Where's the Rent? Statutory and Contractual Payment Excuses in Pandemic Bankruptcies

By Erin R. Fay[*]

I. Introduction

By any measure, 2020 was an exceedingly challenging year for businesses. Market analysts reported 60 major retail bankruptcies, the largest number since the 2009 financial markets crisis,[1] 160 consumer-facing business bankruptcies, and more than 12,200 store closures.[2] Indeed, the pandemic appears to have accelerated long-anticipated changes in consumer behavior and exacerbated the existing abundance of retail square footage in the United States.[3]

The Bankruptcy Code contains numerous tools for debtors with large lease portfolios to restructure their businesses. The Bankruptcy Code, in turn, contains certain protections for landlords while a tenant is in bankruptcy. The pandemic tested the boundaries of these sometimes competing provisions as tenants' revenues dried up overnight, but landlords required rent streams to enable them to pay their mortgages and maintain properties. Although the Bankruptcy Code would appear to contain little flexibility as to a debtor paying its post-petition rent, pandemic courts were hesitant to swiftly enforce rent payment obligations. Unsurprisingly, rent payment was a key issue in many pandemic retail bankruptcies.[4]

Throughout the pandemic, debtors asked for relief from their post-petition rent obligations in a variety of ways—from extending rent payment dates to "mothballing" their operations and chapter 11 cases to abating or suspending rent payments. Despite section 365(d)(3) of the Bankruptcy Code which appears to require rent payments to be made *when due* (especially after the initial 60 days of a chapter 11 case), debtors were remarkably successful in delaying, reducing, or making no rent payments particularly in the beginning of the pandemic. Moreover, many of the relevant proceedings laid bare the procedural challenges required for courts to make nuanced decisions regarding portfolios of leases in a meaningful timeframe for all parties. Finally, these proceedings highlighted a potential statutory gap in that the Bankruptcy Code does not dictate the remedy if rent is not timely paid.

II. Section 365(d)(3) of the Bankruptcy Code

Section 365(d)(3) of the Bankruptcy Code ("Section 365(d)(3)") requires a debtor to timely pay rent as required under a lease that arises in the period

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after the petition date and until the lease is assumed or rejected, unless the court finds cause to extend the payment date for up to 60 days post-petition. More specifically, it states, in relevant part, as follows:

> The trustee shall timely perform all the obligations of the debtor . . . arising from and after the order for relief under any unexpired lease of nonresidential real property, until such lease is assumed or rejected, notwithstanding section 503(b)(1) of this title. The court may extend, for cause, the time for performance of any such obligation that arises within 60 days after the date of the order for relief, but the time for performance shall not be extended beyond such 60-day period.

11 U.S.C. § 365(d)(3).

The "notwithstanding" reference to Bankruptcy Code section 503(b)(1) is notable, as such section would otherwise engraft the requirement for an administrative expense that the payment be "actual necessary costs and expenses of preserving the estate." Instead, the implication from the plain language is that lease payments are not run-of-the-mill administrative expenses and the amount to be paid is the amount stated in the lease. Although rent payments do not have a technical superpriority, the requirement of current payment in Section 365(d)(3) can be read to provide a functional superpriority of payment. Moreover, the legislative history around the provision reflects a congressional concern for landlords being unwillingly forced to supply credit to a debtor.[5] Nevertheless, there is disagreement in the case law regarding the administrative claim status of obligations under a lease, which, as discussed below, became important in the pandemic.

Further, the language in Section 365(d)(3) refers to the "obligations of the debtor" under a lease or contract. This language points the court to the specific language of the applicable agreement and related applicable law. During the pandemic, *force majeure* clauses took on a life of their own in many areas of law, including bankruptcy. In addition to other arguments, debtors asserted that their obligations under Section 365(d)(3) were affected by the pandemic itself or by various regulations limiting or prohibiting business operations. Additionally, debtors argued that state common law defenses applied to further minimize rent obligations. As discussed below, these novel questions were met with a variety of responses by different bankruptcy courts.

III. Various Approaches to Delay or Avoid Rent Payments

A. Strategy 1: Mothballing

At the beginning of the pandemic, already pending cases were caught in precarious position. Some of these debtors had filed to liquidate their assets, which often requires "going out of business" sales. These sales, of course, could not happen in the expected timeframe without customers shopping in stores. Other debtors intended to operate their businesses and continue to generate revenue to fund their cases. With broad stay-at-home mandates issued in all states, income streams were decimated overnight in a variety of industries. Nevertheless, administrative costs such as rent and professional fees continued to accrue. Budgets underlying the financing or use of cash collateral in the cases were built on suddenly unachievable assumptions.

Some of these cases converted to chapter 7 proceedings,[6] while others attempted to freeze or mothball their operations and chapter 11 cases.

Often as a part of mothballing, debtors requested orders confirming the 60-day extension for cause under Section 365(d)(3). Courts were generally receptive to granting such relief.[7] Some courts were additionally willing to take these orders a step further and limit the availability of non-emergency hearings for parties seeking other relief that would arguably undermine the 60-day breathing spell, such as stay relief to foreclose or to compel immediate assumption or rejection.[8]

1. *In re Modell's Sporting Goods, Inc.*

One of the first cases where mothballing was approved was In re Modell's Sporting Goods, Inc., et al., Case No. 20-14179 (Bankr. D.N.J.). The Modell's debtors filed on March 11, 2020 to effectuate an orderly liquidation of their assets through, *inter alia,* going out of business sales at their 134 stores.[9] As of the petition date, Modell's had been experiencing liquidity issues and had failed to pay rent at most of its stores for several months.[10] In addition, as a part of its attempts to address liquidity issues, Modell's had negotiated rent relief or other concessions from landlords both in early 2019 and the weeks leading up to the petition date.[11] As a result, many landlords entered the case without having received rent for several months and with recently renegotiated leases or lease concessions.

