APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

No. 19-1161

MONTREAL MAINE & ATLANTIC RAILWAY, LTD.,
Debtor.

ROBERT JAMES KEACH, Estate Representative of Post-Effective Date Estate of Montreal, Maine, and Atlantic Railway, Ltd.,
Appellant,

v.

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

Appeal from the United States Bankruptcy Court
for the District of Maine
Hon. Peter G. Cary, U.S. Bankruptcy Judge

Filed March 10, 2020

Before: Torruella, Thompson, and Barron, Circuit Judges.

* * *

OPINION

BARRON, Circuit Judge:

This case arises out of the 2013 petition for bankruptcy that the Montreal Maine & Atlantic Railway, Ltd. ("MMA") filed in the United States Bankruptcy Court for the District of Maine. The dispute concerns whether priority status should be given to certain claims that creditor railroads filed with the Bankruptcy Court. The creditor railroads in these claims sought to recover their share of the payments that the MMA was to collect for charges that had been billed to customers that had shipped freight on routes that spanned rail systems that were owned at the time by, respectively, the MMA and the creditor railroads.

The creditor railroads argued that, because the MMA incurred the debt for their share of these payments so close in time to the MMA's bankruptcy, their claims qualified as what are known as "Six Months Rule" claims under 11 U.S.C. § 1171(b) of the Bankruptcy Code and so must be paid in full before other claims. *See generally Czyzewski v. Jevic Holding Corp.*, 137 S. Ct. 973, 979 (2017) (explaining bankruptcy priority rules). The Bankruptcy Court and the Bankruptcy Appellate Panel ("BAP") agreed. We now affirm.

I.

The debtor in bankruptcy is the MMA. For more than a decade, the MMA owned and operated a rail system that stretched throughout northern New England and into the Canadian provinces of Québec and New Brunswick.

The creditor railroads are the New Brunswick Southern Railway Company Limited and the Maine Northern Railway Company (collectively, "the Irving Railroads"). While the MMA's rail system was operating in New England and Canada, the Irving Railroads

owned and operated their own rail systems, which operated in Maine and New Brunswick and were able to connect with the MMA's.

The Irving Railroads and the MMA each used their own locomotives and tracks to haul freight along routes that spanned these interconnected rail systems. As a result, the MMA and the Irving Railroads needed a means to coordinate the payments that they each would be owed for the charges that customers would be billed for shipping freight via these rail systems.

The MMA is a participant in the Interline Settlement System ("ISS"). The ISS is a centralized clearinghouse that many railroads across the country use to process payments for the charges that are made to customers that ship freight between interconnected rail systems. These payments are often referred to as interline payments.

Under the ISS, the railroad that owns the rail system on which the freight traffic originates bills the entire freight charge to the customer that ships the freight. The billing railroad does so even though that charge is based in part on the fact that the freight has traversed for some part of its journey a rail system that the billing railroad does not own. To account for this fact, the ISS provides that the billing railroad will, within a certain period of time, pay the appropriate share of the payment for that freight charge to each railroad that owns one of the interconnected rail systems through which the freight traveled.

The problem that the Irving Railroads and the MMA encountered was that, unlike the MMA, the Irving Railroads did not participate in the ISS. That was so in large part because of the resources and expertise that the Irving Railroads would have needed to partici-

pate in the ISS and in part because the Irving Railroads did not want to duplicate the efforts of the MMA and other connecting railroads that were ISS participants. Thus, the MMA and the Irving Railroads needed to devise a payment processing system of their own.

The parties' solution to this problem took the form of an agreement that they entered into with each other in 2003. The parties refer to this agreement, which took advantage of the MMA's role as an ISS participant, as a "swap" arrangement.

The agreement accounted for different scenarios. The first scenario concerned the situation in which a customer's freight originated on the rail system of the MMA or of the Irving Railroads and then interchanged with the other rail system. In that situation, the agreement provided that the MMA would bill the customer directly for the full charge for shipping that freight, even though the charge to that customer was based, in part, on the freight traveling via rail systems that the MMA did not own and operate but that were interconnected with the MMA's rail system. The second scenario concerned the situation in which the freight originated with the rail system of another ISS-participating railroad—and thus originated on neither the MMA's nor the Irving Railroads' rail systems—but subsequently passed through the MMA's and the Irving Railroads' rail systems. In that event, under the agreement, the MMA would collect from the billing railroad its share of the payment for the charge that the customer had been billed by the railroad that owned the originating rail system. In addition, per the agreement, the MMA would collect from the billing railroad the share of the payment for the charge to the customer shipping the freight that represented the share of that payment due to the Irving Railroads for

the freight having been shipped, in part, via their rail systems.

As to each of these scenarios, the agreement specified how the Irving Railroads would receive from the MMA their share of the payment for the charge to the customer for shipping the freight that the MMA would collect. The agreement provided that, within a discrete number of days of the Irving Railroads' handling of freight traffic for which the MMA was responsible for collecting payments either directly from the customer that had shipped the freight or from the billing railroad, the MMA would transfer to the Irving Railroads their share of those payments. Specifically, the agreement stated that the Irving Railroads would submit an invoice every Wednesday "for the seven days ending with the second preceding Friday," and that the MMA should pay the Irving Railroads "within 21 days from receipt of the invoice." The railroads referred to this as a 33-day deadline for the MMA making the payment, apparently because that was how long the MMA would have, under these terms, to pay the Irving Railroads their share of the payment charged to a customer who shipped freight with the Irving Railroads' rail systems from the time that such customer made such a shipment.

The agreement addressed one other circumstance that bears on the issues that we confront here. This circumstance arose from the fact that the Irving Railroads' affiliates were among the customers that would ship freight through the MMA's rail system. These affiliates are several paper companies in the region: Irving Pulp and Paper, Limited; Irving Paper Limited; and J.D. Irving, Limited; or, collectively, "the Irving Paper Companies."

The agreement provided that the Irving Paper Companies would transfer the payments that they owed to the MMA for their use of its rail system at the same time as the MMA transferred to the Irving Railroads their share of the payments that the MMA was to receive directly from other customers, or from the billing railroad through the ISS, for customers having shipped freight through the Irving Railroads' rail systems. In this way, the agreement permitted the Irving Paper Companies to withhold payment to the MMA if the MMA failed to transfer to the Irving Railroads their share of the payments charged to customers for having shipped freight via their rail systems.

In practice, the payments that the Irving Paper Companies owed the MMA usually dwarfed the share of the payments that the MMA owed to the Irving Railroads for customers' use of their rail systems. The arrangement thus provided some assurance to the Irving Railroads that they would be paid their share of the payment for the charge to the shipping customer that the MMA was responsible for collecting, given what the MMA stood to lose from not transferring to the Irving Railroads what they were owed for freight having traveled by means of their rail systems.

The agreement that the parties hammered out appeared to serve them well until sometime in 2012. At that point, however, the MMA and the Irving Railroads began hauling a significant volume of crude oil to refineries in St. John, New Brunswick, across their interconnected rail systems.

Importantly, the jump in the volume of crude meant that, in the course of the parties' regular swap of payments, the amount of funds that the MMA owed to the Irving Railroads typically would exceed the amount

of funds that the Irving Paper Companies owed to the MMA. But, this new development also created the following practical problem.

Payments for the charges to customers for making these oil shipments were processed through the ISS. It would typically take 45 to 60 days after the MMA handled the railcars for a given shipment of freight for the MMA to receive the ISS payments that it was owed for charges to customers that were billed, pursuant to the ISS, by the railroad on which the oil shipment originated. That period of time exceeded the amount of time that it would typically take for the MMA to receive, pursuant to the agreement, payment for charges for which it directly billed customers.

Thus, in practice, the MMA usually received payments that included the Irving Railroads' share of the payment for the charge to a customer for an oil shipment about 45 to 60 days after the Irving Railroads handled the shipment. The result was that the MMA had trouble ensuring that the Irving Railroads received their share of the payment for the charge to the customer for that oil shipment within the 33-day period that the swap arrangement had specified.

To account for this new difficulty occasioned by the oil shipments to St. John, the parties, in July of 2012, modified the swap arrangement. The new agreement carved out from the old one any payments that were attributable to freight traffic originating on a railroad other than the MMA or the Irving Railroads—in other words, payments contemplated by the second scenario addressed in the swap arrangement. Thus, the new agreement necessarily carved out from the old one those payments that were owed to the Irving Railroads in consequence of charges to customers for oil ship-

ments going to St. John, as none of those shipments originated on the rail systems of either the MMA or the Irving Railroads.

Under the new agreement, moreover, the Irving Railroads authorized the MMA to pay them their share of any carved-out payments that the MMA collected up to five days after the MMA had done so. The new agreement otherwise left the old one in place, save for one additional modification that the parties made to it. Under the new agreement, payments for charges to customers for freight shipments that originated on the rail systems of the Irving Railroads or the MMA, which were contemplated in the first scenario addressed by the swap arrangement, would be paid in accord with the terms of the original swap arrangement, except that the MMA would be required to pay the Irving Railroads their share of the charge to a customer for any such freight shipment that the MMA was to collect within 30 days of handling the freight.

The modified version of the agreement remained in place through July of 2013. At that time, though, there was yet another new development, and it is that new development that most directly led to the dispute that is now before us.

In that month, an MMA train hauling 72 cars filled with crude oil derailed in Lac-Mégantic, Québec. The derailment led to several explosions, killed 47 people, caused severe property damage, and required a major environmental response effort.

In consequence, the MMA became insolvent and petitioned the United States Bankruptcy Court for the District of Maine for Chapter 11 bankruptcy on August 7, 2013. Soon thereafter, the Irving Railroads filed the

claims with the Bankruptcy Court that are now before us.

The claims seek to recover payments that the Irving Railroads contend are owed to them by the MMA for "[f]reight services provided to the Debtor in connection with interline rail shipments." The claims, in other words, seek payments that represent what the Irving Railroads assert is their share of the payments for the freight charges to customers that the MMA was responsible for collecting but that the MMA had yet to pass on to the Irving Railroads. In this respect, the claims seek recovery not only of the Irving Railroads' share of payments that the MMA was responsible for collecting that were tied to charges to customers for their oil shipments to St. John but also the Irving Railroads' share of payments that the MMA was responsible for collecting that were tied to charges to other customers for having shipped other types of freight via, in part, the Irving Railroads' rail systems.

The Irving Railroads asserted that the claims for the payments at issue were entitled to priority under 11 U.S.C. § 1171(b) as "Six Months Rule" claims. The trustee of the bankruptcy estate, Robert J. Keach,[1] objected. He argued that the claims should be treated as general, unsecured claims and thus should not be given priority under § 1171(b) as Six Months Rule claims.

The Bankruptcy Court agreed with the Irving Railroads and held that the claims were entitled to priority pursuant to § 1171(b) because they were Six Months Rule claims. Keach appealed to the BAP,

[1] Per the liquidation plan approved by the U.S. District Court for the District of Maine, Keach is no longer the trustee, and is instead the "estate representative of the post-effective date estate."

which affirmed. He then moved for reconsideration of the issue in front of the Bankruptcy Court, which denied the motion and again held that the claims at issue here were priority claims under § 1171(b).

At that juncture, the parties jointly requested permission from this Court to appeal both orders of the Bankruptcy Court directly. *See* 28 U.S.C. § 158(d)(2)(A). We allowed the appeal, which is now before us.

II.

We ordinarily do not defer to the district court or to the BAP in reviewing a bankruptcy court's decision. *See In re Vázquez Laboy*, 647 F.3d 367, 373 (1st Cir. 2011). Thus, "[o]ur review of the bankruptcy court's decision is de novo, though we will only upset the court's factual determinations in the case of clear error." *Id.*

III.

This appeal turns, at least initially, on the proper interpretation of a nearly 40-year-old precedent from this Circuit. It thus presents a pure question of law, which we review de novo.

The precedent in question holds, the parties agree, that the Bankruptcy Code at the time of that decision impliedly incorporated what is known as the Six Months Rule via one of its provisions. The parties further agree that, by virtue of that precedent, claims by creditors that qualify as Six Months Rule claims were entitled to priority status under the Bankruptcy Code at that time even if those claims otherwise would not have been entitled to such status.

The precedent in question is *In re Boston & Maine Corp.* (*Boston & Maine II*), 634 F.2d 1359 (1st Cir. 1980). It addressed when certain claims by creditors against a debtor railroad were entitled to priority status under a provision of the Bankruptcy Code, 11 U.S.C. § 205(b) (1976), that is no longer operative. *Id.* at 1366.

That provision of the Bankruptcy Code, however, was a precursor to the one that is our concern in this appeal: § 1171(b). By the time that *Boston & Maine II* was decided, moreover, § 1171(b) had been enacted. And, notably, *Boston & Maine II* expressly recognized that § 1171(b) was "the same in substance" as § 205(b). 634 F.2d at 1366 n.15; *see also id.* at 1379 n.35 ("The provision enacted as 11 U.S.C. [§] 1171(b) … substantially continues the language of [§ 205(b)].").

Thus, the parties proceed in this case on the understanding that *Boston & Maine II*'s analysis of § 205(b) applies equally to § 1171(b), such that, if *Boston & Maine II*'s analysis of § 205(b) would be controlling if § 205(b) were still operative, then that same analysis applies to § 1171(b). We proceed on that same understanding in analyzing *Boston & Maine II* and its significance to this appeal.

In construing § 205(b), *Boston & Maine II* explained that the Six Months Rule was the name for the more-than-century-old practice of courts in reorganization proceedings granting priority status to certain kinds of claims that creditors brought against railroads in receivership but that otherwise would not have been entitled to such privileged status. *See* 634 F.2d at 1366. *Boston & Maine II* then held that § 205(b) was best construed to have, albeit impliedly, incorporated the Six Months Rule. *Id.* *Boston & Maine II* thus held

that a creditor's claim against a railroad in bankruptcy that otherwise would not qualify for priority status under the Bankruptcy Code would so qualify, per § 205(b), if the Six Months Rule encompassed it. *See id.*

Boston & Maine II explained that, just as the name for the Six Months Rule suggests, and in accord with the past practice on which the rule is based, there was a temporal limitation on how old a debt could be in order for a claim to recover payment for it to be given priority pursuant to § 205(b) as a Six Months Rule claim. *See id.* at 1379. This temporal limitation ensured that priority status for claims encompassed by the Six Months Rule would "extend[] backward to the period preceding reorganization" only "to the extent necessary to assure that there is continuity in the payment of indispensable operating expenses … so long as the current expenses of the pre-reorganization period … are not so dated as to forbid the conclusion that they are in fact current." *Id.* *Boston & Maine II* explained, however, that, despite the Six Months Rule's name, "six months is not an inflexible time limit" for a claim to qualify as a Six Months Rule claim. *Id.* Thus, some claims to recover payments for debts of an older vintage might qualify, too. *Id.*

For present purposes, there is no dispute between the parties that the claims for which the Irving Railroads seek priority status as Six Months Rule claims under § 1171(b) fall within the *temporal* scope of the Six Months Rule. There is a threshold dispute, though, over whether *Boston & Maine II* properly defined the *substantive* scope of the Six Months Rule that, in light of longstanding practice, it had held that § 205(b) impliedly incorporated. Thus, our analysis begins with that dispute.

The dispute arises because Keach contends that *Boston & Maine II* misconstrued the Six Months Rule in a manner that makes it far broader than it is. He then contends that we must depart from *Boston & Maine II*'s holding on that score and that, once we do, we must reverse the Bankruptcy Court's ruling, because the claims at issue here cannot in that event qualify as Six Months Rule claims.

As we will explain, we reject Keach's contention that, because *Boston & Maine II* (in his view) erroneously defined the substantive scope of the Six Months Rule, we are not bound by *Boston & Maine II*'s construction of it. We also reject Keach's argument that, even pursuant to the test set forth in *Boston & Maine II*, the type of claims that the Irving Railroads seek to recover are categorically ineligible for Six Months Rule priority. However, even though we reject Keach's more wide-reaching challenges to the Bankruptcy Court's priority finding, our work is by no means done. Instead, we also must address Keach's various case-specific fallback challenges, in which he argues, respectively, (1) that the Bankruptcy Court erred in describing the test that *Boston & Maine II* set forth for determining whether a claim qualifies as a Six Months Rule claim and (2) that, even if the Bankruptcy Court did not so err, it nonetheless erred because the record fails to support its findings that the claims at issue qualified as Six Months Rule claims under that same test. But, before we explain why those case-specific fallback arguments fail to persuade, first things first.

A.

Keach's threshold challenge to *Boston & Maine II*'s construction of the substantive scope of the Six Months Rule zeroes in on the fact that *Boston & Maine II* held

that the Six Months Rule reflects "two essentially different principles, neither of which limits the operation of the other." 634 F.2d at 1377. Keach argues that, properly understood, the Six Months Rule in fact reflects only the first of the two principles that *Boston & Maine II* described that rule as reflecting. Thus, Keach contends, even if § 1171(b) does encompass the Six Months Rule, that provision may not be properly construed to encompass the expansive version of it that *Boston & Maine II* describes.

This contention is critical to Keach's argument. The parties agree that the claims at issue here qualify as Six Months Rule claims—insofar as they do—only under the second of the two independent principles that *Boston & Maine II* described the Six Months Rule as reflecting. Thus, if Keach is right that *Boston & Maine II* was wrong to construe the Six Months Rule to reflect that second principle, then he is right that the claims at issue here cannot qualify as Six Months Rule claims.[2]

As we will explain, however, we reject Keach's contention that we are not bound by *Boston & Maine II*'s holding that the Six Months Rule reflects that second principle, given our duty to adhere to our prior prece-

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[2] The Irving Railroads contend that this argument has been waived. But, while Keach did repeatedly concede to the Bankruptcy Court and the BAP that there was no diversion requirement under the Six Months Rule, any argument to the contrary would have been hopeless given the precedent we describe. Thus, because there would have been no reason for Keach to argue this point in front of the lower courts, we decline to treat his argument as waived. *See Bennett v. City of Holyoke*, 362 F.3d 1, 7 (1st Cir. 2004) ("[W]e will excuse a party for failing to raise a defense … when the defense, if timely asserted, would have been futile under binding precedent.").

dent under the law-of-the-circuit doctrine. *See United States v. Holloway*, 630 F.3d 252, 258 (1st Cir. 2011). To explain why we reach that conclusion, we begin by describing what *Boston & Maine II* held with respect to each of the two principles. We then consider Keach's arguments for why we should not follow *Boston & Maine's II*'s holding that the Six Months Rule reflects the second of those two principles.

1.

Boston & Maine II traced the first principle that it held that the Six Months Rule reflected to the late nineteenth century United States Supreme Court precedent of *Fosdick v. Schall*, 99 U.S. 235, 253 (1878). *Boston & Maine II* read that precedent to support the conclusion that, in general, a debtor railroad in bankruptcy "must restore to operating creditors revenues [that were] diverted" from a current expense fund to pay off the railroad's mortgagees before the railroad entered into bankruptcy. 634 F.2d at 1377 (citing *Fosdick*, 99 U.S. at 253).

Boston & Maine II did not describe the precise scope of this *Fosdick*-based diversion requirement. But, *Boston & Maine II* did clearly hold that claims by creditors that satisfy the requirement that the debtor railroad had engaged in a diversion of revenues from a current expense fund to mortgagees may qualify for priority status in some circumstances, per the long-recognized Six Months Rule. Specifically, *Boston & Maine II* made clear that such claims could so qualify so long as those claims were also for the recovery of debts that the debtor railroad incurred within the relevant six-months window prior to its entering bankruptcy and so long as the debtor railroad had been expected

to pay those debts out of current operating expenses. *See id*. at 1368-69, 1380, 1382.

Because the parties agree that no such diversion of funds occurred here, Keach understandably has little to say about what *Boston & Maine II* held with regard to this first principle. Instead, he trains his focus on what *Boston & Maine II* had to say about the second principle that it held that the Six Months Rule reflected. After all, it is because *Boston & Maine II* held that the Six Months Rule also reflected that second principle, and thus not only the *Fosdick*-based principle, that the Bankruptcy Court held that the claims at issue here qualified as Six Months Rule claims under *Boston & Maine II* even though they cannot satisfy the *Fosdick*-based diversion requirement.

