SO ORDERED.

SIGNED this 20th day of December, 2019.

BENJAMIN A. KAHN
UNITED STATES BANKRUPTCY JUDGE

IN THE UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION

In re:	)	Case No. 18-80856
	)	
AE Bicycle Liquidation, Inc., et al.,[1]	)	Chapter 11
	)	
	)	(Jointly Administered)
Debtors.	)	

INTERIM ORDER SUSTAINING OBJECTION TO THE PRIORITY STATUS OF CLAIM NO. 34

This case is before the Court on Debtors' Objection to Claim No. 34 (the "Objection"). ECF No. 1292. With the consent of the claimant, Adrian Aguirre ("Claimant"), and Debtors, the Court conducted an interim hearing on December 10, 2019, solely to consider whether any portion of Claim No. 34 filed in Case. No. 18-80858 (the "Claim") is entitled to priority under 11 U.S.C.

[1] The Debtors in these jointly administered chapter 11 cases, along with each case number, are as follows: AE Bicycle Liquidation, Inc. f/k/a Advanced Sports Enterprises, Inc. (Case No. 18-80856); AI Bicycle Liquidation, Inc. f/k/a Advanced Sports, Inc. (Case No. 18-80857); Performance Direct, Inc. (Case No. 18-80860); Bitech, Inc. (Case No. 18-80858); and Nashbar Direct, Inc. (Case No. 18-80859).

§ 507(a)(8). For the reasons set forth herein, the Court concludes that no portion of the Claim is entitled to priority under 11 U.S.C. § 507(a)(8). Therefore, the Court will sustain the Objection to the extent Debtors object to the priority status of any portion of the Claim.

Jurisdiction and Authority

The Court has jurisdiction over the subject matter of this proceeding pursuant to 28 U.S.C. § 1334. Under 28 U.S.C. § 157(a), the United States District Court for the Middle District of North Carolina has referred this case and this proceeding to this Court by its Local Rule 83.11. This is a statutorily core proceeding under 28 U.S.C. §§ 157(b)(2)(A) and (B). This Court has constitutional authority to enter final judgment. Wiswall v. Campbell, 93 U.S. 347, 350-351 (1876).

Background

In October 2016, Claimant, a former employee of Debtor Bitech, Inc. ("Bitech"), filed a class action complaint against Bitech in California state court, alleging violations of various provisions of the California Business & Professions Code and the California Labor Code relating to wages and hours. Claimant amended his complaint in March 2017 to assert an additional claim under the

California Labor Code Private Attorneys General Act of 2004 ("PAGA"), Cal. Lab. Code §§ 2698–2699.6.[2] ECF No. 1338 at 4.[3]

While Claimant's lawsuit against Bitech was pending in California state court, Debtors filed petitions for relief under chapter 11 of title 11 in this Court. Claimant timely filed the Claim on February 15, 2019. Claim No. 34-1. Claimant attached Schedule 1 to the Claim, which categorically itemizes the amounts claimed into "Meal Break Damages," "Statutory Penalties," "Civil Penalties," and "Interest." Id., pt. 2. Claimant asserts the entitlement to interest only against the amount claimed as actual damages. Among the amounts asserted in the Claim, Claimant seeks to recover $5,945,850 for civil penalties under Sections 226 and 1198 of the California Labor Code and PAGA (the "Civil Penalties").

[2] Section 2699(a) of the California Labor Code provides that, wherever the code provides for a civil penalty to be assessed and collected by the Labor and Workforce Development Agency for a violation of the code, the penalty may be recovered through a civil action brought by an aggrieved employee. Where there is a violation of the Code for which no civil penalty is specifically provided, § 2699(f) establishes civil penalties recoverable for such violations by a PAGA plaintiff. Section 2699(g) permits a PAGA plaintiff to recover attorneys' fees and costs and makes clear that any civil penalties "shall [not] operate to limit an employee's right to pursue or recover other remedies available under state or federal law . . . ." Section 2699(i) provides that most civil penalties recovered by a PAGA plaintiff are distributed seventy-five percent to the Labor and Workforce Development agency "for enforcement of labor laws, including administration of this part . . . ," and twenty-five percent to the aggrieved employees.

[3] Claimant did not attach a copy of the underlying complaint or the amended complaint to his claim. Nevertheless, according to Claimant, his original complaint asserted the following claims: "Unfair Competition in violation of California Business & Professions Code §§ 17200, et seq.; failure to pay overtime wages in violation of California Labor Code §§ 510, et seq.; failure to provide accurate itemized wage statements in violation of California Labor Code § 226; and failure to provide wages when due in violation of California Labor Code §§ 201, 202, and 203." ECF No. 1338 at 4.

