



LJN'S

Equipment Leasing

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Post-Petition Rent Obligations: Use and Occupancy v. Due Date

By Leslie A. Berkoff and
Sandra M. Ishaq

Confused about when a real property landlord or equipment lessor can commence charging post-petition rental payments? Does a debtor's obligation under Section 365(d)(3) of the Bankruptcy Code, (hereinafter, the "Code") to timely perform all obligations arising after the order for relief (or under Section 365(d)(10), 60 days after the order of relief), mean those obligations that "arise" by virtue of actual post-petition use of the property as opposed to obligations that arise by virtue of the "due date" of the rental payment by contract or invoice?

The two competing theories advanced in determining what obligations should be deemed a post-petition obligation under Section 365(d)(3) of the Code are: 1) the proration rule (majority approach); and 2) the billing date or performance date rule (minority approach). To date, three Circuits have addressed these theories as applied to non-residential real property leases. See *In re Montgomery Ward Holding Corp.*, 268 F.3d 205 (3rd Cir. 2001); *In re Koenig Sporting Goods, Inc.*, 203 F.3d 986 (6th Cir. 2000); *In re Handy Andy Home Improvement Ctrs., Inc.*, 144 F.3d 1125 (7th Cir. 1998). To date, no Circuit has

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Recovering Attorneys' Fees As an Administrative Expense

By Anthony L. Lamm

In counseling clients on whether to structure a transaction as a lease or a loan, there are several financial considerations. The first is the potential that the client's customer could file for bankruptcy, and its impact upon recovering rent payments as a priority administrative expense. In that case, attorneys' fees are a factor as well. The Bankruptcy Code provisions that govern the rights and remedies of an equipment lessor in comparison to the rights and remedies of a secured lender differ significantly — they may be considered more favorable to an equipment lessor than a secured lender for the reasons discussed later in this article, although certain provisions of the Code that address the remedies of a secured lender are applied to an equipment lessor as well. Section 365(d)(10) of the Bankruptcy Code provides that:

"The trustee shall timely perform all of the obligations of the Debtor, except those specified in Section 365(b)(2), first arising from or after 60 days after the order for relief in a case under Chapter 11 of this title under an unexpired lease of personal property ... until such lease is assumed or rejected notwithstanding section 503(b)(1) of this title, unless the court, after notice and a hearing and based on the equities of the case, orders otherwise with respect to the obligations or timely performance thereof ... "

The language of this statute and its Congressional history have been interpreted and relied upon by bankruptcy courts in many circuits of the country. The courts have used the statute to grant an equipment lessor an automatic administrative expense for unpaid post-petition lease payments where the lessee remains in possession of the leased equipment on or after the 60th day from filing a bankruptcy petition until eventually assuming or rejecting the lease. This expense has been granted without the usual proofs required under Section 503(b)(1)(A) (to show actual, necessary costs of preserving the estate). *In re: Furley's Transport, Inc.*, 263 B.R. 733 (Bankr. D. Md. 2001); *In re: Russell Cave Co.*, 247 B.R. 656, 659 (Bankr. E.D.Ky.

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2000); *In re: The Elder-Beerman Stores Corp.*, 201 B.R. 759, 763 (Bankr. S.D. Ohio, 1996); *In re: Brennick*, 178 B.R. 305, 307 (Bankr. D. Mass. 1995). This extraordinary benefit from 365(d)(10) is not applicable to the first 59 days after the debtor's petition is filed but 503(b)(1)(A) is, according to the majority of courts particularly in cases where the lessee or debtor uses the leased equipment post-petition and gains some benefit from the property. *In re: Raymond Cossette Trucking, Inc.*, 231 B.R. 80 (Bankr. D.N.D. 1999); *In re: Thompson*, 788 F.2d 560 (9th Cir. 1986); *Kinman & Kinman P'Ship v. Agristor Leasing*, 116 B.R. 162 (D. Neb. 1990); *In re: Furlley's Transport, Inc.* 263 B.R. 733, 740-41 (Bankr. D. M. 2001); *In re: Muma's Services, Inc.*, 279 B.R. 478 (Bankr. D. Del 2002).

By comparison, a secured lender must demonstrate that the adequate protection afforded it by a debtor is inadequate in order to compel a super priority administrative expense status for the debtor's post-petition payments. Here, then, in this secured transaction setting (as compared with the equipment lessor scenario), the secured lender must actually have lost its secured status (in part or in whole) and have seen its claim become either bifurcated or completely unsecured to marshal the treatment of its claim for unpaid contract installments as an administrative expense, and garnish priority payments for the debtor's post petition use of the secured lender's property. 11 U.S.C. 507(b).

The issue of recovering attorney's fees in the post-petition setting is also measurably different and perhaps slightly more favorable to an equipment lessor than a secured lender. An

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equipment lessor may be entitled to a 365(d)(10) administrative claim for its attorneys' fees if those fees were incurred to enforce the equipment lessor's rights in a manner consistent with section 365. *In re: Muma Services, Inc.*, 279 B.R. 478 (Bankr. D. Del. 2002); See also, *In re: Shangra-La, Inc.*, 167 F.3d 843, 849 (4th Cir. 1999).

