# BANKRUPTCY LAW NEWSLETTER

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## ASSUMPTION OF COMMERCIAL LEASES AFTER THE 1984 AMENDMENTS

*By Jeffrey S. Battershall and Kathleen M. Hanenburg**

### Introduction

Section 365 of the Bankruptcy Code governs the assumption of leases and executory contracts in force at the commencement of a case in bankruptcy. This section was substantially amended by the Bankruptcy Amendments in the Federal Judgeship Act of 1984.[1] The intent of the 1984 amendments was to afford greater protection to commercial lessors (that is, to anyone leasing nonresidential real property to debtors) by (i) shortening the time period in which the trustee is allowed to assume a lease, (ii) requiring performance of all obligations under a lease during such period, and (iii) restricting the conditions under which shopping center leases may be assumed or assigned. This article chronicles some of the issues that have arisen in connection with the first of these amendments -- the shortened time period for assumption of nonresidential real property leases.

### I. Distinction Between Residential and Nonresidential Real Property.

The shortened time period for assumption in Section 365 applies only to leases of "nonresidential" "real property". Neither of these terms is defined in Section 365 and as a result the meaning of both terms has been the subject of litigation.

Some courts have viewed leases for the right to remove natural resources, e.g., to drill for oil or gas or to remove timber, as not creating a sufficient right in real property under state law to constitute leases for real property.[2] Other courts have looked to the definition of a lease in Section 365(m) of the Bankruptcy Code, and concluded that mineral rights fall within that definition.[3]

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In determining whether a real property lease is residential or nonresidential, some courts have looked to the underlying character of the property, while other courts have looked to the character of the lease agreement.[5] The emerging majority view appears to focus on the underlying character of the property, not the lease.[6]

## II. What Constitutes "Assumption" of a Lease

Under Section 365, as amended, the trustee or debtor in possession must assume a lease for nonresidential real property within 60 days from the commencement of the case. Section 365 is silent, however, as to the exact procedure to be followed in order to effectively assume such a lease and as a result this question has given rise to a great deal of litigation.

The courts have formulated three distinct approaches to this issue:

1. Assumption requires the trustee to both file a formal motion to assume the lease and obtain court approval of that motion within the 60 day period;

2. Assumption requires the trustee to file a motion to assume the lease within the 60 day period but does not require court approval within that period; and

3. Assumption may be accomplished through less formal means than filing a motion with the court, mainly by the word, deed, or conduct of the trustee, evidencing an intent to assume the lease.

Initially, some courts adopted the first position, requiring a trustee to both assume and obtain court approval of a motion to assume a lease for nonresidential real property within the 60 day period. Though this strict rule found favor for a short period, later decisions have consistently rejected this view and it is not now considered a correct interpretation of Section 365.

The third approach, which would allow a trustee or debtor in possession to assume a lease by some form of action less formal than a motion, has also apparently been rejected. Though some courts have suggested that in theory assumption may be accomplished by such means, few reported cases have actually allowed such assumption,[7] while several cases have disallowed a trustee's effort to assume leases other than by motion.[8]

Courts now appear uniform in adopting the second approach.[9] That is, the trustee must file a formal motion with the court within the 60 day period but the court need not approve the motion within that period for effective assumption of a lease. One principal rationale behind this approach is that it would be unfair to a debtor to deem a lease rejected by operation of law simply because the court cannot manage to schedule a hearing and approve the debtor's motion within the 60 day period.

As a practical matter, counsel for debtors should always file a formal motion with the court within the 60 day period in order to assume a lease for nonresidential real property. As interpreted by a clear majority of courts, it will not be necessary for the court to schedule a hearing or approve such a motion within the 60 day period so long as the motion itself is filed within such period. Counsel should not rely on any means less formal than a motion, such as a letter or a phone conversation with the lessor.

## II. Extension of Time to Assume a Lease.

Section 365 permits extension of the 60 day period upon a showing of cause,[10] with Court approval. This provision has been the source of several interpretive and procedural uncertainties. First, as with assumption, the question has arisen whether it is sufficient for a trustee merely to file a motion with the court requesting an extension within the 60 day period or whether the court must approve the request within the same period. Second, the courts have addressed the issue of whether multiple and successive extensions of time may be allowed. Third, the issue has arisen as to whether or not a motion for extension of time may be heard on an ex parte basis or only after notice to adverse parties with opportunity for a hearing.

