

# DEBTOR/CREDITOR

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## *Bankruptcy Sale Strips Lease*

The federal bankruptcy statute permits a Chapter 11 debtor to sell property free and clear of liens and interests. This would include a real property lease, and would dispossess the tenant. The statute also permits rejection of a lease without selling the property. However, the tenant of a rejected lease has the option to remain in possession and pay the rent. Most courts that have considered the interplay of these two provisions have treated a sale free and clear of interests as an implied rejection and have not permitted a debtor to sell free of the tenant's right to continue in possession.

However, a Federal Appeals Court in San Francisco recently ruled that the bankruptcy statute permits sale of property free and clear of a lease, thereby terminating the lease and permitting eviction of the tenant.

*Pinnacle Restaurant at Big Sky, LLC v. CH SP Acquisitions, LLC (In re Spanish Peaks Holdings II, LLC)*, 862 F.3d 1148 (9<sup>th</sup> Cir. 2017).

## *Discharge Denied for Undervaluing Asset*

Jason Worley's failed real estate investments forced him to file a Chapter 7 case. At the time he filed, Worley owned a 49% interest in an LLC which owned 10% of another LLC which owned timberland worth \$1,300,000. Applying those percentages to the timberland's value would make Worley's interest worth \$65,000.

However, on his bankruptcy schedules, Worley valued his 49% interest at \$2,500, which he arrived at by taking the largest annual distribution he had ever received from the LLC (\$483) rounding up to \$500 and applying a capitalization rate of five. On the objection of a creditor, the court denied Worley a discharge. Although the court conceded that Worley's illiquid LLC interest would sell for

less than the proportionate value of the underlying timberland, the court concluded that his estimate of value was "so low as to be unrealistic."

*Van Robinson v. Worley*, 849 F.3d 577 (4<sup>th</sup> Cir. 2017).

## *Dumping Property Costs on Lender*

An individual moved out of her over-encumbered condominium unit and filed a Chapter 13 case. Her Chapter 13 plan provided that title to the condominium unit would be transferred to the mortgage lender. The plan was confirmed without objection from the lender, who likely never read it. Subsequently, the condominium association sued the debtor for her post-bankruptcy condo fees.

The Maryland bankruptcy judge ruled that the debtor owed condo fees only for the period of time from the filing of her case to confirmation of her plan. Because a Chapter 13 plan may provide for "vesting of property... in the debtor or in any other entity," subsequent to confirmation, the lender owned the condominium and was liable to pay the condo fees.

*In re Peterson*, 2018 Bankr. LEXIS 330 (Bankr. D. Md. Feb. 7, 2018).



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Prepared by James C. Olson, Attorney and Counselor at Law