Claimant asserts that the Civil Penalties are entitled to priority under § 507(a)(8)(D), (E), or (G). Claimant also asserts a general unsecured claim in the amount of $5,167,888.34, $2,096,198.34 of which is attributable to Claimant's alleged actual damages and interest. Claim No. 34-1.

On October 25, 2019, the Court entered the Order Confirming Debtors' First Amended Joint Plan of Liquidation (the "Confirmed Plan"). ECF No. 1129. Under the terms of the Confirmed Plan, the plan administrator is required to make an initial distribution of Net Available Cash[4] on or before December 15, 2019. Id. at 33.

Although Debtors object to the Claim in its entirety, the Objection requests that the Court conduct an interim hearing solely to determine whether any portion of the Claim is entitled to priority under § 507(a)(8). ECF No. 1292 at 5. Debtors assert that a determination as to the validity of the Claim's alleged priority status is urgent due to the impending deadline for the

[4] Section 2.42 of the Confirmed Plan defines "Net Available Cash" as follows:

> With respect to each Debtor, all net proceeds recovered or generated from the liquidation of Assets or from any other sources (excluding Net Recoveries on Bankruptcy Causes of Action), less payment or provisions for Allowed Administrative Expense Claims, Allowed Priority Claims, and Allowed Priority Tax Claims. Any unexpended balance of reserves created for payment of Allowed Administrative Expense Claims, Allowed Priority Claims, and Allowed Priority Tax Claims, the Benefits Claim Reserve, the post-confirmation reserve, and any other reserves, whether established pursuant to the Cash Collateral Order, the Plan or otherwise, shall be added to Net Available Cash once such claims have been determined and paid.

ECF No. 1129 at 18.

plan administrator to make an initial distribution. Id. at 4. Because the Confirmed Plan requires the plan administrator to set aside reserves for alleged priority claims, Debtors assert that they "will not have Net Available Cash for distribution in the Bitech Inc. case until the priority status of the Claim is resolved." Id. at 5. The Court granted Debtors' motion to expedite and scheduled an interim hearing for December 10, 2019. ECF No. 1294.

Claimant responded in opposition to the Objection on December 5, 2019 (the "Response"), and indicated that he did not object to the Court conducting an interim hearing to determine priority. ECF No. 1338. Debtors filed a Memorandum of Law in support of the Objection on December 7, 2019. ECF No. 1351. Following the arguments of counsel at the hearing, the Court took the Objection under advisement.

Discussion

This case presents the issue of whether a claim filed by a private individual for amounts allegedly owed by a debtor under the California Labor Code and PAGA for civil penalties is entitled to priority under § 507(a)(8) (D), (E), or (G). Because § 507(a)(8) affords priority to "allowed unsecured claims of governmental units" to the extent such claims are for certain types of tax obligations and related penalties, the Court must consider whether: (1) the Civil Penalties asserted by Claimant are "claims

of governmental units" for purposes of § 507(a)(8), and (2) the Civil Penalties constitute an obligation of the kind under § 507(a)(8)(D) or (E), or are a penalty related to a claim of the kind that is afforded priority under § 507(a)(8)(A)-(F).

"The presumption in bankruptcy cases is that the debtor's limited resources will be equally distributed among the creditors. Thus, statutory priorities must be narrowly construed." Ford Motor Credit Co. v. Dobbins, 35 F.3d 860, 865 (4th Cir. 1994) (citations omitted). "[T]he burden to demonstrate that the requisite elements for a priority status are met rests upon the claimants." In re Heritage Vill. Church & Missionary Fellowship, Inc., 137 B.R. 888, 892 (Bankr. D.S.C. 1991); see also In re City Sports, Inc., 554 B.R. 329, 333 (Bankr. D. Del. 2016) ("The burden is on the party seeking to claim priority status to prove that the claim qualifies for priority status." (quoting In re Util. Craft, Inc., 2008 WL 5429667, at *2 (Bankr. M.D.N.C. Dec. 29, 2008))).

I. The Court does not need to determine whether the Civil Penalties are "claims of governmental units" for purposes of § 507(a)(8) in this case.

Section 507(a)(8) grants priority to certain "claims of governmental units." Debtors assert that the Claim is not entitled to priority because Claimant is not a governmental unit. Claimant asserts that he should be considered a "governmental unit" for purposes of § 507(a)(8) because "[b]y bringing a PAGA action, [Claimant] stepped into the shoes of the governmental agency as

its proxy." ECF No. 1338 at 8. Debtors assert that "the facially clear language of section 101(27)" precludes a finding that Claimant is a "governmental unit" for purposes of § 507(a)(8), ECF No. 1351 at 2, and "applicable caselaw establishes that the term 'governmental unit' is limited to actual governmental entities, and does not include private persons (even if that private person is fulfilling a governmental function)." Id. at 2–3.