Boston & Maine II traced this second principle to a different late nineteenth century United States Supreme Court case from *Fosdick*. That case was *Miltenberger v. Logansport, C. & S.W.R. Co.*, 106 U.S. 286 (1882).

Boston & Maine II read *Miltenberger*, along with other precedents that aligned with its reasoning, to elaborate on the Six Months Rule in a manner that accounted for the fact "that a 'railroad is authorized to be constructed more for the public good to be subserved, than for private gain.'" *Boston & Maine II*, 634 F.2d at 1377 (quoting *Barton v. Barbour*, 104 U.S. 126, 135 (1881)). *Boston & Maine II* further construed the Six Months Rule, based on its reading of the *Miltenberger*-based line of precedent, to encompass claims for payment of debts incurred by the debtor railroad if, when those debts were incurred, "a stoppage of the continuance of such business relations would be a probable re-

sult … of nonpayment." *Id.* (quoting *Miltenberger*, 106 U.S. at 312).

Thus, based on this reading of the import of the *Miltenberger*-based line of authority, *Boston & Maine II* held that creditors need not show a diversion by the debtor railroad of operating revenues from operating expenses to pay a mortgagee to show, as the *Fosdick* principle otherwise would require, that their claims merited Six Months Rule priority under the Bankruptcy Code. *See id.* at 1380. Rather, *Boston & Maine II* explained that, per its understanding of the logic of the *Miltenberger* line of precedent, claims to recover payments from debtor railroads for services that resulted in the debtor railroad incurring certain critical expenses also could qualify as Six Months Rule claims, despite the absence of any showing by a creditor that would satisfy the *Fosdick*-based diversion requirement. *Id.* at 1382.

To be sure, consistent with Keach's contention about the proper construction of the Six Months Rule, other courts had at the time of *Boston & Maine II* read *Miltenberger* differently from how *Boston & Maine II* read it. These courts treated *Miltenberger* as addressing a different rule applicable to railroad receiverships than the Six Months Rule, the "Necessity of Payment Rule," and thus not to be addressing the Six Months Rule at all. *See, e.g.*, *In re N.Y., New Haven & Hartford R.R. Co.*, 278 F. Supp. 592, 602 n.15 (D. Conn. 1967), *aff'd*, 405 F.2d 50 (2d Cir. 1968) (critiquing courts that read *Miltenberger* as a Six Months Rule case for having "inexplicably merged the two rules by making necessity of payment a requirement of the six months rule and eliminating diversion as a requirement for" the Six Months Rule).

Boston & Maine II itself recognized the difference between the Six Months Rule and the Necessity of Payment Rule. It explained that the Necessity of Payment Rule "does not confer rights on claimants" like the Six Months Rule. 634 F.2d at 1382. Instead, the Necessity of Payment Rule "reflects the existence of a judicial power to authorize trustees in reorganization to pay claims where such payment is exacted as the price of providing goods or services indispensably necessary to continuing the rail service" even though these trustees did not receive court approval to pay such expenses ex ante. *Id.*

But, *Boston & Maine II* observed that *Miltenberger* used "ambigu[ous] … language" in characterizing the nature of the rule that *Miltenberger* was setting forth with respect to whether it concerned the Six Months Rule or only the Necessity of Payment Rule. *Id.* at 1378. And, further, *Boston & Maine II* rejected an interpretation of *Miltenberger* that read it, or the subsequent Supreme Court precedent applying it, to be solely addressing the scope of the Necessity of Payment Rule. *Id.* Instead, *Boston & Maine II* held both that the Necessity of Payment Rule was a "distinct … principle" from either the *Fosdick*-based diversion principle or the *Miltenberger*-based principle concerning nonpayment of debts arising from a debtor railroad's necessarily incurred expenses and that the Six Months Rule reflected, in part, this latter, *Miltenberger*-based principle. *Id.* at 1382. Accordingly, *Boston & Maine II* held that the principle emerging from *Miltenberger* was not merely one that would allow a court to sanction certain expenditures made by a railroad receiver after the fact pursuant to the Necessity of Payment Rule, but also a priority rule "provid[ing] for payment of claims on the same basis and from the

same operating income as administration expenses" pursuant to the strictures of the Six Months Rule. *Id.* at 1382.

Of course, under *Boston & Maine II*, claims based on this *Miltenberger* principle—no less than claims based on the principle drawn from *Fosdick*—qualify as Six Months Rule claims only if they seek the recovery of a payment for a debt that the debtor railroad incurred within, roughly, six months of the debtor railroad petitioning for bankruptcy. *See id.* at 1378-79. And, further, under *Boston & Maine II*, such claims qualify as Six Months Rule claims on the basis of this second principle only if the creditor expected that it would be paid for this debt from the debtor railroad's operating revenues and not in reliance on the railroad's general credit. *Id.*

But, the key point for purposes of assessing Keach's threshold challenge is that *Boston & Maine II* construed the Six Months Rule, as codified in § 205(b), to be rooted in more than a concern about diversion of funds, per the *Fosdick* principle. Instead, based on the *Miltenberger* line of authority, *Boston & Maine II* construed the Six Months Rule also to reflect a concern about ensuring equal treatment of claims that sought the recovery of payments for expenses that were of sufficient importance to the debtor railroad to make them distinct from claims that sought recovery for payment for the debtor railroad's less critical expenses.

Boston & Maine II explained in this regard that claims of this *Miltenberger*-derived sort are "inevitably … indistinguishable from and essentially contemporaneous with expenses paid by the railroad before reorganization, *and* will be indistinguishable from currently paid administration expenses" during the reorganiza-

tion period.[3] *Id.* (emphasis added). In this way, *Boston & Maine II* construed the Six Months Rule as one that aims, by expanding the types of claims entitled to priority, to "eliminate[]" "[t]he inequity in treatment arising out of the accidental circumstance of non-payment before the filing of the petition" of creditors' claims. *Id.* at 1379. For, *Boston & Maine II* indicates, claims that qualify as Six Months Rule claims seek recovery for debts arising from expenses that are at least as necessarily incurred by the debtor railroad as are the debtor railroad's administrative expenses, and claims by creditors to recover debts arising from those expenses of the debtor railroad do receive priority under the Bankruptcy Code. *Id.*

In addition to tracing the Six Months Rule back to the *Miltenberger* line of authority, *Boston & Maine II* also set forth a three-prong test for determining whether a creditor's claim qualifies for priority status under the Bankruptcy Code as a Six Months Rule claim. Notably, that three-prong test does not include any requirement that the creditor satisfy the diversion requirement that a creditor would have to meet if *Boston & Maine II* reflected only the *Fosdick*-based principle. *See id.* at 1378. The test instead sounds in the necessity-based, equal-treatment-aiming principle that *Boston & Maine II* derived from the *Miltenberger* line of authority. Specifically, under the test that *Boston & Maine II* announced, a claim falls within the scope of the Six Months Rule so long as:

> (1) it represents a current operating expense necessarily incurred, (2) was incurred within

[3] Certain expenses incurred by the bankruptcy estate are deemed to be "administrative expenses," 11 U.S.C. § 503(b), and entitled to priority, *see id.* § 507(a)(2).

> six months before the reorganization petition was filed, and (3) the goods or services were delivered in the expectation that they would be paid for out of current operating revenues of the railroad, and not in reliance on the road's general credit.

Id.

Before we circle back to Keach's challenge to the way that *Boston & Maine II* construed the Six Months Rule, two further points about *Boston & Maine II*'s construction of the Six Months Rule warrant further elaboration, as each of these points figures prominently in some of Keach's fallback challenges. We thus briefly address each of those points here.

The first of these points concerns the fact that the *Boston & Maine II* test emphasizes the critical nature of the expense of the debtor railroad that gives rise to the creditor's claim, as that expense must be an expense that is "necessarily incurred." *Id.* Or, as *Boston & Maine II* also phrased it, the claim must be one to recover a debt arising from an expense "for a service or supply indispensable to the maintenance and operation of the railroad." *Id.*

Significantly, however, the test does not turn on whether "the claimant has the naked power to exert economic duress" over the debtor. *Id.* Instead, *Boston & Maine II* clarifies that the test focuses on whether the claim at issue "represent[s] indebtedness for ordinary and necessary current operating expenses indispensable to continued rail service *of the kinds being paid currently as expenses of administration*." *Id.* at 1380 (emphasis added). For, *Boston & Maine II* makes clear, creditors that failed to receive payment for such debts only due to the relatively temporally proximate

"intervention of the reorganization petition before expiration of the ordinary billing and payment period," *id.*, possess a "superior equity" as compared to other unsecured creditors of the debtor railroad, *S. Ry. Co. v. Carnegie Steel Co.*, 176 U.S. 257, 285 (1900), no less than do those creditors that are owed administrative expenses. In that respect, *Boston & Maine II*'s rejection of a "naked duress" test of necessity accords with its equal-treatment aims.

Second, the third prong of the *Boston & Maine II* test contains an important limitation apart from that imposed by the "necessarily incurred" prong on the capacity of claims by creditors of debtor railroads to qualify as Six Months Rule claims. Per the third prong of its test, *Boston & Maine II* makes clear that creditors who "intention[ally] exten[ded] … credit to the railroad," and thus whose contracts with the railroad presumably reflect the risk of the railroad's default, are taken to have assumed the risk of non-payment in their extension of credit. *Boston & Maine II*, 634 F.2d at 1380. Thus, under the *Boston & Maine II* test, that class of creditors is not entitled to priority in bankruptcy under the Six Months Rule, no matter that the rule would otherwise encompass claims brought by that class of creditors. *Id.* at 1378.

2.

With this background in place, we are now well positioned to see the problem with Keach's threshold contention that *Boston & Maine II* confused the Six Months Rule with the Necessity of Payment Rule and that *Boston & Maine II* therefore erred in holding that the Six Months Rule encompassed a class of claims that could not satisfy a *Fosdick*-based diversion requirement. *See id.* at 1382. The problem is that, as the fore-

going review makes clear, *Boston & Maine II* clearly did recognize that the Six Months Rule could encompass claims that could not satisfy that diversion requirement, and we are bound as a three-judge panel to follow the law-of-the-circuit doctrine, which dictates that "newly constituted panels ordinarily are constrained by prior panel decisions directly (or even closely) on point." *Holloway*, 630 F.3d at 258 (quoting *United States v. Guzmán*, 419 F.3d 27, 31 (1st Cir. 2005)).

Keach is right that there are two exceptions to this rule of fidelity to our prior precedent. We may deviate from a prior panel's treatment of an issue where the "existing panel decision may be undermined by controlling authority, subsequently announced," *Guzmán*, 419 F.3d at 31 (quoting *Williams v. Ashland Eng'g Co.*, 45 F.3d 588, 592 (1st Cir. 1995)), and, under "hen's-teeth rare" circumstances, we may do so where "authority that postdates the original decision, although not directly controlling, may nevertheless offer a compelling reason for believing that the former panel, in light of new developments, would change its collective mind," *id*. But, Keach points to no authority post-dating *Boston & Maine II*, and, given the authority he does cite, we do not see how this is the exceptionally rare circumstance that would trigger the law of the circuit's second exception.[4]

Keach points first to subsequent statutory developments—particularly, the codification of "paradigmat-

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[4] For the purposes of this case, we set aside any additional limitations that might apply due to principles of statutory stare decisis. *See Kimble v. Marvel Entm't, LLC*, 135 S. Ct. 2401, 2409 (2015) ("[S]tare decisis carries enhanced force when a decision … interprets a statute.").

ic" Six Months Rule-like claims elsewhere in the Bankruptcy Code, *see, e.g.*, 11 U.S.C. § 503(b)(9) (granting priority to claims for the value of goods received by the debtor up to 20 days before filing). He contends that these developments should cause us to revisit *Boston & Maine II*'s holding that the Six Months Rule that it found incorporated into § 205(b) reflects more than the *Fosdick*-based principle and thus that claims need not meet the diversion requirement set forth in *Fosdick* to qualify as Six Months Rule claims.

But, these enactments tell us nothing about what Congress meant in 1978 when it enacted § 1171(b). *See Bruesewitz v. Wyeth LLC*, 562 U.S. 223, 242 (2011) ("Post-enactment legislative history … is not a legitimate tool of statutory interpretation."). In fact, § 1171(b) remains on the books without Congress having made any relevant modifications to it in the interim. *But cf.* Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 522, 98 Stat. 333, 388 (1984) (modifying § 1171(b) to change "such priority" to "the same priority").

Keach also points to a variety of out-of-circuit cases that he argues read the Supreme Court's precedent to impose a *Fosdick*-based diversion requirement for claims to qualify as Six Months Rule claims. *See, e.g.*, *Alco Prods., Inc. v. Trs. of Prop. of N.Y., New Haven and Hartford R.R. Co.* (*In re N.Y., New Haven & Hartford R.R. Co.*), 405 F.2d 50, 52 (2d Cir. 1968). But, not one of these precedents postdates *Boston & Maine II*. Thus, for that reason alone, none supplies a basis, under the law-of-the-circuit doctrine, for us to decline to adhere to what *Boston & Maine II* held in the relevant respect.

The result is that Keach cannot succeed in overturning the finding below that the claims at issue here qualify for priority status under § 1171(b) as Six Months Rule claims through his frontal assault on *Boston & Maine II*. Instead, if he is to succeed, he must show that those claims fail to satisfy the test for identifying such claims that *Boston & Maine II* derived from the *Miltenberger* line of precedent, rather than because *Boston & Maine II* was wrong to derive a test from that line of authority that allows claims to qualify as Six Months Rule claims even when they do not seek to recoup funds diverted in the way that *Fosdick* contemplates. Accordingly, we now turn to his arguments on that score.

B.

The first of the arguments of this kind that Keach presses is quite sweeping in its own right, even though it purports to take *Boston & Maine II* at its word. He contends that the type of claims for which the Irving Railroads seek priority status under § 1171(b) are by their very nature—and without regard to the facts found below—not encompassed by the Six Months Rule, even under the three-prong *Boston & Maine II* test.

To understand this contention, we need first to say a bit more about the particular type of claim that we understand Keach—at least for purposes of this aspect of his argument—to agree is at issue here. That type of claim is what is known as an interline claim, and it arises in the following way.

As this Court described in *Matter of Boston & Maine Corp.* (*Boston & Maine I*), 600 F.2d 307, 308 (1st Cir. 1979), interlining is the practice of interconnected

railroads "loaning cars to one another rather than loading and unloading freight every time a shipment passes onto rails belonging to a different road." This practice, by its nature, contemplates that there will be a system in place by which the interlining railroads will coordinate payments between them. It is through that system that the interlining railroads account for the fact that the customers who ship freight on these interconnected lines ship it across rail systems that are separately owned. Interline claims, then, are the claims that creditor railroads bring against debtor railroads to recover the interline payments that they are owed for the services that they provided in connection with the practice of interlining. *See Boston & Maine II*, 634 F.2d at 1361, 1369.

We understand Keach to agree, at least for the purpose of contending that the claims at issue here can never qualify as Six Months Rule claims even under the *Boston & Maine II* test, that the claims asserted by the Irving Railroads are properly treated as a species of interline claim. Keach's agreement to that proposition is fundamental to this aspect of his challenge. He contends that the creditor railroads' claims cannot satisfy the test that *Boston & Maine II* set forth for qualifying as Six Months Rule claims precisely because interline claims, by their nature, never can.

To support that categorical contention, Keach argues that *Boston & Maine II* did not itself hold that interline claims could qualify as Six Months Rule claims under its three-prong, *Miltenberger*-derived test, as he contends that *Boston & Maine II* had no occasion to do so, given the issues that arose on appeal in that case. He then points to a variety of precedents from outside this Circuit that he argues demonstrate that interline claims are "per se general unsecured claims" that can-

not receive priority in bankruptcy. Thus, he asks us to follow these other precedents—out-of-circuit though they are—and decide what he contends *Boston & Maine II* did not have occasion to decide: that, even under the three-prong test for defining Six Months Rule claims that *Boston & Maine II* sets forth, interline claims can never qualify as Six Months Rule claims.

We, however, read *Boston & Maine II*'s treatment of interline claims differently from Keach. In consequence, we conclude that, once again, the law-of-the-circuit doctrine stands in the way of his argument.

1.

It is true that, as Keach argues, *Boston & Maine II* did not expressly hold that the interline claims at issue in that appeal were entitled to priority; it instead remanded for the District Court to identify a class of creditors entitled to priority under the *Miltenberger*-derived three-prong test for determining whether a claim qualifies as a Six Months Rule claim that *Boston & Maine II* set forth. *See Boston & Maine II*, 634 F.2d at 1382. However, *Boston & Maine II* read *Miltenberger* to support its conclusion that there is a separate, non-*Fosdick* basis for Six Months Rule status, and Keach concedes that this aspect of *Boston & Maine II* was a holding. *See id.* Thus, we do not see how we can square *Boston & Maine II*'s clear holding that the Six Months Rule reflects the principle it attributed to *Miltenberger* with Keach's contention that the specific class of claims that *Miltenberger* identified as pertaining to "indispensable business relations," 106 U.S. at 312—interline claims—are categorically ineligible for priority under the Six Months Rule under the "necessarily incurred" prong of the *Boston & Maine II* test.

Boston & Maine II makes clear that it read *Miltenberger* to establish, at the very least, that "interline claims" *can* in some circumstances fall within "the class of claims entitled to priority of payment" because the "disastrous consequences of failing to pay" such claims could include the possibility of "a stoppage of traffic interchange." 634 F.2d at 1377-78. Moreover, *Boston & Maine II* described *Miltenberger* as "defining the classes of claims payment of which was indispensable to the business of the road." *Id.* at 1377.

It is thus significant that *Miltenberger* expressly affirmed a railroad receiver's authority to "pay indebtedness … to other connecting lines of road, in settlement of … freight accounts and balances." 106 U.S. at 308. In fact, the Court there stated that "[i]t is easy to see that … the payment of limited amounts due to … connecting lines of road … for unpaid ticket and freight balances … may well place such payments in the category of payments … entitle[d] … to be made a first lien." *Id.* at 311-12. What is more, in the critical passage of *Miltenberger* that *Boston & Maine II* quoted, *Miltenberger* stated that "non-payment" of the expenses there at issue—interline payments—would produce the "probable result" of a "stoppage" of "*indispensable* business relations." *Boston & Maine II*, 634 F.2d at 1370, 1377 (emphasis added) (quoting *Miltenberger*, 106 U.S. at 312).

Moreover, even if we were to treat as dicta *Boston & Maine II*'s discussion of whether the nonpayment of interline claims could interfere with indispensable business relations, that dicta is of the carefully considered variety. Accordingly, it "must carry great weight, and may even … be regarded as conclusive." *McCoy v. Mass. Inst. of Tech.*, 950 F.2d 13, 19 (1st Cir. 1991) (alteration in original) (quoting Charles A. Wright, The Law of Federal Courts § 58, at 374 (4th ed. 1983)).

2.

Against this background, Keach's invocation of a number of out-of-circuit precedents that he asserts support his argument that the Six Months Rule necessarily excludes interline claims as a categorical matter does little to aid his cause. The simple point is that, even if they do support Keach's contention about the nature of interline claims, *Boston & Maine II* cannot be squared with them. But, it is also worth observing, none of the non-controlling precedents on which he relies in fact raise meaningful questions about the correctness of *Boston & Maine II*'s treatment of interline claims as the type of claims that could, in their nature, qualify as Six Months Rule claims.

Keach is right that some out-of-circuit precedents decided after *Boston & Maine II* include broad language that deems interline claims to be "general, unsecured" claims. *See*, *e.g.*, *Union Pac. R.R. Co. v. Moritz* (*Matter of Iowa R.R. Co.*), 840 F.2d 535, 545 (7th Cir. 1988). But, two of the ones that he cites deem interline claims to be general unsecured claims only in the course of rejecting other, distinct arguments that these claims should receive special treatment in bankruptcy without thereby purporting to address whether they might qualify nonetheless as Six Months Rule claims. *See id.* (rejecting an argument that interline claims should be treated as being held in trust); *In re Bangor & Aroostook R.R. Co.*, 320 B.R. 226, 236, 240 (Bankr. D. Me. 2005), *aff'd*, No. 01-11565, 2007 WL 607867 (D. Me. Feb. 23, 2007) (similar).

