Text

[64] Local Loan Co. v. Hunt, 292 U.S. 234, 243 (1934) (finding that pre−petition liens should not encumber property acquired post−petition unless said property has arisen from or is connected with preexisting property); *see also* In re Copeland, 388 F. Supp. 1280, 1285−86 (D. Del. 1974) (using doctrine of *Local Loan* for dischargeability issue); In re Attanasio, 218 B.R. 180, 194 (Bankr. N.D. Ala. 1998) (discussing decision of *Local Loan* and its applicability). Back To Text

[65] *See* Unsecured Creditors Comm. v. Marepcon Fin. Corp. (In re Bumper Sales, Inc.), 907 F.2d 1430, 1436 (4th Cir. 1990) (noting § 552(a)'s fresh start for debtors); Alliance Capital Mgmt. L.P. v. County of Orange (In re County of Orange), 179 B.R. 185, 191 (Bankr. C.D. Cal. 1995) (interpreting § 552(a) broadly to allow debtor fresh start); In re Transportation Design and Tech., Inc., 48 B.R. 635, 640 (Bankr. S.D. Cal. 1985) (referencing legislative history of Code indicating fresh start imperative in examining character of post−petition patent). Back To Text

[66] *See* Great−West Life and Annuity Assurance Co. v. Parke Imperial Canton, Ltd., 177 B.R. 843, 851 (N.D. Ohio 1994) (stating meaning of § 552(b) is found in both statutory interpretation and congressional intent); In re Wiegmann, 95 B.R. 90, 93 (Bankr. S.D. Ill. 1989) (considering character of post−petition farm revenue in light of Commercial Code); In re Transportation Design and Tech., Inc., 48 B.R. at 641 (using California Commercial Code definition of "proceeds" as tool with which to examine post−petition patent). Back To Text

[67] *See, e.g.*, New Hampshire Bus. Dev. Corp. v. Cross Baking Co., Inc. (*In re* Cross Baking Co.), 818 F.2d 1027, 1033 (1st Cir. 1987) (using Senate Judiciary Committee report to determine scope of § 552(b)); Brever v. State Bank of Young Am. (In re Kohls), 94 B.R. 1006, 1010 n.8 (Bankr. D. Minn. 1987) (reasoning that "proceeds" should have broader definition than that of U.C.C. for purposes of bankruptcy). Back To Text

[68] *See* infra Section IV.B. Back To Text

[69] *See* Local Loan, 292 U.S. at 242 (noting that wages earned after adjudication become property of bankrupt, free of all creditors claims**)**; *see also* In re Corpus Christi Hotel Partners, Ltd., 133 B.R. 850, 855 (Bankr. S.D. Tex. 1991) (citing to *Local Loan* in applying logic that hotel accounts and revenues generated post−petition are not subject to pre−petition liens on accounts or rents). *See generally* Fitzsimmons v. Walsh (In re Fitzsimmons), 725 F.2d 1208, 1210 (9th Cir. 1984) (analyzing § 541 problem). The *Fitzsimmons* court stated that under the post−petition earnings exception, § 541(a)(6), services performed by an individual were not property of the estate. *See* id. at 1210−11. However, the *Fitzsimmons* court, by reading the word "personal" into the statute, delineated between services performed by an individual debtor and services performed by employees. *See* id. Unlike the former, the latter services were considered proceeds of the estate. *See* id. at 1211. However, the *Fitzsimmons* court was contemplating a sole proprietorship bankruptcy and would arguably have reached a different result given different facts. In the later case of *In re Cooley*, the court confronted the bankruptcy of a world−famous heart surgeon. In re Cooley, 87 B.R. 432, 438 (Bankr. S.D. Tex. 1988). The surgeon employed associate surgeons who assisted him in the operation of his sole proprietorship. In re Cooley, 87 B.R. at 434. Disagreeing with the *Fitzsimmons* reading of § 541(a)(6), the court

concluded that the services performed by the individual debtor were exempt from being proceeds of the estate. *See* id. at 439−41. Rather, the court found that there was a presumption that all of a debtor's post−petition service earnings were exempt and that the creditor/movant bore the burden of demonstrating what portion of the debtor's post−petition income was the work product of employees. *See* id. What is important to note is that both of these cases considered post−petition service earnings not to be proceeds of the estate. Their reasoning was grounded in both the fresh−start policy and Thirteenth Amendment concerns over involuntary servitude. Back To Text

[70] *See* Local Loan Co. v. Hunt, 292 U.S. 234, 242−43 (1934) (discussing principle that wages earned after discharge in bankruptcy were not in existence at time security arrangement was made); Gwilliam v. United States (In re Gwilliam), 519 F. 2d. 407, 410 (9th Cir. 1975) (noting that purpose of Bankruptcy Act was to allow discharged bankrupt to start over); In re Braund, 289 F. Supp. 604, 607 (C.D. Cal. 1968) (referencing *Local Loan* principle of new start for bankrupt). Back To Text

[71] *See* Philip Morris Capital Corp. v. Bering Trader, Inc. (In re Bering Trader, Inc.), 944 F.2d 500, 502 (9th Cir. 1991) (holding that creditor's security interest in pre−petition rents from charter of vessel does not extend to post−petition rents); In re Kids Creek Partners, L.P., 210 B.R. 547, 555 (Bankr. N.D. Ill. 1997) (asserting that proceeds from sale of debtor's real property after bankruptcy filing was not subject to pre−petition lien); In re HRC Joint Venture, 175 B.R. 948, 953 (Bankr. S.D. Ohio 1994) (deciding that security interest in hotel's accounts receivable is cut off by bankruptcy filing when proceeds were generated by post−petition acts); *see also* infra notes 127−131 and accompanying text (discussing cases involving hotel bankruptcies). The principle was applied particularly in the hotel industry several years ago and also to other service industries. *See* Pavilion Hotel, Inc. v. Valley Nat'l Bank of Ariz., 885 P.2d 186, 190−91 (Ariz. Ct. App. 1994) (noting that where hotel revenues did not arise from pre−petition assets, those post−petition revenues are not proceeds, and creditor's interest in them is cut off upon bankruptcy filing). Back To Text