Shortly after Modell's filed its petitions, COVID began to take hold and various state and local orders were issued restricting business operations. As a result, on March 23, 2020, Modell's filed an emergency motion to suspend its bankruptcy cases and operations for a period of 60 days pursuant to sections 105 and 305 of the Bankruptcy Code.[12] The Suspension Motion sought to suspend all deadlines and activities in the chapter 11 cases, to defer payment of all but certain essential expenses under a modified budget, cease in-person operations, and to terminate almost all employees.[13]

The Modell's debtors argued that Bankruptcy Code section 305 supported the relief requested by permitting a court to "suspend all proceedings in a case under this title, at any time if—(1) the interests of creditors and the debtor would be better served by such dismissal or suspension." 11 U.S.C. § 305(a)(1). The debtors further argued that section 105(a) of the Bankruptcy Code - which provides that "[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title" - supported their requested relief.[14] It was clear in Modell's that the debtors did not have sufficient funds to pay the necessary rent until after their going out of business sales generated proceeds, so there was a practical payment issue.[15]

Numerous landlords objected to the Suspension Motion arguing that the Bankruptcy Code did not permit the relief requested and that the landlords should not be forced to bear the extreme burden of the suspension.[16] In particular, the landlords argued that the requested relief was in direct contradiction to Section 365(d)(3) and that neither section 305 or 105 of the Bank-

ruptcy Code can be used as requested and in a manner that overrides explicit Bankruptcy Code provisions.[17] Further, the landlords requested varying forms of adequate protection.[18]

Four days after the Suspension Motion was filed, the court entered an initial order granting the majority of the requested relief on a temporary basis through April 30, 2020.[19] Such order was further extended through May 31, 2020 and then June 15, 2020.[20] In entering the interim versions of such orders, the court took into consideration the circumstances of all parties and the lack of then-present liquidity.[21] The court also noted that in addition to rent not being paid, the secured lenders were not being paid and there was no final waiver of the estate's right to surcharge the lenders' collateral pursuant to section 506(c) of the Bankruptcy Code.[22] Taking these and other considerations into account, the court determined that brief deferrals of the debtors' time to pay rent were appropriate and in all parties' interests.[23] The court encouraged the parties to negotiate a resolution and did not enjoin parties from making requests for emergency relief as needed.[24]

During these extensions, Modell's, dozens of its landlords, the official committee of unsecured creditors and the debtors' senior secured lenders engaged in court-ordered mediation sessions that ultimately resulted in a June 10, 2020 stipulation that provided, *inter alia*, for (i) payment of certain post-petition rent at varying levels depending on the status of operations, (ii) reservations of rights as to unpaid amounts and other issues, (iii) landlords' agreement to not seek payment of unpaid amounts until a date certain, and (iv) rejection of leases and property surrender by August 31, 2020. Under this structure, Modell's resumed its store closing sales in late June and later confirmed a liquidating plan that provided for full payment of administrative claims.[25]

B. Strategy 2: Extending the 60-day period in Section 365(d)(3)

As a part of the mothballing strategy or as a standalone additional strategy, some debtors sought to extend the time to satisfy lease obligations far beyond the stated period in Section 365(d)(3). Unlike *Modell's*, some bankruptcy cases were well into their chapter 11 processes when the pandemic hit and the 60-day period in Section 365(d)(3) was significantly advanced. One such case was In re Pier 1 Imports, Inc., Case No. 20-30805 (Bankr. E.D. Va.). The Pier 1 debtors filed chapter 11 petitions on February 17, 2020 with the stated goal of confirming a chapter 11 plan in 60 days.[26] Instead, one month into the case, their stores closed for an unknown duration.[27]

Shortly thereafter, the debtors filed a motion seeking emergency relief related to operating under a limited budget that did not pay rent, and adjourning a wide variety of filed motions and certain later filed motions, including those that would seek relief related to unpaid post-petition rent.[28] In support of this relief, the debtors cited sections 105 and 365(d)(2) of the Bankruptcy Code, the terms of their leases and various theories of state law, including doctrines related to governmental takings, frustration of purpose, and impossibility.[29] Landlords and other parties objected to the motion on bases

similar to those raised in opposition to the Modell's motion.[30]

Six days after the debtors filed the motion, the court approved it, including rent deferral, on an interim basis. The court issued a further approval order on May 5, 2020.[31] In total, the relief granted by the court, among other things, permitted the Pier 1 debtors to pause their obligation to pay post-petition rent for 104 days after the petition date and to defer payments an even longer period of time.[32]

In its memorandum approval order, the court based its ruling on section 105(a) of the Bankruptcy Code noting that the order "will not override any explicit mandate to the contrary set forth in the Bankruptcy Code."[33] The court went on to analogize the relief from payment of post-petition obligations to the relief from payment of pre-petition obligations explicit within the Bankruptcy Code, finding the deferral necessary for a "breathing spell."[34] The court further explained that its ruling did not contradict explicit Bankruptcy Code provisions, namely Section 365(d)(3), because that provision does not "give the Lessors a right to compel payment." Instead, the landlords are left with administrative claims to be paid in accordance with a chapter 11 plan.[35] Additionally to this point, the court determined that "[t]o compel payment by the Debtors now would be to elevate payment of rent to the Lessors to a superpriority status" and that the lessors were not entitled to such relief.[36] To the extent the lessors were entitled to adequate protection, the court found that the debtors' continued payment of insurance and utility costs and the debtors' assurance that deferred rent would be paid in July was sufficient.[37]

Thereafter, the Pier 1 debtors began paying rent for all stores on June 1, 2020.[38] Unfortunately, the debtors had to liquidate all of their assets and contemporaneously filed a chapter 11 liquidation plan. Instead of the debtors' promise that unpaid deferred rent for April and May would be paid in July, the plan provided that such rent would either be paid in full by September 12, 2020 if the landlords permitted the debtors to conduct store closing sales as needed, or would be deemed to be treated the same as administrative claims were treated under the debtors' chapter 11 plan.[39] The plan, in turn, proposed to pay administrative claimants only a pro rata amount and projected administrative claim recoveries at 10%-40%.[40] This outcome may not have vindicated the court's ruling that a promise of later payment is adequate protection.

