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OCT 20 1998

NEVIN E. O'BRIEN
UNITED STATES
BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

IN RE:	**In Proceedings Under Chapter 11**
BCE WEST, L.P., et al.,	**Case Nos. 98-12547 through 98-12570-PHX-CGC**
DEBTORS.	**Jointly Administered**
EID: 38-3196719	**AMENDED LIMITED OBJECTION OF FEDERAL REAL ESTATE INVESTMENT TRUST, NEW PLAN EXCEL REALTY TRUST AND PALM SPRINGS MILE ASSOCIATES, LTD. TO DEBTORS' MOTION FOR ORDER AUTHORIZING REJECTION OF NONRESIDENTIAL REAL PROPERTY**

TO THE HONORABLE CHARLES G. CASE, JUDGE OF THE SAID COURT:

Federal Realty Investment Trust ("Federal") **New Plan Excel Realty Trust** ("New Plan") and **Palm Springs Mile Associates, Ltd.** ("PSM") by their attorneys, **Ballard Spahr Andrews &**

Ingersoll, LLP, make this Limited Objection to the Debtors' Motion for Order Authorizing the Rejection of Nonresidential Real Property Leases (the "Motion"), and in support thereof aver:

1. On or about October 7, 1998, Debtors filed the Motion seeking authority to reject certain leases in shopping centers owned or managed by Federal, New Plan, and PSM. Federal, New Plan and PSM are hereinafter collectively referred to as "Objecting Landlords".

2. Among the leases which Debtors intend to reject are the following leased stores of Objecting Landlords:

#0037	Congressional Plaza	Rockville, MD	Federal
#0497	Rose Pavillion	Pleasanton, CA	New Plan
#0739	Palm Springs Mile S. Ctr.	Hialeah, FL	PSM
#1049	Laurel Shopping Center	Laurel, MD	Federal

3. By the Motion Debtors seek to reject these leases effective as of the earlier of the date the Debtors vacated the premises or the date of entry of this Court's order granting the Motion.

4. Objecting Landlords do not challenge either Debtors' authority to reject the subject leases or its business judgment in determining to reject these leases. Rather, Objecting Landlords challenge only Debtors' attempt to reject the leases retroactive to a date prior to the date of entry of the Order granting the relief requested.

5. Section 365(a) of the Code provides that the debtor-in-possession may, subject to court approval, assume or reject its leases. Bankruptcy Rule 6006 provides that a proceeding to assume or reject an unexpired lease is governed by Bankruptcy Rule 9014 (Contested Matters) and requires notice and a hearing.

6. The majority position on the effective date of a lease rejection, which is grounded on the plain meaning of the statute, holds that the rejection is not effective until approved by the court and that the obligation to pay administrative rent continues through to that effective date. Section

365(a):

> "requires two distinct actions, one by the trustee [or debtor-in-possession] and one by the court. The trustee is to assume or reject, and the court is to approve or disapprove. Therefore, under Section 365(a), rejection of an unexpired lease can be accomplished only by an order of the bankruptcy court." [Emphasis added]

In Re Arizona Appetito's Stores, Inc., 893 F. 2d 216 (9th Cir. 1990). And see, *In Re Thinking Machines*, 67 F.3d 1021 (1st Cir. 1995); *In Re: Revco D.S., Inc.*, 109 B.R. 264 (Bankr. N.D. Ohio 1989); *In Re Worths Stores Corp.*, 130 B.R. 531 (Bankr. E.D. Mo. 1991); *In Re Federated Department Stores, Inc., et al.*, 131 B.R. 808 (S.D. Ohio, 1991); *In Re Paul Harris Stores, Inc., et al.*, 148 B.R. 307 (S.D.Ind. 1992); *In Re 1 Potato 2, Inc.*, 182 B.R. 540 (Bankr. D.Minn. 1995); *In Re Appliance Store, Inc.*, 148 B.R. 234 (Bankr. W.D.Pa. 1992); *In Re Valley Steel Products Co., Inc.*, 147 B.R. 168 (Bankr. E.D.Mo. 1992); *In Re D'Lites of America, Inc.*, 86 B.R. 299 (Bankr. N.D. Ga. 1988); *In Re Garfinckel's, Inc.*, 118 B.R. 154 (Bankr. D.C. 1990); and, *In Re Virginia Packaging Supply Co., Inc.*, 122 B.R. 491 (Bankr. E.D.Va. 1990).