[72] 292 U.S. at 243 (asserting that post−petition earnings are not subject to pre−petition liens where they were "brought into being solely as the fruit of the subsequent labor of the bankrupt"); *see also* In re Baker, 217 B.R. 609, 610−11 (Bankr. N.D. Cal. 1998) (recognizing Supreme Court's decision in *Local Loan* found that there was no lien on debtor's income earned after filing bankruptcy); In re Rumker, 184 B.R. 621, 627−28 (Bankr. S.D. Ga. 1995) (observing that principle that assignment of post−petition wages does not constitute lien was first articulated by Supreme Court in *Local Loan*). Back To Text

[73] *See* Local Loan, 292 U.S. at 238. Back To Text

[74] *See* id. Back To Text

[75] *See* Local Loan, 292 U.S. at 238. Back To Text

[76] Local Loan Co. v. Hunt, 292 U.S. 234, 243 (1934). Back To Text

[77] *See* In re Corpus Christi Hotel Partners, Ltd., 133 B.R. 850, 856 (Bankr. S.D. Tex. 1991) (determining that while hotel revenues owed on date of filing would be subject to creditor's security interest, post−petition revenues from post−petition operations were cut off from security interest); *see also* Financial Sec. Assurance v. Days Cal. Riverside Ltd. Partnership (In re Days Cal. Riverside Ltd. Partnership), 27 F.3d 374, 376−77 (9th Cir. 1994) (acknowledging that there is distinction between hotel's revenues which come from sale of food and other services and revenues "produced by the property"); Airport Inn Assocs. v. Travelers Ins. Co., 132 B.R. 951, 954−60 (Bankr. D. Colo. 1990) (stating that hotel room revenue is not rent but is personal property, in addition that pre−petition lien does not apply to revenues generated post−petition). Back To Text

[78] 133 B.R. 850 (Bankr. S.D. Tex. 1991). Back To Text

[79] *See* id. at 855. Many courts have come to differing results when determining if a hotel's revenues are proceeds or rents. *Compare* In re Tri−Growth Centre City, Ltd., 133 B.R. 524, 526 (Bankr. S.D. Cal. 1991) (asserting that hotel revenues are proceeds resulting from payments for goods and services), *with In re S.F. Drake Hotel Assocs., 131 B.R.*

156, 160 (Bankr. N.D. Cal. 1991) (deciding that hotel room revenues are rents). Back To Text

80 *See* In re Corpus Christi Hotel Partners, Ltd., 133 B.R. at 855 (relying on *Local Loan* in reaching its conclusion that post−petition hotel revenues are not subject to pre−petition lien). Back To Text

81 *See* infra notes 128−39 and accompanying text (explaining that reasoning of *Local Loan.* has been extended to characterize post−petition hotel revenues, tipping fees on landfill sites, and service related revenues of golf and racquet clubs as non−proceeds or after−acquired property of debtor and free from pre−petition liens); *see also* In re Big Hook Land & Cattle Co., 81 B.R. 1001, 1004 (Bankr. D. Mont. 1988) (holding that post−petition increases in cattle herd not subject to lien of security agreement); First Nat'l Bank of Lafayette v. Texas Tri−Collar, Inc. (In re Texas Tri−Collar, Inc.), 29 B.R. 724, 725 (Bankr. W.D. La. 1983) (finding that accounts receivable were not proceeds, thus pre−petition lien did not extend to post−petition); In re Hamilton, 18 B. R. 868, 871 (Bankr. D. Colo. 1982) (deciding crops planted post−petition were after−acquired property and not subject to pre−petition lien). Back To Text

82 *See* Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934); *see also* United Virginia Bank v. Slab Fork Coal Co. (In re Slab Fork Coal Co.), 784 F.2d 1188, 1191 (4th Cir. 1985) (noting that in deciding character of post−petition property balance between creditors' rights with rehabilitative purpose of Code must be struck); Investment Hotel Properties, Ltd. v. New W. Fed. Sav. and Loan Assoc. (In re Investment Hotel Properties, Ltd.), 109 B.R. 990, 995 (Bankr. D. Colo. 1990) (stating that "§ 552(a) was drafted to facilitate debtor's fresh start by not subjecting property acquired post−petition to pre−petition security agreement");

In re Transportation Design and Tech., Inc., 48 B.R. 635, 640 (Bankr. S.D. Cal. 1985) (considering impact of court's judgment on debtor's ability to enjoy fresh start while examining character of post−petition patent); In re Lawrence, 41 B.R. 36, 38 (Bankr. D. Minn. 1984) (stating that § 552(a) was embodiment of Code's fresh start policy, that court should remain "conscientious in interpreting the Code in a manner consistent with the 'fresh start' and 'rehabilitative' themes of bankruptcy law"). Back To Text