In determining whether Claimant's PAGA claims are "claims of governmental units" for purposes of § 507(a)(8), the Court's "[a]nalysis properly begins with the pertinent language of the Bankruptcy Code." U.S. ex rel. Kolbeck v. Point Blank Sols., Inc., 444 B.R. 336, 338 (E.D. Va. 2011). The Code defines the term "governmental unit" as follows:

> The term "governmental unit" means United States; State; Commonwealth; District; Territory; municipality; foreign state; department, agency, or instrumentality of the United States (but not a United States trustee while serving as a trustee in a case under this title), a State, a Commonwealth, a District, a Territory, a municipality, or a foreign state; or other foreign or domestic government.

11 U.S.C. § 101(27).

As Debtors correctly note, a number of courts have construed the term "governmental unit" narrowly when considering whether certain actions brought by private citizens to enforce various state and federal laws, including PAGA, are excepted from the automatic stay under § 362(b)(4). See e.g., Porter v. Nabors

Drilling USA, L.P., 854 F.3d 1057, 1063 (9th Cir. 2017) (holding that "the governmental unit exception to the automatic bankruptcy stay does not apply to [a private individual's] PAGA action"); In re Revere Copper & Brass, Inc., 32 B.R. 725, 727 (S.D.N.Y. 1983) (holding that "both the statutory language and the legislative history demonstrate that the term 'governmental unit' in the [B]ankruptcy [C]ode refers exclusively to actual governmental groups and not to organizations acting in a governmental capacity").[5] In refusing to expand the definition of "governmental unit" to those entities acting on behalf of the government under PAGA, the court in Porter observed that the automatic stay "'serves as one of the most important protections in bankruptcy law.'" 854 F.3d at 1061 (quoting Eskanos & Adler, P.C. v. Leetien, 309 F.3d 1210, 1214 (9th Cir. 2002)). Because of the fundamental importance of the automatic stay, the court declined "to read the phrase 'by a governmental unit' out of the governmental unit exception," and held that a PAGA claimant's action to enforce civil penalties was

[5] Although Congress has since amended the definition of the term "governmental unit," the subsequent amendments did not abrogate the holding in Revere Copper & Brass. When Revere Copper & Brass was decided in 1983, the Code defined the term "governmental unit" as follows:

> "governmental unit" means United States; State; Commonwealth; District; Territory; municipality; foreign state; department, agency or instrumentality of the United States, a State, a Commonwealth, a District, a Territory, a municipality, or a foreign state; or other foreign or domestic government.

not excepted from the automatic stay as an action by a governmental unit. Id. at 1062.

At the hearing, Claimant's counsel argued that the Court should not follow Porter because there is a functional difference between excepting a governmental unit's action from the automatic stay and affording a governmental unit's claim priority. Counsel argued that allowing PAGA claimants to proceed as governmental units for purposes of § 362(b)(4) would allow a private citizen to operate outside the bounds and oversight of the bankruptcy court. In contrast, even if a claimant is afforded status as a governmental unit for purposes of § 507(a)(8), that claim must be asserted in the bankruptcy court and under its auspices. This distinction, although true, misses the point. The fact that the claim must be asserted in this Court does not alter the definition of a governmental unit as required by the statute, and Claimant's argument fails to appreciate the similarity between the fundamental bankruptcy principals that require the Court to strictly construe both the exceptions to the automatic stay and the exceptions to the policy of equality of distribution among similarly situated creditors. The concerns expressed by the court in Porter regarding a broad interpretation of "governmental unit" for purposes of the scope of the automatic stay equally apply to overbroad interpretations of priority claims.

The priority system, like the automatic stay, is a fundamental aspect of the Bankruptcy Code. Compare Czyzewski v. Jevic Holding Corp., --- U.S. ---, 137 S. Ct. 973, 984 (2017) ("The priority system applicable to . . . distributions has long been considered fundamental to the Bankruptcy Code's operation."), and Howard Delivery Serv., Inc. v. Zurich Am. Ins. Co., 547 U.S. 651, 655 (2006) ("[W]e are mindful that the Bankruptcy Code aims, in the main, to secure equal distribution among creditors."), with Midlantic Nat. Bank v. New Jersey Dep't of Envtl. Prot., 474 U.S. 494, 503 (1986) ("The automatic stay provision of the Bankruptcy Code . . . has been described as one of the fundamental debtor protections provided by the bankruptcy laws.") (internal quotations and citations omitted). And exceptions to the Code's statutory priorities, like exceptions to the automatic stay, are construed narrowly. Compare Howard Delivery Serv., 547 U.S. at 655 ("We take into account, as well, the complementary principle that preferential treatment of a class of creditors is in order only when clearly authorized by Congress."), and Dobbins, 35 F.3d at 865 ("The presumption in bankruptcy cases is that the debtor's limited resources will be equally distributed among the creditors. Thus, statutory priorities must be narrowly construed.") (internal quotations and citations omitted), with In re Stringer, 847 F.2d 549, 552 (9th Cir. 1988) ("Congress clearly intended the automatic stay to be quite broad. Exemptions to the stay, on the other hand,