In fact, while *Iowa Railroad Co.* does refer to interline claims as claims for "general, unsecured debts," 840 F.2d at 545, the opinion also specifically recognizes that "[c]ourts [have] applied the[] principles [of the Six

Months Rule] … to interline balances," *id.* at 537. And, further, rather than disputing that conclusion of those other courts, the Seventh Circuit accepts it and considers it to be evidence for its conclusion that "interline balances are general, unsecured debts." *Id.* Thus, *Iowa Railroad Co.*, in characterizing interline claims as ones that seek recovery for general, unsecured debts, is not at odds with *Boston & Maine II*'s characterizing the subset of interline claims that seeks recovery of payments for debts incurred temporally close to the debtor railroad's bankruptcy as being capable of qualifying as Six Months Rule claims.

Keach does point out that *Iowa Railroad Co.* reasoned that, because affording priority to interline-claim creditors will necessarily penalize other creditors, those other creditors will respond to the preference for interline-claim creditors by simply demanding more from railroads in exchange for the services they provide. *Id.* at 542. In other words, the court concluded, no matter the priority rules, "in the end, someone bears the whole risk, and shippers pay the full cost." *Id.* And, on that basis, *Iowa Railroad Co.* rejected the interline creditors' argument in that case that prioritizing their claims, based on the federal common law, was "essential to the preservation of a national transportation system." *Id.*

But, *Boston & Maine II* is not necessarily at odds with *Iowa Railroad Co.* in that respect either. *Boston & Maine II* expressly rejects a "naked power to exert economic duress" test for determining whether a creditor's claim that seeks to recover a debt that arises from an expense that the debtor railroad necessarily incurred qualifies as a Six Months Rule claim. 634 F.2d at 1378. *Boston & Maine II* explains that the Six Months Rule reflects in significant part an equal treatment principle. The idea is to ensure that, because creditors with claims

for administrative expenses *are* entitled to priority on their claims, the sudden advent of bankruptcy does not disadvantage certain pre-petition creditors who seek to recover payments for debts arising from the expenses necessarily incurred by the debtor railroad that are similar to administrative expenses. *See id.* at 1379; *see also* 11 U.S.C. § 503(b), 507(a)(2).

That leaves Keach with but one post-*Boston & Maine II* case that accords with his view: *In re McLean Industries, Inc.*, 103 B.R. 424 (Bankr. S.D.N.Y. 1989). That out-of-circuit bankruptcy court case based its conclusion on the fact that "Congress, in enacting the Bankruptcy Code, expressly rejected a proposal that debtor railroads be required to pay interline balances." *Id.* at 426. The rejected statutory provision on which that bankruptcy court relied, however, would have immediately required a debtor railroad to pay all pre-bankruptcy interline debts without any need for court approval. *See* S. 2266, 95th Cong. § 1169 (1978); *see also Boston & Maine I*, 600 F.2d at 313 ("The legislative history of this provision indicates that .... Congress chose ... to place the timing of payment of [interline] claims exclusively in the discretion of the reorganization court."). Thus, Congress's choice not to enact a special provision for interline claims reveals little about whether Congress meant for creditors to receive the weaker protection of the Six Months Rule via § 1171(b) for the subset of interline claims that seek payment for debts incurred by the debtor railroad sufficiently near to the time of its bankruptcy to fall within the temporal scope of the Six Months Rule. *See Zucker v. Rodríguez*, 919 F.3d 649, 660 (1st Cir. 2019) ("The fact that Congress rejected a provision about one thing tells us little about what Congress intended in enacting a provision about something else.").

We note, moreover, that the only other Court of Appeals that Keach identifies as having read the Six Months Rule to include a *Miltenberger*-based principle, and not merely a *Fosdick*-based one, is the Fourth Circuit. *See S. Ry. Co. v. Flournoy*, 301 F.2d 847, 851 (4th Cir. 1962). But, that Circuit has held that interline claims may be entitled to priority status under the Six Months Rule. *Id.* at 853-54. Thus, in addition to the fact that *Boston & Maine II* itself cannot be squared with the notion that interline claims are categorially barred from qualifying as Six Months Rule claims, the precedents that Keach relies on fail to indicate that it was wrong in that regard.

3.

Keach does briefly suggest another reason to conclude that interline claims—as a class—cannot qualify as Six Months Rule claims under *Boston & Maine II*'s three-prong test. He contends, in this regard, that federal law required the Irving Railroads to allow the MMA to interchange with their railroads and thus that the payments that the MMA owed to them in consequence of their being interconnected are, inherently, expenses that are not "necessarily" incurred.

As authority for this proposition, Keach cites to an out-of-circuit district court case, *Matter of Penn Central Transportation Co.*, 458 F. Supp. 1234 (E.D. Pa. 1978). There, the court stated in dicta that a similar mandate "renders the necessity of payment rule"—which, as we have explained, is an entirely different rule from the Six Months Rule—"totally inapplicable." *Id.* at 1332 n.93. Keach then alleges that we conflated the Necessity of Payment Rule with the Six Months Rule in *Boston & Maine II* and that we therefore

should read *Penn Central*'s dicta on the former rule to apply to our caselaw concerning the latter one.

But, to the extent that this argument by Keach is not waived for lack of development, *see United States v. Zannino*, 895 F.2d 1, 17 (1st Cir. 1990), it necessarily fails under the law-of-the-circuit doctrine if for no other reason than that *Penn Central* was decided before *Boston & Maine II*. But, we should add, *Boston & Maine II* itself recognized that "the interlining of freight cars is mandatory under the Interstate Commerce Act." 634 F.2d at 1362.

C.

Keach still is not done, however. Even accepting that *Boston & Maine II*'s test is sound and that interline claims are not categorically barred from qualifying as Six Months Rule claims under that test, he asserts that the ruling below as to these particular interline claims cannot stand for three case-specific reasons. We thus close out our consideration of this appeal by considering each one of these more narrowly drawn challenges.

1.

Keach first contends that the Bankruptcy Court erred because, at one point in its oral opinion, it stated with regard to the *Boston & Maine II* test that "it is sufficient [that] claims are for a current expense, goods and services and bringing ordinary operation of the rail." Based on this language, Keach contends that the Bankruptcy Court mistakenly required that the claims at issue need only represent current expenses of the debtor railroad to qualify as Six Months Rule claims. He thus argues that the Bankruptcy Court effectively dispensed with the necessity requirement that *Boston & Maine II* set forth for discerning a claim as one that

the Six Months Rule encompasses. As a result, he argues that, at the very least, the ruling below must be vacated and remanded.

The Bankruptcy Court's oral opinion, however, cited to *Boston & Maine II* and correctly described the test that it set forth as requiring a showing that a claim is for the recovery of a debt arising from "a current operating expense *necessarily* incurred." (emphasis added). Moreover, the Bankruptcy Court's written order overruling Keach's objections on this point confirmed that the claims at issue concern debts arising from "current operating expenses that were *necessarily* incurred by MMA in connection with its on-going operations." (emphasis added). Thus, we see no reason to attribute to the Bankruptcy Court the mistake that Keach contends that it made.

2.

Keach next takes aim at the evidentiary basis for the Bankruptcy Court's ruling that, per the *Miltenberger*-derived test set forth in *Boston & Maine II*, the claims are for debts arising from "current operating expense[s] *necessarily incurred*." *Boston & Maine II*, 634 F.2d at 1378 (emphasis added). Once again, we are not persuaded.

Keach is right that *Boston & Maine II* held that Six Months Rule claims must be "for a service or supply *indispensable* to the maintenance and operation of the railroad," *id*. at 1378 (emphasis added), and he points us to a variety of out-of-circuit cases that limit Six Months Rule claims to those based on expenditures of that ilk, *see, e.g.*, *Chicago & A.R. Co. v. U.S. & Mexican Tr. Co.*, 225 F. 940, 945-46 (8th Cir. 1915). But, we do not agree with Keach's further contention that, because the evi-

dence clearly showed that the MMA could have continued operating without interchanging with the Irving Railroads, the Irving Railroads' claims are not for the recovery of payments for debts arising from "expense[s] necessarily incurred." *Boston & Maine II*, 634 F.2d at 1378.

We have already noted that *Boston & Maine II* made clear that "[t]he test is not whether the claimant has the naked power to exert economic duress," *id*. at 1378, and, to an extent, Keach recognizes this point. For example, the Irving Railroads point out, Keach acknowledged to the Bankruptcy Court that a creditor's claim to recover about $7,000 based on repair costs incurred by a debtor railroad would merit priority status under the Six Months Rule. He did so, moreover, even though he recognizes that there may be no argument that this one repair expense to this one service provider, standing on its own, was necessary to keep the railroad going. That is because, as Keach admits in his reply brief, the test is not "whether the specific [claim] at issue," if withheld, "would have forced a total shutdown of operations." Rather, he contends, "it is the *genre* of the claim that is relevant to the analysis."

Indeed, a focus on whether the claimant seeks payment for a debt arising from an expense—the particular repair—that is independently essential to the ongoing operation of the railroad would likely render few if any claims indispensable. It would be the rare repair that, in and of itself, would be so essential that the railroad could not go without it.

Nevertheless, Keach contends that the interline claims that are at issue here are not like those that seek recovery of payments for debts arising from expenses incurred by a debtor railroad to make repairs, because

the very route on which the freight traveled that led the claimants to be entitled to recovery for debts incurred by the MMA for the interline payments was abandoned post-bankruptcy by the MMA. He argues that, in consequence, these claims seek payments in connection with expenses that cannot possibly have been "necessarily incurred" by the MMA.

But, Keach offers no authority to support the proposition on which this argument necessarily rests: that we must construe the words "indispensable" and "necessary" in *Boston & Maine II* to make the necessity to the operation of the railroad of the particular route over which the freight traversed itself determinative of whether an expense incurred in operating that particular route was necessary or indispensable to the railroad's operation. Nor do either *Miltenberger* or *Boston & Maine II* require that we endorse such a proposition.

In *Miltenberger*, the Supreme Court affirmed the receiver's decision immediately to pay out freight balances that he deemed to be "indispensable to the business of the road," and without which, "the business of the road would suffer great detriment." *See* 106 U.S. at 311. The Court found that it was "easy to see that … the payment of limited amounts due to … connecting lines of road … for unpaid ticket and freight balances" could be so significant as to authorize such payment, because "a stoppage of the continuance of [indispensable] business relations would be a probable result … of non-payment." *Id.* at 311-12. The Court at no point conducted an inquiry into the necessity of any particular line to the railroad's capacity to stay in business, even if in a much-diminished state.

Similarly, *Boston & Maine II* read *Miltenberger* to be "defining the classes of claims payment of which was

indispensable to the business of the road." *Boston & Maine II*, 634 F.2d at 1377. *Boston & Maine II* then went on to indicate, again based on *Miltenberger*, that interline claims may fall into that class because the "disastrous consequences of failing to pay … interline claims" include "a stoppage of traffic interchange." *Id.* *Boston & Maine II* did not in so stating at any point suggest that the necessity of making interline payments hinges on whether those interline payments were made in connection with a route that itself is one without which the railroad could not operate, even in a much-reduced manner.

Keach's suggested approach to defining "necessarily incurred" is also in tension with some of his own contentions. If the proper inquiry were focused on the necessity of the line to the debtor railroad's operations rather than on the necessity of the expense in consequence of the debtor railroad operating that line, then it would be hard to see how claims for expenses the debtor railroad incurred to pay for fuel, labor, or even repairs could qualify as Six Months Rule claims insofar as those expenses were incurred in connection with any aspect of the operation of an important line for a debtor railroad that the debtor railroad could jettison post-bankruptcy and survive. Yet Keach portrays each of those types of claims—whether concerning fuel, labor, or repairs—as quintessential types of qualifying claims without suggesting that their ability to qualify as Six Months Rule claims depends on whether they seek recovery of debts that arise from expenses incurred by the debtor railroad in connection with its operation of a rail route without which the debtor railroad could not remain a going concern.

That leaves, then, only the question whether, in operating the particular route at issue, the MMA neces-

sarily incurred the expenses represented by the share of the interline payments that the Irving Railroads seek to recover with their claims. But, Keach does not dispute that the record here adequately supports the Bankruptcy Court's finding that "the inability of MMA to interchange traffic with the [Irving Railroads] on the … 'critical rail artery' … between St. John and Montreal would have had a significant adverse effect on MMA's operations, including … the possible loss of business with Irving as well as a reduction in revenue." Nor do we see how he could, given the testimony that the Bankruptcy Court deemed credible from Ian Simpson, the General Manager for the Irving Railroads. Simpson's testimony, moreover, also supports the Bankruptcy Court's finding that "it would not be practical or economical" for the MMA to use an alternative route to ship oil to St. John.[5]

Keach does cite to a number of cases that he contends emphasize that the bar for an expense to qualify

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[5] Keach at various points in his briefing suggests that the MMA was only a "collection agent" for the Irving Railroads. If Keach means to argue that the expenses incurred by the MMA could not have been "necessarily incurred" because the Irving Railroads could simply have bypassed the MMA and collected the payments itself directly from the customers whose freight shipments traversed their lines, he fails to develop this argument and has therefore waived it. *See Zannino*, 895 F.2d at 17. In any case, this argument would ignore the Bankruptcy Court's findings that the MMA's business at the relevant time depended in large part on shipping oil toward St. John. Thus, we have difficulty seeing how it would be clear error to find that the MMA's payments to compensate the Irving Railroads for the services the Irving Railroads performed in shipping the freight of customers were necessarily incurred, as they compensated the Irving Railroads for a service that was critical to the MMA's operation of that key aspect of its business at the time.

as being "necessarily incurred" is a high one. But, most of those cases neither elaborate on the contours of the necessity test nor deal with facts analogous to the ones presented here. *See Commonwealth Edison Co. v. Cont'l Nat. Bank & Tr. Co. of Chi.*, 93 F.2d 265, 266 (7th Cir. 1937) (determining that electricity used to operate a railroad's "trains, lights and equipment" was "essential to the operation of its road"); *N.Y. Guar. & Indem. Co. v. Tacoma Ry. & Motor Co.*, 83 F. 365, 368 (9th Cir. 1897) (deeming a cable rope "necessary" to a street railroad because "[i]t is impossible to imagine a case where anything was more necessary to keep [a] portion of the street railway a going concern"); *Cent. Tr. Co. of N.Y. v. E. Tenn., V. & G.R. Co.*, 80 F. 624, 631 (6th Cir. 1897) (denying priority for advertising without invoking the necessity test). And, one of these cases even holds that legal expenses relating to "personal injury suits, collection actions, union contract disputes, and employee claims" are "necessary to the continued operation of the railroad." *In re Mich. Interstate Ry. Co., Inc.*, 87 B.R. 921, 923 (Bankr. E.D. Mich. 1988). It is hard to divine the metric by which the payment for the legal services at issue there were necessary to the operation of the debtor railroad but the payments that the MMA had to make to the Irving railroads for the freight services that they provided are not.

The Eighth Circuit did, in an additional case highlighted by Keach, hold that claims to recover payments for debts arising from expenses incurred by a debtor railroad to support the operation of its *non-railroad* businesses are not eligible for priority. *See Ill. Tr. & Sav. Bank v. Doud*, 105 F. 123, 127-28 (8th Cir. 1900). But, *Illinois Trust & Savings Bank* merely stands for the commonsense proposition that the necessity prong of the test articulated in *Boston & Maine II* asks

whether an expense was necessary for the operation of the railroad's rail system, not for other side businesses operated by the railroad. *Id.*

That proposition, which follows from *Boston & Maine II*'s conclusion that *Miltenberger* had established the important role that interline payments played in facilitating effective rail service to the public, *see Boston & Maine II*, 634 F.2d at 1377, does not conflict with the findings by the Bankruptcy Court regarding the interline claims in this case. The expenses were incurred in connection with the operation of a rail route rather than a side business, and, moreover, the Bankruptcy Court supportably found that the rail route itself was a critical one.

The remaining case that Keach cites, *Chicago & A.R. Co.*, does hold that evidence that the unpaid interline balances of a railroad "would disrupt [its] freight, and be a serious detriment to [its] business" was insufficient to prove "that the preferential payment of the … claim was … necessary to keep the … railroad a going concern." 225 F. at 946. But, *Chicago & A.R. Co.* based its restrictive reading of the necessity prong of the Six Months Rule on its conclusion that post-*Miltenberger* decisions of the Supreme Court "so narrowly limit … preferential claims" that if the then-current Court had revisited the facts of *Miltenberger*, the creditors "would be denied preference." *Id.* at 945. *Boston & Maine II*, however, precludes us from adopting the limited view of *Miltenberger*'s precedential value that *Chicago & A.R. Co.* recognized, because *Boston & Maine II* specifically considered and rejected the view of cases like *Chicago & A.R. Co.* that read subsequent Supreme Court precedent to have "reduc[ed] *Miltenberger* to a … holding [of] the starkest economic duress form." *Boston & Maine II*, 634 F.2d at 1378; *see also id.* at

1374 (describing *Chicago & A.R. Co.* as one of the cases adopting this reading of Supreme Court precedent).

3.

The last of Keach's more narrowly drawn arguments focuses, unlike the two others that we have just considered, on the third prong of the Six Months Rule test. That prong, as we explained earlier, concerns the means by which the debtor railroad was expected to pay the debt for which the creditor railroads' claims seek recovery. That prong does so by focusing not on whether a claim is for payment of an expense that was necessarily incurred by the debtor railroad but on whether the creditor was expecting payment "out of current operating revenues of the railroad." *Id.* at 1378. If, instead of relying on such revenues, a creditor made a payment "in reliance on the road's general credit," then it cannot obtain the benefit of priority under the Six Months Rule. *Id.*

We note that, although *Boston & Maine II* did not have occasion to address the issue, the presence of a security arrangement might inform an inquiry under the third prong of the *Boston & Maine II* test into whether a claimant had expected to be "paid for out of current operating revenues of the railroad." *Id.* at 1378. As some courts have observed, a creditor's insistence on such an arrangement might show that it thought that payment from current operating revenues was uncertain and thus that the creditor was not relying on those revenues for payment. *See Lackawanna Iron & Coal Co. v. Farmers' Loan & Tr. Co.*, 176 U.S. 298, 316 (1900) (identifying the existence of a large "collateral security" as "a circumstance tending to show that [the creditor] … relied upon the general credit of the railroad company"); *Commonwealth Edison Co.*, 93

F.2d at 270 (noting that "evidentiary facts of other security taken" could establish a "lack of expectation or intention that [the claimant] should be paid out of current earnings").

Keach contends that, notwithstanding the contrary findings of the Bankruptcy Court, the record precludes the claimants from making the showing required by this third prong of the *Miltenberger*-derived test that *Boston & Maine II* sets forth. But, for the following reasons, we do not agree. We begin by saying a bit more about how we apply the third prong of the test. We then explain why we conclude that the Bankruptcy Court supportably found it met.

a.

As we have explained, the third prong of the *Boston & Maine II* test reflects a sensible intuition. The Six Months Rule, as elaborated in *Boston & Maine II*, is designed to protect providers of certain critical goods and services who were expecting to be paid out of the railroad's current operating expenses in the ordinary course of business. *See* 634 F.2d at 1378. Thus, it makes sense that the Six Months Rule would not permit a creditor to reap the benefits of priority in bankruptcy if that creditor implicitly assumed the risk that the debtor railroad would not remain solvent, say, by hedging against that risk through a contract with interest terms that reflected its trust in the railroad's general financial health rather than an expectation of being promptly paid out of the railroad's current revenues in the normal course for debts arising from expenses necessarily incurred. *See id.* at 1379-80. Similarly, it makes sense that the Six Months Rule would not protect a creditor who hedges against the risk of nonpayment from operating expenses through a de-

mand for security. *See Lackawanna Iron & Coal Co.*, 176 U.S. at 316.

But, despite the sensible intuition that the third prong of the test reflects, it is not always easy to discern whether this prong has been met. As we have said before, "reliance on the general credit of the railroad" is somewhat of "an illusory concept," *Boston & Maine II*, 634 F.2d at 1379, because of the wide variety of circumstances in which a party might expect payment from a railroad. In fact, in accord with that observation, the Bankruptcy Court recognized in this very case that it is possible that a party "might well rely on both the current operating revenues of the railroad as well as its general credit."