C. Rent Abatement

With no end to the pandemic in sight, debtors next began seeking to suspend or abate rent under several theories, including force majeure lease clauses and state law doctrines of frustration of purpose and impossibility. Notably, subject to certain exceptions, the Bankruptcy Code does not vitiate underlying lease provisions or state landlord-tenant law.[41] Section 365(d)(3) expressly requires a debtor to timely perform its obligations under a lease. Consequently, if there is an applicable *force majeure* clause in a lease or state law defense to payment, Section 365(d)(3) arguably does not alter that provision or its potential applicability. Prior to the pandemic, the interplay

between these Code provisions and state law defenses was only occasionally at issue. During the pandemic, however, certain debtors attempted to use these arguments to avoid lease obligations for very large portfolios of leases.[42]

1. CEC Entertainment

The debtors in *In re CEC Entertainment, Inc.* operated nationwide Chuck E. Cheese venues, which provide a mixture of arcade games, entertainment and dining options.[43] The debtors filed their chapter 11 petitions on June 2, 2020 largely citing the pandemic as the cause of their filing.[44] Prior to the petition date, the debtors had drawn down on their loan facility and later they received a significant post-petition financing facility.[45] As a result, the CEC debtors had significant cash on hand before and during their chapter 11 cases.[46]

Despite their cash balances, revenues were certainly down during the pandemic due to government restrictions that limited operations.[47] Different states imposed various restrictions on the debtors' operations. For locations where gaming remained prohibited, "CEC reached a business decision that offering in person dining without arcade games would hurt its business" as children would have a negative experience of sitting in the venue and looking at all the games they could not play.[48] As a result, the debtors made the business decision to limit their operations, and therefore their revenues, more strictly than state and local regulations would have required.[49]

The debtors filed a motion, a few days after the first-day hearing in the case, to extend the time to comply with their lease obligations through the 60-day Section 365(d)(3) period.[50] The court granted the request on an interim basis on one day's notice and then approved the relief on a final basis on the record at a hearing held on August 3, 2020.[51] On even date with such hearing, the debtors filed a motion to abate rent payments at 141 locations.[52]

The debtors' abatement motion included a sum total of 4 pages of argument purporting to provide a separate basis to abate rent under leases for 141 locations in 12 states.[53] The motion generally argued that the Court could provide the requested relief of entirely excusing the debtors from paying any rent until all governmental regulations were lifted pursuant to (i) the frustration of purpose doctrine, (ii) force majeure lease clauses, or (iii) the court's inherent equitable powers.[54]

Many landlords objected to the motion and evidentiary hearings were held in September 2020 and December 2020 with regard to several objecting lessors with locations in three states.[55] On December 14, 2020, almost six months after the debtors filed their petitions and almost four months after the debtors' abatement motion was filed, the court issued an opinion denying the motion.[56] The opinion was issued one day before the hearing where the debtors' chapter 11 plan was confirmed. Despite the opinion denying the motion, given the timing, the debtors effectively succeeded at delaying certain rent payments for the entirety of their chapter 11 case.

As to the opinion's specific findings, the court first found that it did not

have the unilateral equitable power to grant the requested relief. The court disagreed with the Pier 1 court, finding that the mandate of Section 365(d)(3) is clear and "unambiguously requires that debtors timely perform their obligations under commercial leases."[57] Accordingly, the court would not use the general mandate section 105(a) of the Bankruptcy Code to override the specific requirements of Section 365(d)(3).[58]

The court next found that the force majeure clauses of the leases at issue did not permit the debtors to delay rent payments.[59] In its abatement motion, the debtors had pointed to a force majeure clause that was in its "standard lease" and that permitted an extension of the time to perform on account of governmental restrictions or other cause.[60] None of the applicable leases appeared to contain this language and instead many included either force majeure clauses that specifically excluded rent payments from excused or extended obligations or "anti-force majeure" clauses.[61]

Finally, the *CEC* bankruptcy court found that the frustration of purpose doctrine did not apply because the force majeure clauses superseded the doctrine or the purpose of the leases was not fully frustrated.[62] As to the first finding, the court reviewed applicable state law providing that when parties specifically allocate risk such as in a force majeure clause, the frustration of purpose doctrine is inapplicable.[63] Moreover, the court noted certain inconsistencies or fallacies in the debtors' positions, including that frustration of purpose requires a permanent or total loss of value and yet the debtors had not rejected the leases.[64] The court also could not locate case law finding that a "temporary reduction in the value of the lease was adequate for the Court to determine that there had been a frustration of purpose."[65] Similarly, although the debtors may have chosen to limit their use of the leased premises, many of the use clauses in the leases permitted a broader use that may have been less impacted by the pandemic.[66] Consequently, the debtors' business decision to limit use and "prioritize [their] own long term business interests over near term profits, does not totally destroy the value of the lease."[67]

Further, the court noted that the remedy for frustration is typically contract rescission, *i.e.*, the end of the contract.[68] Instead of rescission, the debtors were seeking to simply escape one portion of their responsibilities under the leases while the landlords were to remain fully bound to their obligations.[69]

As noted above, the court's abatement ruling came one day before the hearing on confirmation of the debtors' chapter 11 plan. Even though the opinion left open what remedy for non-payment would be appropriate given the denial of the abatement motion, it appears that the debtors resolved remaining landlord issues without further hearings. The opinion is helpful in its clear analysis of the potential arguments for abatement; however, it also leaves open the question of what happens when a debtor ignores the mandate of Section 365(d)(3). In a single sentence, the opinion appears to indicate that it would use its equitable powers to fashion a remedy: "[t]he Court's equitable powers will be tested at the remedy stage."[70] As the debtors resolved their remaining landlord issues, there will not be further remedies' proceed-

ings in CEC Entertainment.[71]

IV. Observations

1. Pandemic Case Law

It remains to be seen whether pandemic decisions will have a lasting effect on bankruptcy jurisprudence or will be viewed as factually distinguishable once-in-a-lifetime case law. Often courts granting extraordinary relief, such as the Modell's court, were faced with incredibly harsh facts where the debtor lacked the present ability to pay and almost all parties would have fared the same or worse in chapter 7 or with lease rejection. The Modell's court also took stock of all the other constituents who were not receiving expected payments such as the debtors' senior secured lenders and the debtors' many employees who had been furloughed or terminated. These facts are arguably irrelevant under Section 365(d)(3), but such section clearly was not drafted with a pandemic - or seemingly even a lack of payment when required under such section - in mind.