Unlike the holdings concerning the procedure for assumption, where a clear majority of courts allow approval to fall outside of the 60 day period, in the extension context authority appears more closely divided. A fair number of courts allow extensions only when the trustee both files a request and obtains court approval within the 60 day period.[11]

With respect to the second issue, the clear weight of authority, including the Fifth and Ninth Circuits, allows the granting of multiple extensions of the time in which the trustee must decide to assume or reject a lease.[12] In so holding, courts have reasoned that if only one extension is allowed, courts will give trustees a long extension thereby undermining the intended effect of the statute to shorten the time period for a decision. Additionally, courts have noted that under the literal terms of Section 365, "in the event of such a lengthy extension, lessors are given no assurance or right to request a redetermination of such an extension."[12] *

With respect to the third issue, the majority position, including opinions of the Fifth and Ninth Circuits, is that motions for an extension of time may be heard and granted on an ex parte basis.[13]

In practice, requests for extensions are likely to be common, particularly in large and complicated bankruptcy cases. Counsel for debtors should file a formal motion to request an extension. Such motions should be filed well within the 60 day period and if possible court approval should be obtained within the 60 day period as well.

Moreover, though such evidence has not been required in all cases, a debtor may be more likely to receive an extension of the time if it can establish that it is capable of making all rent payments and satisfying all lease obligations arising during the initial 60 day period.

## IV. Waiver and Estoppel.

Another source of contention has been the application of the equitable doctrines of waiver and estoppel to the rights provided for in Section 365. These doctrines are of potential importance to both debtors and lessors because even though a trustee may have failed to assume an unexpired lease, a court may effectively reverse the operation of Section 365 by finding that the lessor

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[12] * Though this is apparently the emerging trend of legal authority, it is the aut2hor's view that multiple extensions of the time to assume are in contravention of the intended purpose of the act and should not be allowed. As a practical matter they have served to allow debtors extensive delays in the decision whether to assume or reject and may simply promote procrastination by debtors in possession or trustees in deciding whether to assume or reject.

waived its rights or should be estopped from treating the lease as rejected a seeking to regain control of the leased property. Presently, authority i divided concerning the application of waiver and estoppel to the rights o lessors under Section 365. The statute specifically provides that acceptance of rent payments and other performance during the 60 day period does not constitute waiver or relinquishment of the lessor's rights under the lease or under Section 365. The statute is silent, however, as to the effect of such acceptance after the 60 day period. Some courts have held that acceptance of rent or other performance outside the 60 day period constitutes a waiver on the part of the lessor.[14] Other courts have held to the contrary, reasoning that such actions could not resurrect property rights terminated by the operation of Section 365.[15]

Lessors and their counsel should be cautious not to undertake equivocal actions which could be construed as a waiver or grounds for estoppel against the right to treat a lease as having been deemed rejected pursuant to operation of law under Section 365. Some courts have suggested practical measures a lessor may take to preclude a finding that it has waived its rights by continuing to accept rent outside the 60 day period. Though each case will ultimately turn on the question of the individual lessor's intent as evidenced in the specific facts of the case, courts have held that lessors who send the debtor a letter stating their intent to treat the lease as terminated,[16] or file a motion seeking immediate possession,[17] or place rent payments in a separate escrow account,[18] may continue to accept rent payments without waiving any other rights under Section 365.

Perhaps the best course for a lessor wishing to treat a lease as rejected is simply to seek immediate surrender of the property following statutory rejection under Section 365, and to refuse to accept any further rent payments.

## V. Effect of Deemed Rejection.

Section 365(d)(4) as amended provides that after the deemed rejection of a lease, the trustee shall immediately surrender the leased property to the lessor. This provision remains a matter of judicial uncertainty. Courts addressing this issue have evidenced considerable confusion over the meaning of the provision in practice and exactly what power it confers on the court to displace the debtor. Specifically, courts have differed as to whether (i) relief from the automatic stay must still be sought despite the immediate surrender provision of Section 365, and (ii) whether lessors must seek actual eviction under state law because the bankruptcy courts lack the power to directly order a debtor to vacate the leased premises.