Nevertheless, *Boston & Maine II* provides us with some guidance as to how to draw this nebulous line. *Boston & Maine II* provides that:

> it will be for the reorganization court to determine … whether the non-payment reflects an intentional extension of credit to the railroad, or the intervention of the reorganization petition before expiration of the ordinary billing and payment period, or some noncontractual indulgence or inadvertence on the part of the claimant, or deferment of payment on the part of the railroad; and whether, if the transaction giving rise to the claim had any credit term, it was compatible with a general expectation of payment from current receipts or indicated reliance on the railroad's general credit.

Id. at 1380. In an early case elaborating on this constraint on Six Months Rule priority, moreover, the Supreme Court explained that among the factors to be considered are "the amount of the debt, the time and

terms of payment, and all other circumstances attending the transaction." *Carnegie Steel Co.*, 176 U.S. at 285. We thus apply this guidance in assessing the findings of the Bankruptcy Court that bear on this third prong of the *Boston & Maine II* test.

b.

The Bankruptcy Court found here that the Irving Railroads expected to be paid from current receipts of the MMA and did not rely on the MMA's general credit or a security arrangement. To understand the finding, it helps to recall some of the details of the swap arrangement that was in place as of 2013, which is the year when all the debts for which the claims at issue sought recovery were incurred.

By then, as we noted at the outset, the volume of oil shipped across the rail systems of the Irving Railroads and the MMA to St. John had increased dramatically. As a result, the MMA typically owed the Irving Railroads more in interline payments than the Irving Paper Companies owed the MMA for shipping their freight. The increased oil volume also meant that the MMA at that time had difficulty meeting the timeline for payment under the then-existing agreement between the parties.

In consequence, in 2012, the Irving Railroads and the MMA carved certain payments out of their preexisting swap arrangement. Thus, based on the bifurcated agreement in place as of 2013, the Irving Railroads were expecting to receive two types of relevant payments from the MMA.

First, the MMA owed the Irving Railroads payments for freight shipments on the rail system that were to be collected by the MMA directly from the cus-

tomer shipping the freight, namely payments for freight shipments that originated on lines belonging to either the Irving Railroads or the MMA. For these shipments, in which MMA was the billing railroad, the MMA would make them to the Irving Railroads at the same time that the Irving Railroads' affiliates, the Irving Paper Companies, would pay the MMA for what it was owed for their freight having traveled, at least in part, on its rail system. The MMA's transfers to the Irving Railroads would take place within 30 days of the freight having been shipped.

Second, the MMA owed the Irving Railroads their share of payments for charges to customers whose freight shipments traversed the Irving Railroads' rail systems but did not originate on either those rail systems or the MMA's rail system. After all, the MMA received through the ISS both its share of the payment for the charge to customers for shipping that freight and the Irving Railroads' share.

The share of the payments that the MMA owed to the Irving Railroads primarily related to shipments of oil to St. John. Moreover, all payments for charges to customers for oil shipments to St. John were payments of this type.

The MMA had to send the Irving Railroads their share of these payments within five days of the MMA's receipt of the payments that it collected through the ISS. Due to the 45-to-60-day turnaround time for payments made to the MMA through the ISS, however, the Irving Railroads could expect to wait up to 65 days to receive their share of these payments.

In finding that, for both sets of these payments, the Irving Railroads counted on the current operating revenues of the MMA for payment, the Bankruptcy Court

relied on witness testimony that indicated that the Irving Railroads intended to avoid relying on the MMA's credit. In so finding, the Bankruptcy Court explained that it "didn't find anything in that deal or that arrangement that had incorporated common conditions of the commercial credit, security interests, and the like."

The Bankruptcy Court supportably relied in particular on testimony from Karl Hansen, the General Manager of Corporate Credit and Financial for the Irving Paper Companies, who testified that the Irving Railroads "absolutely" did not rely on the MMA's general creditworthiness, but instead relied on the regularity of the ISS payments to the MMA. The Bankruptcy Court similarly pointed to testimony from Ian Simpson, the General Manager for the Irving Railroads, who testified that "[w]hen [the MMA] got paid, we were to be paid."

This testimony was consistent with the nature of the swap agreement between the Irving Railroads and the MMA after the payment timeframe was extended in July 2012, which is the only relevant timeframe for our purposes, given when the debts that the claims at issue seek to recover were incurred. By then, the swap arrangement had been modified to account for the change occasioned by the oil shipments to St. John. Nonetheless, the swap arrangement still required the MMA to send the Irving Railroads their share of the payments that the MMA collected within five days of the MMA itself receiving the payments, and nothing in the modified agreement suggests that the Irving Railroads received interest or any other compensation in exchange for the additional risk they took on by accepting this extended delay. *See Boston & Maine II*, 634 U.S. at 1380 (asking whether a "credit term … was

compatible with a general expectation of payment from current receipts").

It is true that, as Keach notes, under the modified swap arrangement, the Irving Railroads could expect to wait as long as 65 days to be paid what the MMA owed with respect to at least some of what they were owed. But, we find supportable on this record the Bankruptcy Court's conclusion that—notwithstanding that delay—payments due to the Irving Railroads were still tied to the MMA's receipt of payments through the ISS and therefore were made in reliance on the current operating revenues of the MMA.

Notably, the Supreme Court has approved of affording priority to creditors based on contracts with payment terms of three and four months. *See Carnegie Steel Co.*, 176 U.S. at 286-87 (describing the claimant's credit arrangement as "short credit given"). The payment terms that it has found to be indicative of a reliance on the general credit of a railroad, by contrast, have been far lengthier than those that we confront here. *See Lackawanna Iron & Coal Co.*, 176 U.S. at 316-17 (holding that a "long period of credit"—a six-month repayment term that was renewable by the railroad—was, as part of a totality-of-the-circumstances analysis, evidence that the debtor was relying on the railroad's general credit).

Indeed, the Bankruptcy Court recognized that, prior to 2012, when the swap arrangement still covered all payments between the parties, Keach may have had a "more powerful" argument that the Irving Railroads were not counting on the MMA's operating revenues for repayment. After all, at that point, the payments owed from the Irving Paper Companies to the MMA were much larger than the payments owed from the

MMA to the Irving Railroads, and all of the payments owed to the Irving Railroads thus were made pursuant to a swap arrangement that, at least arguably, protected the Irving Railroads in the event that the MMA failed to pay.

In 2012, though, the Bankruptcy Court explained, "the oil started shipping," the MMA stopped being able to make all its payments under the swap arrangement, and the parties entered a "new reality." That new reality was reflected, in turn, in the new agreement that they reached to account for the change, as that new agreement carved out from the swap arrangement the payments for the charges to customers for the critical oil shipments.

Under this new reality, the increased volume of oil shipments meant that the MMA typically owed more to the Irving Railroads than it expected to receive from the Irving Paper Companies. Thus, as Keach concedes, the Irving Railroads were as of that time "undersecured."

Thus, we read the Bankruptcy Court to have impliedly found that the swap arrangement was no longer serving whatever security function it may have served at the beginning of the parties' relationship. Rather, we understand the Bankruptcy Court to have determined that, by that point in time, the Irving Railroads continued to do business with the MMA because they expected that the MMA could pay them from the revenue that it was receiving in the form of both the interline payments that it received through the ISS and the payments that it received from customers that it directly billed. In other words, we understand the Bankruptcy Court to have supportably found that the parties' "new system" in 2012 no longer depended on the

swap arrangement for security but instead on the Irving Railroads' confidence in the cash flow of the MMA.

Because we see no basis, on clear error review, for rejecting these findings, we conclude that the Bankruptcy Court supportably found that the Irving Railroads expected to be paid out of the MMA's "current receipts," namely the ISS payments or other similar payments that the MMA collected, and not the general credit of the MMA or a security arrangement. As a result, the Bankruptcy Court's findings suffice to show that the claims in question satisfy the third prong of the test for giving them priority under the *Miltenberger*-derived test that *Boston & Maine II* sets forth.

Keach's attempts to resist this conclusion are not persuasive. Keach argues that the fact that the railroads laid out their ongoing business relationship in a written contract is evidence that the parties depended on each other's credit and not on their current operating revenues to cover the debts incurred. But, a detailed, documented agreement is perfectly compatible with repeated transactions made in reliance on current operating revenues. Indeed, the case Keach cites on this point, *Louisville Bridge Co. v. Chicago, I. & L. Ry. Co.*, 253 F. 631, 634 (7th Cir. 1918), merely found that the specific contractual provisions at issue in that case, including a provision allowing the creditor to terminate the contract upon the railroad's failure to repay, when combined with other facts, such as the creditor's decision to delay receipt of payment, showed an extension of credit to the railroad. *Louisville Bridge Co.* does not stand for the implausible converse proposition that a contract specifying payment terms in and of itself shows that the parties did not contemplate payment from current operating revenues.

Keach also contends that, because the Irving Railroads had what he contends was a "special security arrangement" with the MMA in the form of its swap agreement, they could not have been relying on the operating revenues of the MMA to pay the debts at issue. But, we see no basis for adopting a hard-and-fast rule—insofar as Keach means to ask us to do so—that the mere existence of a "'special security' ... excepts creditors from the protections of the six months rule" regardless of its terms and limitations or practical effect.

The out-of-circuit cases to which Keach cites are not to the contrary. They merely show that—just as the Bankruptcy Court recognized here—such arrangements may be relevant, depending on the facts, to the Six Months Rule analysis. *See Flournoy*, 301 F.2d at 856 (finding that a cash-on-delivery arrangement, in which the railroad paid the creditor for old debts at the time of delivery, showed that the creditor "was not looking to current earnings for payment of current deliveries but rather for payment of the old balance"); *Commonwealth Edison Co.*, 93 F.2d at 270 (summarizing the Six Months Rule as including a requirement that credit not be "given in reliance upon the railroad company's personal credit or some special security" (quoting Franklin W. M. Cutcheon, Some Legal Phases of Corporate Financing, Reorganization and Regulation 106 (1931))); *Gregg v. Mercantile Tr. Co.*, 109 F. 220, 223 (6th Cir. 1901) (finding that a lessor's right to "resume possession, and declare the lease forfeited" shows that "the lessor did not rely upon its rentals as constituting an equitable charge upon the current income of the lessee company"); *In re Third Ave. Transit Corp.*, 138 F. Supp. 623, 625 (S.D.N.Y. 1955) (same quotation as *Commonwealth Edison Co.*).

Nor does Keach's contention fare better if we look at the actual details of the swap arrangement and how it worked in practice. As we have already explained, by the time the expenses relating to the claims at issue here were incurred, the Bankruptcy Court supportably found, the Irving Railroads were no longer relying on the swap arrangement for security. Thus, keeping in mind that "each case 'must depend largely upon its special facts,'" *Boston & Maine II*, 634 F.2d at 1379 (quoting *Carnegie Steel Co.*, 176 U.S. at 292), and that it is "for the reorganization court to determine … whether the non-payment reflects an intentional extension of credit to the railroad," *id.* at 1380, we reject this final aspect of Keach's challenge to the ruling below.[6]

IV.

Accordingly, we ***affirm*** the decision of the Bankruptcy Court.

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[6] Keach also reasons, by analogy to the preferential transfer rules of 11 U.S.C. § 547, that the bankruptcy laws are designed to punish creditors who attempt to gain an advantage vis-à-vis similarly situated creditors through non-ordinary transactions, and that disqualifying creditors who resort to such measures from Six Months Rule protection is therefore appropriate. But, the preferential transfer rules are designed to place similarly situated creditors in the same position, not to punish the recipients of preferential transfers relative to those who did not receive such transfers. *See* 5 Collier on Bankruptcy ¶ 547.01 (Richard Levin & Henry J. Sommer eds., 16th ed. 2020) (identifying as the primary purpose of § 547 "the prime bankruptcy policy of equality of distribution among creditors of the debtor"). Thus, even accepting Keach's characterization of the parties' contract as out of the ordinary, there is little reason to extrapolate from the preferential transfer rules a general bankruptcy policy of penalizing creditors who resort to unusual contract terms to protect themselves prior to bankruptcy.

APPENDIX B

FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL
FOR THE FIRST CIRCUIT

BAP NO. EB 16-015
Bankruptcy Case No. 13-10670-PGC

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

ROBERT J. KEACH, CHAPTER 11 TRUSTEE,
Appellant,

v.

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

Appeal from the United States Bankruptcy Court
for the District of Maine
(Hon. Peter G. Cary, U.S. Bankruptcy Judge)

Filed October 21, 2016

Before: Feeney, Deasy, and Harwood, United States Bankruptcy Appellate Panel Judges.

* * *

OPINION

FEENEY, Chief U.S. Bankruptcy Appellate Panel Judge.

Robert J. Keach, the former chapter 11 trustee (the "Appellant"),[1] appeals the bankruptcy court's February 26, 2016 order (the "Order") overruling in part his objections to certain proofs of claim filed by New Brunswick Southern Railway Company Limited ("NBSR") and Maine Northern Railway Company ("MNR" and, collectively with NBSR, the "Irving Railroads"). The Appellant appeals the bankruptcy court's ruling that the Irving Railroads' claims qualified as so-called "six months claims" entitled to priority under § 1171(b).[2] For the reasons set forth below, we **AFFIRM**.

BACKGROUND

I. PRE-BANKRUPTCY EVENTS

From January 2003 until May 2014, Montreal, Maine & Atlantic Railway, Ltd. ("MMA") owned and operated an integrated, international shortline freight railroad system with its wholly owned Canadian subsidiary, Montreal, Maine & Atlantic Canada Co.[3] This

[1] The Appellant states that in accordance with the Trustee's Revised First Amended Plan of Liquidation Dated July 15, 2015 (as amended on October 8, 2015) (the "Plan"), upon the effective date of the Plan (which occurred on December 22, 2015), he is no longer the chapter 11 trustee of the bankruptcy estate, but is the Estate Representative of the Post-Effective Date Estate (as defined in the Plan). He further states that, as the Estate Representative, he acquired all rights and duties with respect to the prosecution of this appeal and its underlying claims. The appellees do not challenge these averments.

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

[3] MMA was formed in 2003 to acquire the assets of the Bangor & Aroostook Railroad Company and its affiliated railways ("Bangor & Aroostook") from their bankruptcy estates. MMA commenced rail operations in January 2003.

railroad system included 510 route miles of track in Maine, Vermont, and Québec, and was a substantial component of the rail transportation systems in northern Maine, northern New England, Québec, and New Brunswick. Among other things, it provided the shortest rail transportation route between Maine and Montréal, and was a "critical rail artery" between St. John, New Brunswick and Montréal. In order to provide freight transportation services to customers throughout the system, MMA interchanged freight traffic with other railroads, including the Irving Railroads, with which its operations were interconnected.

A. The Interline Settlement System

MMA, like most railroads, participated in the Interline Settlement System (the "ISS"). The ISS provides a central clearing house for all participating railroads involved in the interchange of freight traffic among multiple rail carriers to settle accounts receivable and accounts payable arising from the interchange of such traffic. Railroads participating in the ISS that originate traffic are known as "billing" or "originating" railroads and invoice the customer for all freight charges from the point of origin to the point of destination, even if the shipment is interchanged with other railroads along the route. The customer is responsible for paying the billing railroad the entire invoice, and the billing railroad is responsible for paying the other railroads involved in the shipment along the line for their share of the freight charges. Railroads participating in the ISS calculate on a monthly basis the accounts receivable and accounts payable arising from the interchange of traffic that are due and owing to each participant, and the payment of the net amount due and owing is made on the second business day of each month. One of

the benefits of participating in the ISS is that billing railroads are obligated to pay the other participating railroads regardless of whether the customer pays the billing railroad.

B. The Relationship between MMA and the Irving Railroads

The business relationship between MMA and the Irving Railroads began in January 2003, when MMA entered into a Commercial Agreement (the "Commercial Agreement") with NBSR and one of NBSR's affiliates, Eastern Maine Railway Company ("EMR"),[4] setting forth various terms and conditions governing the interchange of freight traffic between MMA and the Irving Railroads. Pursuant to the Commercial Agreement and a separate Interchange Agreement between MMA and EMR, the Irving Railroads and MMA agreed to interchange freight traffic at MMA's Brownville Junction Yard in Maine. Section 2 of the Commercial Agreement, entitled "Performance of Transportation Services," provided as follows:

> The parties agree that from and after the Effective Date, EMR/NBS[R] shall move loaded freight cars and associated empty cars between points located on its lines or reached by it under Canadian interswitch rules and Brownville Junction at rates as set out in this Agreement. MMA shall act as the interline tariff carrier on a junction settlement basis. By "junction settlement basis" the parties mean that MMA shall negotiate through rates and make contracts and

[4] NBSR operated various railroad lines in New Brunswick. EMR operated a railroad line in Maine which connected with NBSR's lines. EMR is a "sister company" of NBSR.

> provide quotations, and shall be responsible for car supply to the extent requested by NBS[R] and reasonably available from MMA and in rail cars customarily supplied by railroad carries, all in accordance with the provisions of this Agreement. MMA shall continue to render one freight bill, and assess and collect the total amount of freight charges … and remit the portion pertaining to EMR/NBS[R's] transportation services to EMR/NBS[R] in accordance with the procedures in this Agreement.

At the evidentiary hearing described below, and while addressing the freight carried by MMA to the interchange point with the Irving Railroads, Ian Simpson, general manager of the Irving Railroads, explained that the interchange of freight traffic involved the decoupling of freight cars from MMA's locomotives and connecting them to the Irving Railroads' locomotives, which then carried the freight cars to their final destination.

The Irving Railroads did not participate in the ISS.[5] As a result, pursuant to the Commercial Agreement, MMA acted as the billing railroad when either of the Irving Railroads originated traffic and interchanged with MMA, as well as when MMA originated traffic and interchanged with either of the Irving Railroads. MMA also collected from the ISS freight revenue attributable to freight services provided by the Irving Railroads in connection with shipments originated by other carriers

[5] According to Mr. Simpson, the Irving Railroads did not participate in the ISS for several reasons, including lack of resources and the existence of relationships with other carriers that rendered participation in the ISS unnecessary. He also testified the decision not to participate in the ISS was not influenced in any way by the credit worthiness of MMA.

that were interchanged by such carriers with MMA and then by MMA with the Irving Railroads. Periodically, MMA and the Irving Railroads settled their accounts payable and receivable as between themselves. Other than certain amounts for repair of cars owned or leased by MMA, the Irving Railroads' claims, as described below, arose from MMA's collection of funds either from customers or through the ISS and its failure to pay amounts due to the Irving Railroads.

C. The "Payment Swap" Arrangement

At the time MMA and the Irving Railroads began doing business, Karl Hansen, general manager of Corporate Credit and Finance for the Irving Railroads and their affiliated companies, had concerns MMA would not be able to pay the Irving Railroads due to the troubled history of MMA's predecessor, Bangor & Aroostook. As a result, the Irving Railroads, together with certain of their affiliated paper companies, Irving Pulp and Paper, Limited, Irving Paper Limited, and J.D. Irving, Limited (collectively, the "Irving Paper Companies"), which were among MMA's largest customers, agreed with MMA on a process to settle their respective accounts receivable and accounts payable by concurrently exchanging payments through wire transfers of amounts owed to each other. Included in this "payment swap" arrangement[6] were: (1) accounts pay-

[6] The Appellant characterizes this arrangement as a "triangular setoff," contending the Irving Paper Companies would "withhold payment" on MMA's accounts receivable until MMA agreed to pay the Irving Railroads and, therefore, those payments acted as "collateral for … a secured credit relationship." The Irving Railroads disagree with that characterization, contending they concurrently exchanged wire transfers of cash with MMA on the settlement date and, therefore, the arrangement was a "cash swap." The bankruptcy court referred to the arrangement as a

able owed by the Irving Paper Companies to MMA for freight services provided by MMA to the Irving Paper Companies; (2) accounts payable owed to MMA by the Irving Railroads for interline freight services provided by MMA; and (3) accounts receivable owed by MMA to the Irving Railroads for interline freight services provided by them. Under this arrangement, the parties would determine, based upon the payment terms in effect between them, the amounts due from the Irving Railroads and the Irving Paper Companies to MMA, and the amounts due from MMA to the Irving Railroads, and then concurrently exchange cash payments in the agreed upon amounts. Initially, the amounts owed to MMA by the Irving Railroads and the Irving Paper Companies each week greatly exceeded the amounts owed by MMA to the Irving Railroads. Mr. Hansen explained the reason for entering into this arrangement as follows: "I was determined that I was not going to take a credit risk, I was not relying on their credit to [e]nsure we got paid."

