

THE BANKRUPT TENANT AND YOU PART 3 – WILL YOU GET PAID?

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In our June edition of this series we discussed the landlord's right to contractual rent after the tenant has filed for bankruptcy. Aside from receiving rent directly from the tenant, there are other sources of potential recovery that we will explore in this installment.

Proof of Claim for Past and Future Rent - The rejection of a lease in a bankruptcy case constitutes a breach and allows the landlord to recover damages. Bankruptcy courts follow the state law for damage calculations with one crucial caveat – since a landlord's claim for future rent may dwarf any other unsecured claim, the landlord's claim is limited to the greater of (1) one year's worth of rent or (2) 15% of the remaining rent due, but not more than 36 months of rent. If there is money in the estate to pay unsecured creditors, the landlord will get a pro-rated share of this limited amount. Rent that was due before the bankruptcy case was filed (prepetition rent) is not limited and the landlord's claim should include that amount also.

In order to be entitled to share in any proceeds, the landlord must file a proof of claim within a period of time prescribed by the court (usually 90-120 days after the case is filed). In rare circumstances, the court may set a quicker "bar date" so read your notices carefully. If you miss the filing deadline, you may be out of the money.

The proof of claim should contain commentary on how the calculation was made, and relevant ledgers and the lease should be attached. This writer has found that the more detail the better. It reduces the chances of claim objections. The claim must also provide for any offsets to the amount owed. Consequently, if there is a security deposit, the claim ought to note that it is offset by that deposit. The proof of claim must be signed by a representative the landlord/creditor who must declare under penalty of perjury that the information provided in the claim is true and correct to the best of that person's knowledge, information, and reasonable belief.

After the claim is filed, do not be surprised if you hear nothing from the former tenant or court for a while. Usually claims are not handled until after a plan of reorganization is approved or until the debtor or trustee has had a chance to collect money that is owed to the estate. This may take months or years.

Security Deposits – Letters of Credit - After a tenant files for bankruptcy you cannot draw down the cash security deposit without permission of the court. As long as you show that money is due and owing in excess of the deposit, you should have no problem in getting that permission. Letters of credit are a different creature. You do not need court permission to draw on a letter of credit because it is the obligation of a third party against whom the automatic stay does not apply. However, as is the case of a security deposit, there better be an obligation in excess of the letter of credit proceeds, or you may be in violation of your covenants under the letter of credit. If you file a proof of claim, you cannot pull down a security deposit or a letter of credit in an amount in excess of back rent owed and capped future rent.

Sales/Auctions from Premises – Ever been faced with the dreaded Going Out Of Business Sale from your retail property complete with big yellow signs in windows, clowns directing traffic and other trappings of failure? And for all of this, you may not be compensated unless you raise a stink. Most courts will allow sales from a bankrupt tenant's property with reasonable landlord protections. Your goal should be to restrict the sale to reasonable signage that does not interfere with other tenants, a reasonable time for the sale, limits on advertising along the street or in common areas, insurance and indemnity, and most of all - - compensation for the use of the premises. However you may not get these terms unless you object.

The same thing applies to auctions of merchandise, fixtures, or equipment -- you need limits and protection. Recently, however, more auctions are being conducted on the internet with maybe a viewing period prior to the auction and a period for the winning bidder to pick up its property. Regardless of the method, it is still important to ask for reasonable restrictions and make sure you get paid for the use of the premises.

Sale of Claims -- Finally, in some large bankruptcies, a company may send you a letter offering to buy your claim. The advantage is that you can receive an infusion of cash quickly. The disadvantages are numerous, but two stand out. First, the assignment the buyer may want you to sign will be one-sided unless you negotiate better terms. Second, the sale price will be greatly discounted for what you could recover if you waited. This writer usually ignores these inquiries. Proceed at your own risk!