A fair number of courts have held that the immediate surrender provision of Section 365 does not eliminate the need for a lift of the automatic stay of Section 362.[19] Among those courts, some have also adopted the view that after a lessor obtains relief from the stay, actual eviction of the debtor may be obtained only in accordance with rights and remedies under state law. Other courts have appeared willing, after granting the lessor relief from the stay, to issue an order directing the debtor to vacate the premises, without requiring the lessor to seek eviction in state court.

Alternatively, what appears to be an emerging majority of courts (including the Ninth Circuit) have treated Section 365(d)(4) as eliminating any need to obtain relief from the automatic stay.[20] These courts have interpreted the immediate surrender provision of Section 365 as conferring authority on bankruptcy courts to directly order a debtor to vacate the leased premises. In holding that Section 365 does not require lessors to seek eviction of a debtor in state courts, the courts have reasoned that state law should not operate to

ow a debtor to remain in possession of leased property when the lease has en deemed rejected and the lessor has the right to immediate repossession nder the Bankruptcy Code. Specific orders for debtors to vacate leased premises have allowed some reasonable period of time varying from 10 days to one month.

In light of these decisions, counsel for lessors may and should file a formal motion with the court upon rejection of a lease pursuant to Section 365, requesting that the debtor be ordered immediately to vacate the leased premises.

## VI. Conclusion.

Counsel for both debtors and lessors should be aware of the various means by which courts balance their competing interests under Section 365. Debtors must act promptly to retain the benefits of desirable leases and to obtain whatever extensions may be necessary in order to assess accurately whether the lease is in fact beneficial. Lessors must be vigilant in assuring that delays do not prejudice their rights under Section 365 and, upon rejection, should promptly seek to obtain the maximum rights available through the bankruptcy courts to recover possession of the leased properties.

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NOTE: A greatly expanded version of this article will be appearing in the Fall 1990 edition of The American Bankruptcy Law Journal.

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1. Pub. L. No. 98-353, 98 Stat. 333 (July 10, 1984). Hereinafter cited as the 1984 legislation or 1984 amendments.

2. In re Clark Resources, Inc., 68 B.R. 358 (Bkrtcy. N.D. Okla. 1986); see also, In re Harris Pine Mills, 862 F.2d 217 (9th Cir. 1988)

3. In re Gasoil, Inc., 59 B.R. 804 (Bkrtcy. N.D. Ohio 1986).

4. In re Independence Village, Inc., 52 B.R. 715 (Bkrtcy. E.D. Mich., N.D. 1985); see also, In re Sonora Convalescent Hospital, Inc., 69 B.R. 134 (Bkrtcy. E.D. Cal. 1986).

5. In the Matter of Condominium Administrative Services, Inc., 55 B.R. 792 (Bkrtcy. M.D. Fla. 1985).

6. See In re Care Givers, Inc., ---B.R.---, 1989 WL 201613 (Bkrtcy. N. D. Tex.).

7. In re Tulp, 108 B.R. 214 (Bkrtcy. N.D. Iowa 1989).

8. In the Matter of Burns Fabricating Co., 61 B.R. 955, 958 (Bkrtcy. E. D. Mich. S.D. 1986); see also Sea Harvest Corp. v. Riviera Land Co. 868 F.2d 1077 (9th Cir. 1989) (holding that documents entitled "Affirmation and Assumption of Executory Contracts" filed by debtors did not constitute acceptable motions for assumption as they did not move the court to do anything, but simply stated debtors' intentions).

9. In re Delta Paper Co., Inc., 74 B.R. 58, 60 (Bkrtcy. E.D. Tenn. 1987); In re BDM Corp., 71 B.R. 142, 145 (Bkrtcy. N.D. Ill., E.D. 1987); In re Diamond Head Emporium, Inc., 69 B.R. 487, 493 (Bkrtcy. Haw. 1987); In the Matter of Burns Fabricating Co., 61 B.R. 955, 958 (Bkrtcy. E.D. Mich. S.D. 1986); ("60-day period of sec. 365(d)(4) refers to the time in which the trustee or debtor must decide to assume or reject, and not the time in which the entire process must be completed.")

10. For interpretation of the cause requirement, see In re Babylon Ltd., 76 B.R. 270, 274 (Bkrtcy. S.D.N.Y. 1987) and cases cited therein.