D. The Agreement Regarding Oil Shipments

The payment swap arrangement worked well until the volume of crude oil shipments carried by MMA and interchanged with the Irving Railroads for delivery to refineries in St. John, New Brunswick began to increase significantly in 2012. In the two years leading up to the bankruptcy filing, MMA benefited from the increased use of trains to move oil from the central and

"weekly payment swap system," finding the transfers were done "virtually simultaneously." At the hearing, Mr. Hansen testified that if MMA did not pay, he would have "held the wire" but he would not have offset the amount owed by MMA from the amounts the Irving Paper Companies owed MMA because it was "too messy" from an accounting perspective.

western regions of the United States to refineries in the east. United States and Canadian oil drillers were producing oil faster than the new pipelines could be built, and trains were needed to transport crude oil to refineries. During this time, MMA was hauling 500,000 barrels of oil monthly through Québec and Maine. For the majority of such oil shipments, the originating railroad was Canadian Pacific Railway Company and its affiliates ("CP"), which participated in the ISS. CP was the first railroad to haul the oil, and the shipment would then travel across the country over a number of railway lines until it eventually interchanged with MMA. MMA would haul the oil over its lines and then interchange the freight with the Irving Railroads, which delivered the oil to its final destination at the Irving Oil refinery in St. John, New Brunswick.[7]

The payments for the oil shipments were processed through the ISS. Because the Irving Railroads were not members of the ISS, they could not collect from the ISS for their share of freight interline charges. Rather, the ISS paid MMA, and MMA paid the Irving Railroads pursuant to the terms of their payment arrangement.

Typically, MMA did not receive payments through the ISS until 45 to 60 days following the shipments. Under the terms of payment in effect with the Irving Railroads, however, MMA was obligated to pay the Irving Railroads its share of the freight charges for oil shipments within 33 days of shipment. This was not a problem when the Irving Paper Companies owed MMA more than MMA owed them. But eventually, due to the significant increase in oil shipments carried by

[7] It is undisputed that Irving Oil is not affiliated with the Irving Railroads or the Irving Paper Companies.

MMA and interchanged with the Irving Railroads for delivery to St. John, New Brunswick, the amounts owed by MMA for interline freight services provided by the Irving Railroads began to exceed the amounts owed by the Irving Paper Companies to MMA, and MMA did not have enough cash to make the simultaneous payments under the swap arrangement.

In order to address this situation, in July 2012, the parties agreed MMA would pay the Irving Railroads for their share of freight charges earned in connection with oil shipments promptly upon MMA's receipt of payment from the ISS, and in no event later than five days thereafter. According to the Irving Railroads, the amounts owed to them for interline freight charges incurred in connection with oil shipments were "carved out of the swap arrangement, and instead, those charges would be paid to the Irving Railroads upon MMA's receipt of payment from the ISS of the amounts owed to MMA for such shipments." As to "local" shipments (those which were originated either by MMA and interchanged with the Irving Railroads, or those originated by the Irving Railroads and interchanged with MMA), the swap arrangement remained in effect.

II. THE DERAILMENT AND MMA'S BANKRUPTCY FILING

On July 6, 2013, an unmanned train operated by MMA containing 72 tank cars filled with crude oil derailed in Lac-Mégantic, Québec, causing several large explosions, the death of 47 people, and significant property and environmental damage. After the derailment, train activity was temporarily halted between Maine and Québec, resulting in the immediate loss of most of MMA's freight business and a drastic fall in MMA's gross revenues.

On August 7, 2013, MMA filed a chapter 11 petition in the U.S. Bankruptcy Court for the District of Maine, and the Appellant was subsequently appointed as the chapter 11 trustee. On January 24, 2014, the bankruptcy court entered an order approving the sale of substantially all of MMA's assets as a going concern to Railroad Acquisition Holdings LLC. The sale of MMA's assets closed on May 15, 2014.

On June 13, 2014, MNR and NBSR timely filed proofs of claim (collectively, the "Claims").[8] In Claim 259-1, NBSR asserted claims in the aggregate amount of $2,164,471.30 arising from "[f]reight services provided to [MMA] in connection with interline rail shipments." Of the total amount claimed, NBSR asserted not less than $1,971,834.67 was "secured by equitable liens against all property of [MMA] under the Six Month[s] Rule applicable in federal court receiverships, and [we]re entitled to priority pursuant to 11 U.S.C. § 1171(b)," because such claims: (1) related to current operating expenses incurred by MMA that were necessary for the on-going operation of MMA's railroad; (2) were incurred within six months prior to the commencement of MMA's bankruptcy case; and (3) were for services provided by NBSR with the expectation they would be paid out of current operating revenue and not in reliance on MMA's general credit.

[8] MNR also filed Proof of Claim No. 242-1, which was identical to Claim 257-1, and NBSR filed Proof of Claim 243-1, which was identical to Claim 259-1. The Appellant objected to Claim Nos. 242-1 and 243-1 on the grounds that they were duplicate claims and should be disallowed in their entirety. Prior to the hearing on the Appellant's objection, MNR and NBSR withdrew the duplicate claims. Therefore, they were not at issue before the bankruptcy court, and are not at issue in this appeal.

In Claim 257-1, MNR asserted claims in the aggregate amount of $355,101.19 arising from "[f]reight services provided to [MMA] in connection with interline rail shipments." Of the total amount claimed, MNR asserted approximately $167,228.89 was entitled to priority (b) for the same reasons advanced by NBSR in under § 1171Claim 259-1.

On July 16, 2015, the Appellant filed the Plan and Revised First Amended Disclosure Statement ("Disclosure Statement").[9] The Irving Railroads objected to confirmation of the Plan arguing, among other things, that it failed to provide the same treatment for allowed § 1171(b) claims as it provided for administrative expense claims—i.e., payment in full following confirmation of the Plan.

On October 9, 2015, the bankruptcy court entered an order confirming the Plan ("Confirmation Order"). The Confirmation Order provided, in relevant part:

> In resolution of the [Irving Railroads'] Objection, any 1171(b) Claims of the [Irving Railroads] shall be paid in full, in Cash, on the later of the Initial Distribution date or thirty (30) days after the date such Claims become Allowed Claims. In the event the Bankruptcy Court has not determined, prior to the Initial Distribution Date, the existence of and/or the amount of any Allowed 1171(b) Claims of the [Irving Railroads], if any, as of such date, the Trustee shall set aside, and not distribute pend-

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[9] In the Disclosure Statement, the Appellant indicated that the Plan was a plan of liquidation of MMA's assets, as well as a plan which created and distributed a substantial settlement fund for the benefit of all victims of the derailment.

> ing further order of the Bankruptcy Court making such determination, $2,139,063.56 to secure any payment, to the extent required, with respect to such Allowed 1171(b) Claims, when and if determined.

On October 19, 2015, the Appellant filed an objection to the Claims (the "Claims Objection"), on the ground they were improperly asserted as priority claims and should be allowed only as general unsecured claims.

Specifically, the Appellant argued, "as a matter of controlling law in this circuit," pre-petition interline freight claims of the type asserted by the Irving Railroads are general unsecured claims and do not qualify as six months claims entitled to priority under § 1171(b), citing *In re Boston & Maine Corp.*, 600 F.2d 307 (1st Cir. 1979) ("*Boston & Maine I*"). The Appellant also argued, in furnishing services to MMA, the Irving Railroads relied—not on MMA's operating revenues at the time the service was provided—but upon MMA's general credit and, as a consequence, their claims were not entitled to priority as § 1171(b) claims, citing *In re Boston & Maine Corp.*, 634 F.2d 1359 (1st Cir. 1980) ("*Boston & Maine II*").

In their response ("Irving Railroads' Response"), the Irving Railroads argued *Boston & Maine I* was not applicable or controlling law on the issue because the court did not decide, or even address, the issue of whether interline freight claims qualify as six months claims entitled to priority in a railroad reorganization; rather, *Boston & Maine I* only addressed the question of the timing of the payment of such claims. The Irving Railroads also contended the question of whether the interline freight claims asserted in *Boston & Maine I*

were entitled to treatment as priority claims under the plan of reorganization was addressed by the U.S. Court of Appeals for the First Circuit in the subsequent case of *Boston & Maine II*. According to the Irving Railroads, in *Boston & Maine II*, the First Circuit reversed a decision of the district court ruling those claims should be treated as general unsecured claims, holding instead that per diem claims, such as those asserted by the interlining railroads, constituted six months claims entitled to priority, if such claims: (1) represented a current operating expense necessarily incurred; (2) were incurred within six months before the reorganization petition was filed; and (3) the goods or services were delivered in the expectation that they would be paid for out of current operating revenues of the railroad, and not in reliance on the railroad's general credit. And, the Irving Railroads maintained, the evidence clearly established the Claims satisfied the test articulated in *Boston & Maine II*.

On November 19, 2015, the parties filed stipulations with respect to the Claims Objection, in which they stipulated to certain facts and agreed the only issue to be addressed at the hearing on the Claims Objection was whether the Claims qualified as six months claims entitled to priority under § 1171(b); the amount of such Claims would be determined at a subsequent hearing, if required.

On November 20, 2015, the bankruptcy court held an evidentiary hearing during which Mr. Hansen and Mr. Simpson testified. Following the hearing, the bankruptcy court took the matter under advisement, and directed the parties to submit post-trial briefs. Both parties filed post-trial briefs on December 10, 2015.

On February 5, 2016, the bankruptcy court issued oral findings of fact and conclusions of law, determining the Claims were entitled to priority as six months claims under § 1171(b). In its ruling, the bankruptcy court rejected the Appellant's contention that claims arising from interline freight services cannot, as a matter of law, qualify for priority under § 1171(b), stating:

> I read *Boston [&] Maine II* to have reversed the decision of the District Court, which denied priority treatment of the claims of interlining railroads which sought six-month priority status for their per diem claims. … [A]s a matter of law, the mere fact that the claims are for interline freight services does not exclude them from possible priority consideration.

The bankruptcy court then stated "if the claimant railways can satisfy the judicially established three elements required for the 1171(b) claims [set forth in *Boston & Maine II*], then they're entitled to priority treatment." Turning to the evidence, the bankruptcy court found the Claims satisfied each of the elements of the *Boston & Maine II* test.

As to the "necessity of the charges," the bankruptcy court looked at the testimony of Mr. Hansen and Mr. Simpson regarding the importance of the "critical rail artery" between St. John, New Brunswick and Montréal to MMA and found MMA's inability to interchange traffic with the Irving Railroads on that route would have had a significant adverse effect on MMA's operations, including possible loss of business with Irving Paper Companies as well as a reduction in revenue. As to this prong, the bankruptcy court concluded:

> Based upon this and the other evidence adduced at the hearing, I conclude that the claim-

> ant railways satisfied their burden on the necessity issue. I don't ascribe to the narrow view of what a necessity is. I find that [ ] sufficient claims are for a current expense, goods and services and [ ] ordinary operation of the rail.

As to the second prong—whether the Claims were incurred within six months before the petition was filed—the bankruptcy court determined there had been "no meaningful challenge" to this asserted element.

As to the third prong—whether the goods or services were delivered in the expectation that they be paid for out of MMA's current operating revenues and not in reliance on MMA's general credit—the bankruptcy court concluded:

> Based on testimony … as well as other evidence presented at the hearing, I conclude that the claimant railways met their burden as to the third element of the 1171(b) claims. Testimony shows that, in order to keep the interchange of services going between the parties, claimant railways agreed to wait for the ISS system to process payment and then to pay … them to MMA before MMA would pay the claimant railways. I do not conclude that this was reliance on MMA's credit, nor do I conclude that this was some sort of special security arrangement which excepts the claimant railways from the protection of the six-months rule.
>
> I didn't find anything in that deal or that arrangement that had incorporated common conditions of the commercial credit, security interests, and the like.

> I do not find that the existence of the Wheeling line of credit changes my conclusion. Mr. Hansen was not aware that MMA had a line of credit with Wheeling, he so testified. Mr. Simpson admitted he was aware of it "anecdotally," but had no knowledge of how it "worked," and was not familiar with it. Nobody, according to the testimony, ever advised Mr. Hansen or Mr. Simpson that MMA's ability to pay claimant railroads was dependent on MMA being able to draw on the Wheeling line of credit.
>
> So based upon the unique facts and my analysis of the equities asserted by MMA, on one hand, and [t]he claimant railroads, on the other, I conclude that the claimant railways have met their burden. The claims shall be allowed as 1171(b) claims.

Thereafter, the bankruptcy court entered the Order, which memorialized its ruling as follows:

> Based upon the unique facts of this matter and the Court's analysis of the equities asserted by MMA, on the one hand, and the [Irving Railroads], on the other, the [Irving Railroads] met their burden of establishing that the Asserted 1171(b) Claims qualify as claims that are entitled to priority under § 1171(b) of the Code because:
>
> > (1) the Asserted 1171(b) Claims represent current operating expenses that were necessarily incurred by MMA in connection with its on-going operations;

> (2) the Asserted 1171(b) Claims were incurred within six months prior to the commencement of this case; and
>
> (3) the services that are the subject of the Asserted 1171(b) Claims were provided to MMA with the expectation that they would be paid for out of the current operating revenues of MMA, and not in reliance on its general creditworthiness.

The Order also provided:

> The Asserted 1171(b) Claims, to the extent allowed, are afforded priority status under § 1171(b). The amount of the Asserted 1171(b) Claims is not determined by this Order, and thus those Asserted 1171(b) Claims are not allowed in any amount at this time. The [Appellant]'s rights to object to the amount of the Asserted 1171(b) Claims are fully reserved.

The Appellant timely filed a notice of appeal of the Order, and a motion for leave to appeal. The Irving Railroads filed a response to the motion for leave to appeal, stating they did not oppose the motion because they agreed the resolution of the pending appeal might advance the final disposition of litigation with the Appellant in several matters pending before the bankruptcy court. In an order dated March 29, 2016, the Panel granted the motion for leave to appeal.[10]

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[10] The Panel exercised its discretion under 28 U.S.C. § 158(a)(3) to hear this interlocutory appeal because the Order involved a controlling issue of law, and because both parties agreed that resolution of this appeal could materially advance the ultimate termination of the claims adjudication process and the preference litigation pending in the bankruptcy court.

JURISDICTION

The Panel has jurisdiction to hear appeals from: (1) final judgments, orders and decrees; or (2) with leave of court, from certain interlocutory orders. 28 U.S.C. § 158(a); *Fleet Data Processing Corp. v. Branch (In re Bank of New Eng. Corp.)*, 218 B.R. 643, 645 (B.A.P. 1st Cir. 1998). A decision is considered final if it "ends the litigation on the merits and leaves nothing for the court to do but execute the judgment." *Id.* at 646 (citations omitted). An interlocutory order, however, "only decides some intervening matter pertaining to the cause, and requires further steps to be taken in order to enable the court to adjudicate the cause on the merits." *Id.* (quoting *In re American Colonial Broad. Corp.*, 758 F.2d 794, 801 (1st Cir. 1985)).

In the Order, the bankruptcy court ruled that the Claims would be afforded priority status under § 1171(b), but it did not determine whether the Claims would be allowed and if so, in what amount. Thus, the Order did not resolve all of the issues relating to the Claims, and is interlocutory. As noted above, however, the Panel exercised its discretion under 28 U.S.C. § 158(a)(3) to hear this interlocutory appeal.

STANDARD OF REVIEW

The Panel reviews a bankruptcy court's findings of fact for clear error and its conclusions of law de novo. *See Castellanos Grp. Law Firm, L.L.C. v. F.D.I.C. (In re MJS Las Croabas Props., Inc.)*, 545 B.R. 401, 417 (B.A.P. 1st Cir. 2016) (citation omitted). The question as to whether the bankruptcy court correctly held, as a matter of law, that interline freight claims may qualify for priority status under § 1171(b) if they satisfy the test adopted by the First Circuit in *Boston & Maine II*

is a legal question which is subject to de novo review. *See United States v. Cushing (In re Cushing)*, 401 B.R. 528, 532 (B.A.P. 1st Cir. 2009); *Morad v. Xifaras (In re Morad)*, 323 B.R. 818, 822 (B.A.P. 1st Cir. 2005). The bankruptcy court's findings that the Claims did, in fact, satisfy each of the elements of the *Boston & Maine II* test are findings of fact subject to review under the clearly erroneous standard and should not be overturned unless this Panel is left with "a 'strong, unyielding belief' that the bankruptcy judge made a mistake." *Sharfarz v. Goguen (In re Goguen)*, 691 F.3d 62, 69 (1st Cir. 2012) (quoting *Cumpiano v. Banco Santander P.R.*, 902 F.2d 148, 152 (1st Cir. 1990)).

DISCUSSION

I. THE LEGAL STANDARD

A. Claims Allowance

Sections 501 and 502 govern the filing and allowance of creditor claims in bankruptcy proceedings. When a debtor files for relief, each creditor is entitled to file a proof of claim against the debtor's estate pursuant to § 501. Section 502(a) provides that a proof of claim filed under § 501 "is deemed allowed, unless a party in interest … objects." 11 U.S.C. § 502(a). When a party in interest objects to a proof of claim, "the court, after notice and a hearing, shall determine the amount of such claim in lawful currency of the United States as of the date of the filing of the petition, and shall allow such claim in such amount," unless one of statutory grounds for disallowance applies. 11 U.S.C. § 502(b).

"A proof of claim executed and filed in accordance with these rules shall constitute prima facie evidence of the validity and amount of the claim." Fed. R. Bankr.

P. 3001(f); *see also In re Long*, 353 B.R. 1, 13 (Bankr. D. Mass. 2006) (citing *Juniper Dev. Grp. v. Kahn (In re Hemingway Transp., Inc.)*, 993 F.2d 915, 925 (1st Cir. 1993)). In order to rebut this prima facie evidence, the objecting party must produce "substantial evidence" in opposition to it. *See In re Perron*, 474 B.R. 310, 313 (Bankr. D. Me. 2012) (citations omitted); *In re Long*, 353 B.R. at 13; *see also Am. Express Bank, FSB v. Askenaizer (In re Plourde)*, 418 B.R. 495, 504 (B.A.P. 1st Cir. 2009); *United States v. Clifford (In re Clifford)*, 255 B.R. 258, 262 (D. Mass. 2000). If the objecting party produces substantial evidence in opposition to the proof of claim and thereby rebuts the prima facie evidence, the burden shifts to the claimant to establish the validity of its claim by a preponderance of the evidence. *In re Long*, 353 B.R. at 13 (citing *Hemingway Transport*, 993 F.2d at 925); *In re Plourde*, 418 B.R. at 504 (citations omitted).

Here, the Irving Railroads asserted unsecured claims, a portion of which they claimed were entitled to priority under § 1171(b). The Appellant did not challenge the Irving Railroads' assertion of unsecured claims, but rather the priority asserted in the Claims.[11] The bankruptcy court determined the Appellant put forth sufficient evidence to negate the prima facie validity of the Claims and the priority asserted for the Claims, and, therefore, the burden was on the Irving Railroads to establish that the Claims were entitled to priority under § 1171(b).

[11] Pursuant to the Order, the Appellant also reserved his right to object to the amount of the Claims.

B. Claims Entitled to Priority Under § 1171(b)

A fundamental principle of bankruptcy law requires that all unsecured creditors of an equal class be treated in a like manner throughout the bankruptcy proceeding. *See In re CoServ, L.L.C.*, 273 B.R. 487, 494 (Bankr. N.D. Tex. 2002) ("[T]he entire scheme of the Bankruptcy Code favors equal (and simultaneous) treatment of equal allowed claims."). Thus, payments to unsecured creditors are distributed according to the priority schemes set forth in the Bankruptcy Code. Section 507 specifies the kinds of unsecured claims that are entitled to priority in distribution and the order of such priority. In chapter 11 cases, priority claims must be paid in full in order to confirm a reorganization plan. *See* 11 U.S.C. § 1129(a)(9). Although § 507 is the designated section governing priorities upon distribution of assets to unsecured creditors, however, other sections of the Bankruptcy Code relate to and may have an effect on these priorities. One such section is § 1171(b), which accords certain claims the same priority in railroad reorganization cases as would be recognized if a receiver in equity had been appointed. Section 1171(b) provides:

> Any unsecured claim against the debtor that would have been entitled to priority if a receiver in equity of the property of the debtor had been appointed by a Federal court on the date of the order for relief under this title shall be entitled to the same priority in the case under this chapter.

