

DEBTOR/CREDITOR

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Landlord Damages Capped

A Chapter 11 case is sometimes used by a debtor to walk away from unwanted leases. When a debtor rejects a real property lease, the bankruptcy statute caps the landlord's claim at the sum of any existing arrearage plus one year's future rent. Any security deposit is credited towards payment of that capped claim.

A California appellate court recently examined whether a different result ensues if a letter of credit is posted as security. The debtor had arranged for its bank to issue a letter of credit to the landlord as security for the rent obligation. When the debtor defaulted, the bank paid the landlord pursuant to the letter of credit. The landlord argued that the bank's payment could be applied to amounts owed above the cap, because the statute only capped claims against the debtor.

The Court rejected the landlord's argument, noting that the bank held collateral for the letter of credit. Because the bank's payment to the landlord would be recouped from the collateral, the Court applied the letter of credit payment to reduce the capped claim against the debtor.

Redback Networks, Inc. v. Mayan Networks Corp. (In re Mayan Networks Corp.), 306 B.R. 295 (Bankr. 9th Cir. 2004).

Piercing a Trust

Under a legal theory known as "piercing the corporate veil," a creditor of corporation can reach the assets of the corporation's shareholders. Generally, in order to pierce the corporate veil, a creditor must show that the shareholder treated corporate assets as his/her own, intermingled corporate and personal funds, or used the corporation for fraudulent purposes.

A New York bankruptcy court has decided that this legal theory also applies to trusts. A debtor set up an

irrevocable trust for the benefit of his children. Even though the debtor retained no reversionary interest in the trust, the bankruptcy court determined that the debtor had used the trust assets to conduct his own business affairs. Therefore, the trust's assets became assets in the bankruptcy case.

Trustees of family trusts should take care in the use of trust assets, lest those assets become available to creditors. *Pergament v. Maghazeh Family Trust (In re Maghazeh)*, 310 B.R. 5 (Bankr. E.D.N.Y. 2004).

Failure to Investigate Punished

A debtor filed a petition for bankruptcy relief and failed to list a particular creditor on the schedules. As a result, the creditor did not receive a notice of the September 8, 2003 deadline for filing claims against the debtor. On June 25, 2003, the debtor's attorney sent the creditor's attorney a letter stating that a bankruptcy had been filed and that the debtor would amend the schedules to include the creditor. On September 5, 2003, the amended schedules were filed. The Creditor filed a proof of claim on the November 3, 2003.

The court disallowed the creditors claim, even though the creditor was initially given no notice of the bankruptcy, because there was sufficient time between June 25 and September 8 for the creditor to investigate and determine the claims filing deadline.

In re Bourgoin, 306 B.R. 442 (Bankr. D. Conn. 2004).



This newsletter is intended to inform its readers of developments in the area of debtor/creditor relations. It is not legal advice or a legal opinion regarding any specific matter. You should consult a lawyer regarding any questions relating to your particular situation.

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