11. By-Rite I, 47 B.R. 660, 670 (Bkrtcy. Utah 1985), rev'd on other grounds, By-Rite II, 55 B.R. 740 (Utah 1985); In re House of Emeralds, Inc., 57 B.R. 31, 35 (Bkrtcy. Haw. 1985), rev'd on other grounds, In re Diamond Head Emporium, Inc., 69 B.R. 487 (Bkrtcy. Haw. 1987); see also, In re Taynton Freight Systems, Inc., 55 B.R. 668, 671 (Bkrtcy. M.D. Penn. 1985); In re Las Margaritas, Inc., 54 B.R. 98, 99 (Bkrtcy. Nev. 1985); In the Matter of Coastal Ind., Inc., 58 B.R. 48, 51 (Bkrtcy. N.J. 1986).

12. In re Victoria Station, Inc., 88 B.R. 231, 236 (9th Cir BAP 1988), aff'd, 875 F.2d 1380 (9th Cir. 1989); Chapman Inv. Assoc. v. American Healthcare Management, Inc., 94 B.R. 420 (N.D. Tex. 1989), aff'd, 900 F.2d 827 (5th Cir. 1990); Tigr Restaurant, Inc., 79 B.R. 954, 960 (E.D.N.Y. 1987); (all supporting multiple extensions).

13. Chapman, 94 B.R. at 420, aff'd, 900 F.2d 827 (5th Cir. 1990); Victoria, 88 B.R. at 238 (9th Cir. 1989); By-Rite I, 47 B.R. at 670, rev'd on other grounds, By-Rite II, 55 B.R. at 470.

14. In the Matter of J. Woodson Hays, Inc., 69 B.R. 303 (Bkrtcy. M.D. Fla. 1987); In the Matter of Lew Mark Cleaners Corp., 86 B.R. 331, 335 (Bkrtcy. E.D.N.Y. 1988); In re Fosko Markets, Inc., 74 B.R. 384, 389 (Bkrtcy. S.D.N.Y. 1987); In re T.F.P. Resources, Inc., 56 B.R. 112, 113 (Bkrtcy. S.D.N.Y. 1985).

15. In re Re-Trac Corp., 59 B.R. 251, 257 (Bkrtcy. Minn. 1986) (citing Lovitt v. Appleatchee Riders Ass'n., 757 F.2d 1035, 1041 (9th Cir. 1985), cert denied, 474 U.S. 849 (1985); see also, In re Chandel Enter., Inc., 64 B.R. 607, 610 (Bkrtcy. C.D. Cal. 1986).

16. Re-Trac, 59 B.R. at 258.

17. Fosko, 74 B.R. at 389.

18. In re Southern Motel Assoc., Ltd, 81 B.R. 112, 118 (Bkrtcy. M.D. Fla. 1987).

19. In the Matter of Dublin Pub. Inc., 81 B.R. 735, 737 (Bkrtcy. N.D. Ga. 1988); In re Swiss Hot Dog, Inc., 72 B.R. 569, 571 (Colo. 1987); In re Diamond Head Emporium, 69 B.R. 487, 493 (Bkrtcy. Haw. 1987).

20. See Harvest Corp. v. Riviera Land Co., 868 F.2d 1077 (9th Cir. 1989); In re U.S. Fax, Inc., ---B.R.---, 1990 WL 61175 (E.D. Penn.); In the Matter of Emory Properties, Ltd., 106 B.R. 318 (Bkrtcy. N.D. Ga. 1989); In the Matter of Burns Fabricating Co., 61 B.R. 955, 959 (Bkrtcy. E.D. Mich. 1986).

## STEERING COMMITTEE MEETING MINUTES

A meeting was held on July 20, 1990 at noon at the Peninsular Club.

1. Discussion was had regarding the Shanty Creek Seminar. Presently, 84 people have signed up for the same. If you are a seminar participant, your materials should be forwarded to Robert W. Sawdey by no later than August 1, 1990. If you are unable to attend the seminar but would still like a copy of the course materials, please contact Brett Rodgers.

2. James A. Engbers reported on the status of various forms of entertainment planned for the afternoons at Shanty Creek, such as golf, tennis, canoeing, fishing, shopping and bicycling. If you have not yet signed up for any of these events and desire to participate, please contact Mr. Engbers.

3. Michael V. Maggio announced that for the present time he is the attorney in charge of the local office of the U.S. Trustee.