11 U.S.C. § 1171(b).

Section 1171(b) codified a long-established equitable doctrine referred to as the "Six Months Rule" which developed in railroad receivership cases based on the practice of allowing railroad receivers to pay certain

necessary expenses incurred in the period immediately preceding the receivership. *See Boston & Maine II*, 634 F.2d at 1366-1379. Under the Six Months Rule, railroad receivers were entitled to pay the unpaid claims of operations creditors arising in the six months preceding the reorganization before paying mortgagees and secured creditors, giving these claims a priority status. "The justification for [the] doctrine was that it would be inequitable to operating creditors, supplying the necessary services and products for the railroad's continued existence and revenue generation, if the resulting operating revenue benefited secured creditors, who were not entitled to the operating revenue of the railroad until a receiver was appointed." *In re Jeans.com, Inc.*, 502 B.R. 250, 253 (Bankr. D.P.R. 2013) (citation omitted) (internal quotations omitted). "In essence, the rule gave pre-bankruptcy unsecured claims of vendors and other operating creditors that arose within six months before the receivership priority in payment over secured creditors." *Id.* (citation omitted) (internal quotations omitted).

The Six Months Rule was given statutory recognition in § 77(b) of the Bankruptcy Act of 1898 ("Bankruptcy Act"), 11 U.S.C. § 205(b) (repealed 1976), and then codified in § 1171(b) of the Bankruptcy Code.[12] Although the statute does not expressly mention the

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[12] The language of § 1171(b) is substantively the same as that of § 77(b) for the former Bankruptcy Act. Moreover, the legislative history of this section indicates that it is an expansion of the priorities afforded under § 507. The Senate Report on § 1171(b) indicates that the priority traditionally accorded by § 77(b) of the former Bankruptcy Act is a priority for "claims by rail creditors for necessary services rendered during the 6 months preceding the filing of the petition in bankruptcy." S. Rep. No. 95-989, 95th Cong. 2d Sess. at 135, 136 (1978).

Six Months Rule, it is well settled that § 1171(b) makes the doctrine applicable to railroad reorganizations and the prior equity receivership law survived enactment of the statute. *See B & W Enters., Inc. v. Goodman Oil Co. (In re B & W Enters., Inc.)*, 713 F.2d 534, 536 (9th Cir. 1983) ("[T]here is little doubt that Congress intended that § 1171(b) operate to continue the Six Months Rule in granting certain creditors priority.") (citing H.R. Doc. No. 137, 93d Cong., 1st Sess. 424 (1978); *Boston & Maine II*, 634 F.2d at 1379-80 n.35; Alan N. Resnick and Henry J, Sommer, 5 *Collier on Bankruptcy* ¶ 1171.02 (15th ed. 1979)). Thus, the claims entitled to priority under § 1171(b) are often referred to as "six months claims."

Section 1171(b) does not, however, set forth the terms or conditions which give rise to a priority for six months claims. Thus, it was left to the courts to "'determine the precise contours of the priority recognized by this subsection'" in each case. *In re Michigan Interstate Ry. Co.*, 87 B.R. 921, 926 (Bankr. E.D. Mich. 1988) (quoting H.R. Rep. No. 95-595, 95th Cong. 1st Sess. at 424 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5787, 6380). Here, the bankruptcy court determined the First Circuit's decision in *Boston & Maine II* sets forth the applicable standard for determining whether a claim is entitled to priority as a six months claim under § 1171(b). Thus, we turn to the First Circuit's two opinions in the Boston & Maine Corp. case.

C. The Boston & Maine Corp. Decisions

The First Circuit addressed interline claims in two appeals arising from the reorganization of the Boston & Maine Corp., formerly known as the Boston & Maine Railroad Co. The first decision, *Boston & Maine I*, involved an appeal from the district court's refusal to order

immediate payment of pre-petition "per diem" charges owed to certain interline carriers.[13] 600 F.2d at 307. During the course of a 15-year dispute over the reasonableness of the per diem charges, the Interstate Commerce Commission (the "ICC") entered an order establishing the per diem rates that could properly be charged for the period from 1953 through August 1, 1969, and directing that interlining railroads pay per diem charges at the prescribed rates from August 1, 1969 onward.

After Boston & Maine Corp. filed its bankruptcy petition on March 12, 1970, several of its interline carriers sought an order compelling the trustee to pay immediately: (1) the difference between what Boston & Maine Corp. had actually paid for per diem charges that had accrued prior to August 1, 1969, and what should have been paid under the rates established by the ICC; and (2) per diem charges accruing on and after August 1, 1969 at the prescribed rates. The interline carriers argued that because the trustee's operation of Boston & Maine Corp. was subject to the jurisdiction of the ICC, and because the ICC had established the rates and had ordered payment of the charges at specific times, neither the trustee nor the court had discretion to defer their payment. *Id*. at 308.

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[13] The practice of "interlining" freight cars means loaning cars to one another rather than loading and unloading freight every time a shipment passes onto rails belonging to a different railroad. *Boston & Maine I*, 600 F.2d at 307. "Per diem" charges are charges owed by one railroad to another railroad for the use of that railroad's cars in connection with the interline shipment of freight. *Id*. The Appellant conceded below that per diem charges and interline freight charges are functionally equivalent for purposes of determining priority under § 1171(b). *See* Trustee's Claims Objection at 10 ("Interline rail shipments are in the nature of 'per diem' charges under an interline settlement system like the ISS."). Thus, the Boston & Maine Corp. decisions are relevant to our inquiry.

The First Circuit rejected the interline carriers' argument, finding "there is no specific provision in either the Bankruptcy Act or the Interstate Commerce Act giving the ICC the power to override the reorganization court's discretion in setting the time for payment of claims against the estate." *Id.* at 310. Citing with approval the Third Circuit's decision in *In re Penn Central Transportation Co.*, 553 F.2d 12 (3d Cir. 1977), the court held that the "'countless financial and operating exigencies'" that arise on a daily basis in a reorganization proceeding mandate that the reorganization court be free to exercise its discretion in approving payments of pre-petition obligations during the course of the proceeding. *Boston & Maine I*, 600 F.2d at 311-12. Based upon the circumstances present in the Boston & Maine Corp. reorganization, the court held that the district court had not abused its discretion in refusing to order the immediate payment of the pre-petition per diem charges. *Id.* The First Circuit did not address whether the pre-petition per diem claims of the interline carriers would qualify for priority status as six months claims under a plan of reorganization as might be eventually proposed in the case.

The same per diem claims were again before the First Circuit in *Boston & Maine II*. In that case, the interline carriers, having lost the right to immediate payment of their per diem claims at the outset of the bankruptcy, sought, among other things, priority in Boston & Maine Corp.'s plan of reorganization for $3,000,000 of their claims that had accrued within six months of bankruptcy. The district court determined their claims were not entitled to priority. *See In re Boston & Me. Corp.*, 468 F. Supp. 996 (D. Mass. 1979). In rejecting the interline carriers' claims of priority, the district court relied upon a line of authorities that had

evolved from the Supreme Court's decision in *Fosdick v. Schall*, 99 U.S. 235 (1879), which held that in order to qualify for priority as a six months claim, the claimant was required to establish, among other things, that the debtor railroad had generated a "current debt fund" (i.e., current earnings in excess of operating expenses) out of which priority payments could be made. 468 F. Supp. at 1002. Finding that no current debt fund existed, the district court held the interline carriers' claims did not qualify for priority under the Six Months Rule. *Id.* at 1008. The interline carriers appealed.

Following a lengthy review of the relevant case law interpreting the equity receivership rules that had developed in railroad receiverships and incorporated in § 77(b) of the Bankruptcy Act, the First Circuit reversed, and ruled that per diem claims of interline carriers may be entitled to priority under the Six Months Rule without regard to a current debt fund. Relying upon a separate line of cases interpreting the Supreme Court's decision in *Miltenberger v. Logansport Railway Co.*, 106 U.S. 286 (1882),[14] the First Circuit held that

[14] *Miltenberger* is the seminal case on the Necessity of Payment Rule, which is another principle of railroad receiverships and is often confused with the Six Months Rule. Whereas the Six Months Rule is a rule of priority, the Necessity of Payment Rule is one of payment. *See In re Boston & Me. Corp.*, 468 F. Supp. at 1008. This rule developed to allow trustees to pay pre-petition debts under threats of creditors in order to obtain continued supplies or services essential to the continued operation of the debtor's business. *See In re B & W Enters., Inc.*, 713 F.2d at 537. *Miltenberger* involved an appeal of an order directing a railroad receiver's immediate payment of certain pre-receivership claims. In *Miltenberger*, interline railroads threatened to cease furnishing supplies and interline traffic exchanges unless the railroad receiver immediately paid pre-receivership claims. The Supreme Court affirmed the circuit court order directing the railroad receiver to pay the pre-receivership claims prior to reorganization. In ap-

the district court had incorrectly required, in addition to these criteria, the existence of a current debt fund as prerequisite for according priority to these types of six months claims, stating:

> In any event, it must be concluded that the class of creditors entitled to the priority contemplated by Section 77(b) [of the Bankruptcy Act], is not limited to participation in the current debt (expense) fund defined in terms of *Fosdick* equitable restitution, but extends to participation in reorganization railway operating revenues essentially on the same basis as administration expenses incurred during the reorganization period.

Boston & Maine II, 634 F.2d at 1380. As the First Circuit noted: "*Miltenberger* [wa]s concerned, not with the 'diversion' [debt fund] precept of *Fosdick*, but with the more general authority of the receivership court to accord priority status to pre-receivership claims in order to prevent the stoppage of a business impressed with the public interest." *Id.* at 1370. Thus, the First Circuit ruled that the per diem claims of the interline carriers were entitled to priority as six months claims if each such claim met the following three criteria:

> (1) it represent[ed] a current operating expense necessarily incurred, (2) was incurred within six months before the reorganization petition was filed, and (3) the goods or services were de-

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proving the payments, the Court gave the following justification: "Many circumstances may exist which may make it necessary and indispensable to the business of the road and the preservation of the property, for the receiver to pay pre-existing debts … where a stoppage of the continuance of such business relations would be a probable result, in case of non-payment." 106 U.S. at 312.

> livered in the expectation that they would be paid for out of current operating revenues of the railroad, and not in reliance on the [rail]road's general credit … .

Id.[15]

In its opinion, the First Circuit specifically identified "interline claims" as a type of claim which could qualify for priority as a six months claim, referring to the possible "stoppage of traffic interchange" as one of the "disastrous consequences" of failing to pay such claims. *Id.* at 1377-78. The court also cited with approval a number of cases which recognized interline freight claims as quintessential examples of six months claims. For example, the First Circuit cited *Southern Ry. Co. v. Flournoy*, 301 F.2d 847 (4th Cir. 1962), in which the Fourth Circuit emphasized that, from *Miltenberger* forward, "public concern with the continued operation of the railroad has been a factor supporting the priority accorded general creditors." 634 F.2d at 1375. The Fourth Circuit accorded interline traffic balances and other interline accounts a priority over the mortgage bondholders, treating the six month limitation as preventing operating claims from undermining the mortgage through secret liens. *Id.* The First Circuit also cited *Finance Co. v. Charleston, C. & C. R. Co.*, 62 F. 205, 208 (4th Cir. 1894), in which the court held that interline claims for freight and freight balanc-

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[15] Other courts have similarly recognized these three criteria for priority as a six months claim. *See, e.g., In re Mich. Interstate Ry. Co.*, 87 B.R. at 922-26; *see also In re New York, New Haven & Hartford. R.R. Co.*, 278 F. Supp. 592, 596 (D. Conn. 1967). Courts differ, however, as to whether claimants are entitled to establish any additional elements, such as the existence of a "current debt fund" as set forth in *Fosdick* and its progeny.

es could be given priority depending upon the facts and circumstances of the particular case, and the character of the claims. 634 F.2d at 1371-72. And the First Circuit noted that in *In re Tenn. Cent. Ry. Co.*, 316 F. Supp. 1103, 1110 (M.D. Tenn. 1970), *vacated on other grounds*, 463 F.2d 73 (6th Cir. 1972), the court accorded a priority for claims for interline freight balances, relying in part on the special character of interline freight balances as collections for which the railroad had to account to connecting carriers. 634 F.2d at 1376.

Having found that the district court had failed to apply the correct legal standard in considering whether the interline carriers' per diem claims were to be accorded priority as six months claims, the First Circuit remanded the case for further proceedings consistent with its opinion. *Id.* at 1382. On remand, the district court held, "in accordance with the principles in *Boston & Maine [II]*," that the interline carriers' per diem claims in the amount of $3,000,000 were to be treated as six months priority claims in the railroad's plan of reorganization, and were to be paid in full and in cash on the effective date of the plan. *See In re Boston & Me. Corp.*, 46 B.R. 930, 941, 956 (D. Mass. 1983).

In this case, the bankruptcy court held that the three-part test set forth in *Boston & Maine II* is the applicable standard in the First Circuit for determining whether the Claims were entitled to priority as six months claims under § 1171(b). Turning to the evidence, the bankruptcy court found the Claims satisfied each element of that test. The Appellant argues, however, that the Claims are not entitled to priority under § 1171(b) for several reasons. First, he argues that interline freight claims of the type asserted by the Irving Railroads are not eligible, as a matter of law, for priority under § 1171(b). Second, the Appellant contends the

bankruptcy court applied incorrect legal standards and made clearly erroneous findings of fact when it determined the Claims met the three criteria set forth in *Boston & Maine II*.

II. WHETHER THE BANKRUPTCY COURT ERRED IN FAILING TO RULE THAT INTERLINE CHARGES ARE NOT ELIGIBLE, AS A MATTER OF LAW, FOR PRIORITY UNDER § 1171(B)?

The Appellant argues that under post-Bankruptcy Code law, interline charges are general unsecured claims that are not eligible, as a matter of law, for priority under § 1171(b). In support, he relies on three decisions: *Union Pac. R.R. Co. v. Moritz (In re Iowa R.R. Co.)*, 840 F.2d 535 (7th Cir. 1988) ("*Iowa Railroad*"); *Howard v. Burlington N. & Santa Fe Ry. Co. (In re Bangor & Aroostook R.R. Co.)*, 320 B.R. 226 (Bankr. D. Me. 2005), *aff'd*, No. 06-141-B-H, 2007 WL 607867 (D. Me. Feb. 23, 2007) ("*Bangor & Aroostook*"); and *In re McLean Indus. Inc.*, 103 B.R. 424 (Bankr. S.D.N.Y. 1989) ("*McLean Industries*"). The Appellant, however, fails to acknowledge that the First Circuit in *Boston & Maine II* specifically identified "interline claims" as one type of claim which may be eligible for priority as a six months claim if certain requirements are met. Moreover, the cases cited by the Appellant do not stand for the proposition that interline charges are ineligible, as a matter of law, for priority under § 1171(b).

In *Iowa Railroad*, the court addressed whether interline balances were trust funds which the debtor railroad was obligated to turn over to the interline carriers, or whether they were debt obligations owed to the carriers. The Seventh Circuit reversed the lower court's ruling that the interline freight balances were trust funds, holding instead that the relationship of the

bankrupt railroad with its interline carriers was that of debtor and creditor. In so holding, the court observed:

> Interline operations have been common since the founding of American roads, so the treatment of interline balances also is an old subject. *See Miltenberger v. Logansport Ry.*, 106 U.S. 286, 293, 1 S. Ct. 140, 27 L. Ed. 117 (1882). Until 1933, when Congress added § 77 to the old Code, 11 U.S.C. § 205 (1976), all railroad bankruptcies were handled as equity receiverships … The rules for equity receiverships permitted courts to enhance the priority of debts incurred as operating expenses within the six months prior to insolvency or necessary to the continued operation of the debtor. *See Miltenberger*, 106 U.S. at 311. Courts applied these principles, without extended discussion, to interline balances. This approach assumed that interline balances are general, unsecured debts. Not until 1967 did any interline creditor argue that the balances are "trust funds" or otherwise entitled to priority exceeding that available to other operating expenses.

840 F.2d at 537 (citations omitted).

The court's reference to the historical assumption that interline balances are "general, unsecured debts" does not, however, establish a per se rule that those debts are ineligible for priority under current case law. Moreover, the court characterized interline balances as "general, unsecured debts" when rejecting the assertion that they should be viewed as trust funds which the debtor was obligated to immediately turn over to the interline carriers. The *Iowa Railroad* court did not address whether the unsecured debts owed to interline

freight carriers might qualify for priority under § 1171(b), and a "per se" ineligibility rule is an unwarranted interpretation of the court's discussion.

Similarly, the *Bangor & Aroostook* court did not address whether interline freight claims qualify for priority under § 1171(b). In *Bangor & Aroostook*, the trustee brought a preference action against a number of interline carriers which, through setoffs exercised within 90 days prior to the commencement of bankruptcy, had collected freight charges owed to them by the debtor. The interline carriers moved for summary judgment on the basis that the interline freight balances owed to them were trust funds. The court, relying in large part on *Iowa Railroad*, held that the interline carriers were "creditors, rather than trust beneficiaries" and denied their motions for summary judgment. 320 B.R. at 242. The court did not discuss whether the interline claims at issue might qualify for priority under § 1171(b). The Appellant argues, however, that if the *Bangor & Aroostook* court believed the interline creditors held priority six months claims, "the court would have granted the interline creditor[s] summary judgment." By declining to grant summary judgment, the Appellant infers that the court determined the interline creditors to have general unsecured claims as a matter of law. Such an argument is based on mere conjecture and lacks merit. Preference actions are rarely decided on a motion for summary judgment due to their factual nature, and, therefore, the *Bangor & Aroostook* court's failure to grant summary judgment is not support for a rule that interline creditors were ineligible, as a matter of law, to assert priority as six months claims.

The Appellant's reliance on *McLean Industries* also is misplaced. The debtor in *McLean Industries* was a steamship company, not a railroad, and therefore, the

court held, § 1171(b) did not apply to the claims in that case. Thus, McLean Industries stands for the proposition that the Six Months Rule of priority does not apply in a non-railroad chapter 11 case. The Appellant, however, focuses upon the following dicta in the opinion to support his contention that in enacting the current version of the Bankruptcy Code, Congress "addressed and rejected the priority that the Bankruptcy Court afforded the Irving Railroads."

> Congress, in enacting the Bankruptcy Code, expressly rejected a proposal that debtor railroads be required to pay interline balances stating that to do so would distort the central bankruptcy principle of equality of treatment of unsecured creditors.

103 B.R. at 426 (citation omitted).

From that statement, the Appellant concludes that Congress rejected § 1171(b) priority for interline freight claims. The Appellant's interpretation, however, reflects his misreading of the legislative history leading up to enactment of the Bankruptcy Code. The relevant legislative history demonstrates Congress did not reject a proposal establishing priority status for interline freight claims.[16]

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[16] "[C]ourts must presume that a legislature says in a statute what it means and means in a statute what it says there." *Conn. Nat'l Bank v. Germain*, 503 U.S. 249, 253-54 (1992) (collecting authorities). Thus, if the statutory language is unambiguous, the court need not resort to legislative history to construe the plain text of the statute. Where statutory language is ambiguous, however, courts look to the statute's "historical context, its legislative history, and the underlying policies that animate its provisions" to determine legislative intent. *Marrama v. Citizens Bank of Mass. (In re Marrama)*, 430 F.3d 474, 480 (1st Cir. 2005) (quoting *United States v. Yellin (In re Weinstein)*, 272 F.3d 39, 48 (1st Cir. 2001)),

Prior to the enactment of the Bankruptcy Code, there was a split among the circuits on the question of whether a railroad reorganization trustee had authority, without first seeking court approval, to pay interline balances when they came due under ICC rules. In *In re Penn Central Transp. Co.*, 486 F.2d 519 (3d Cir. 1973), and later in *In re Penn Central Transp. Co.*, *supra*, the Third Circuit held that a trustee was not empowered to make immediate payment of interline balances absent authorization from the court. The Seventh Circuit came to the opposite conclusion in *Chicago, Rock Island & Pacific R.R. Co. v. Atchison, Topeka & Santa Fe Railway Co.*, 537 F.2d 906 (7th Cir. 1976) ("*Rock Island*"), holding that a trustee is bound by ICC rules to pay interline claims immediately as they come due, without the need for court authorization.