7. In the matter of *Surf City Squeeze, Inc.*, pending in this Court at docket 97-00451-PHX-GBN, the Honorable George B. Nielsen, Jr., was called upon to decide a similar issue. Judge Nielsen held that a lease is not rejected until the court issues its order approving rejection and that rent must be paid through the rejection date. (See Bench Decision attached as Exhibit "A" hereto, at p. 10, ln. 8-15 and p. 11 ln. 4-16.)

8. As the *Revco, supra*, and *Federated, supra*, cases have held, to hold that something less than court approval of a debtor's rejection of a lease (except where the lease is deemed rejected under Section 365(d)(4) of the Code) is required would be to place every landlord at risk if it takes any action in reliance of the debtor's notification of rejection (by way of motion or otherwise) but in the absence of a court order. Even if the debtor notifies a landlord that it has vacated the premises, intends to reject same, turns over the keys and simultaneously files a motion to reject, as the debtor

did in *Worths, supra*, the landlord is still left in "no-man's land" until the court enters an order approving the rejection. The creditors' committee or some other interested party may object to the rejection as not being in the best interest of the estate.

WHEREFORE, Objecting Landlords pray that Debtors' Motion be granted as of the later of the date of entry of this Court's Order approving rejection of the leases or the date that Debtors actually surrender the subject premises to Federal in the condition required by the applicable leases; and

WHEREFORE, Objecting Landlords pray that this Court order the Debtors to immediately pay to Objecting Landlords all post-petition rentals; and,

WHEREFORE, Objecting Landlords pray for such other and further relief as may be just under the circumstances.

BALLARD SPAHR ANDREWS & INGERSOLL

BY: _____

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ORIGINAL

UNITED STATES BANKRUPTCY COURT
DISTRICT OF ARIZONA

In Re.		
SURF CITY SQUEEZE, INC.	CH. 11	97-00451-PHX-GBN
ORAL ARGUMENT ON THE LEGAL QUESTION WHEN THE REJECTION IS DEEMED EFFECTIVE		

U.S. Bankruptcy Court
2929 N. Central Ave., 9th Floor
Phoenix, Arizona 85012

April 9, 1997
9:04 a.m.

BEFORE THE HONORABLE GEORGE B. NIELSEN, JR., Judge
(Designation of Record)

APPEARANCES:

For the Debtor: Samantha G. Masters-Brown
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For Official Committee of Unsecured Creditors: Charles R. Sterbach
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For MaceRich Company, Westfield Corporation, Inc.: Thomas J. Leanse
KATTEN MUCHIN & ZAVIS
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For Kravco Company, New Plan Realty Trust, General Growth Management, The Equitable Life Assurance Society of the U.S.: David L. Pollack
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1 APPEARANCES: (Continued)

2 For Kravco Company, New Plan Realty Trust, General Growth Management, and The Equitable Life Assurance Society of the U.S.:

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4

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6 For Simon Debartolo Group, Century III Associates, Knickerbocker Properties:

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Attorney at Law
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25 Proceedings recorded by electronic sound technician, Jo-Ann Stawarski; transcript produced by A/V Tronics, Inc.