4. The next Steering Committee meeting was scheduled for 7:45 a.m. on Friday, August 24, at Shanty Creek. This will be a breakfast meeting and will be limited to the present bankruptcy Steering Committee members. The meeting will be held at the bar-porch area overlooking the lake. At that time future Steering Committee members will be determined and the Committee will act on the policy statement concerning Steering Committee membership, which statement is included in this Newsletter.

*Larry A. Ver Merris*

## LOCAL BANKRUPTCY STATISTICS

The following is a summary of the number of bankruptcy cases commenced in the United States Bankruptcy Court for the Western District of Michigan during the period from January 1, 1990 through June 30, 1990. These filings are compared to those made during the same period one year ago, and two years ago.

| | 1/1/90 - 6/30/90 | 1/1/89 - 6/30/89 | 1/1/88 - 6/30/88 |
|---|---|---|---|
| Chapter 7 | 2,017 | 1,695 | 1,427 |
| Chapter 11 | 74 | 54 | 57 |
| Chapter 12 | 9 | 5 | 17 |
| Chapter 13 | 821 | 604 | 567 |

**FROM THE BANKRUPTCY COURT:**

**THE CLERK'S OFFICE HAS NOW MOVED. THE NEW ADDRESS IS 299 FEDERAL BUILDING, 110 MICHIGAN STREET, N.W., GRAND RAPIDS, MICHIGAN 49503.**

UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF MICHIGAN

DEBTOR: _____
CASE NO.: _____

ANNUAL REPORT ON CONFIRMED PLAN

1. On the date of this report have you paid all administrative expenses required to be paid at this date by the Plan of Reorganization?

( ) Yes
( ) No Please explain if no.

2. On the date of this report have you paid all the priority taxes required to be paid at this date by the Plan of Reorganization?

( ) Yes
( ) No Please explain if no.

3. On the date of this report have you paid all payments to secured creditors required to be paid by this date by the Plan of Reorganization?

( ) Yes
( ) No Please explain if no.

4. On the date of this report have you paid all the payments to unsecured creditors required to be paid at this date by the Plan of Reorganization?

( ) Yes
( ) No Please explain if no.

5. On the date of this report are there any other acts or payments which were required to be made by this date which have not yet been accomplished?

( ) Yes
( ) No Please explain if yes.

Name: _____
Agent: _____
Address: _____

POLICY REGARDING
STEERING COMMITTEE MEMBERSHIP
FBA BANKRUPTCY SECTION

The number of Steering Committee members shall not be less than nine (9), nor greater than twelve (12), but the number may be changed from time to time by amendment to this policy.

At the 2nd Annual Bankruptcy Section Seminar in August of 1990, the existing Steering Committee shall meet and appoint, by rule of the Chairman, nine (9) members to the Steering Committee. The eight (8) existing Steering Committee members and Chairman shall be reappointed to their existing positions if they desire to continue to serve. If all the existing members are reappointed, then one (1) additional member will be appointed by the Chairman. If any of the existing members desire to resign their position, then they will be replaced by additional appointees so that the number of Steering Committee members will equal nine (9).

The nine (9) newly appointed Steering Committee members, including the Chairman, shall then by random selection (draw straws) serve staggered terms as follows:

A. One-third (1/3) of its composition shall serve for three (3) years.

B. One-third (1/3) of its composition shall serve for two (2) years.

C. One-third (1/3) of its composition shall serve for one (1) year.

Thereafter, as each of the above terms expires, these membership seats shall stand for reappointment each year at the annual meeting which is contemplated to be held each year in August at the annual seminar.

A vacancy among the Steering Committee membership shall be filled by appointment by a simple majority of the remaining Steering Committee members, from individuals meeting the qualifications of this Section, and any written policy adopted by the Steering Committee from time to time. A vacancy shall be filled only for the unexpired portion of the original term, at which time the Committee member shall be elected in the manner prescribed herein.

Qualifications for serving as a Steering Committee member shall simply be that of being a member of the Federal Bar Association for the Western District of Michigan, and a licensed practitioner in the State of Michigan in the practice of law.

## RECENT BANKRUPTCY DECISIONS:

The following are summaries of recent court decisions that address important issues of bankruptcy law and procedure. These summaries were prepared by Patrick E. Mears with the assistance of Larry A. Ver Merris.