During the legislative process that resulted in the passage of the Bankruptcy Reform Act of 1978, Pub. L. 95-598, Nov. 6, 1978, 92 Stat. 2643, the bankruptcy bill introduced in the Senate, S. 2266, 95th Cong. (1977), contained provisions which would have codified the Seventh Circuit's holding in *Rock Island* by providing authority to a railroad's trustee to pay all pre-bankruptcy interline balances without the need for court approval. The House version of the bankruptcy bill did not contain these provisions and in enacting the Bankruptcy Code the Senate capitulated. As explained by the Seventh Circuit in *Boston & Maine Corp. v. Chicago Pacific Corp.*, 785 F.2d 562 (7th Cir. 1986), which the *McLean Industries* court relied upon when making its statement regarding Congressional intent:

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aff'd, 549 U.S. 365 (2007). As the body of case law reflects, the language of § 1171(b) is not unambiguous and, therefore, it is appropriate to look to the legislative history.

> Congress rejected our holding [in *Rock Island*] that the rules of the ICC, rather than principles of bankruptcy, should govern the question of whether prereorganization per diem charges should be *paid immediately*.

785 F.2d at 568-69 (emphasis added).

The provisions in the Senate bill rejected by Congress in enacting the Bankruptcy Code dealt only with the issue of whether interline charges could be *paid immediately* during the course of the bankruptcy, pursuant to ICC orders or rules, without the need for bankruptcy court approval. *See* S. 2266, § 1169. They did not address the priority to which such claims were entitled under a plan of reorganization, which is the issue to be resolved in this appeal. That issue is addressed by § 1171(b), and the equity receivership rules which Congress incorporated into § 1171(b).

For the reasons set forth above, we are not persuaded by the cases cited by the Appellant and conclude the bankruptcy court did not err when it failed to rule that interline charges are not eligible, as a matter of law, for priority as six months claims under § 1171(b). Rather, the bankruptcy court correctly ruled that the Claims could qualify for priority status under § 1171(b) if they satisfied the three-part test set forth in *Boston & Maine II*.

III. WHETHER THE BANKRUPTCY COURT ERRED IN RULING THAT THE CLAIMS SATISFIED THE *BOSTON & MAINE II* TEST?

The Appellant does not challenge the bankruptcy court's determination that the Irving Railroads met their burden of establishing the Claims were incurred within the six-month period preceding the bankruptcy

filing. Thus, the focus in this appeal is on the other criteria under the *Boston & Maine II* test—whether the Claims were for a good or service, whether they represent current operating expenses necessarily incurred, and whether the services were delivered by the Irving Railroads with the expectation that they would be paid for out of MMA's current operating revenues of the railroad, and not in reliance on MMA's general credit.

A. Were the Claims for a good or service?

The Appellant argues the bankruptcy court erred by failing to consider his argument that the Claims did not involve a "good or service," as required under the *Boston & Maine II* test, and because the Irving Railroads failed to meet their burden of proof on this issue. The Appellant argued below that the Irving Railroads did not provide a "good or service" because MMA's interchange of freight with the Irving Railroads involved nothing more than permission for MMA to use Irving Railroads' tracks for a fee.

Although the bankruptcy court did not expressly address the Appellant's contention in its oral ruling, it found that the Irving Railroads provided freight services to MMA that were more than mere use of their tracks. The bankruptcy court specifically noted Mr. Hansen's testimony at the trial regarding the nature of the freight services provided by the Irving Railroads as they related to oil shipments, finding as follows:

> Beginning in 2012, the amounts owed by MMA for interline freight services provided by the claimant railways began to exceed the amounts owed by Irving to MMA. As Mr. Hansen put it at trial, "Well, the shipment of oil would have been coming out of the Dakotas by [CP]. They

> would hit MMA's line, They would interchange with MMA, Then the oil would come—the train would come down through until it hit NB Southern [NBSR]'s line, *NB Southern [NBSR] would transport it from then into St. John, New Brunswick*."

(emphasis added). Thus, the court expressly acknowledged that the Irving Railroads provided interline freight services to MMA and, specifically, that the Irving Railroads transported freight into St. John, New Brunswick. The bankruptcy court also recognized Mr. Simpson's testimony at the trial regarding "the freight services provided to MMA." Mr. Simpson explained that, with respect to freight carried by MMA to the interchange point with the Irving Railroads, the interchange of freight traffic involved the de-coupling of freight cars from MMA's locomotives and connecting them to the Irving Railroads' locomotives, which then carried the freight cars to their final destination. The bankruptcy court specifically found that Mr. Simpson's "persuasive testimony" regarding the freight services provided to MMA was uncontroverted.

In his brief on appeal, the Appellant reasserts his contention that the freight services which were the basis for the Claims "consisted largely, if not entirely, of use of the track of the Irving Railroads by MMA." He does not, however, point to any evidence to support his contention. Rather, he argues that the bankruptcy court erred because the Claims originated, in part, from MMA's "role as collection agent for the Irving Railroads and its subsequent failure to remit amounts collected," rather than from any good or service provided to MMA.

Although the bankruptcy court did not specifically address this argument in its oral ruling, the issue was squarely determined by the bankruptcy court when it found, based on the evidence presented at the hearing, that the Irving Railroads provided freight services to MMA in accordance with the agreement between the parties. The record supports the bankruptcy court's ruling.

In considering the Appellant's argument that the bankruptcy court erred in this finding, we review how railway freight shipping operates. "The nation's railroads function in many ways as a single system." *In re Penn Cent. Transp. Co.*, 486 F.2d at 521. The *Bangor & Aroostook* court described the system as follows:

> Shipping freight any distance by rail generally requires the services of several railroad lines. Shipments come and go throughout the country, originating and traveling on multiple railroads. Shippers routinely pay one carrier (the "collecting carrier") a charge for the entire journey. That amount includes the charges of each railroad along the way. Thus, with regard to inter-line shipments, each railroad may be at once the collecting carrier for some, receiving funds and accruing obligations to participating carriers; and for others a participating carrier, accruing rights to freight charges for shipments which travel over its rails.

320 B.R. at 228. Under this system, "[e]ach interline freight shipment triggers charges attributable to the services provided by each of several railroads." *Id.* at 231. "The collecting railroad takes in the entire fare—and owes prescribed portions of it to each participating carrier." *Id.* "That there are multiple shipments and

multiple parties is of no moment. The circumstances reduce to sets of bilateral relationships in which one railroad owes freight charges to another, and the second owes freight charges back to the first." *Id.*

The bankruptcy court found that the ISS provides a central clearing house for all participating railroads involved in the interchange of freight traffic among multiple rail carriers to settle accounts receivable and accounts payable arising from the interchange of such traffic. Because the Irving Railroads were not members of the ISS, they needed MMA to serve as their "front man," not only for the purpose of assessing and collecting the total amount of freight charges that otherwise would have been paid directly to the Irving Railroads for its transportation services, but also to negotiate freight rates, make contracts, and provide quotations for services to be rendered. The Commercial Agreement provides clear evidence that the Irving Railroads were providing "transportation services" to MMA. The stated purpose of the Commercial Agreement was "to establish the hauling of freight for MMA." Moreover, Section 2 set forth the agreement between the parties regarding Irving Railroads' "Performance of Transportation Services":

> The parties agree that from and after the Effective Date, [the Irving Railroads] shall move loaded freight cars and associated empty cars between points located on its lines or reached by it under Canadian interswitch rules and Brownville Junction at rates as set out in this Agreement. MMA shall act as the interline tariff carrier on a junction settlement basis. By "junction settlement basis" the parties mean that MMA shall negotiate through rates and make contracts and provide quotations, and

> shall be responsible for car supply to the extent requested by NB[R]S and reasonably available from MMA and in rail cars customarily supplied by railroad carriers, all in accordance with the provisions of this Agreement. MMA shall continue to render one freight bill, and assess and collect the total amount of freight charges … and *remit the portion pertaining to [the Irving Railroads'] transportation services to [the Irving Railroads] in accordance with the procedures in this Agreement.*

(emphasis added). Thus, although MMA acted, in part, as the billing railroad and, therefore, collected payments either directly from the customer or from the ISS, that does not change the nature of the services provided by the Irving Railroads to MMA.

Based on the foregoing, the record supports the bankruptcy court's finding that the Irving Railroads provided services to MMA by shipping freight across its railway lines pursuant to its agreement with MMA, and, therefore, the "freight charges," which are the basis of the Claims, all originated from the Irving Railroads' *service* of shipping freight pursuant to its agreement with MMA. Therefore, the bankruptcy court did not err in finding that the Claims satisfied this requirement of the *Boston & Maine II* test.

B. Were the Claims for "current operating expenses necessarily incurred" by MMA?

To qualify for priority under § 1171(b), the Claims must be for current operating expenses necessarily incurred by MMA in connection with its rail operations. The Appellant asserts an operating expense is "necessary" for purposes of § 1171(b) "when its non-payment

would cause the debtor railroad to cease, or clearly risk cessation of, operations." Thus, the Appellant maintains, claims satisfy this prong of the § 1171(b) test if they arise from goods or services that are "indispensable to the continued performance of the transportation service." The Appellant argues the bankruptcy court applied an improper legal standard because it held that the Claims need only be for "current operating expenses," rather than considering whether the services provided by the Irving Railroads were "indispensable" to MMA's business as a going concern. And, he contends, the services Irving Railroads provided to MMA were not "necessary" or "indispensable" because the Irving Railroads' refusal to interchange freight with MMA would not have shut down MMA's rail operations, and because they were required by ICC rules to accept the interchange of traffic from MMA.

As to the applicable legal standard, the Appellant's articulation of an "end of the world" or "doomsday" standard appears to be at odds with that articulated by the First Circuit in *Boston & Maine II*. In *Boston & Maine II*, the First Circuit indicated the test is not whether the individual claimant has the power to shut down the operation of the railroad, but whether the claim falls within a "class of claims" which are indispensable to the operation of the business. 634 F.2d at 1377-78. In addressing the Supreme Court's decision in *Miltenberger*, which held that interline freight claims were eligible for immediate payment, the First Circuit observed:

> The [*Miltenberger*] Court's rationale excludes the inference that only those creditors are entitled to priority of payment who demand immediate payment as a condition of continuing to supply a service or commodity of which they

> are monopolists. The Court was defining the *classes* of claims payment of which was indispensable to the business of the [rail]road and which, "unless the receiver was authorized to provide for them at once, the business of the [rail]road would suffer great detriment." [106 U.S.] at 311.

Boston & Maine II, 634 F.2d at 1377 (emphasis added) (footnote omitted) (citation omitted).

The First Circuit went on to identify interline claims as one of the "classes of claims" that qualify for priority:

> The [*Miltenberger*] Court's depiction of the disastrous consequences of failing to pay labor claims—a work stoppage—or *interline claims—a stoppage of traffic interchange*—is directed to restricting the class of claims entitled to priority of payment to claims for those goods and services that are indispensable to the continued performance of the transportation service. … *The test is not whether the claimant has the naked power to exert economic duress, but whether the expenses have the characteristics of those that the receiver pays from revenue as expenses of administration.* …

Id. at 1377-78 (emphasis added) (footnote omitted) (citation omitted). Thus, the First Circuit has specifically recognized that the interchanging of freight among railroads is indispensable to the continued performance of a railroad's operations and, therefore, that interline claims such as those asserted in the Claims fall within the "class of claims" which are entitled to priority under § 1171(b). As a result, we conclude the bankruptcy

court did not err by declining to adopt the Appellant's "doomsday" approach to determining whether the Claims were for "current operating expenses necessarily incurred" by MMA.

The bankruptcy court found, based on the testimony of Mr. Hansen and Mr. Simpson, as well as the statements in the Disclosure Statement, that the Irving Railroads met their burden of establishing that the Claims satisfied the "necessity" element of the *Boston & Maine II* test. The evidence supports the bankruptcy court's finding. As the bankruptcy court noted, in the Disclosure Statement, the Appellant acknowledged the importance of the rail route serviced by MMA and the Irving Railroads as being "[t]he shortest rail transportation route between Maine and Montréal and a critical rail artery between Saint John, New Brunswick and Montréal." That route provided outlets for, among others, "major producers of paper, lumber, wood and agricultural products in eastern and northern Maine," and "[i]n-bound transportation for chemicals and other products used by paper producers and consumers in Maine." Thus, there was a public interest in continued rail service along this route. The bankruptcy court also found that the evidence established the importance of that "critical rail artery" to MMA's business operations. As the Appellant explained in the Disclosure Statement:

> In the two years leading up to the commencement of the Chapter 11 case, the Debtor had benefited from the dramatic increased use of trains to move oil from the central and western regions of the United States, specifically, the Bakken oil fields in North Dakota, to refineries in the east. United States and Canadian oil drillers were producing oil faster than new

> pipelines could be built, and trains were needed to transport crude oil to refiners. Prior to the Derailment, the Debtor had been hauling about 500,000 barrels of oil monthly through Québec and Maine. Due to this business, the Debtor enjoyed a significant increase in gross revenue, and, for a short time, positive net operating income, although needed capital expenditures remained deferred and unfunded.

As the bankruptcy court noted, Mr. Simpson confirmed the importance of the rail artery between Montréal and Saint John, New Brunswick to MMA, characterizing it as the most direct, economical and practical route for the shipment of oil to refineries in Saint John, New Brunswick.

The Appellant argues, however, that the services provided by the Irving Railroads were not really necessary to MMA's operations, because if the Irving Railroads refused to accept an interchange of traffic from MMA, there were alternate routes that could have been pursued. The bankruptcy court rejected this argument, however, as the evidence showed that without being able to interchange traffic with the Irving Railroads, MMA lost essentially the entire St. John, New Brunswick market, which is where the oil that was being produced in North Dakota was being transported to over several years, prior to the derailment, and which was a source of tremendous revenue for MMA. If MMA would have been forced to choose alternative routes, they would not have been competitive in terms of being able to successfully obtain the business from the shippers in North Dakota, and they would have lost that particular business. There simply was no practical way for them to deliver the oil to St. John, New Brunswick without interchanging with the Irving Railroads. This

would have had a substantial negative impact on MMA's operations. The bankruptcy court also pointed to testimony at the hearing which established that the inability of MMA to interchange traffic with the Irving Railroads would have had a significant adverse impact on MMA's operations, including, among other things, the loss of business with the Irving Paper Companies, which were among MMA's largest customers, and a substantial reduction in revenue generated from the shipment of oil to the refineries in Saint John, New Brunswick.

The Appellant also argues that the Claims were not "necessary" because the Irving Railroads were required under applicable provisions of federal transportation law to accept the interchange of traffic from MMA. As the First Circuit remarked in *Boston & Maine II*, "the interlining of freight cars is mandatory under the Interstate Commerce Act, 49 U.S.C. [§§] 1(4), (10), (11), (14), (15), and (17)." 634 F.2d at 1362. Notwithstanding the requirement under the Interstate Commerce Act that railroads interline freight cars with Boston & Maine Corp., the First Circuit held their per diem claims were, nonetheless, entitled to priority as six months claims. Thus, the Appellant's argument that the Claims are not entitled to priority status because the Irving Railroads were required to accept the interchange of freight traffic is unpersuasive. Moreover, the inability of a railroad to refuse to interchange freight traffic under the ICC underscores how essential the interchange of freight traffic is to the railroad freight shipping system.

In light of the foregoing, we conclude the bankruptcy court applied the correct legal standard for determining whether the Claims were for operating expenses necessarily incurred in connection with MMA's

rail operations, and the bankruptcy court did not err in determining that the Claims satisfied this part of the test.

C. Did the Irving Railroads deliver services to MMA with the expectation they would be paid from MMA's current operating revenue rather than relying on MMA's creditworthiness?

The Appellant contends the bankruptcy court applied an improper legal standard in determining that the Claims satisfied this part of the § 1171(b) test. According to the Appellant, "creditors with 'special security arrangements' do not benefit from the protections afforded six months creditors because the presence of such arrangements negates any possibility of reliance only upon immediate cash flow." Therefore, he argues, the alleged "triangular setoff" arrangement between the parties establishes, as a matter of law, that the Irving Railroads provided services to MMA in reliance upon MMA's general creditworthiness rather than with the expectation that payment would be made from current operating revenue. He maintains the bankruptcy court applied the wrong standard because it held that to disqualify a claim from § 1171(b) priority status, the "special security arrangement" must qualify as a security interest under the Uniform Commercial Code. The Appellant further argues that, based upon the application of the wrong legal standard, the bankruptcy court erred in finding that the Irving Railroads provided services to MMA with the expectation that payment would be made from current operating revenue, rather than in reliance on MMA's general credit.

Again we turn to *Boston & Maine II* for guidance on the standard to be applied. The First Circuit articulated the standard as follows:

> [W]hen the time comes to determine membership in the class it will be for the reorganization court to determine … whether the nonpayment reflects an intentional extension of credit of the railroad, or the intervention of the reorganization petition before expiration of the ordinary billing and payment period, or some noncontractual indulgence or inadvertence on the part of the claimant, or deferment of payment on the part of the railroad; and whether, if the transaction giving rise to the claim had any credit term, it was compatible with a general expectation of payment from current receipts or indicated reliance on the railroad's general credit.

Id. at 1379-80 (footnote omitted).

The Appellant asserts, however, the bankruptcy court went further, and held, as a matter of law, that the *only* security arrangement that would disqualify a creditor from the protection of § 1171(b) is one in which "the would-be 1171(b) creditor enjoys a 'commercial credit[] security interest[].'" In advancing this argument, the Appellant has misrepresented the bankruptcy court's ruling. In ruling that the Irving Railways had met their burden of establishing that services were provided with the expectation that they would be paid from current operating revenues, as opposed to MMA's general creditworthiness, the bankruptcy court singled out those services related to oil shipments interchanged by MMA with the Irving Railroads, which were not part of the payment swap arrangement, and stated:

> Testimony shows that, in order to keep the interchange of services going between the parties, claimant railways agreed to wait for the

> ISS system to process payment and then to pay—the ISS to pay them to MMA before MMA would pay the claimant railways. I do not conclude that this was reliance on MMA's credit, nor do I conclude that this was some sort of special security arrangement which excepts the claimant railways from the protection of the six-months rule. I didn't find anything in that deal or that arrangement that had incorporated common conditions of the commercial credit, security interests, and the like.

The arrangement the bankruptcy court was discussing was completely separate from the payment swap arrangement that the Appellant characterizes as a "triangular setoff." The bankruptcy court simply found, based on the evidence presented, that nothing in the agreement of the parties covering oil shipments incorporated characteristics of general credit extension or special security arrangements. Thus, the bankruptcy court did not hold as a matter of law that only an Article 9 security interest would disqualify a claim from receiving § 1171(b) priority and, therefore, applied the correct legal standard.

The Appellant also argues that the bankruptcy court ignored the Irving Railroads' extension of credit and clearly erred in finding that they relied on MMA's current operating revenues. The Appellant contends the Irving Railroads knowingly extended credit to MMA and then mitigated the credit risk they willingly assumed by unilaterally establishing a system of triangular setoffs using payables owed to MMA by the Irving Railroads and Irving Paper Companies as collateral to secure the payment of MMA's obligations to the Irving Railroads. He also argues the Irving Railroads relied entirely on that collateral and not on MMA's cash

flow in securing such payments until they found themselves "undercollateralized," at which time they agreed to an additional payment arrangement pursuant to which MMA would collect amounts through the ISS system for their benefit and remit them on agreed credit terms.