should be read narrowly to secure the broad grant of relief to the debtor."). The different contexts in which the non-state actor may be proceeding are insufficient to overcome the need to have narrowly construed exceptions to both the automatic stay and the presumption of equality of distribution, and do not justify a different or more expansive interpretation of "governmental unit" for purposes of § 507(a)(8) than that in § 362(b)(4). As in Porter, the California Labor & Workforce Development Agency ("LWDA") has not sought to intervene in Claimant's PAGA action or in this contested matter, and the Court finds no sufficient reason to find a different meaning of "governmental unit" under § 507(a)(8) than the same phrase under § 362(b)(4). Cf. In re Oi Brasil Holdings Coöperatief U.A., 578 B.R. 169, 200 (Bankr. S.D.N.Y. 2017) (stating that it is "instructive to review a few similarly phrased provisions in the Bankruptcy Code to see how such language is used;" and gathering cases for the general rule of statutory construction that similar phrases within the Bankruptcy Code should be afforded similar meanings, including Ratzlaf v. U.S., 510 U.S. 135, 143 (1994) ("A term appearing in several places in a statutory text is generally read the same way each time it appears.")).

Prior to the Ninth Circuit's opinion in Porter, at least one lower court within the Ninth Circuit determined that a PAGA plaintiff's claim was non-dischargeable as a "debt . . . for a

fine, penalty, or forfeiture payable to and for the benefit of a government unit . . .” under 11 U.S.C. § 523(a)(7). Medina v. Vander Poel, 523 B.R. 820 (E.D. Cal. 2015). In determining that the claim was payable “to and for the benefit of a governmental unit” and despite recognizing that exceptions to dischargeability should be construed narrowly, id. at 827-28, the district court in Medina determined that, even though the PAGA claimant was entitled to bring the action on behalf of the LWDA, the “state is the party with the property interest in the PAGA claim, it is the party that has the right to payment.” Id. at 827. Therefore, the court concluded that a PAGA claim is payable to and for the benefit of a governmental unit, even if a PAGA claimant is authorized to pursue it. Id. This portion of the holding in Medina has been brought into doubt by the Ninth Circuit’s opinion in Porter.[6] Neither Porter nor Medina are binding precedent in this Court. In any event, even if Claimant were a “governmental unit” for purposes

[6] The Court notes that there is a distinction in the language of the three sections involved, which may distinguish the issues in Medina and this case from Porter. Under § 523(a)(7), the exception to discharge is limited to a debt “payable to and for the benefit of a governmental unit.” (emphasis added). As observed by the court in Medina, the debt was payable to the state, even if asserted by a PAGA claimant. 523 B.R. at 826–27. Similarly, § 507(a)(8) gives priority to “claims of a governmental unit” (emphasis added), without regard to whether the claim is asserted thereby. In contrast, the exception to the stay applies only to “an action or proceeding by a governmental unit . . . .” An action under PAGA is not maintained by a governmental unit. Despite this distinction in the language, the court in Porter based its decision on the need for a narrow interpretation of the exceptions to the automatic stay, a rationale equally applicable to the priority scheme at issue here, and the distinction between the terms “by” and “of” may be too thin a semantic reed on which to depart from such fundamental bankruptcy tenets.

of § 507(a)(8), Claimant has failed to demonstrate that the Civil Penalties qualify as a type of tax obligation that is entitled to priority under § 507(a)(8)(D) or (E), or as a penalty of the kind entitled to priority under § 507(a)(8)(G). Therefore, the Court need not determine in this case whether PAGA claimants' claims are "claims of governmental units" for purposes of § 507(a)(8).

II. Any civil penalties asserted for violations of the California Labor Code are non-compensatory penalties, whether asserted under PAGA or otherwise.

The factual and statutory bases for Claimant's underlying claims are not entirely clear from either the Claim or the Response. The only sections of the California Labor Code cited in the portion of the Claim for which Claimant asserts priority are §§ 226[7] and 1198.[8] In his Response and in the non-priority portion of Schedule 1 to the Claim, Claimant additionally cites §§ 201,

[7] Section 226 requires certain itemized statements of wages and deductions and to maintain related records. Although not cited in the Claim or the Response, § 226.3 imposes civil penalties for violations of § 226(a). Section 226(e) allows an employee damaged by a violation of § 226(a) to recover the greater of certain statutory damages or actual damages, plus attorneys' fees.