1 THE COURT: Lady and gentlemen, I'll make a ruling
2 now in connection with this difficult matter. I'll make my
3 ruling part of the records of this case by announcing it
4 orally at this time. Any interested party who wishes a
5 complete copy of my ruling, my reasons therefore, may obtain
6 it by contracting with the court technician obtaining thereby
7 either a tape or transcript of this hearing.
8 And this has been oral argument on a legal question
9 arising in a Chapter 11 business reorganization case, the
10 question being when the rejection date of certain commercial
11 leases is to be deemed effective.
12 A debtor, subject to the Court's approval, may
13 assume or reject executory contracts and unexpired leases.
14 Where the debtor is a lessee under an unexpired lease of
15 nonresidential real property, the debtor has 60 days to
16 decide whether to assume or reject. During that period, the
17 debtor must continue to perform all of the obligations of the
18 debtor under the lease. That's the rule of the Ninth Circuit
19 in In re Pacific Atlantic Trading Company, 27 F.3d 401 at
20 403.
21 Notwithstanding this general analysis of § 365(a)
22 and 365(d)(3), the question is does the Court have the
23 authority to make a rejection retroactive to the date the
24 rejection motion was filed. While the Ninth Circuit has not
25 squarely addressed this issue, the First Circuit certainly

1 has. That case is In re Thinking Machines Corporation, 67
2 F.3d 1021.
3 The First Circuit summarized as follows:
4 "Here the protagonists assure us the
5 statutory language is plain. We need not
6 go beyond it. Debtor says rejection of a
7 nonresidential lease plainly becomes
8 effective on the motion filing date
9 subject to defeasance in the event a
10 judge vetoes the decision."
11 The landlord said the rejection plainly cannot become
12 effective until the court approval date. See 67 F.3d at 1025.
13 The Court noted authorities are divided on the
14 question. The minority view is that § 365 should be read to
15 align judicial approval as a condition subsequent to the
16 independently effective rejection of a non-residential lease.
17 The majority view reads 365(a) to require judicial approval
18 as a condition precedent to an effective rejection.
19 While noting that § 365(a) was ambiguous as to
20 whether approval constitutes a condition precedent or
21 subsequent to rejection, the First Circuit held § 365(a) is
22 most faithfully read as making court approval a condition
23 precedent to effectiveness of rejection. Therefore, the date
24 of court approval, not the motion filing date, controls.
25 The court cited four reasons for adopting the

1 majority view. I don't think it's necessary to go into those
2 reasons. Given the above reasons, the court adopted the
3 majority view, however, and this is the language that helps
4 set the stage for this present dispute. The court went on to
5 state that nothing precludes a bankruptcy court in an
6 appropriate § 365(a) case from approving a rejection of a
7 non-residential lease retroactive to the motion filing date.
8 See the First Circuit opinion at page 1028.
9 The court noted that bankruptcy courts are courts
10 of equity and may sometimes abandon mechanical solutions in
11 favor or fairness. In the § 365 context this means
12 bankruptcy courts may enter retroactive orders of approval
13 and may do so when the balance of equities predominates in
14 favor of such remediation.
15 In a footnote the court found a retroactive
16 approval order would not violate § 365(d)(3) which commands
17 debtor to pay rent at the contract rate until a
18 non-residential lease is rejected because it does not
19 stipulate that a rejection cannot be made to apply
20 retroactively. See 67 F.3d at page 1028, footnote 3.
21 The First Circuit did note that equitable powers
22 are not unlimited. See page 1028. Thus, a bankruptcy
23 court's exercise of its residual equitable powers must be
24 connected to and advance the purposes of the specific
25 provisions in the code. There is little question, however,

1 that a retroactive order may be appropriate as long as it
2 promotes the purpose of § 365(a).
3 I believe I should adopt the majority view that
4 rejection is not effective until approved by the court. See
5 In re 1 Potato 2, Incorporated, 182 B.R. 540 at 541. But I
6 believe that I'm required by the orientation of the Ninth
7 Circuit to resist the notion that a rejection date can be
8 applied retroactively as the First Circuit advances.
9 First of all, as noted by the Ninth Circuit
10 Bankruptcy Appellate Panel, it is true that bankruptcy courts
11 sit as courts of equity. However, a fundamental principal of
12 equity jurisprudence is that equity follows the law. Court
13 of equity are bound to follow express statutory commands to
14 the same extent as are courts of law. Bankruptcy courts are
15 no more entitled to ignore the law than are other courts.
16 See the BAP's decision in Hoffman Brothers, 173 B.R. 177 at
17 186 citing an earlier Ninth Circuit case In re Shoreline
18 Concrete, 831 F.2d 903 at 905.
19 In the present case while the First Circuit
20 minimizes the impact of 365(d)(3) by holding that subsection
21 (d)(3) does not stipulate that a rejection cannot be made to
22 apply retroactively, see footnote three, I believe that the
23 fact remains § 365(d)(3) compels the debtor, at least in this
24 circuit, to perform all these obligations prior to assumption
25 or rejection. It would seem a retroactive rejection order