Conversely, the *CEC Entertainment* debtors had some cash liquidity (but not their lenders' consent) and the court was still unwilling to mandate payment while the issue of abatement loomed. This factual scenario is more concerning for landlords in post-pandemic cases, although perhaps these concerns are mitigated by the unlikelihood of a large-scale triggering of force majeure clauses. Landlords no doubt have also looked closely at the force majeure clauses in their leases, which may be their best defense. At a minimum, the cases may represent a momentary weakening of landlord protections under the Bankruptcy Code. Notably, none of the resulting case law has answered the question of the appropriate remedy should the court find no excuse for payment under Section 365(d)(3) and a failure to pay.

Over a year into the pandemic, it appears that debtors are not utilizing the same approaches in court as they did at the height of the crisis. Perhaps this is a recognition that the factual underpinnings are not equivalent and that courts may be less flexible at this point. The courts themselves sometimes issued warnings as to the limited and non-citable nature of their rulings.[72]

Leaving aside their factually *sui generis* nature, these decisions may also be susceptible to attack as a matter of law. For example, the Pier 1 court relied primarily on its prior decision in In re Circuit City Stores, Inc., 447 B.R. 475 (Bankr. E.D. Va. 2009) to support its ruling that Section 365(d)(3) is not a basis to require immediate payment and that landlords are left with an administrative claim.[73] The Circuit City opinion related to solely to payment of stub rent amounts and the court found that stub rent not due as of the petition date (because it would be paid in arrears at a date post-petition) should be timely paid pursuant to the terms of the lease.[74] The Pier 1 court did not explain why stub rent arrearage payments are not analogous to go-forward rent. As to the Modell's ruling, the court did not rely on any cases with even a facial similarity to the Modell's cases and did not thoroughly explain the basis on which it suspended the proceedings and yet continued the automatic stay.

2. Practical Concerns in Bankruptcy Abatement Proceedings

Abatement proceedings also raised practical concerns as to efficient determinations under Section 365(d)(3). As discussed above, the potential defenses to payment include a panoply of state law doctrines and review of numerous contractual provisions. These defenses to payment are highly fact intensive and must be analyzed on a lease-by-lease basis. For instance (and as many lawyers have learned post-pandemic), force majeure clauses vary dramatically both in scope of the covered events and the relief afforded. Frustration of purpose and impossibility doctrines, in turn, may require an understanding of the range of capacities at which a business can operate under state law and the permitted uses under the lease. A typical large retail debtor has hundreds of non-uniform leases across many states. In contrast, a landlord may have a single lease and yet can become embroiled in litigation where costs quickly exceed the rents owed.

The individualized nature of these inquiries proved problematic for debtors, landlords, and courts. As described herein, in *CEC Entertainment*, the debtors filed their barebones abatement motion on August 3, 2020. The parties then engaged in further detailed briefing and the court held a series of evidentiary hearings for a small number of landlords who requested such hearings. Four months after the debtors' motion filing, on December 14, 2020, the court issued its opinion regarding payment of rent beginning July 1, 2020.[75] In *Cinemex*, the debtor filed their briefing on May 12, 2020 and June 17, 2020 and the landlord moved to compel compliance with Section 365(d)(3) on July 7, 2020. On October 2, 2020, the court rendered its ruling regarding payment of rent for the period beginning June 1, 2020.[76] Given the length of time it took for decisions to be rendered, the process may have also effectively granted relief for the necessary time period to the debtors' advantage.

Moreover, each of these matters involved only a few landlords willing to litigate and the issues encountered in timing and process would be significantly magnified if more widespread litigation ensued. The court in RTI Holding Company, LLC (d/b/a Ruby Tuesday's), Case No. 20-12456 (Bankr. D. Del.) approved a litigation protocol that sought to avoid some of these issues.[77] In that case, the debtors attempted to fast track bellwether cases with groups of landlords in different jurisdictions by filing complaints and then seeking summary judgement solely on the legal issue of whether abatement was possible.[78] This process would have been followed by a second "quantification" phase.[79] Objecting landlords had numerous concerns with the approach.

The court ultimately approved the protocol, but attempted to assuage landlord concerns by (i) permitting expedited intervention proceedings for any non-defendant landlord in an adversary with issues that could affect the intervenor, (ii) clarifying that rulings in any adversary would not have preclusive effect on non-parties to the adversary, and (iii) permitting landlords ultimately sued to seek relief from the earlier filed procedures order.[80] Indeed, the court likened the complexity of the process to multi-

district litigation.[81] Ultimately, the debtors resolved all lease issues and the adversary cases did not proceed to trial.

Finally, as a different sort of practical consideration, commercial real estate is in its own heightened state of distress.[82] Although other segments of the economy saw increased bankruptcy filings in 2020, real estate sector filings were one of the hardest hit, jumping from 605 filings in 2019 to 985 filings in 2020.[83] At least three major real estate companies including CBL & Associates Properties, Inc. (107 properties), Pennsylvania Real Estate Investment Trust ("PREIT") (26 properties) and Washington Prime (102 properties) have already filed for chapter 11 protection citing pandemic closures and tenant rent relief as causes.[84] If retailers continue to file for chapter 11 protection, without a fair and efficient path to resolve rent issues, additional real estate companies may be forced to file companion cases of their own.