Contrary to the Appellant's assertions, the bankruptcy court's findings are supported by the record. The evidence presented at the hearing showed that, from the inception of their business relationship with MMA, the Irving Railroads were not willing to rely on the creditworthiness of MMA, which was the successor to the bankrupt Bangor & Aroostook railroad. Mr. Hansen testified that the Irving Railroads did not in any way rely on MMA's general creditworthiness, stating:

> Q: Mr. Hansen, in providing freight services in connection with the interchange of traffic with the MMA did the Irving [R]ailroads rely upon MMA's general creditworthiness?
>
> A: Absolutely not.
>
> Q: What did the Irving [R]ailroads rely upon?
>
> A: We relied on them being paid out of the ISS system, which I felt was secure, and that meant I would be paid shortly thereafter.
>
> Q: And were you secure that they could rely upon receiving money from the ISS system?
>
> A: That is correct.

The evidence showed MMA acquired its assets from Bangor & Aroostook out of bankruptcy, and there was a troubled history with respect to that railroad. Mr. Hansen testified that, in order to avoid taking any

credit risk, he created a "swap" arrangement with MMA that involved the Irving Paper Companies, which were affiliated with the Irving Railroads and were among the largest customers of MMA. Pursuant to this arrangement, the parties, on a weekly basis, would simultaneously exchange wire transfers of the amounts each owed to the other. Often, the payments for freight services that MMA owed the Irving Railroads actually involved freight from the Irving Paper Companies that was being delivered from their mills in Canada to other destinations. With this arrangement, he stated, the Irving Railroads were not relying on the general creditworthiness of MMA. Rather, the source of the payment for the Irving Railroads was essentially the cash that was being paid to MMA by the Irving Paper Companies. Moreover, Mr. Hansen testified that, although the Irving Railroads may have had the ability to set off the amounts owed to MMA from the amounts MMA owed to it, they never did so.

Thus, the bankruptcy court's findings are supported by the record.

CONCLUSION

For the reasons set forth above, we conclude the bankruptcy court did not err in ruling that the Claims qualified as six months claims entitled to priority under § 1171(b). Thus, we **AFFIRM** the Order.

APPENDIX C

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MAINE

Case No.: 13-10670
Chapter 11

IN RE:
MONTREAL MAINE
&
ATLANTIC RAILWAY, LTD.,

Debtor.

Filed February 26, 2016

ORDER SUSTAINING IN PART AND OVERRULING IN PART TRUSTEE'S OBJECTION TO PROOFS OF CLAIM FILED BY NEW BRUNSWICK SOUTHERN RAILWAY COMPANY LIMITED AND MAINE NORTHERN RAILWAY COMPANY LIMITED ON THE BASIS THAT CERTAIN OF SUCH CLAIMS ARE DUPLICATIVE OF OTHERS, AND SUCH OTHERS ARE IMPROPERLY ASSERTED AS ADMINISTRATIVE AND/OR PRIORITY CLAIMS

This matter came before the Court on the *Trustee's Objection to Proofs of Claim Filed by New Brunswick Southern Railway Company Limited and Maine Northern Railway Company Limited on the Basis that Certain of Such Claims Are Duplicative of Others, and Such Others Are Improperly Asserted as Secured and/or Priority Claims* (the "*Objection*") (Docket En-

try "DE" 1826) filed by Robert J. Keach, the chapter 11 trustee (the "*Trustee*") of Montreal Maine & Atlantic Railway, Ltd. (the "*Debtor*" or "*MMA*"), in relation to (a) Proofs of Claim No. No. 242-1 (the "*MN Duplicate Claim*") and 257-1 ("Claim 257") filed by Maine Northern Railway Company Limited ("*MN Railway*") and (b) Proofs of Claim No. 243-1 ("*NB Duplicate Claim*," and together with the MN Duplicate Claim, the "Duplicate Claims") and 259-1 ("Claim 259," and together with Claim 257, the "*Asserted 1171(b) Claims*") filed by New Brunswick Southern Railway Company Limited ("*NB Railway*", and together with MN Railway, the "*Claimant Railways*"). After such notice and opportunity for hearing as was required by the United States Bankruptcy Code (the "*Code*"), the Federal Rules of Bankruptcy Procedure, and the Local Bankruptcy Rules for the District of Maine, and after due consideration of, among other things, the Objection, the Response of the Claimant Railways to the Objection (DE 1855), the Trustee's Reply (DE 1878), the Stipulations of the parties (the "Stipulations") (DE 1877), the admissions and other filings of the parties, and the testimony and documentary evidence presented at the November 20, 2015 evidentiary hearing held in this matter (the "Hearing"); and for the reasons set forth on the record by the Court on February 5, 2016[1], the Court made certain findings of fact and conclusions of law in accordance with Fed. R. Bankr. P. 7002. Several of those factual findings and conclusions of law are as follows[2]:

[1] A transcript of the hearing is set forth at DE 1955.

[2] This Order does not enumerate all of the factual findings and conclusions of law set forth at the Hearing and no special significance is intended by that fact.

A. Pursuant to 28 U.S.C. §§ 157(a) and 1334(b), and Rule 83.6 of the Local Rules of the United States District Court for the District of Maine, this Court has jurisdiction over the Objection, including but not limited to, the Asserted 1171(b) Claims and the Duplicate Claims.

B. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2), and the Court has constitutional authority to enter judgment in this matter.

C. Pursuant to the Stipulations, the only issue addressed at the Hearing was whether the Asserted 1171(b) Claims claims qualify as "six-month" claims entitled to priority under 11 U.S.C. §1171(b) of the Code. If so, the amount of such claims would be determined at a subsequent hearing, if required.

D. Based upon the unique facts of this matter and the Court's analysis of the equities asserted by MMA, on the one hand, and the Claimant Railways, on the other, the Claimant Railways met their burden of establishing that the Asserted 1171(b) Claims qualify as claims that are entitled to priority under §1171(b) of the Code because:

(1) the Asserted 1171(b) Claims represent current operating expenses that were necessarily incurred by MMA in connection with its on-going operations;

(2) the Asserted 1171(b) Claims were incurred within six months prior to the commencement of this case; and

(3) the services that are the subject of the Asserted 1171(b) Claims were provided to MMA with the expectation that they would be paid for out of

the current operating revenues of MMA, and not in reliance on its general creditworthiness.

For these reasons, as well as those set forth on the record at the Hearing, it is hereby **ORDERED**, **ADJUDGED**, and **DECREED** that:

1. The Objection is sustained in part and overruled in part, as set forth herein.

2. The Duplicate Claims shall be disallowed in their entireties and expunged from the Debtor's claims register.

3. The Asserted 1171(b) Claims, to the extent allowed, are afforded priority status under § 1171(b). The amount of the Asserted 1171(b) Claims is not determined by this Order, and thus those Asserted 1171(b) Claims are not allowed in any amount at this time. The Trustee's rights to object to the amount of the Asserted 1171(b) Claims are fully reserved.

4. Notwithstanding the minute entry at DE 1947, this Order constitutes the Court's ruling and judgment on the matters read into the record on February 5, 2016. The time period within which parties must appeal this Order in accordance with the Bankruptcy Rules thus runs from the date hereof.

Dated: February 26, 2016 /s/Peter G. Cary

Peter G. Cary
Chief Judge, United States Bankruptcy Court District of Maine

APPENDIX D

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MAINE

No. 13-10670

MONTREAL MAINE &
ATLANTIC RAILWAY LTD.

Case Type:	bk
Case Number:	13-10670
Case Title:	Montreal Maine & Atlantic Railway Ltd.
Audio Date\Time:	2/5/2016 9:02:00 AM
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APPENDIX E

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MAINE

Bk. No. 13-10670
Chapter 11

IN RE: MONTREAL MAINE & ATLANTIC RAILWAY, LTD.,
Debtor.

Filed September 6, 2018

ORDER (I) OVERRULING THE AMENDED OBJECTION OF THE ESTATE REPRESENTATIVE TO THE PROOFS OF CLAIM FILED BY NEW BRUNSWICK SOUTHERN RAILWAY COMPANY LIMITED AND MAINE NORTHERN RAILWAY COMPANY, [DOCKET NO. 2313], (II) DETERMINING THE ALLOWED AMOUNTS OF THE PRIORITY AND GENERAL UNSECURED CLAIMS OF NEW BRUNSWICK SOUTHERN RAILWAY COMPANY LIMITED AND MAINE NORTHERN RAILWAY COMPANY, AND (III) DETERMINING AMOUNTS OWED BY NEW BRUNSWICK SOUTHERN RAILWAY COMPANY LIMITED AND MAINE NORTHERN RAILWAY COMPANY TO THE DEBTOR

This matter having come before the Bankruptcy Court (the "**Court**") on the Amended Objection of the Estate Representative to Proofs of Claim Filed by New

Brunswick Southern Railway Company Limited and Maine Northern Railway Company on the Basis That Certain of Such Claims Are Duplicative of Others, and Such Others Are Improperly Asserted as Administrative and/or Priority Claims, in an Inaccurate Amount, and Subject to Disallowance Under Bankruptcy Code Section 502(d) [Docket No. 2313] (the "**Amended Objection**")[1] filed by Robert J. Keach, the estate representative ("**Estate Representative**") for the post effective date estate of Montreal Maine & Atlantic Railway, Ltd., (the "**Debtor**") related to his objection [Docket No. 1826] to (a) Proof of Claim 257-1 ("**MNR Claim**") filed by Maine Northern Railway Company ("**MNR**") and (b) Proof of Claim No. 259-1 ("**NBSR Claim**," and together with the MNR Claim, the "**Irving Claims**") filed by New Brunswick Southern Railway Company Limited ("**NBSR**," and together with MNR, the "**Irving Railways**"); and after such notice and opportunity for hearing as was required by the United States Bankruptcy Code, the Federal Rules of Bankruptcy Procedure, and this Court's local rules, and after due consideration of: the Amended Objection [Docket No. 2313], the response of the Irving Railways to the Amended Objection [Docket No. 2323], the Estate Representative's Reply in Support of the Amended Objection [Docket No. 2351], the Motion of the Irving Railways for (I) Application of Judicial Estoppel and (II) Partial Summary Judgment [Docket No. 2399], the Estate Representative's Motion to Strike and Opposition to New Brunswick Southern Railway Company Limited and Maine Northern Railway Company's Motion for (I) Application of Judicial Estoppel and (II) Partial

[1] Capitalized terms not defined in this Order shall have the meanings ascribed to such terms in the Amended Objection.

Summary Judgment [Docket No. 2404], the Estate Representative's Post Trial Brief [Docket No. 2436], the Post Trial Brief of the Irving Railways [Docket No. 2437], the Reply of the Irving Railways to the Estate Representative's Post Trial Brief [Docket No. 2440], the Response of the Estate Representative to the Post Trial Brief of the Irving Railways [Docket No. 2443], the Stipulations with Regard to Trustee's Objection to Proofs of Claim Filed by New Brunswick Southern Railway Company Limited and Maine Northern Railway Company Limited [Docket No. 1877] (the "**First Set of Stipulations**"), the Second Set of Stipulations with Regard to Trustee's Amended Objection to Proofs of Claim Filed by New Brunswick Southern Railway Company Limited and Maine Northern Railway Company [Docket No. 2387] (the "**Second Set of Stipulations**"), the Trustee's Revised First Amended Plan of Liquidation Dated July 15, 2015 [Docket No. 1534] (the "**Plan**"), the Revised First Amended Disclosure Statement for the Trustee's Plan of Liquidation Dated July 15, 2015 [Docket No. 1535] (the "**Disclosure Statement**"), the testimony and documentary evidence presented at the November 20, 2015 evidentiary hearing held in this matter, this Court's oral ruling on February 5, 2016, this Court's Order memorializing its oral ruling dated February 26, 2016 [Docket No. 2034] (the "**Initial Court Order**"), the opinion of the United States Bankruptcy Appellate Panel for the First Circuit (the "**BAP**") dated October 21, 2016 affirming the Initial Court Order on all points ("**BAP Opinion**"), and the testimony and documentary evidence presented at the November 8, 2017 evidentiary hearing held in this matter; and for the reasons set forth on the record by the Court at the hearing on August 22, 2018, the transcript

of which is incorporated herein by reference, **THE COURT HEREBY FINDS** as follows:

A. Pursuant to 28 U.S.C. §§ 157(a) and 1334(b), and Rule 83.6(a) of the Local Rules of the United States District Court for the District of Maine, this Court has jurisdiction over the Irving Claims, and the Estate Representative's Amended Objection thereto.

B. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2), and the Court has constitutional authority to enter judgment in this matter.

C. In the Initial Court Order, this Court determined that the Irving Railways' claims for amounts owed for freight services provided to the Debtor within six (6) months prior to the Petition Date were entitled to priority under section 1171(b) of the Bankruptcy Code, but reserved for future determination the allowed amount of such claims.

D. The Estate Representative's Amended Objection and the Parties' various submissions presented the following issues for resolution by the Court:

i. whether the Court should reconsider the Initial Court Order, in which the Court rejected the Estate Representative's contention that the cash swap arrangement among the Debtors, the Irving Railways and the Irving Paper Companies disqualified the Irving Railways' interline freight claims from being accorded priority under section 1171(b) of the Bankruptcy Code;

ii. whether the NBSR Claim should be disallowed in its entirety because the amounts claimed by NBSR are obligations of Montreal Maine & Atlantic Canada Co. ("**MMA Canada**") rather than of the Debtor;

iii. whether approximately 57% of the amount claimed by NBSR was actually owed to Eastern Maine Railway Company ("**EMR**"), and is not allowable because EMR did not file a proof of claim in the Debtor's chapter 11 case;

iv. whether MNR is entitled to priority treatment for $22,952.15 in charges for "running rights" incurred within six months prior to the Petition Date;

v. whether MNR owes the Debtor $64,809.02 for freight services, in addition to the $265,367.66 that the Parties stipulated MNR owes to the Debtor; and

vi. whether NBSR owes the Debtor $626.92, in addition to the $734.90 that the Parties stipulated NBSR owes to the Debtor.

E. With respect to the Estate Representative's request that the Court reconsider the Initial Court Order, the Estate Representative failed to provide a sufficient basis for such request. The evidence cited by the Estate Representative was consistent with previous evidence presented to the Court and with the Court's previous finding that the Debtor and NBSR reached an agreement in mid-2012 to carve out oil shipments from the cash swap arrangement, and require the Debtor, instead, to pay NBSR the freight charges associated with oil shipments promptly upon the Debtor's receipt of funds from the Interline Settlement System. The cash swap arrangement, which continued for non-oil shipments up to the time of the derailment at Lac Megantic, Quebec, and pursuant to which funds collected by the Debtor from the Irving Paper Companies provided the Debtor with the cash used to pay the Irving Railways for such shipments, did not disqualify any of

the Irving Railways' interline freight claims from being accorded priority under section 1171(b) of the Bankruptcy Code.

F. All of the claims asserted by NBSR in Proof of Claim 259-1 are obligations of the Debtor that are owed to NBSR.

G. The claims asserted by NBSR in Proof of Claim 259-1 were not obligations of MMA Canada.

H. No portion of the claims asserted by NBSR in Proof of Claim 259-1 were obligations owed by the Debtor to EMR.

I. As agreed by the Parties in the Second Set of Stipulations, of the total amount asserted in the NBSR Claim, (a) $2,020,719.59 is owed for freight services and (b) $1,952.27 is owed for car repairs, in each case for services provided to the Debtor during the six (6) month period prior to the Petition Date. Thus, the total amount of the NBSR Claim for services provided to the Debtor during the six (6) month period prior to the Petition Date is $2,022,671.86. The remaining balance of the NBSR Claim in the amount of $141,799.44 is owed for pre-petition services that were provided to the Debtor more than six (6) months prior to the Petition Date.

J. As agreed by the Parties in the Second Set of Stipulations, of the total amount asserted in the MNR Claim, (a) $143,071.70 is owed by the Debtor to MNR for freight services and (b) $1,205.04 is owed by the Debtor to MNR for car inspection, in each case for services provided to the Debtor during the six (6) month period prior to the Petition Date.

K. The Debtor is also indebted to MNR in the amount of $22,952.15 for charges relating to "running

rights" that accrued within six (6) months prior to the Petition Date.

L. The total amount of the MNR Claim for services provided to the Debtor during the six (6) month period prior to the Petition Date is $167,228.89. The remaining balance of the MNR Claim in the amount of $187,872.30 is owed for pre-petition services that were provided to the Debtor more than six (6) months prior to the Petition Date.

M. Based upon the agreement of the Parties in the Second Set of Stipulations, and the evidence presented at trial, MNR is indebted to the Debtor for freight services provided by the Debtor to MNR in the amount of $275,247.99. The Estate Representative failed to sustain his burden of establishing that the additional amount he claimed is owed by MNR to the Debtor (i.e., $54,928.69) was, in fact, due and owing.

N. Based upon the agreement of the Parties in the Second Set of Stipulations, and the evidence presented at trial, NBSR is indebted to the Debtor for freight services provided by the Debtor to NBSR in the amount of $1,361.82.

Based upon the foregoing, it is hereby **ORDERED**, **ADJUDGED**, and **DECREED** as follows:

1. The Estate Representative's request for reconsideration of the Initial Court Order is denied.

2. The Estate Representative's Amended Objection to the NBSR Claim and the MNR claim is overruled.

3. Pursuant to 11 U.S.C. § 1171(b), NBSR is granted an allowed priority claim in the amount of $2,022,671.86.

4. The remaining balance of the NBSR Claim in the amount of $141,799.44 is allowed as a general unsecured claim.

5. Pursuant to 11 U.S.C. § 1171(b), MNR is granted an allowed priority claim in the amount of $167,228.89.

6. The remaining balance of the MNR Claim in the amount of $187,872.30 is allowed as a general unsecured claim.

7. NBSR was indebted to the Debtor as of the Petition Date in the amount of $1,361.82.

8. MNR was indebted to the Debtor as of the Petition Date in the amount of $275,247.99.

9. Payment of the Irving Railways' § 1171(b) priority claims shall be made in accordance with this Court's *Order Confirming Trustee's Revised First Amended Plan of Liquidation Dated July 15, 2013 and Authorizing and Directing Certain Actions in Connection Therewith* [Docket No. 1801] (the "Confirmation Order"). Pending such payment, funds previously set aside pursuant to the Confirmation Order as security for such claims shall continue to secure the estate's obligation to make such payment.

10. Notwithstanding the minute entry by the Court on August 22, 2018 [Docket No. 2475], this Order constitutes the Court's final judgment on the matters addressed in the Court's oral ruling on August 22, 2018 and is a final Order overruling the Estate Representative's Amended Objection and resolving all issues raised in connection therewith. The time period within which parties may appeal this Order in accordance with the Federal Rules of Bankruptcy Procedure runs from the date of the entry of this Order.

Dated: September 6, 2018 /s/Peter G. Cary

Peter G. Cary
Chief Judge, United
States Bankruptcy
Court District of Maine

APPENDIX F

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

No. 19-1161

IN RE: MONTREAL MAINE & ATLANTIC RAILWAY, LTD.,
Debtor.

ROBERT JAMES KEACH, Estate Representative
of the Post-Effective Date Estate of Montreal,
Maine and Atlantic Railway, Ltd.,
Appellant.

v.

NEW BRUNSWICK SOUTHERN RAILWAY COMPANY
LIMITED; MAINE NORTHERN RAILWAY COMPANY
Appellees.

Entered: April 7, 2020

Before
Howard, *Chief Judge*
Torruella, Lynch, Thompson, Kattaya,[*] and Barron,
Circuit Judges.

[*] Judge Kayatta is recused and did not participate in the consideration of this matter.

ORDER OF COURT

Pursuant to First Circuit Internal Operating Procedure X(C), the petition for rehearing en banc has also been treated as a petition for rehearing before the original panel. The petition for rehearing having been denied by the panel of judges who decided the case, and the petition for rehearing en banc having been submitted to the active judges of this court and a majority of the judges not having voted that the case be heard en banc, it is ordered that the petition for rehearing and petition for rehearing en banc be denied.

By the Court:

Maria R. Hamilton, Clerk

cc:
Robert James Keach
D. Sam Anderson
Lindsay Zahradka Milne
Roma N. Desai
Adam R. Prescott
James F. Molleur
Roger A. Clement Jr.
Nathaniel Richard Hull
Keith J. Cunningham
Alan R. Lepene
Stephen G. Morrell