83 *See* Local Loan, 292 U.S. at 244 (discussing general purpose of Bankruptcy Act is to provide honest debtor with new opportunity in life unhampered by preexisting debt); *see also* Fezler v. Davis (In re Davis), 194 F.3d 570, 574 (5th Cir. 1999) (citing *Local Loan.* in stating public and private interest in providing honest debtor with new opportunity without preexisting debt); In re Attanasio, 218 B.R. 180, 194 (Bankr. N.D. Ala. 1998) (quoting *Local Loan.* in construing § 707(b) of Bankruptcy Code). Back To Text

84 *See* Local Loan, 292 U.S. at 244 (asserting that debtor emerging from bankruptcy burdened by preexisting liens loses incentive to work); *see also* In re Attanasio, 218 B.R. at 194 (finding that debtor burdened by preexisting liens is likely to give up rather than continue to work for sole purpose of satisfying preexisting debt); Pillow v. Avco Fin. Serv. (In re Pillow), 8 B.R. 404, 420 (Bankr. D. Utah 1981) (noting that liens surviving bankruptcy put stranglehold on policy of providing fresh start for debtor). Back To Text

85 *See* Local Loan, 292 U.S. at 244 (*citing* Williams v. U.S. Fidelity & Guaranty Co., 236 U.S. 549, 554−55 (1915)); *see also* In re Davis, 194 F.3d at 574 (quoting *Local Loan Co v. Hunt*, 292 U.S. 234, 244 (1934)); Brown v. Cunningham, 303 Ill. App. 307, 309, 25 N.E. 2d 113, 115 (Ill. App. 3d 1940) (applying rationale of *Local Loan* to situation involving assignment of expectancy). Back To Text

86 *See* Local Loan, 292 U.S. at 244 (noting private with public interests in providing fresh start for debtor); *see also* In re Davis, 194 F.3d at 574 (observing private along with public purposes involved in not allowing preexisting liens to burden post−petition debtors). Back To Text

87 *See* Local Loan Co. v. Hunt, 292 U.S 234, 244 (1934) (explaining public interest in providing fresh start for debtor); *see also* In re Davis, 194 F.3d at 574 (following *Local Loan* analysis); *In re* Forgay, 140 F. Supp. 473, 475−77 (D. Utah 1956) (discussing public interest in providing fresh start for debtor). Back To Text

[88] *See, e.g.,* In re Bering Trader Inc., 944 F.2d 500, 502 (9th Cir. 1991) (using fresh start policy as basis for holding pre−petition security interest encumbering accounts from debtor's chartered vessels did not extend to post−petition rents on vessels); American President Lines, Ltd. v. Lykes Bros. Steamship Co. (In re Lykes Bros. Steamship Co.), 216 B.R. 856, 864 (Bankr. M.D. Fla. 1996) (applying fresh start policy in finding charter hire payments were not proceeds of collateral); In re Photo Promotion Assoc., Inc., 53 B.R. 759, 763 (Bankr. S.D.N.Y. 1985) (using fresh start as policy justification buttressing characterization of post−petition receivables as after−acquired property). Back To Text

[89] *See* In re Photo Promotion Assoc., Inc., 53 B.R. at 763 (construing § 552 to characterize post−petition receivables as after−acquired property); s*ee also* Investment Hotel Properties, Ltd. v. New W. Fed. Sav. and Loan Assoc. (In re Investment Hotel Properties, Ltd.), 109 B.R. 990, 995 (Bankr. D. Colo. 1990) (applying § 552 to invalidate security interest in post−petition accounts receivable); In re Hamilton, 18 B.R. 868, 871 (Bankr. D. Colo. 1982) (characterizing crops planted after petition as after−acquired property with § 552 cut off lien). Back To Text

[90] *See* United Va. Bank v. Slab Fork Coal Co. (In re Slab Fork Coal Co.), 784 F.2d 1188, 1191 (4th Cir. 1986) (discussing rehabilitative policy goal of Bankruptcy Code in evaluating equitable considerations under § 552(b)'s final clause); *see also* In re Corpus Christi Hotel Partners, Ltd., 133 B.R. 850, 854−55 (Bankr. S.D. Tex. 1991) (recognizing rehabilitative policy goal of Act is considered in distinguishing proceeds from after−acquired property); *In re Investment Hotel Properties, Ltd.*, 109 B.R. at 995 (noting fresh start goal of Act in applying § 552 to invalidate pre−petition security agreement granting security interest in post−petition accounts). Back To Text

[91] *See* In re Slab Fork Coal Co., 784 F.2d at 1189 (depicting dispute related to characterization of debtor's accounts); *see also* In re Sunberg, 729 F.2d 561, 562 (8th Cir.1984) (determining properly perfected post−petition security interest coupled with state law meant that creditor retained perfected lien in proceeds arising from contracts signed pre−petition, even though payments would occur post−petition); In re Patio & Porch Sys., Inc., 194 B.R. 569, 573 (Bankr. D. Md. 1996) (holding that because of *In re Slab Fork Coal Co*., creditor's security interest in debtor's accounts receivable included right to receive payments on contract claims); In re Rumker, 184 B.R. 621, 626 (Bankr. S.D. Ga. 1995) (relying on *In re Slab Fork Coal Co*. to bolster its distinction between accounts and proceeds within the context of § 552). Back To Text

[92] *See* In re Slab Fork Coal Co., 784 F.2d at 1191. The *Slab Fork* Court held that the cash proceeds generated under a pre−bankruptcy contract for the supply of coal were subject to pre−petition liens on the contract and its proceeds, even those received after petition. *See* id. at 1189. Having thus decided, the court went on to state that:

[n]otwithstanding our decision today, it should be noted that § 552(b) gives the bankruptcy court considerable latitude in applying pre−petition security interests to post−petition proceeds . . . It appears clear from the legislative history related to § 552 that Congress undertook in that section to find an appropriate balance between the rights of secured creditors and the rehabilitative purpose of the Bankruptcy Code.

