

# BUSINESS BANKRUPTCY ALERT

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## RECENT BANKRUPTCY COURT DECISION ALLOWS DEBTOR TO AVOID PAYMENT OF DEFAULT INTEREST

The Bankruptcy Code permits a debtor to cure prepetition defaults pursuant to a confirmed plan of reorganization and avoid the consequences of that default. 11 U.S.C. § 1123(a)(5)(G). A plan of reorganization may, as a means of implementing the plan, cure or waive any default. However, the cost of the “cure” can present significant issues, including whether default interest and late charges can be tacked onto the outstanding payments.

In one recent case, a debtor proposed a plan to make cash payments equal to the number of monthly payments in arrears less payments made by the debtor to its secured creditor during bankruptcy. *In re Phoenix Business Park Limited Partnership*, 257 B.R. 517 (Bankr. D. Ariz. 2001). The debt was secured by commercial real estate, and the secured creditor believed that it would be entitled to default interest, late fees and other charges as part of any cure payment. The court concluded that only interest at the contract rate, not at the default rate, was needed to effectuate a cure. Moreover, the court also found that the debtor did not need to pay late charges in order to effectuate a cure under Section 1124(2) of the Bankruptcy Code.

In addition to seeking default interest, the oversecured creditor in *In re Phoenix Business Park* sought to collect as part of a cure its attorney’s fees, foreclosure notice fees and court costs. Section 1124(2)(c)(3) provides that a secured creditor may receive damages incurred as a result of reasonable reliance on contractual charges based upon a default as part of any cure. Thus, the court held that the secured creditor could be compensated for damages incurred in reliance upon the note’s acceleration clause and efforts to enforce its rights as a result of acceleration. These damages must be paid as part of any cure payment in order to deaccelerate a loan and avoid the payment of default interest. This section protects creditors from out-of-pocket losses incurred when a debtor files bankruptcy and undoes prepetition acceleration. To be compensable, the damage should arise as a result of actions taken in reliance upon the existence of an acceleration clause and not merely upon the existence of a contractual right to a remedy.

In conclusion, unimpairment by curing past defaults pursuant to a plan of reorganization is available as a means of avoiding default interest and the payment of late charges that would otherwise be available to an oversecured creditor.

IF YOU HAVE ANY QUESTIONS OR COMMENTS ABOUT ANY OF THE FOREGOING, WISH TO BE REMOVED FROM THIS DISTRIBUTION LIST OR KNOW OF SOMEONE WHO WOULD LIKE TO BE ADDED, PLEASE CONTACT:

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