[8] Section 1198 sets the maximum hours of work and the standard conditions of labor at those fixed by the California Labor Commission and prohibits violations of the hours and standards set by the Commission.

202, 203,[9] "226e,"[10] 226.7,[11] 510,[12] 512,[13] and 540[14] of the California Labor Code, along with the definitional § 2698, the operational § 2699, and the procedural § 2699.3 of PAGA. ECF No. 1338 at 4-6.[15] Claimant alleges that Bitech breached these statutes by failing to provide overtime wages (§ 510), failing to provide accurate itemized wage statements (§ 226), and failing to provide wages when due (§§ 201, 202, and 203). Id. at 4. Claimant alleges that 33% of his workdays included meal period violations, and that Bitech's "meal and rest period policy facially violates California

[9] Sections 201 and 202 require immediate payment of wages on discharge or layoff, or resignation, respectively, and section 203 imposes a penalty equal to the unpaid wages for a maximum of 30 days if the wages are not timely paid.

[10] The Court assumes this is a reference to Cal. Lab. Code § 226(e). See note 15, infra.

[11] Section 226.7 requires certain "recovery periods" during work hours for meals or rest, and § 226.7 imposes a penalty of one additional hour of pay for each workday during which a recovery period is not provided.

[12] Section 510 defines overtime as time in excess of eight hours in one day and forty hours in a week, and requires one and one half times the regular pay for overtime, and twice the regular rate of pay for work time in excess of 12 hours in a single day.

[13] Section 512 requires a meal period of at least 30 minutes for any workday in excess of 5 hours and a second meal period if the workday exceeds 10 hours, and allows a waiver of meal periods by the employee under certain conditions.

[14] There does not appear to be a § 540 of the California Labor Code.

[15] Schedule 1 to the Claim asserts a total of $3,071,690.00 in "Statutory Penalties" with a reference to Cal. Lab. Code §§ 203 and "226e," and $5,945,850 in in "Civil Penalties" with a reference to Cal. Lab. Code §§ 226 and 1198. The Claim asserts that only the "Civil Penalties" are entitled to priority. To the extent that Claimant seeks civil penalties under § 226(e) in addition to those under §§ 2699(a) or (f) of PAGA, such recoveries appear to be duplicative in the case of § 2699(a), which permits a private plaintiff to recover civil penalties on behalf and in lieu of the LWDA where the California Labor Code provides for such penalties, and not authorized in the case of § 2699(f), which permits PAGA civil penalties only if the California Labor Code does not otherwise provide a civil penalty for the stated violation. The Court need not determine this issue for purposes of this Order.

labor laws." Id. at 6. Claimant conceded at the hearing that all of the Civil Penalties for these alleged violations are recoverable in addition to, rather than in lieu of, any actual damages suffered by Claimant or any putative class members. See also Cal. Lab. Code § 2699(g)(1).

"Section 507(a)(8) specifies seven categories of tax obligations that are entitled to priority." 4 Collier on Bankruptcy ("Collier") ¶ 507.11[1] (16th ed. 2019). Claimant specifically asserts that a portion of his claim is entitled to priority under § 507(a)(8)(D) and (G), and he cites a number of cases finding that certain assessments are entitled to priority under § 507(a)(8)(E). Section 507(a)(8) provides in relevant part:

> (a) The following expenses and claims have priority in the following order:
>
> > (8) Eighth, allowed unsecured claims of governmental units, only to the extent that such claims are for—
> >
> > > (D) an employment tax on a wage, salary, or commission of a kind specified in paragraph (4) of this subsection earned from the debtor before the date of the filing of the petition, whether or not actually paid before such date, for which a return is last due, under applicable law or under any extension, after three years before the date of the filing of the petition;
> >
> > > (E) an excise tax on--
> > >
> > > > (i) a transaction occurring before the date of the filing of the petition for which a return, if required, is last due, under applicable law or under any extension, after three years before the date of the filing of the petition; or

> (ii) if a return is not required, a transaction occurring during the three years immediately preceding the date of the filing of the petition;
>
> (G) a penalty related to a claim of a kind specified in this paragraph and in compensation for actual pecuniary loss.