Id.*; see also* In re River Village Assocs., 181 B.R. 795, 808 (Bankr. E.D. Pa. 1995) (finding § 552(b) to provide that even where pre−petition security interest would extend to post−petition proceeds, court, "after notice and hearing and based on the equities of the case," could provide otherwise); Great−West Life & Annuity Assur. Co. v. Parke Imperial Canton, Ltd., 177 B.R. 843, 855 (Bankr. N.D. Ohio 1994) (holding that bankruptcy judge should find appropriate balance between rights of secured creditors with rehabilitative purposes of Bankruptcy Code if circumstances indicate that expectations of general creditors have been frustrated by § 552(b)). Back To Text

[93] *See* In re Slab Fork Coal Co., 784 F.2d at 1191. *But see* In re Grynberg, 986 F.2d 367 (10th Cir. 1993) (holding that Bankruptcy Code's fresh start policy to be subordinate to collection of revenue in that Congress made it extremely difficult for debtor to avoid payment of taxes); In re Investment Hotel Properties, Ltd., 109 B.R. 990, 998 (Bankr. D. Colo. 1990) (finding it inappropriate to apply equitable exception of § 552(b) because there were not enough facts to determine that interest of rehabilitative purposes of Code outweighed secured creditor's rights to post−petition proceeds). Back To Text

[94] In re Slab Fork Coal Co., 784 F.2d at 1191. Back To Text

[95] 11 U.S.C. § 552(b) (1994); *see also* James Cable Partners v. Citibank (*In re* James Cable Partners), 141 B.R. 772, 774−75 (Bankr. M.D. Ga. 1992) (noting that security interest attaches to post−petition proceeds if permitted by pre−petition security agreement or applicable nonbankruptcy law, and applying state law in determining nature and extent of security interest). Indeed, state law governs a creditor's interest in post−petition income and property. *See* Butner v. United States, 440 U.S. 48, 54 (1979) (finding that right to rents collected during period between mortgagor's bankruptcy and foreclosure sale of mortgaged property is determined by law of state where property is located, not by federal rule of equity); Lewis v. Mfrs. Nat'l Bank, 364 U.S. 603, 609 (1961) (asserting that uniform treatment of property interests by both state and federal courts within state serves to reduce uncertainty, to discourage forum shopping, and to prevent windfalls due to occurrence of bankruptcy); In re Barkley 3A Investors, Ltd., 175 B.R. 755, 758 n.6 (Bankr. D. Kan. 1994) (observing that inquiries into state law may decrease with enactment of Bankruptcy Reform Act of 1994 because state law will no longer determine whether pre−petition security interest extends to post−petition rental income under that Act). Back To Text

[96] *See* infra Section III; s*ee also* In re Patio & Porch Sys., Inc., 194 B.R. 569, 574 (Bankr. D. Md. 1996) (deciding that proceeds is to be defined by state law); In re Investment Hotel Properties, Ltd., 109 B.R. at 997 (finding, based on cases construing § 552(b), that state's version of U.C.C. is determinative of whether security interest in proceeds survived filing of bankruptcy); Carlson v. W.J. Menefee Constr. Co. (In re Grassridge Industries, Inc.), 78 B.R. 978, 979−80 (Bankr. W.D. Mo. 1987) (noting that security agreement and Kansas version of U.C.C. allowed bank's interest in specifically identified contract to survive filing of debtor's petition under § 552(b)). Back To Text

[97] *See* Unsecured Creditors Comm. v. Marepcon Fin. Corp. (In re Bumper Sales, Inc.), 907 F.2d 1430, 1438 (4th Cir. 1990) (looking to U.C.C. § 9−306 as proper approach to analyzing whether security agreement extends to post−petition proceeds of pre−petition collateral); In re Patio & Porch Sys., Inc., 194 B.R. at 574 (applying state's version of U.C.C. § 9−306 in defining proceeds to determine creditor's security interest in pre−petition and post−petition proceeds); In re Corpus Christi Hotel Partners, Ltd., 133 B.R. 850, 855 (Bankr. S.D. Tex. 1991) (beginning analysis of whether hotel revenues are proceeds by focusing on Texas Commercial Code § 9.306); In re Transportation Design and Tech., Inc., 48 B.R. 635, 641 (Bankr. S.D. Cal. 1985) (asserting that whether secured party has security interest in proceeds is determined by state law, thus applying California Commercial Code § 9306(1)). Back To Text

[98] U.C.C. § 9−306(a) (1998). Back To Text

[99] *See* In re Bumper Sales, Inc., 907 F.2d at 1437 (finding that "§ 552's invalidation of after−acquired property clauses did not prevent creditor from acquiring security interest in property acquired by debtor after bankruptcy filing, to extent such property was traceable to proceeds from sale of pre−petition inventory in which creditor had security interest"); In re Corpus Christi Hotel Partners, Ltd., 133 B.R. at 855−56 (relying upon legislative intent behind § 552 in determining term "proceeds" is meant to have broader definition under Bankruptcy Code than restrictive Uniform Commercial Code); In re Transp. Design and Tech., Inc., 48 B.R. at 641 (holding that creditor's argument that Court should give security agreement's terms broad definition opposed to definition contained in California Commercial Code was not sound). Back To Text