1 would necessarily violate 365(d)(3) since under the majority
2 view the rejection order is a condition precedent to
3 rejection, and as such, absent that order, if the debtor is
4 required to comply with § 365(d)(3).
5 The Ninth Circuit has certainly endorsed this
6 position. In Pacific Atlantic an involuntary petition was
7 filed. At about that time the debtor ceased to conduct
8 business and was in arrears in a one-month's rental payment,
9 and totally in arrears on payments for subsequent months. By
10 the time the petition was filed the debtor owed over $145,000
11 in unpaid rent. See 27 F.3d at page 402.
12 After the order for relief was entered on October
13 31st of 1988, a trustee was appointed. The trustee had a
14 conversation with the sublessor. The sublessor expected the
15 estate to pay rent. The trustee made no payments. Trustee's
16 counsel informed the sublessor that the sublessor was under a
17 misapprehension in believing the trustee was bound by the
18 sublease or that the sublessor was entitled to administrative
19 rent.
20 Trustee indicated to his attorney that he did not
21 intend to assume the lease, that the estate was not subject
22 to the lease and the estate was liable only to the extent it
23 used the premises; trustee was not using the premises in that
24 case, was promptly removing certain odds and ends from the
25 premises and the sublessor should do what it needed to to

1 lease the premises. Nonetheless, the sublessor filed an
2 administrative claim for rent at the contract rate during the
3 60 day pre-rejection period.
4 The court squarely ruled that the trustee's failure
5 to pay the full amount of the debtor's rent obligation under
6 a non-residential real estate lease for the period following
7 bankruptcy but prior to rejection under 365(d)(4) gave rise
8 to an administrative claim for the full amount regardless of
9 the actual value conferred by the lease upon the estate.
10 As noted by our circuit, the trustee was required
11 by § 365(d)(3) to make a lease payment prior to the end of
12 the 60-day period pending assumption or rejection. Moreover,
13 the circuit found that prior to the 1984 amendments the
14 trustee did not have to timely perform. Lessors were
15 entitled to an administrative priority for occupancy but only
16 to the extent equal to the reasonable value of the debtor's
17 actual use and occupancy. See 27 F.3d at 403.
18 The court stated legislative history indicates the
19 statute was enacted to ameliorate the immediate financial
20 burden borne by lessors during the period in which trustees
21 decided whether to assume. The problem is that during the
22 time debtor has vacated space but not yet decided to assume
23 or reject. The trustee has stopped making payments. In this
24 situation the landlord is forced to provide current services.
25 No other creditor is put in this position.

1 The court discussed an earlier Bankruptcy Appellate
2 Panel decision, Orvco, where the panel diverged from these
3 authorities in the words of the Ninth Circuit. See 27 F.3d
4 at 404. The Bankruptcy Appellate Panel concluded that where
5 a lease of non-residential real property is deemed rejected
6 and the trustee is not paid rent prior to rejection, a lessor
7 must nonetheless establish its claim under § 503(b)(1)(A).
8 The court rejected this analysis stating:
9 "The plain unconditional language of the
10 statute demands that a trustee promptly
11 pay the full amount of rent due under a
12 non-residential real property lease
13 during the 60-day period pending
14 assumption or rejection."
15 Under Orvco a trustee can evade this responsibility merely by
16 refusing to pay the rent prior to rejection. All the while
17 the lessor would be forced to provide current services at its
18 own expense. This is wholly inconsistent with the mandate of
19 § 365(d)(3). See page 404 of 27 F.3d.
20 In the present case the debtor's primary argument
21 is that it abandoned -- not abandoned in the bankruptcy term
22 but abandoned the leases pre-petition. There's some dispute
23 of fact on this that was presented from the landlords at oral
24 argument. But assuming the debtor is correct, does this
25 abandonment mean the lease was no longer unexpired when the

1 debtor filed bankruptcy?