Maislin Industries, U.S., Inc. v. Primary Steel, Inc., Case No. 89-624 (U.S.S.Ct. June 21, 1990). In this decision, the United States Supreme Court upheld what has been termed the "filed rate" doctrine requiring motor common carriers and their bankrupt estates to collect their rates in tariffs filed with the Interstate Commerce Commission ("ICC"). The Supreme Court declared unenforceable the so-called "Negotiated Rates Decisions" issued by the ICC, which permit that agency to prohibit collection of the filed rate when the carrier had previously negotiated a lower rate with its customer.

In this case, Quinn Freight Lines, Inc. ("Quinn") a subsidiary of a bankruptcy motor carrier, Maislin Industries, U.S., Inc. ("Maislin"), had privately negotiated interstate shipment rates with Primary Steel, Inc. These lower rates were never published with the ICC. After Maislin commenced a bankruptcy case, the agents of its estate commenced a collection action in the United States District Court for the Western District of Missouri to collect the "undercharges", viz., the difference between the filed rate and the negotiated rate. The District Court referred this dispute to the ICC and stayed the civil action in the meantime. The ICC thereafter ruled in Primary Steel's favor, finding that Primary Steel had relied on Quinn to file the negotiated rates, which it had not. The ICC therefore concluded that Maislin's bankruptcy estate could not collect these undercharges. Maislin's appeal to the Eighth Circuit Court of Appeals was affirmed, that Court deferring to the ICC's decision. On appeal, the Supreme Court reversed the Court of Appeals and remanded the matter "for further proceedings consistent with" its opinion.

Begier v. Internal Revenue Service, 110 S.Ct. 2258 (1990). In this decision, the United States Supreme Court held that payments of federal trust fund taxes made by a debtor/taxpayer within the preference period to the Internal Revenue Service cannot be recovered as preferences by the taxpayer's bankruptcy trustee even though those payments were not made from monies deposited in a special bank account designated to be the source for those payments. The Supreme Court, per Justice Marshall, reasoned that these funds were impressed by a trust in favor of the United States and, therefore, were categorized neither as "property of the estate" within the meaning of 11 U.S.C. § 541 nor as "property of the debtor" within the scope of 11 U.S.C. § 547(b).

Pennsylvania Dept. of Public Welfare v. Davenport, 110 S.Ct. 2126 (1990). In this case, the United States Supreme Court held in a decision also authored by Justice Marshall that a prepetition criminal restitution obligation constitutes a "debt" under 11 U.S.C. § 101(11) that may be discharged in a Chapter 13 case. Justice Marshall stated that the language and structure of the Bankruptcy Code do not reflect a Congressional intent that these obligations should be exempt from the broad discharge provisions of Chapter 13. Justice Marshall distinguished the Court's earlier decision in Kelly v. Robinson, 479 U.S. 36 (1986), which held that restitution obligations imposed as conditions of probation in state criminal actions are nondischargeable in Chapter 7 cases. In Kelly, the Supreme Court relied upon the language of 11 U.S.C. § 523(a)(7), applicable only to Chapter 7 cases.

In re Arnold, Case No. 89-6085 (6th Cir. July 11, 1990). This Sixth Circuit decision addresses the scope of 11 U.S.C. § 549(a) as it applies to post-petition payments made by a general contractor to a supplier of a bankrupt subcontractor. In 1986, the State of Tennessee contracted with J. Harold Shankle Construction Company ("Shankle") for the renovation of a public building. Under this renovation contract, Shankle was obligated to pay for all labor and materials used in the project. Shankle then retained the debtor as an electrical subcontractor who thereafter purchased materials on credit from Braid Electric Company ("Braid"). On May 20, 1987, Shankle terminated debtor for cause and the next day debtor commenced a Chapter 7 case in the United States Bankruptcy Court for the Middle District of Tennessee. As of that date, Shankle owed debtor $61,756.14 under the subcontract, of which $6,175.61 (10%) was classified as retainage. Also at the filing date, debtor owed Braid the sum of $69,820.84 for materials supplied by Braid on this project.

After debtor commenced its Chapter 7 case, Shankle paid Braid the sum of $61,756.14 for the materials used in the project pursuant to its contractual obligations with the State of Tennessee. Thereafter, the debtor's Chapter 7 trustee commenced an adversary proceeding against Braid to recover these payments on the theory that they were unauthorized post-petition transfers of estate property. Both the Bankruptcy and District Courts agreed with this theory and Braid appealed from the judgment rendered against it to the Sixth Circuit Court of Appeals.