[100] 0 *See, e.g.,* In re Corpus Christi Hotel Partners, Ltd., 133 B.R. at 856 (determining that revenues from hotel customers that were owed on date of filing were accounts receivable, additionally that payment of those accounts post−petition would constitute "proceeds," while all post−petition receipts on account of post−petition operations of hotel−debtor were cut off by § 552(a)); Super 8 Motels, Inc. v. M. Vickers, Ltd. (In re M. Vickers, Ltd.), 111 B.R. 332, 333− 36 (D. Colo. 1990) (finding that motel "profits" were accounts under Colorado law); In re Blue Ridge Motel Assocs., 106 B.R. 81, 82 (Bankr. W.D. Pa. 1989) (positing that motel room proceeds fell within description of account). Back To Text

[101] *See* Wolinsky v. Vermont Fed. Bank, FSB (In re Vermont Knitting Co.), 111 B.R. 464, 467−69 (Bankr. D. Vt. 1990) (claiming that deposit on aborted post−petition sale was not proceeds because collateral machinery was not actually "sold" within meaning of Trustee's Request for Bids or Vermont's version of U.C.C.). Back To Text

[102] *See* In re Mintz, 192 B.R. 313, 318−20 (Bankr. D. Mass. 1996) (stating that future payment of debtor's interest in partnership was not proceeds, profits or product of pre−petition collateral as matter of law); *see also* In re S & J Holding Corp., 42 B.R. 249, 250−51 (Bankr. S.D. Fla. 1984) (applying similar rationale in finding coins deposited in video games not proceeds of gaming machines); General Elec. Credit Corp. v. Cleary Bros. Constr. Co., Inc. (In re Cleary Bros. Constr. Co. Inc.), 9 B.R. 40, 41 (Bankr. S.D. Fla. 1980) (using similar rationale in holding rental of collateral did not produce proceeds). Back To Text

[103] *See* FDIC v. Hastie (In re Hastie), 2 F.3d 1042, 1046 (10th Cir. 1993) (determining that ordinary cash dividends are not proceeds because distribution of capital surplus does not amount to sale or disposition); *see also* In re Mintz, 192 B.R. at 319 (discussing *In re Hastie*); In re S & J Holding Corp., 42 B.R. at 250 (applying similar rationale). Back To Text

[104] *See* Covey v. Ipava State Bank (In re Ladd), 106 B.R. 174, 176 (Bankr. C.D. Ill. 1989) (holding that agricultural disaster payments under Disaster Assistance Act of 1988 were not proceeds because farmer not required to sell or dispose of crop to qualify); *see also* In re Mintz, 192 B.R. at 319 (referring to *In re Ladd*); In re Cleary Bros. Constr. Co., Inc., 9 B.R. at 41 (applying similar rationale). Back To Text

[105] *See* In re Corpus Christi Hotel Partners, Ltd., 133 B.R. 850, 855 (Bankr. S.D. Tex. 1991) (holding that hotel revenues were not proceeds because there is no permanent disposition of property); *see also In re Allied Tex. Inv., No. 389−30056−SAF−11, 1989 WL 265432 at *2 (Bankr. N.D. Tex. Oct 16, 1989) (denying hotel rents as cash collateral); In re Cleary Bros. Constr. Inc., 9 B.R. at 41 (excluding rent from proceeds on ground that rent was derived from temporary use rather than permanent use or final conversion). Back To Text*

[106] In re Corpus Christi Hotel Partners, Ltd.,133 B.R. at 855 (finding hotel revenues not proceeds because property temporarily used by hotel guests); *see also* In re Cleary Bros. Constr. Co., Inc., 9 B.R. at 41 (finding temporary use of property excluded rent from being classified proceeds). *Back To Text*

[107] *See* In re S & J Holding Corp., 42 B.R. at 250 (noting that revenue generated from coin−operated video game machines was not proceeds because not received through sale or disposition of collateral game machines); *see also* Wolinsky v. Vermont Fed. Bank, FSB (In re Vermont Knitting Co.), 111 B.R. 464, 467−69 (Bankr. D. Vt. 1990) (applying similar rationale); In re Ladd, 106 B.R. at 176 (applying similar rationale). Back To Text

[108] In re S & J Holding Corp., 42 B.R. 249, 250 (Bankr. S.D. Fla. 1984); *see also* Great−West Life & Annuity Assurance Co. v. Parke Imperial Canton, Ltd., 177 B.R. 843, 851 (N.D. Ohio 1994) (finding post−petition hotel and banquet room revenues did not constitute proceeds of mortgaged hotel real estate because there had been no "conversion or transmutation" of collateral); General Elec. Credit Corp. v. Cleary Bros. Constr. Co., Inc. (In re Cleary Bros. Constr. Co. Inc.), 9 B.R. 40, 41 (Bankr. S.D. Fla. 1980) (holding that rental income from crane held collateral was not proceeds because crane was only temporarily used, not sold or permanently converted). Back To Text

[109] *See* Pigeon v. Production Credit Ass'n. of Minot (In re Pigeon), 49 B.R. 657, 660 (Bankr.D. N.D. 1985) (looking to broad definition of proceeds in legislative history and still finding post−petition milk product not to be proceeds subject to pre−petition lien); McLemore v. Mid−South Agri−Chemical Corp (In re Judkins), 41 B.R. 369, 372 (Bankr. M.D. Tenn. 1984) (finding that government payment−in−kind entitlements constituted proceeds for farmers because earned under contract right, where such payment−in−kind entitlements substitute for would−be harvest); Wapakoneta Production Credit v. Cupp (In re Cupp), 38 B.R. 953, 958 (Bankr. N.D. Ohio 1984) (holding that because USDA payment−in−kind program compensates farmers for crops not grown, such payments to farmer were proceeds). Back To Text

[110] H.R. Rep. No. 95−595, at 376−77 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5787, 6333. Back To Text

[111] *See* Apple v. Miami Valley Prod. Credit Ass'n, 614 F. Supp. 119, 124 (S.D. Ohio 1985) (finding *Cupp*'s reasoning and policy of liberal meaning of proceeds persuasive; hence, payment−in−kind entitlements fall within meaning of proceeds); Nolin Prod. Credit Ass'n v. Stone (In re Stone), 52 B.R. 305, 307 (Bankr. W.D. Ky. 1985) (holding that insurance and tort payments are within broad definition of proceeds); s*ee also* supra note 109 and accompanying text.