A. Section 507(a)(8)(D) and (E)

For an assessment to be entitled to priority under § 507(a)(8)(D) or (E), unlike under § 507(a)(8)(G), the assessment must be a tax, not a penalty. Therefore, before the Court may consider the particular requirements of § 507(a)(8)(D) and (E), the Court first must decide whether the assessment allegedly owed by Bitech under PAGA is a tax or a penalty. Although the California Labor Code, including PAGA, refers to the amounts allegedly owed by Bitech as "civil penalties," see e.g., Cal. Lab. Code §§ 226.3, 2699(f)–(j), the Court must "look[] behind the label placed on the exaction and rest[] its answer directly on the operation of the provision using the term in question." U.S. v. Reorganized CF & I Fabricators of Utah, Inc., 518 U.S. 213, 220 (1996).

Claimant urges the Court to follow Williams v. Motley, 925 F.2d 741 (4th Cir. 1991), and determine that the assessment allegedly owed by Bitech under PAGA is a tax. In Williams, the court did not consider the distinction between a tax and a penalty, nor did it consider whether the amount in question was entitled to priority. Instead, the court was asked to determine whether an

uninsured motor vehicle assessment under Virginia law was a fee or an excise tax for dischargeability purposes. 925 F.2d at 743–44.[16] The Fourth Circuit did not consider in Williams whether the uninsured motor vehicle assessment was a penalty because "the assessment was not issued as a consequence of the violation of a state law, but rather was a charge imposed on drivers who chose not to insure their vehicles in the Commonwealth of Virginia." In re DeJesus, 243 B.R. 241, 249 (Bankr. D.N.J. 1999).

Williams also was decided nearly five years before the Supreme Court's more illuminating opinion on the issue before this Court in Reorganized CF & I Fabricators of Utah. In Reorganized CF & I Fabricators of Utah, the debtor and its subsidiaries sponsored two pension plans. 518 U.S. at 216. The IRS assessed 10 percent penalties against the debtors due to the underfunding of the pension plans, and asserted that the penalties were entitled to priority either as an excise tax under § 507(a)(8)(E),[17] or as a compensatory penalty under § 507(a)(8)(G). Id. at 216-17. The bankruptcy court disallowed the priority, determining that the

[16] In establishing a test for distinguishing between fees and taxes, the Fourth Circuit held that an assessment is generally a tax instead of a fee if it is: "(a) An involuntary pecuniary burden, regardless of name, laid upon individuals or property; (b) Imposed by, or under authority of the legislature; (c) For public purposes, including the purposes of defraying expenses of government or undertakings authorized by it; (d) Under the police or taxing power of the state." 925 F.2d at 743 (citing New Neighborhoods, Inc. v. West Virginia Workers' Compensation Fund, 886 F.2d 714, 720 n. 7 (4th Cir. 1989)).

[17] In Reorganized CF & I Fabricators of Utah, the Court was construing the statute as previously codified at § 507(a)(7).

penalties were not an excise tax and were penalties that were not compensation for actual pecuniary loss. Id. at 217.[18] In affirming the bankruptcy court, the Court focused on the distinction between a tax and a penalty or debt, and concluded that "if the concept of penalty means anything, it means punishment for an unlawful act or omission, and a punishment for an unlawful omission is what this exaction is." Id. at 224. The penal nature of the exaction was "underscored" by requiring the employer to pay an additional amount equal to the total amount of unfunded liabilities. Id. at 225. Given its punitive function, the Court determined that it "must be treated as imposing a penalty, not authorizing a tax." Id. at 226.

In DeJesus, the court summarized the interplay between the test in Williams and the Supreme Court's holding in Reorganized CF & I Fabricators of Utah as follows:

> In [Reorganized CF & I Fabricators of Utah], the Supreme Court expanded the discussion regarding the designation of an assessment as an excise tax beyond the four characteristics of a tax laid out in earlier cases. The import of the CF & I decision is that even though the CF & I assessment, the "tax" imposed upon the debtor employer as a consequence of funding deficiencies in the debtor's sponsored pension plans, qualified as a tax, its non-tax characteristics, in particular, the penal nature of the assessment, precluded the designation of the assessment as a tax. The CF & I assessment is clearly an involuntary pecuniary burden. Congress properly imposes the penalty upon employers who fail to

[18] The bankruptcy court also equitably subordinated the claims under § 510(c), id. at 218, but that holding, which was vacated by the Court, is not relevant here.

> meet annual pension plan funding requirements, in a valid exercise of its police or taxing power. The public purpose of the 10% "tax" is to deter employers from failing to meet the annual pension plan funding requirements by punishing such employers with a sanction if a violation of the statutory requirement occurs. Notwithstanding qualification of the 10% sanction as a tax under the four[-]prong test, the Supreme Court concluded that the sanction was not a tax under § 507(a)(7)(E), but a penalty to be dealt with as an ordinary, unsecured claim.