On appeal, the Sixth Circuit reversed the decisions below and remanded the case with instructions that judgment be entered in favor of Braid. The Sixth Circuit found that the monies paid by Shankle to Braid did not constitute property of the estate but were the sole property of Shankle. In support of its decision, the Sixth Circuit cited the contract between Shankle and the State requiring Shankle to pay these sums to Braid. The Sixth Circuit also referred to its earlier opinion in Selby v. Ford Motor Co., 590 F.2d 642 (6th Cir. 1979), which recognized an independent obligation owed by a contractor to a materials supplier in the absence of a contract or state statute establishing such an obligation.

Central States, Southeast and Southwest Areas Pension Fund v. Keller, Case No. G 89-50033 (W.D. Mich. July 7, 1990). This decision addresses the scope of Michigan's fraudulent conveyance statute, M.C.L.A. §§ 566.11, et seq., as it applies to entireties property. In this case, the plaintiff, Central States, commenced an action against various defendants, the former owners of the bankrupt company, Skyland, Inc., their wives and other relatives to recover an ERISA withdrawal liability assessment in excess of $640,000. In this proceeding, Central States sought to unwind transfers made by defendants of their marital homes in trust and to recover their increased equity in those homes resulting from regular mortgage and other payments made since the trusts were created. District Judge Robert Holmes Bell refused to grant the relief requested by Central States, noting that, although the trusts themselves might be avoidable as fraudulent transfers, the increase in equity in entireties property could not be recovered. Judge Bell discussed a series of Michigan cases permitting similar recovery in circumstances distinguishable from those before him. Judge Bell concluded as follows:

> [h]ere, in contrast, after stripping away the trusts, the Court finds not extra-ordinary efforts by plaintiffs to defraud creditors, but continued payments in the regular course to satisfy antecedent debts. Yes, the payments were made out of the debtors' individual income. However, such income appears to have been the only income available to either household for the maintenance of their modest residence. In view of all the circumstances present, the Court refused to apply the exception

urged by plaintiffs. The debtors' contributions to the entireties estates appear to have been legitimate; that is, were made in satisfaction of antecedent debts for fair consideration and not with intent to defraud creditors.

Manufacturers National Bank of Detroit v. Auto Specialties Manufacturing Co. (In re Auto Specialties Manufacturing Co.), Case No. G89-50765-CA (W.D. Mich. July 7, 1990). This appellate decision also rendered by District Judge Bell construes language contained in loan documents permitting a bank to recover its attorneys' fees and costs of collection from a debtor. Prior to the commencement of its Chapter 11 case on October 3, 1988, Auto Specialties Manufacturing Co. ("AUSCO") had entered into a series of loan and security agreements with its primary lender, Manufacturers National Bank of Detroit (the "Bank"). These documents granted the Bank the right to charge AUSCO the Bank's reasonable costs of collecting its debt, including attorneys' fees. At the time AUSCO filed its Chapter 11 petition, AUSCO was indebted to Bank in an amount in excess of $4 million. Since Bank was an oversecured creditor, section 506(b) of the Bankruptcy Code, permitting Bank to recover its reasonable attorneys' fees and costs as part of its secured claim, became operative.

After its Chapter 11 filing, AUSCO entered into a post-petition lending agreement with Fidelcor Business Credit Corp. ("Fidelcorp") which provided that Fidelcorp would hold a lien senior to Bank in all of AUSCO's assets. As adequate protection to Bank, AUSCO agreed to create a fund consisting of monies sufficient to pay Bank's claims against Debtor, collection charges and $50,000 "to cover charges which may be added to the [fund] in the future." The appeal before Judge Bell involved paragraph 6 of the adequate protection stipulation concerning this $50,000 deposit, which read as follows:

> On or before March 1, 1989, Debtor shall deposit an additional Fifty Thousand and 00/100 Dollars ($50,000.00) in the Manufacturers Indebtedness Fund to cover additional costs which may be added to the Manufacturers Indebtedness in the future, which shall be free and clear of all liens and encumbrances, including, but not limited to, any lien claimed by Fidelcor in Debtor's pre and post-petition assets subject, however, to Debtor's right to object to the transfer of the same at that time. Furthermore, Manufacturers reserves the right to petition the Court at any time subsequent to March 1, 1989 for the Debtor to transfer additional monies to the Manufacturers Indebtedness Fund to cover additional charges.