3. Statutory Gap and the Consolidated Appropriations Act, 2021

To the extent that Section 365(d)(3) was intended to require a debtor to timely pay rent, particularly after the 61st day of its case, the pandemic has highlighted a gap in the Bankruptcy Code inasmuch as there is no stated remedy for non-payment. Unless Congress acts to close the gap, there will continue to be gray space within with bankruptcy courts will use their equitable powers. Interestingly, Congress did alter several portions of the Bankruptcy Code related to the tenant-landlord relationship, at least on a temporary basis, during the pandemic, but did not revise for the gap identified herein.

On December 27, 2020, President Trump signed the Consolidated Appropriations Act, 2021 (the "CAA"). The CAA included, among other things, a revision to Bankruptcy Code Section 365(d)(3) for entities qualifying as small business debtors pursuant to section 101(51D) of the Bankruptcy Code, as modified by further legislation.[85] For these small business debtors, the 60-day period in section 365(d)(3) may be extended to 120 days upon a showing of material financial hardship due to COVID-19.[86] This change is due to sunset on December 27, 2022 unless further extended, but will apply to all small business debtors filing before such date.[87] Notably, this change was limited to small business debtors and not larger chapter 11 cases.

It remains to be seen whether and how court will consider requests by debtors that are not small business debtors to extend the 60-day period in Section 365(d)(3) given that Congress determined to change the provision only for small business debtors. By providing such relief solely for small business debtors—at a time when the pandemic's realities were well known to Congress—courts may well infer that no extension for other debtors is available. Further, it will be interesting to see how courts apply the stated standard of "material financial hardship due to COVID-19" and whether courts find that something more than this would need to be shown for non-small business debtors or, again, that no extension is permitted at all for such debtors.

The CAA included two additional Bankruptcy Code changes related to

non-residential real property leases: (i) an extension of a debtor's initial deadline to assume or reject a lease from 120 days after the petition date to 210 days after the petition date; and (ii) a carve-out of preference liability for certain "covered payments," which are defined to be payments made pursuant to arrangements entered into between a debtor-tenant and its landlord on or after March 13, 2020 to defer payments due under a lease. These two changes apply for all debtors, not just small business debtors, and perhaps affect leverage points for debtors and landlords.[88]

These pandemic-related amendments to the Bankruptcy Code widen the gap between the statutory requirement of timely performance under a lease and potentially, the likelihood that a debtor-tenant will be directed to timely perform. As the financial effects of the pandemic lessen, it can only be hoped that courts will increasingly demand the same timely performance that the statute requires.

V. Conclusion

As the United States starts to ease out of the pandemic and we consider the long-term effects on our economy and laws, it is far from clear that open store fronts across the nation will begin to fill. Retailers and real estate companies alike face unique challenges and opportunities ahead. Bankruptcy courts will no doubt have a role to play throughout that process given the significant restructuring tools available through the Bankruptcy Code. To date in the pandemic, bankruptcy courts have been asked to afford extraordinary relief and perhaps most obviously so with regard to rent payments. It is entirely possible that case law regarding rent deferred beyond the Section 365(d)(3) period or abating rent altogether will be viewed through the lens of the irreplicable facts of the pandemic. To the extent the fissures that this case law opened in the Bankruptcy Code are widened, there is little doubt that the landlord lobby will express its displeasure to Congress. Without a specific instruction from Congress as to the remedy for failure to pay rent, however, bankruptcy courts will retain the flexibility to consider the practical realities of the cases they administer on this issue.

NOTES:

[1]Retail bankruptcies in 2020 hit the highest levels in more than a decade, and experts say there are more to come, MarketWatch, Dec. 28, 2020, https://www.marketwatch.com/story/retail-bankruptcies-in-2020-hit-the-highest-levels-in-more-than-a-decade-and-experts-say-there-are-more-to-come-11608151350 (last visited June 21, 2021) and U.S. 2021 Retail Vacancy Rate May Rise To 7-Year High After Record Store Closings, Forbes, January 13, 2021 (https://www.forbes.com/sites/andriacheng/2021/01/13/us-2021-retail-vacancy-rate-may-rise-to-7-year-high-after-record-store-closings/?sh=b2f5a7b68e88) (last visited June 22, 2021).

[2]Stage Is Set For Another Record-Breaking Year Of Retail Bankruptcies: Who's Next?, Forbes, Jan. 24, 2021, https://www.forbes.com/sites/pamdanziger/2021/01/24/stage-is-set-for-another-record-breaking-year, -of-retail-bankruptcies-whos-next/?sh=bab7daf1ca9f (last visited June 21, 2021).

[3]The pandemic may have changed some consumer habits permanently, Retail Dive,

April 1, 2021, https://www.retaildive.com/news/the-pandemic-may-have-changed-some-consumer-habits-permanently/597715/ (last visited June 22, 2021) and U.S. 2021 Retail Vacancy Rate May Rise To 7-Year High After Record Store Closings, Forbes, January 13, 2021 (https://www.forbes.com/sites/andriacheng/2021/01/13/us-2021-retail-vacancy-rate-may-rise-to-7-year-high-after-record-store-closings/?sh=b2f5a7b68e88) (last visited June 22, 2021).

[4]The term "rent" is used generally herein with regard to monetary obligations of a tenant under a lease, despite the fact that leases contain a variety of payment obligations that may or may not technically be defined as rent.

[5]See 130 Cong.Rec. S8894-95 (daily ed. June 29, 1984) (statement of Sen. Hatch) reprinted in App. 4 Collier on Bankruptcy, at XX-70—XX-71 (Lawrence P. King et al. eds., 15th ed. 1992):

> A second and related problem is that during the time [before] the debtor has . . . decided whether to assume or reject the lease, the trustee has stopped making payments due under the lease. These payments include rent due the landlord and common charges which are paid by all the tenants according to the amount of space they lease. In this situation, the landlord is forced to provide current services—the use of its property, utilities, security, and other services—without current payment. No other creditor is put in this position.