243 B.R. at 251 (internal quotations and citations omitted). In sum, the four-part test from Williams applies to determine whether an assessment is a fee or a tax, but is not dispositive when, as is the case here, the issue is whether a particular assessment is a penalty as opposed to a tax.

In light of the "patently punitive function" of the Civil Penalties in this case, any amounts allegedly owed by Bitech to Claimant constitute a penalty, not a tax for purposes of § 507(a)(8). Reorganized CF & I Fabricators of Utah, 518 U.S. at 226; see also Medina, 523 B.R. at 826 ("[T]here is no reason to believe that the 'civil penalties' described in PAGA are anything but punitive in nature or that they are 'compensation for actual pecuniary loss'"). Under the applicable provisions of the California Labor Code, including PAGA, "an 'aggrieved employee' may bring a civil action against an employer 'on behalf of himself or herself and other current or former employees' when an employer has violated the California Labor Code." Varsam v. Lab. Corp. of Am., 120 F. Supp. 3d 1173, 1180 (S.D. Cal. 2015) (quoting Cal.

Lab. Code § 2699(a)). In fact, "PAGA . . . authorizes a representative action only for the purpose of seeking statutory penalties for Labor Code violations." Kim v. Reins Int'l California, Inc., 18 Cal. App. 5th 1052, 1057, 227 Cal. Rptr. 3d 375, 378 (2017). As Claimant himself notes, the amounts allegedly owed by Debtors under PAGA stem from Bitech's alleged unlawful violations of various provisions of the California Labor Code relating to wages and hours,[19] and are in addition to any other amounts recoverable by Claimant under applicable state or federal law. See Cal. Lab. Code § 226.3 ("[t]he civil penalties provided for in this section are in addition to any other penalty provided by law"); Cal. Lab. Code § 2699(g)(1) ("[n]othing in this part shall operate to limit an employee's right to pursue or recover other remedies available under state or federal law"). Because any recovery under PAGA is directly attributable to an employer's violation of the California Labor Code and because each of the

[19] Claimant alleges:

> The bases for Creditor' PAGA claims are as follows: Creditor was paid commissions based on sales. Debtor, however, failed to calculate all these nondiscretionary wages into Creditor's regular rate, and as a result, underpaid Plaintiff for his overtime hours worked in violation of California Labor Code §§ 540, et seq. Additionally, Debtor's wage statements failed to state the hourly rate of pay used to pay overtime wages in violation of California Labor Code § 226. This deficiency applied uniformly to every wage statement issued by Debtor. Moreover, Debtor's illegal meal and rest period policy allowed for violations of California Labor Code §§ 226.7 and 512 without any remedy.

ECF No. 1338 at 6 (emphasis added).

sections of the California Labor Code imposing such civil penalties specifically reserve all plaintiffs' other claims under applicable state or federal law, including claims for actual damages, any liability imposed under PAGA is a penalty, not a tax. See Reorganized CF & I Fabricators of Utah, 518 U.S. at 226 ("Given the patently punitive function of [26 U.S.C.] § 4971, we conclude that [26 U.S.C.] § 4971 must be treated as imposing a penalty, not authorizing a tax."). Therefore, the amounts allegedly owed by Bitech to Claimant under PAGA are not entitled to priority § 507(a)(8)(D) or (E).

B. Section 507(a)(8)(G)

For a penalty to be entitled to priority under § 507(a)(8)(G), the claim must: (1) be for a penalty, rather than a tax; (2) relate to one of the kinds of claims covered by §§ 507(a)(8)(A)–(F); and (3) be "in compensation for actual pecuniary loss." Although Claimant contends that a portion of his claim is entitled to priority under § 507(a)(8)(G), he has not carried his burden of demonstrating that any portion of his claim is entitled to priority under § 507(a)(8)(G). See Heritage Vill. Church & Missionary Fellowship, 137 B.R. at 892 ("[T]he burden to demonstrate that the requisite elements for a priority status are met rests upon the claimants.").

As discussed above, the Court has determined that the PAGA Civil Penalties are penalties, rather than taxes. Therefore, the

first element of § 507(a)(8)(G) has been met. However, the second and third elements are not satisfied. Claimant has not made any attempt to demonstrate that, to the extent that the Civil Penalties are true penalties, rather than taxes, that they relate to a claim of the type under § 507(a)(8)(A)-(F). Under the express terms of the California Labor Code, the Civil Penalties are independent of any other claim, including any tax. Therefore, they do not relate "to a claim of a kind specified in" § 507(a)(8)(A)-(F), and are not a type of penalty entitled to priority.