Section 365 contemplates either the trustee/debtor curing the defaults under a lease to assume it, or rejecting the lease and taking steps to enforce the payment of post-petition rent payments. In the first case, attorneys' fees incurred in attempting to collect sums due from debtors following default may be recovered as "pecuniary loss" under section 365(b)(1)(B) if such monies were expended as the result of a default under the contract or lease between the parties and are recoverable under the contract and applicable state law. However, the courts will not allow administrative claims for attorneys' fees that are inconsistent with the debtor's rights under the Bankruptcy Code. *In re: Child World, Inc.*, 161 B.R. 349 (Bankr. S.D.N.Y. 1993); *In re: Best Products, Inc.* 148 B.R. 413 (Bankr. S.D.N.Y. 1992). Therefore, fees to seek to shorten the time within which the debtor must assume or reject the lease and then opposing the debtor's assumption of the lease have been held not recoverable because they were incurred to deny the debtor rights it had under the Bankruptcy Code. *Id. at 414*. If issues raised are peculiar to bankruptcy laws, such as objection to confirmation of Chapter 12 plan, they are not recoverable; *In re: Ryan's Subs Inc.*, 165 B.R. 465, 469 (Bankr. W.D.Mc 1994). Fees, however, for prosecuting a motion to compel a debtor to perform its leases on and after the 60th day post-petition are recoverable as administrative expense claims. *In re: Exchange Resources, Inc.*, 214 B.R. 366 (Bankr. D. Minn. 1997); *In re: Forman Enterprises, Inc.*, 45 Collier Bankr. Cas. 2d (MB) 664 (Bankr. W.D.Pa 2000). Legal fees for services before the 60th day, such as Objections to Debtor's motion to

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Indian Transactions

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argument as to ownership.

Another suggestion is to negotiate collateral or security located outside of the Indian area or tribal ownership, or the assignment of the right to receive payment of the proceeds from others types of contracts. This is what a mortgage bank and real estate development company did in *Rothschild v. Northwestern National Bank of Saint Paul*, 309 Minn. 35, 37, 245 N.W.2d 844, 846 (1976), where Rothschild took as security the right to receive payment from construction contracts on Indian land, rather than an interest in the real property that Rothschild financed, because Rothschild could not have perfected a security interest in real property located on the Reservation.

Lessors may also run into problems when they attempt to recover property located in Indian country. For example, the Yankton Sioux Tribal Code of Creditors' Rights and Responsibilities, Title IX Section 9-1-1 has eliminated all forms of self-help. Most Indian tribes, including the Yankton Sioux, require that before a creditor can recover their property, the creditors must first obtain a judgment in the Tribal Court and then apply to have the appropriate tribal

authorities recover the subject property. The difficulty of repossessing property may further justify lessors negotiating a security interest in external collateral similar to that in *Rothschild*.

Many tribes will recognize foreign judgments. The Oglala Sioux Tribe for example, allows a creditor to enforce a final foreign court judgment after review by the Tribal Court of a written petition that must be filed with the court. This may substantially lessen the expense of repossessing property

Many tribes will recognize foreign judgments

when lessees are in default. Lessors must examine the particular tribe's rules on the recovery of property when calculating risk and the cost of the subject lease.

In recognition of the uncertainty presented to companies dealing with Indian tribes, the National Conference of Commissioners on Uniform State Law (NCCUSL) created the Committee on Liaison with Native American Tribes. The purpose of this committee is to encourage uniformity of laws among tribal nations and the states on appropriate subjects. The hope is that the final product will be beneficial both to tribal governments and enti-

ties wishing to do business in Indian country, but for now lessors must settle with analyzing their transactions on a tribe-by-tribe basis.

There are several sources available to lessors who want to examine a particular tribe's code before entering into a transaction. The University of Oklahoma School of Law maintains an excellent Web site at <http://thorpe.ou.edu> with links to numerous tribal codes and constitutions. Lessors may also contact the Bureau of Indian Affairs for the state where the tribe is located or check the Web site of the particular tribe with which one seeks to do business. When all else fails, contact the tribal counsel or legal department and find out how other lessors are protecting their interest when doing business with that tribe. Most tribes welcome commerce and will provide companies with the information they need to make an informed decision about doing business in Indian country.

Remember, the various tribes' positions on secured transactions and leases vary widely. The issues arise when doing business with an Indian tribe and when doing business in Indian country. Lessors would do well to watch these issues to enhance the likelihood of recovery in the event of a default.



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reject unexpired equipment leases, do not constitute administrative claims. *In re: Kyle Trucking, Inc.*, 239 B.R. 198 (Bankr. N.D. Ind. 1999). If the leases are assumed, the fees for pre-60th day matters may be paid as part of the cure. If rejected, these fees perhaps may be taken up as part of rejection damages.

A secured lender on the other hand can only recover its legal fees if it is an oversecured creditor pursuant to 506(b) which provides, in pertinent part, that:

"To the extent that an allowed secured claim is secured by property the value of which...is greater than the amount of such claim, there shall

be allowed to the holder of such claim, interest or such claim, and any reasonable fees, costs or charges provided for under the agreement under which such claim arose."

If rejected, these fees perhaps may be taken up as part of rejection damages.

In a secured transaction, given that the lender must be undersecured to secure a super-priority administrative expense claim for unpaid post-petition contract payments, it is obviously problematic to recover attorneys' fees as an administrative claim in

light of 506(b). For equipment lessors, 11 U.S.C. 365(b)(1)(B) and 365(d)(10) seem to have done a better job of anticipating lessor's interest in recovering both rent payments and attorneys' fees for, at the minimum, enforcing the payment of same as an administrative expense claim.



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