[6]In re Art Van Furniture, LLC, Case No. 20-10553 (Bankr. D. Del.) [Docket Nos. 1, 263] (case filed on March 8, 2020 to effectuate going out of business sales, in part, and sale of certain stores and assets to a private buyer through a prepackaged plan of reorganization, but converted to a chapter 7 liquidation on April 6, 2020). Notably, however, conversion did not provide a full solution in Art Van Furniture, as the chapter 7 trustee then had to address similar issues related to delaying rent payments and completing going out of business sales. See Docket Nos. 342, 350.

[7]See Transcript Regarding Hearing Held April 30, 2020 [Docket No. 315] ("Modell's Hearing Transcript April 30, 2020") at 63:4–7 (finding cause and stating "there's no more exceptional cause, there's no more cause that could be shown than has been shown here. I've never seen a stronger case. I don't know how else to say it. So that's not a hard one."); See also, In re J.C. Penney Company, Inc., Case No. 20-20182 (Bankr. S.D. Tex. June 11, 2020) [Docket No. 721] (order extending debtors' period to satisfy monetary obligations under non-residential real property leases for 60 days after petition date, but requiring payment promptly thereafter unless the parties reached an agreement.).

[8]See, e.g., In re True Religion Apparel, Inc., Case No. 20-10941 (Bankr. D. Del. Apr. 13, 2020) [Docket No. 221] (suspending payment obligations under leases for 60 day period and indicating that no hearings on motions seeking relief related thereto would occur for a period of several weeks unless the court determined it was time sensitive).

[9]Modell's Sporting Goods, Inc., Case No. 2014179 (Bankr. D. N.J. March 11, 2020), Declaration of Robert J. Duffy in Support of Debtors' Chapter 11 Petitions and First Day Motions [Docket No. 24, ¶¶ 10, 13–17], In re Modell's Sporting Goods, Inc., et al., Case No. 20-14179 (Bankr. D.N.J.) ("Modell's - Duffy Declaration").

[10]Modell's - Duffy Declaration at ¶ 39.

[11]Modell's - Duffy Declaration at ¶¶ 44, 46.

[12]Modell's Sporting Goods, Inc., Case No. 2014179 (Bankr. D. N.J. March 11, 2020), Debtors' Verified Application in Support of Emergency Motion for Entry of an Order Temporarily Suspending Their Chapter 11 Cases Pursuant to 11 U.S.C. §§ 105 and 305 [Docket No. 115] ("Modell's - Suspension Motion").

[13]Modell's - Suspension Motion.

[14]Modell's - Suspension Motion.

[15]Modell's Sporting Goods, Inc., Case No. 2014179 (Bankr. D. N.J. March 11, 2020), Modell's Hearing Transcript April 30, 2020 [Docket No. 315] ("Modell's Hearing Transcript

April 30, 2020") at 13:1–7.

[16]Modell's Hearing Transcript April 30, 2020 at 33:23–83:11.

[17]Modell's Hearing Transcript April 30, 2020. See also Law v. Siegel, 571 U.S. 415, 421, 134 S. Ct. 1188, 188 L. Ed. 2d 146, 59 Bankr. Ct. Dec. (CRR) 43, Bankr. L. Rep. (CCH) P 82592 (2014) ("It is hornbook law that § 105(a) "does not allow the bankruptcy court to override explicit mandates of other sections of the Bankruptcy Code." (citing 2 Collier on Bankruptcy ¶ 105.01[2], p. 105–6 (16th ed. 2013)).

[18]Modell's Hearing Transcript April 30, 2020 at 33:23–83:11.

[19]Modell's Sporting Goods, Inc., Case No. 2014179 (Bankr. D. N.J. March 11, 2020), Order Temporarily Suspending the Debtors' Chapter 11 Cases Pursuant To 11 U.S.C. §§ 105 and 305 [Docket No. 166].

[20]Modell's Sporting Goods, Inc., Case No. 2014179 (Bankr. D. N.J. March 11, 2020), Docket Nos. 294, 371.

[21]Modell's Hearing Transcript April 30, 2020 at 92–113.

[22]Modell's Hearing Transcript April 30, 2020 at 39:23–25 and 40:1–18.

[23]Modell's Hearing Transcript April 30, 2020 at 92–113.

[24]Modell's Hearing Transcript April 30, 2020 at 92–113.

[25]Modell's Sporting Goods, Inc., Case No. 2014179 (Bankr. D. N.J. March 11, 2020), First Amended Disclosure Statement For The Joint Plan Of Modell's Sporting Goods, Inc. And Its Subsidiary Debtors Pursuant To Chapter 11 Of The Bankruptcy Code [Docket No. 759-1] and Finding of Fact, Conclusions of Law, and Order (I) Approving the Disclosure Statement on a Final Basis and (II) Confirming the First Amended Joint Plan of Liquidation of Modell's Sporting Goods, Inc. and It's Subsidiary Debtors pursuant to Chapter 11 of the Bankruptcy Code [Docket No. 827] ("Modell's Disclosure Statement").

[26]Pier 1 Imports, Inc., Case No. 20-30805 (Bankr. E.D. Va. 2020), Declaration Of Robert J. Riesbeck, Chief Executive Officer And Chief Financial Officer Of Pier 1 Imports, Inc., In Support Of Chapter 11 Petitions And First Day Motions, ¶ 54 [Docket No. 30].

[27]In re Pier 1 Imports, Inc., 615 B.R. 196 (Bankr. E.D. Va. 2020).

[28]In re Pier 1 Imports, Inc., 615 B.R. 196 (Bankr. E.D. Va. 2020); see also, Modell's Sporting Goods, Inc., Case No. 2014179 (Bankr. D. N.J. March 11, 2020), Debtors' Emergency Motion For Entry Of An Order (I) Approving Relief Related To The Interim Budget, (II) Temporarily Adjourning Certain Motions And Applications For Payments, And (III) Granting Related Relief [Docket No. 438] ("Pier 1 Motion").