Even if the Civil Penalties related to a claim covered by §§ 507(a)(8)(A)–(F), Claimant has not shown that the Civil Penalties are "in compensation for actual pecuniary loss." As instructed by Collier:

> In most instances, a penalty will not be in compensation for actual pecuniary loss. The nature of a penalty—as a method of punishing unlawful conduct—would seem to preclude the penalty from being in compensation for actual pecuniary loss. If the analysis undertaken by the court determines that a particular obligation is a penalty rather than a tax, it is likely that the same court will decide the penalty is not for an actual pecuniary loss.

Collier ¶ 507.11[8][b].

"'Civil penalties are inherently regulatory, not remedial,' and are intended to secure obedience 'to statutes and regulations validly adopted under the police power.'" Home Depot U.S.A., Inc. v. Superior Court, 191 Cal. App. 4th 210, 225, 120 Cal. Rptr. 3d 166, 176 (2010) (quoting People v. Union Pac. R.R. Co., 141 Cal.

App. 4th 1228, 1257–1258, 47 Cal. Rptr. 3d 92, 112 (2006)). The civil penalties imposed by PAGA were intended to "enhance the enforcement of the labor laws." Julian v. Glenair, Inc., 17 Cal. App. 5th 853, 865 (Ct. App. 2017); see also ZB, N.A. v. Superior Court, 8 Cal. 5th 175, 184, 448 P.3d 239, 243 (2019) ("The Legislature enacted the PAGA in 2003 after deciding that lagging labor law enforcement resources made additional private enforcement necessary to achieve maximum compliance with state labor laws.") (internal quotations and citations omitted); Brown v. Ralphs Grocery Co., 197 Cal. App. 4th 489, 501, 128 Cal. Rptr. 3d 854, 862 (2011) ("The purpose of the PAGA is not to recover damages or restitution, but to create a means of deputizing citizens as private attorneys general to enforce the Labor Code . . . . the relief is in large part for the benefit of the general public rather than the party bringing the action.") (internal quotations and citations omitted). In fact, the civil penalties added by PAGA were intended to be "significant enough to deter violations [of the Labor Code]." Iskanian v. CLS Transp. L.A., LLC, 59 Cal. 4th 348, 379, 327 P.3d 129, 146 (2014) (internal quotations and citations omitted).

The primary purpose of PAGA's civil penalties is to deter violations of the labor laws, not to compensate the government or the aggrieved employees for any "actual pecuniary loss." The flat-rate penalties bear no relationship to the underlying harm caused

by any particular violation or any specific, direct damage caused to the government or the aggrieved employees, and leave fully intact the claimants' remedies. Although seventy-five percent of the civil penalties collected under PAGA are "distributed to the [LWDA] for enforcement of labor laws," Cal. Lab. Code § 2699(i), the government's subsequent use of the funds to enforce labor laws does not demonstrate that the civil penalties are "in compensation for actual pecuniary loss." The generation of funds to enforce labor laws is an incidental benefit of the penalties, not the primary purpose for their imposition. By providing aggrieved employees with twenty-five percent of the civil penalties collected, PAGA is incentivizing aggrieved employees to bring PAGA actions, not compensating the aggrieved employees for any "actual pecuniary loss." Varsam, 120 F. Supp. 3d at 1181 ("[T]he purpose of PAGA is to incentivize private parties to recover civil penalties for the government that otherwise may not have been assessed and collected by overburdened state agencies." (quoting Ochoa–Hernandez v. Cjaders Foods, Inc., 2010 WL 1340777 at *4 (N.D.Cal. Apr. 2, 2010))). Moreover, "[t]he civil penalties recovered on behalf of the state under the PAGA are distinct from the statutory damages to which employees may be entitled in their individual capacities." Iskanian, 59 Cal. 4th at 381, 327 P.3d at 147. See Cal. Lab. Code § 2699(g)(1) ("Nothing in this part shall operate to limit an employee's right to pursue or recover other

remedies available under state or federal law, either separately or concurrently with an action taken under this part."). Accordingly, "there is no reason to believe that the civil penalties described in PAGA are . . . compensation for actual pecuniary loss." Medina, 523 B.R. at 826 (internal quotations omitted).

Therefore, the portion of the Claim for the Civil Penalties allegedly owed by Bitech under PAGA is not entitled to priority under § 507(a)(8)(G) because the Civil Penalties are not related to a claim of the kind contemplated by § 507(a)(8)(A)-(F), and are not "in compensation for actual pecuniary loss."

Conclusion

Based on the foregoing, the Court finds that no portion of the Claim is entitled to priority under 11 U.S.C. § 507(a)(8).

IT IS THEREFORE ORDERED, ADJUDGED, and DECREED that the Objection is sustained to the extent Debtors object to the priority status of any portion of the Claim.

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