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[112] In re Pigeon, 49 B.R. at 660; *see also* In re Corpus Christi Hotel Partners, Ltd., 133 B.R. 850, 856 (Bankr. S.D. Tex. 1991) (observing that "the definition should not be so broad as to swallow the general rule"); United States v. Friend (In re A.E.I. Corp.), 11 B.R. 97, 101 (Bankr. E.D. Pa. 1981) (holding that absent security interest in lease, proceeds referred to permanent or final transformation of collateral); In re Cleary Bros. Constr. Co. Inc., 9 B.R. at 41 (stating same). Back To Text

[113] *See* Local Loan Co. v. Hunt, 292 U.S. 234, 243 (1934) (raising notion that under certain circumstances post−petition revenues might not be subject to pre−petition security interests); *see also* supra notes 69−83 and accompanying text (discussing *Local Loan* and subsequent application to post−petition hotel revenues). *See e.g., In re Angobaldo, 160 B.R. 140, 141 (Bankr. N.D. Cal. 1993) (finding debtor was "major force" in generating post−petition earnings). Back To Text*

[114] *See* Investment Hotel Properties, Ltd. v. New W. Fed. Sav. & Loan Ass'n (In re Investment Hotel Properties, Ltd.), 109 B.R. 990, 995 (Bankr. D. Colo. 1990) (concluding hotel revenues were accounts receivable and consequently proceeds; but security interest in post−petition accounts was not valid under § 552(a)); *see also* supra notes 82−94 and accompanying text (discussing expansion by courts of *Local Loan*'s emphasis of debtor receiving fresh−start). Back To Text

[115] *See* supra notes 95−108 and accompanying text (explaining origin of third test and its general treatment by courts); *see also* 5 COLLIER ON BANKRUPTCY ¶ 552.02, at 552−58 (Lawrence P. King et al. eds., 15th ed. rev. 1997) (indicating some courts use Uniform Commercial Code to differentiate between proceeds and after−acquired property). Back To Text

[116] *See* supra notes 109−113 and accompanying text (reviewing possibilities of interpretation from legislative history of § 552 for term, "proceeds"). Back To Text

[117] Local Loan, 292 U.S. at 243; *see also* Great−West Life & Annuity Assurance Co. v. Parke Imperial Canton, Ltd., 177 B.R. 843, 850−51 (N.D. Ohio 1994) (declining to include monies generated from hotel and banquet room rental, food, beverage and telecommunications sales, house gratuities or gaming as "proceeds, rents or profits," not because security agreement prevented such interpretation, but because § 552 precludes it). *But see* Mid−City Hotel Assocs. v. Prudential Ins. Co. (In re Mid−City Hotel Assocs.), 114 B.R. 634, 642−643 (Bankr. D. Minn. 1990) (determining that legal definitions of "revenue," parties' intentions and common sense all support conclusion that hotel room rates constitute "profits," however sales generated from hotel restaurant and bar may not constitute "profits" because no property interest is thereby assigned). Back To Text

[118] Financial Sec. Assurance v. Days Cal. Riverside Ltd. Partnership (In re Days Cal. Riverside Ltd. Partnership), 27 F.3d 374, 377 (9th Cir. 1994) (noting easy separation in hotel accounting among charges associated with room occupancy, which are "rent," and service charges, which are not); *see also* Great−West Life & Annuity Assurance Co., 177 B.R. at 848, 850−51 (illustrating calculable percentages from various hotel revenue sources, some of which would constitute "rent" or "profits"; delineating hotel room rentals and other, related services such as telephone revenue and food and beverage sales); Airport Inn Assocs. v. Travelers Ins. Co. (In re Airport Inn Assocs.), 132 B.R. 951, 953 (Bankr. D. Colo. 1990) (noting that hotel revenue was derived from many different sources, and that room price included various services and standard hotel amenities). Back To Text

[119] *See* Smoker v. Hill & Assocs., 204 B.R. 966, 974 (Bankr. N.D. Ind. 1997) (stating that Congress clearly intended to incorporate *Local Loan*'s fresh start policy in § 552). "Any analysis of the 'fresh start' provisions of the Bankruptcy Code is *incomplete without reference to the Supreme Court case* [*Local Loan*] which firmly established the fresh start concept in modern American bankruptcy jurisprudence." *In re* Rumker, 184 B.R. 621, 628 (Bankr. S.D. Ga. 1995) (emphasis added); *see also* supra notes 82−94 and accompanying text (discussing expansion by courts of *Local Loan*'s emphasis on debtor receiving fresh−start to corporations). Back To Text

[120] *See* supra Section II (focusing on numerous factors entailed in hospital revenue). Back To Text