[29]Pier 1 Motion.

[30]Pier 1 Imports, 615 B.R. at 200.

[31]Modell's Sporting Goods, Inc., Case No. 2014179 (Bankr. D. N.J. March 11, 2020), Order Granting (I) Relief Related to the Interim Budget, (II) Temporarily Adjourning Certain Motions and Applications for Payments, and (III) Granting Related Relief Motion to Approve [Docket No. 493] and First Supplemental Order (I) Approving Relief Related to the Interim Budget, (II) Temporarily Adjourning Certain Motions and Applications for Payments, and (III) Granting Related Relief [Docket No. 629].

[32]Pier 1 Imports, 615 B.R. at 197.

[33]Pier 1 Imports, 615 B.R. at 201 n.7.

[34]Pier 1 Imports, 615 B.R. at 201 n.7.

[35]Pier 1 Imports, 615 B.R. at 202.

[36]Pier 1 Imports, 615 B.R. at 202. But see In re Hitz Restaurant Group, 616 B.R. 374, 376, 68 Bankr. Ct. Dec. (CRR) 221 (Bankr. N.D. Ill. 2020) (noting that "payments required

under § 365(d)(3) are not mere administrative expenses under § 503(b)(1)" but requiring proportional rent payments due to provisions in lease agreement and status of debtor business operations).

[37]Pier 1 Imports, 615 B.R. at 203.

[38]Pier 1 Modell's Sporting Goods, Inc., Case No. 2014179 (Bankr. D. N.J. March 11, 2020), Disclosure Statement ("Pier 1 Disclosure Statement") at 51.

[39]Pier 1 Disclosure Statement at 51–52.

[40]Pier 1 Disclosure Statement at 15.

[41]See e.g., Butner v. U.S., 440 U.S. 48, 55, 99 S. Ct. 914, 59 L. Ed. 2d 136, 19 C.B.C. 481, Bankr. L. Rep. (CCH) P 67046 (1979) ("Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding. Uniform treatment of property interests by both state and federal courts within a State serves to reduce uncertainty, to discourage forum shopping and to prevent a party from receiving 'a windfall merely by reason of the happenstance of bankruptcy.' "); see also Motion for Order Authorizing Debtors to Abate Rent Payments at Stores Affected by Government Regulations [Docket No. 487].

[42]In re CEC Entertainment, Inc., 625 B.R. 344, 351 (Bankr. S.D. Tex. 2020) ("Of course, if abatement was authorized under applicable non-bankruptcy law, the sixty-day limitation [in section 365(d)(3) would not apply.").

[43]CEC Entertainment, 625 B.R. at 349–50.

[44]CEC Entertainment, Inc., Case No. 20-33163 (Bankr. S.D. Tex. June 25, 2020), (Declaration of James Howell in Support of Debtors' Chapter 11 Petitions and Related Requests for Relief [Docket No. 47] "CEC Declaration").

[45]Declaration of James Howell in Support of Debtors' Chapter 11 Petitions and Related Requests for Relief [Docket No. 47], CEC Declaration, ¶ 17 and CEC Entertainment, Inc., Case No. 20-33163 (Bankr. S.D. Tex. June 25, 2020), Order (I) Authorizing the Debtors to (A) Obtain Postpetition Financing, (B) Grant Senior Secured Liens and Superpriority Administrative Expense Claims, and (C) Utilize Cash Collateral; (II) Granting Adequate Protection to the Prepetition Secured Parties; and (III) Granting Related Relief [Docket No. 1118] (approving $200 million postpetition financing facility).

[46]CEC Entertainment, Inc., Case No. 20-33163 (Bankr. S.D. Tex. June 25, 2020), Interim Order (I) Authorizing the Debtors to Use Cash Collateral, (II) Granting Adequate Protection to the Prepetition Secured Parties, (III) Modifying the Automatic Stay, (IV) Scheduling a Final Hearing, and (V) Granting Related Relief, Exh. A, Initial Budget [Docket No. 114] (showing over $102 million cash on hand at petition date).

[47]See CEC Entertainment, 625 B.R. at 349–351.

[48]CEC Entertainment, 625 B.R. at 350.

[49]CEC Entertainment, 625 B.R. at 350.

[50]CEC Entertainment, Inc., Case No. 20-33163 (Bankr. S.D. Tex. June 25, 2020), Motion for Order Authorizing Debtors to Abate Rent Payments at Stores Affected by Government Regulations [Docket No. 487] ("CEC Rent Abatement Motion").

[51]CEC Entertainment, Inc., Case No. 20-33163 (Bankr. S.D. Tex. June 25, 2020), Docket No. 481 (noting ruling on record that orally authorized deferral of rent for 21 days (i.e., to the last day of the 60-day period under section 365(d)(3)) without a signed order).

[52]CEC Rent Abatement Motion. The Restatement (Second) of Contracts § 265 provides that "[w]here, after a contract is made, a party's principal purpose is substantially frustrated without his fault by the occurrence of an event the non-occurrence of which was a basic assumption on which the contract was made, his remaining duties to render performance are

discharged, unless the language or the circumstances indicate the contrary."

[53]CEC Rent Abatement Motion.

[54]CEC Rent Abatement Motion.

[55]CEC Entertainment, 625 B.R. at 351.

[56]CEC Entertainment, 625 B.R. at 351.

[57]CEC Entertainment, 625 B.R. at 352–53

[58]CEC Entertainment, 625 B.R. at 353 (citing Law v. Siegel, 571 U.S. 415, 421, 134 S. Ct. 1188, 188 L. Ed. 2d 146, 59 Bankr. Ct. Dec. (CRR) 43, Bankr. L. Rep. (CCH) P 82592 (2014)) and In re Mirant Corp., 378 F.3d 511, 523, 43 Bankr. Ct. Dec. (CRR) 111, Bankr. L. Rep. (CCH) P 80139 (5th Cir. 2004)).