2 Even if the debtor turns in the keys, and there's
3 again some factual controversy there, but where a debtor
4 turns in the keys, abandons the premises and immediately
5 files a motion to reject, can a debtor thereby be excused
6 from the requirements of § 365(d)(3) by asking that the lease
7 be deemed rejected on the date the motion was filed.

8 Even if the landlord is on notice the debtor has
9 abandoned the property, has turned in the keys and has filed
10 a motion to reject, § 365(a) requires court approval. §
11 365(d)(3) plainly requires payment of full rent because a
12 rejection is not effective until the court enters the order.
13 The landlord would probably be advised by its bankruptcy
14 counsel that it could not safely rent the property until that
15 rejection order was entered. Yet under the equitable notions
16 espoused by the learned First Circuit, the court might be
17 able to retroactively apply a rejection effectively undoing
18 the protections afforded by § 365(d)(3) to creditors who are
19 still forced to provide current services while being unable
20 to rent the premises.

21 While the Ninth Circuit did not specifically
22 address this issue in Pacific Atlantic, the court did note
23 that rent accrued prior to rejection regardless of the actual
24 value conferred by the lease upon the estate was an
25 administrative claim. See page 401 of the opinion. This

1 implies that the Ninth Circuit would look askance at the
2 equitable notions advanced by the debtor and the committee
3 and endorses a minority position by certain courts.
4 That's why I'm going to reject that position. I do
5 not believe I have that rejection power. Well represented
6 debtors, as this debtor is well represented, can craft other
7 alternatives, and some suggestions were even made to
8 ameliorate any harmful effects caused by the administrative
9 claim that accrues; that would include setting hearings on
10 extremely short notice, possibly even obtain, in appropriate
11 cases, seeking to have a rejection order entered ex parte but
12 expressly subject to reconsideration. There's various
13 techniques that could be utilized here to minimize the
14 administrative claim in these circumstances, but I do not
15 believe a power to deem something retroactive is among those
16 techniques.
17 That's why I'll find against the debtor. I'll deny
18 the debtor's motion and require and find that the
19 administrative claim does accrue until the rejection order is
20 entered.
21 That will be my decision in this matter. Anything
22 else to discuss while we're together?
23 We'll be adjourned in this case then. I'm going to
24 leave the line, gentlemen.
25

1 (Proceedings Concluded)
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3
4 I certify that the foregoing is a correct
5 transcript from the record of proceedings in the
6 above-entitled matter.
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9 April 11, 1997
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Phoenix, Arizona 85004
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KEVIN E. O'BRIEN
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FOR THE DISTRICT OF ARIZONA

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BCE WEST, L.P., et al.,	)	**Case Nos. 98-12547 through 98-12570-PHX-CGC**
DEBTORS.	)	**Jointly Administered**
EID: 38-3196719	)	**AMENDED LIMITED OBJECTION OF FEDERAL REAL ESTATE INVESTMENT TRUST, NEW PLAN EXCEL REALTY TRUST AND PALM SPRINGS MILE ASSOCIATES, LTD. TO DEBTORS' MOTION FOR ORDER AUTHORIZING REJECTION OF NONRESIDENTIAL REAL PROPERTY**

CERTIFICATE OF SERVICE

I certify that a copy of the attached **AMENDED LIMITED OBJECTION OF FEDERAL REAL ESTATE INVESTMENT TRUST, NEW PLAN EXCEL REALTY TRUST AND PALM SPRINGS MILE ASSOCIATES, LTD. TO DEBTORS' MOTION FOR ORDER**

AUTHORIZING REJECTION OF NONRESIDENTIAL REAL PROPERTY was served by **Federal Express** on the following:

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BY: /S/
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Secretary to David L. Pollack
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DATE: October 20, 1998