[121] *See* United States v. Emerald of Puerto Rico, Inc. (*In re* Hospital Nuestra Señora de Guadalupe, Inc.), 20 B.R. 1021, 1023 (Bankr. D.P.R. 1982) (recognizing importance of accounts receivable to hospital's cash flow and post−petition viability); *see also* Foster & Kohn, *supra* note 41, at 1−37 (noting that since 1983 hospitals have been reimbursed by government under prospective payment system); supra Section II. (explaining market structure of healthcare industry and impact of (1) managed care organizations and (2) both private and governmental insurers on hospital receivables). Back To Text

[122] 2U.C.C. § 9−306(1) (1994); *see also* General Elec. Capitol Corp. v. Deere Credit Servs., Inc., 799 F. Supp. 832, 836 (S.D. Ohio 1992) (defining proceeds under U.C.C. § 9−306 as "*whatever* is received upon the sale, exchange, collection or other disposition of *collateral* or *proceeds*") (emphasis in original); Drewes v. Lesmeister (In re Lesmeister), 242 B.R. 920, 924 (Bankr. D.N.D. 1999) (noting that proceeds result, under U.C.C. § 9−306, from disposition of collateral); In re Allegheny Imaging Inst., 69 B.R. 932, 937 (Bankr. W.D. Pa. 1987) (stating same). Back To Text

[123] *See* In re Corpus Christi Hotel Partners, Ltd., 133 B.R. 850, 855 (Bankr. S.D. Tex. 1991) (defining proceeds narrowly so as to protect hotel for debtor under § 552(a)); *In re* Big Hook Land & Cattle Co., 81 B.R. 1001, 1003 (Bankr. D. Mont. 1988) (construing proceeds narrowly so as to give debtor protection under § 552(a)); First Nat'l Bank of Lafayette v. Texas Tri−Collar, Inc. (*In re* Texas Tri−Collar, Inc.), 29 B.R. 724, 727 (Bankr. W.D. La. 1983) (concluding that accounts receivable generated post−petition are not proceeds within meaning of § 552(b)). Back To Text

[124] *See* In re Mintz, 192 B.R. 313, 318−20 (Bankr. D. Mass. 1996) (excluding partnership distributions from definition of proceeds in order to corral application of § 552(b)); Covey v. Ipava State Bank (In re Ladd), 106 B.R. 174, 176−77 (Bankr. C.D. Ill. 1989) (declining to give effect to security statement which covered products of collateral); In re S & J Holding Corp., 42 B.R. 249, 250 (Bankr. S.D. Fla. 1984) (excepting proceeds derived from use of collateral from effects of § 522(b)). Back To Text

[125] *See* supra Section II (describing general background of healthcare industry); supra note 121 (stating same). Back To Text

[126] *See* New Hampshire Bus. Dev. Corp. v. Cross Baking Co. (In re Cross Baking Co.), 818 F.2d 1027, 1033 (1st Cir. 1987) (suggesting that § 552(b) limited to situations where proceeds arise from changed pre−petition collateral); Pigeon v. Production Credit Ass'n of Minot (In re Pigeon), 49 B.R. 657, 660 (Bankr. D.N.D. 1985) (concluding that security interest did not attach to milk produced post−petition because identity of collateral not sufficiently changed); In re Lawrence, 41 B.R. 36, 37 (Bankr. D. Minn. 1984) (asserting that § 552(b)'s exception meant *only* to apply to security interests in raw materials later transformed into inventory). Back To Text

[127] *See* 11 U.S.C. § 552(b)(2) (1994) (adding hotel room revenues to definition of rents in § 552(b)); *see also* Financial Sec. Assurance, Inc. v. Tollman−Hundley Dalton, L.P., 74 F.3d 1120, 1124−5 (11th Cir. 1996) (noting Congressional intent to clarify law regarding hotel revenues); American President Lines, Ltd. v. Lykes Bros. Steamship Co. (In re Lykes Bros. Steamship Co.), 216 B.R. 856, 864 (M.D. Fla. 1996) (stating that 1994 amendments to § 552(b) were specifically implemented to protect hotel revenues which had been pledged as security); TE−Two Real Estate Ltd. Partnership v. Creekstone Apartments Assocs., L.P. (*In re* Creekstone Apartments Assocs.), 1995 U.S. Dist. LEXIS 14876, at * 46 n.12 (M.D. Tenn. September 18, 1995) (recognizing that § 552(b)(2) protects after acquired security interests in rents). Back To Text

[128] *See* In re Northview, 130 B.R. 543, 548 (B.A.P. 9th Cir. 1991) (holding that hotel revenues are not proceeds because they are not encumbered pre−petition property converted into other property post−petition); In re Majestic Motel Assocs., 131 B.R. 523, 525−26 (Bankr. D. Me. 1991) (holding that money generated by hotel business not proceeds of real property); In re Ashoka Enterp., Inc., 125 B.R. 845, 846 (Bankr. S.D. Fla. 1990) (stating same); In re M. Vickers, Ltd., 111 B.R. 332, 336 (Bankr. D. Colo. 1990) (concluding that accounts receivable are not rents or profits because hotel profits are: (1) business revenue, and (2) not produced solely by property); Kearney Hotel Partners v. Richardson (In re Kearney Hotel Partners), 92 B.R. 95, 103 (Bankr. S.D.N.Y. 1988) (stating same); Victor Savings & Loan Assoc. v. Grimm (In re Greater Atl. and Pac. Inv. Group, Inc.), 88 B.R. 356, 359 (Bankr. N.D. Okla.