[59]CEC Entertainment, 625 B.R. at 354–358.

[60]CEC Rent Abatement Motion, at ¶¶ 12–14.

[61]CEC Entertainment, 625 B.R. at 353 (citing force majeure clause stating that "[t]his section shall not apply to the inability to pay any sum of money due hereunder or the failure to perform any other obligation due to the lack of money or inability to raise capital or borrow for any purpose.") and 625 B.R. at 356 (citing "anti-force force majeure" provision stating that "[t]his Lease and the obligations of either party hereunder shall not be affected or impaired because either party is unable to fulfill any of its obligations hereunder or is delayed in doing so, if such inability or delay is caused by reasons of strike, labor troubles, acts of God, or any other cause beyond the reasonable control of either party.").

[62]CEC Entertainment, 625 B.R. at 359, 363.

[63]CEC Entertainment, 625 B.R. at 358–364.

[64]CEC Entertainment, 625 B.R. at 358.

[65]CEC Entertainment, 625 B.R. at 360.

[66]CEC Entertainment, 625 B.R. at 358–364.

[67]CEC Entertainment, 625 B.R. at 364.

[68]CEC Entertainment, 625 B.R. at 357, 361.

[69]CEC Entertainment, 625 B.R. at 361.

[70]CEC Entertainment, 625 B.R. at 353.

[71]At least two additional courts have considered issues similar to the CEC Entertainment court. Applying a similar approach but to different lease provisions, these courts permitted abatement of different varieties. Perhaps the first abatement ruling from a bankruptcy court was In re Hitz Restaurant Group, 616 B.R. 374, 68 Bankr. Ct. Dec. (CRR) 221 (Bankr. N.D. Ill. 2020). The Hitz court found that the force majeure clause in the applicable lease required that rent payments be pro-rated following the issuance of governmental restrictions. The court also required payment by a date certain or it would enter an order granting the landlord stay relief. In re Hitz, 616 B.R. at 379–80. Additionally, another court permitted abatement only during a period of full closure due to the applicable force majeure lease clause. See also In re Cinemex USA Real Estate Holdings, Inc., 627 B.R. 693 (Bankr. S.D. Fla. 2021).

[72]Cinemex USA, 2021 WL 564486 at *6 n.19 (noting that the court's ruling was specific to the lease, location and state law before it and that "[t]he circumstances regarding full closure and reopening may differ from lease to lease and certainly from state to state. Therefore, the Court wants to make clear that parties should not assume that the findings and the holdings of this particular dispute will necessarily translate to litigation involving other cases.").

[73]Pier 1 Imports, Inc., Case No. 20-30805 (Bankr. E.D. Va. 2020), Declaration Of Robert J. Riesbeck, Chief Executive Officer And Chief Financial Officer Of Pier 1 Imports, Inc., In

Support Of Chapter 11 Petitions And First Day Motions, ¶ 54 [Docket No. 30].

[74]In re Circuit City Stores, Inc., 447 B.R. 475, 512 (Bankr. E.D. Va. 2009).

[75]CEC Entertainment, 625 B.R. 344 at 350.

[76]Cinemex USA, 2021 WL 564486.

[77]RTI Holding Company, LLC (d/b/a Ruby Tuesday's), Case No. 20-12456 (Bankr. D. Del. Oct. 7, 2020), Abatement Litigation Procedures Order [Docket No. 689] ("RTI Scheduling Order re: Abatement Litigation").

[78]RTI Holding Company, LLC (d/b/a Ruby Tuesday's), Case No. 20-12456 (Bankr. D. Del. Oct. 7, 2020), Notice of Proposed Abatement Litigation Procedures Re: Relief Requested in Debtors' Motion for Entry of an Order Pursuant to Sections 105(A) and 503(B) of the Bankruptcy Code Abating Rents Under Unexpired Leases of Nonresidential Real Property for Restaurants Affected by Government Regulation [Docket No. 614].

[79]RTI Scheduling Order re: Abatement Litigation.

[80]RTI Holding Company, LLC (d/b/a Ruby Tuesday's), Case No. 20-12456 (Bankr. D. Del. Oct. 7, 2020), Transcript Regarding Hearing Held December 7, 2020 [Docket No. 687] ("RTI Hearing Transcript December 7, 2020"), and RTI Scheduling Order re: Abatement Litigation [Docket No. 689]

[81]RTI Hearing Transcript December 7, 2020 at 18:7–10.

[82]Commercial Real Estate's Pandemic Pain Is Only Just Beginning, Bloomberg, December 22, 2020, https://www.bloomberg.com/graphics/2020-commercial-real-estate/ (last visited June 22, 2021).

[83]Commercial Real Estate's Pandemic Pain Is Only Just Beginning, Bloomberg, December 22, 2020.

[84]Major US Mall owner files for bankruptcy, CNN, June 14, 2021, https://www.cnn.com/2021/06/14/business/washington-prime-group-mall-bankruptcy/index.html (last visited June 22, 2021).

[85]Consolidated Appropriations Act, 2021, Pub. L. 116-260 (2020).

[86]Consolidated Appropriations Act, 2021.

[87]Consolidated Appropriations Act, 2021.

[88]The backdrop for many retail cases includes on-going negotiations between debtors and their landlords as to lease concessions or amendments that inform a debtor's determination to assume or reject a lease. The extension of the deadline for that decision provides a debtor with additional leverage over a landlord who may want their space returned or a forced decision to assume (and cure). Landlords, of course, retain the ability to move to compel assumption or rejection or to seek other relief in the event of non-payment, but there are real costs to seeking such relief which may not be successful, particularly in the early days of a case. The limitations of potential preference liability, in turn, remove leverage for a debtor who would otherwise argue that payments made under pandemic rent accommodations are preferential or that a release of such claims is additional consideration.