Sometime prior to March 1, 1989, Bank requested payment of the $50,000 sum, which demand Debtor refused. On March 13, 1989, Debtor commenced an adversary proceeding against Bank alleging fraud, breach of contract and breach of fiduciary duty and seeking money damages against Bank and equitable subordination of the Bank's claims. Thereafter, Bank filed a motion with the bankruptcy court to compel AUSCO to deposit $50,000 into the fund, arguing that this sum was necessary to pay its attorneys' fees if Bank was successful in defending against the adversary proceeding. Bank argued that these fees were part of the costs of collection that Bank could recover from Debtor pursuant to its underlying loan documents. AUSCO opposed this motion, asserting that the costs of defending against a lawsuit for fraud and breach of fiduciary duty were not the type of costs contemplated by the loan agreements.

Bankruptcy Judge JoAnn Stevenson denied this motion, declaring that these costs were not intended by the parties to be reimbursed to the Bank at the time the loan agreements were executed. Judge Stevenson also stated that, to hold otherwise, would be inequitable to AUSCO since AUSCO would be required to pay

e Bank's attorneys' fees in defending an action based on allegations of the ank's own inequitable actions.

On appeal, District Judge Bell first found that the attorneys' fees language in the loan documents was ambiguous when applied to the facts of the dispute. Judge Bell, in examining the parties intent at the time the documents were signed, found that the parties "did not consider the possibility of fraud and breach of fiduciary duty when the loan agreements were signed." Consequently, Judge Bell held that Bankruptcy Judge Stevenson's decision denying the Bank's motion was not clearly erroneous.

Rosin v RCN Anlagenivestitionen Frodsgesellschaft II, Case No. 1:90-CV-308 (W.D. Mich. June 11, 1990). In this case, the Chapter 11 debtor, RCN, moved to extend its exclusive period in which to file a plan under 11 U.S.C. § 1121(d), which motion was granted by Bankruptcy Judge Laurence Howard. A party in interest opposed the motion and appealed to the District Court from the order below granting the requested extension. District Judge Benjamin Gibson dismissed the appeal on the grounds that (i) the order appealed from was not a final order; and (ii) there was no basis to grant an appellate review of the interlocutory order.

McHenry v. Ward (In re Ward), Case No. G89-40621 (W.D. Mich. March 27, 1990). In 1984, the plaintiffs in the instant action recovered a $60,000 money judgment against defendant in the United States District Court for the Western District of Michigan for securities fraud. After this judgment was entered, defendant commenced a Chapter 7 case in the Grand Rapids Bankruptcy Court. The plaintiffs thereupon commenced an adversary proceeding in that Court for a judgment of nondischargeability on account of debtor's fraud under 11 U.S.C. § 523(a)(2)(A). Summary judgment in favor of plaintiffs was granted on the basis of collateral estoppel in the adversary proceeding, whereupon debtor appealed to the district court. On this first appeal, District Judge Benjamin Gibson remanded the action to Bankruptcy Court, finding that, since the fraud issue in the district court action was not litigated under the "clear and convincing" evidentiary standard, collateral estoppel could not apply.

On remand, the adversary proceeding was tried before Bankruptcy Judge Stevenson, who entered judgment in favor of debtor and discharged the debt. On appeal, District Judge Richard Enslen affirmed the decision below finding no legal or factual error. In his opinion, Judge Enslen stated that, in their action under 11 U.S.C. § 523(a)(2)(A), the plaintiffs were required to establish that debtor received some sort of benefit on account of his alleged fraud. In the absence of such evidence, the action must fail. In his opinion, Judge Enslen also addressed issues of the plaintiff's alleged "reasonable reliance" under 11 U.S.C. § 523(a)(2)(A) and the existence of a fiduciary relationship between plaintiffs and debtor for purposes of 11 U.S.C. § 523(a)(4).

In re Premo, Case No. 87-09410 (Bankr. E.D. Mich. July 3, 1990). In this 47-page opinion, Bankruptcy Judge Arthur Spector sustained an individual debtor's objection to the claim of the Internal Revenue Service for unpaid withholding taxes due by two companies of which debtor was the principal equity owner. This decision addresses issues of who bears burden of proof in tax litigation in the bankruptcy court and the scope of "responsible person" liability under sections 6671 and 6672 of the Internal Revenue Code. Due to the length of the decision, it will not be summarized here.