1988) (stating same); *cf.* In re Bellevue Place Assocs., 173 B.R. 1009, 1021 (Bankr. N.D. Ill. 1994) (splitting service and rent, but still deciding both fall within rent and profit language of Illinois version of § 552(b)). Back To Text

[129] *See* Financial Sec. Assurance v. Days Cal. Riverside Ltd. Partnership (In re Days Cal. Riverside Ltd. Partnership), 27 F.3d 374, 377 (9th Cir. 1994) (differentiating between hotel service revenues, which are accounts, and hotel room rental revenues, which are proceeds or rents of real property); *see also* Chequers Inv. Assocs. v. Hotel Sierra Vista Ltd. Partnership (In re Hotel Sierra Vista Ltd. Partnership), 112 F.3d 429, 432 (9th Cir. 1997) (noting that § 552(b) was revised in 1994 to make clear that hotel room revenues were rent). *But see* In re Financial Sec. Assurance, 74 F.3d at 1122 (concluding that hotel revenues subject to pre−petition lien are not property of debtor's estate). Back To Text

[130] *See* In re Financial Sec. Assurance, 74 F.3d at 1122 (holding that hotel revenues not part of debtor's estate are subject to pre−petition security interests); In re Days Cal. Riverside, Ltd .Partnership, 27 F.3d at 377 (noting that post−petition service income is not attachable under § 552(b)). *But see* In re Hotel Sierra Vist, Ltd. Partnership, 112 F.2d at 432 (stating that 1994 amendments to § 552(b) subject hotel room revenues to prepetiton liens). Back To Text

[131] In re Days Cal. Riverside, Ltd. Partnership, 27 F.3d at 377; *see also* Philip Morris Capital Corp. v. Bering Trader, Inc. (In re Bering Trader), 944 F.2d 500, 502 (9th Cir. 1991) (noting that inclusion of broad term "accounts" in § 522(b) would not be compatible with narrow exceptions specifically listed); In re Shore Haven Motor Inn, Inc., 124 B.R. 617, 618 (Bankr. S.D. Fla. 1991) (holding that hotel revenues are not rent). Back To Text

[132] *See* In re West Chestnut Realty of Haverford, Inc., 166 B.R. 53, 55 (Bankr. E.D. Pa. 1993) (holding that post−petition tipping fees for landfills are not proceeds of land); *see also* In re Majestic Motel Assocs., 131 B.R. at 525−26 (holding money generated by hotel business not proceeds of real property); *Cf.* In re Brandywine River Hotel, Inc., 177 B.R. 10, 15 (Bankr. E.D. Pa. 1995) (suggesting that for security interest to exist in proceeds, assignment must track § 552(b)'s language); Kathryn R. Heidt, The Effect of the 1994 Amendments on Commercial Secured Creditors, 69 Am. Bankr. L.J. 395, 414 (1995) (agreeing with *Brandywine* court's counsel that assignment must track language of § 552(b) for post−petition interest to attach). Back To Text

[133] *See* U & I Sanitation v. City of Columbus, No. 98−1893, 2000 U.S. App. LEXIS 2513, at *2 (8th Cir. Feb. 22, 2000) (describing tipping fee as price charged to haulers for dumping at city owned site); In re Sullivan County Reg'l Refuse Disposal Dist., 165 B.R. 60, 66 n.10 (Bankr. D.N.H. 1994) ("[A] 'tipping fee' is the per ton charge to a party, whether municipal or private, who is delivering solid waste to the incinerator for disposal"); *see also* R.T. Opdenaker & Sons, Inc. v. County of Delaware, Pa. (*In re* R.T. Opdenaker & Sons, Inc.), Nos. 96−13857DAS, 96−0569DAS, No. 96−13856DAS, 96−0570DAS, 1996 Bankr. LEXIS 660, at *2−3 (Bankr. D. Pa. June 11, 1996) (noting probable unconstitutionality of tipping fees designed to act as "flow control ordinances"). Back To Text

[134] *See* In re West Chestnut Realty of Haverford, Inc., 166 B.R. at 54 (asserting post−petition tipping fees are subject to liens). *See generally* In re Financial Sec. Assurance, 74 F.3d at 1122 (holding that hotel revenues not part of debtor's estate subject to pre−petition security interests); In re Days Cal. Riverside, Ltd. Partnership, 27 F.3d at 377 (noting that post−petition service income is not attachable under § 552(b)). Back To Text

[135] *See* In re West Chestnut Realty of Haverford, Inc., 166 B.R. at 54. *Back To Text*

[136] *See* id. at 57. Back To Text

[137] 146 B.R. 453 (Bankr. D. Ariz. 1992). Back To Text

[138] Id. at 456; *see also* Zeeway Corp. v. Rio Salado Bank (In re Zeeway Corp.), 71 B.R. 210, 212 (B.A.P. 9th Cir. 1987) (holding that income generated from post−petition auto races are not included within proceeds, products or rents as it is not derived from rental of real property but from business activities conducted thereon); In re GGVXX, LTD., 130 B.R. 322, 326 (Bankr. D. Colo. 1991) (reasoning that greens fees, club cart rentals, and range ball sales are best characterized as business receipts or personal property, not rental payments). Back To Text

[139] *See* In re Everett Home Town Ltd. Partnership, 146 B.R. at 456; General Elec. Credit Corp. v. Cleary Bros. Constr. Co. (In re Cleary Bros. Constr. Co.), 9 B.R. 40, 41 (Bankr. S.D. Fla. 1980); *see also* In re McKim, 217 B.R. 97, 98 (Bankr. D.R.I. 1998) (holding that membership fees are not cash collateral when they allow for unlimited golf and use of facilities). Back To Text