

PUBLICATION

Reform Bankruptcy Act Provides Relief for Commercial Lessors

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October 17, 2006 marked the one year anniversary of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (the "Reform Act"). The Reform Act has provided some much needed relief to commercial landlords, and the reported decisions of bankruptcy courts during the first year of the Reform Act confirm the effectiveness of the new landlord-friendly provisions.

Assumption and Rejection. It is well known that Title 11 of the United States Code, 11 U.S.C. § 101, et seq. (the "Bankruptcy Code"), gives a debtor in bankruptcy broad powers to assume or reject commercial real estate leases. The debtor has the power to assume a lease provided that the debtor cures the non-monetary defaults under the lease. See 11 U.S.C. § 365. The debtor has the power to reject – that is, terminate – the lease, leaving the landlord with only an unsecured claim for damages. In addition, the debtor has the power to assign the lease, usually in connection with the sale of the debtor's assets, to a purchaser over the landlord's objection, and even under circumstances where the lease prohibits assignment without the landlord's consent. See 11 U.S.C. § 365(f).

The Old Act. Prior versions of the Bankruptcy Code provided considerable protection to debtors at the expense of the rights of commercial landlords. Before the Reform Act, the Bankruptcy Code provided that a debtor was deemed to have rejected a commercial lease if the debtor did not assume or reject the lease within 60 days after filing for bankruptcy protection. However, the Bankruptcy Code also gave the debtor the opportunity to obtain an extension of this time period, and bankruptcy courts were often very liberal in granting these extensions. Debtors were permitted to remain in bankruptcy for months and, in some cases, years without being forced to decide whether to assume or reject their commercial leases. A landlord was placed in the position of knowing that the debtor might reject the lease, without the ability to effectively market the space to a new tenant.

The Reform Act. The Reform Act is more landlord-friendly. See 11 U.S.C. § 365(d)(4); H.R. Rep. No. 109-31(I) (2005).)Granted, the Reform Act extends the initial period that a debtor has to evaluate a commercial real property lease from 60 to 120 days. However, the debtor may only obtain an extension of this period of time for an additional 90 days, for a total of 210 days. This is not the most desirable outcome for the landlord, but, unlike the old Act, a landlord is now able to tell a prospective tenant, that, even under a worst case scenario, the landlord will be able to deliver possession of the property 210 days after the debtor's bankruptcy filing unless the debtor affirms the lease.

The Reform Act is also landlordfriendly with regard to the mechanics of obtaining a time extension. Under the old Act, many courts allowed a debtor to obtain an extension of the time to assume or reject a lease so long as the debtor had its motion on file before end of the 60-day period. See *In re Beautyco, Inc.*, 207 B.R. 225, 229-230 (Bankr. N.D. Okla. 2004). Under the Reform Act, however, the debtor must actually file and obtain an order granting the debtor the extension within the 120 day period. If the debtor does not, the lease is automatically rejected. See, e.g., *In re Tubular Technologies, LLC*, 348 B.R. 699 (Bankr. S.C. 2006). This provision is intended to force debtors to make a decision whether to assume or reject a lease in a timely manner. Sec 3 Collier on Bankruptcy at ¶ 365.04[4], at p. 365-47 (Lawrence P. King, et al. eds., 15th ed. Revised 2005).

Finally, the Reform Act is clear that, upon the rejection of the lease, the debtor must immediately surrender the property to the landlord. This landlord-friendly provision was missing from the old Act, thereby often obstructing the landlord's timely access to property following the rejection of the lease. The Reform Act should give the landlord greater confidence that it will be able to deliver possession of the property to the replacement tenant in a timely manner.

In conclusion, commercial landlords are among the beneficiaries of the provisions of the Reform Act. There are a number of landlordfriendly provisions that place limits on the time that debtors can hold landlords at bay and which facilitate the re-leasing of property subject to leases debtors ultimately decide that they need to reject.