

BANKRUPTCY ALERT

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DEBTOR'S USE OF LEASED PERSONAL PROPERTY RESULTS IN ADMINISTRATIVE CLAIM

A Chapter 11 debtor has until plan confirmation to assume or reject leases of personal property. In the first 60 days of the bankruptcy case, the debtor is not required to pay rent on leased personal property. However, after 60 days from the commencement of the case, Section 365(d)(10) of the Bankruptcy Code requires the debtor to begin paying rent on leased personal property. The typical debtor will have numerous leases governed by these rules, including copiers, equipment, telephones and other items.

Whether a debtor is required to pay rent during the first 60 days of a bankruptcy case has been the subject of conflicting interpretations. Ordinarily, the lessor is entitled to an administrative expense claim to the extent that the use of leased property benefits the debtor's estate. However, some debtors have argued that Section 365(d)(10) provides a moratorium, and therefore no rent is due for the first 60 days of a bankruptcy case.

The conflicting interpretations of Section 365(d)(10) have been clarified by a recent bankruptcy court decision. *In re Russell Cave Company, Inc.*, 247 B.R. 656 (Bankr. E.D. Kent. 2000). The bankruptcy court held that where a debtor uses leased property in the first 60 days of a bankruptcy case and receives a benefit from the use of the property, the lessor is entitled to an administrative expense claim.

Under the bankruptcy court's reasoning, the administrative expense claim received by a lessor is limited to those expenses that are the actual, necessary costs and expenses of preserving the estate during the first 60 days. For such claims, the burden is on the lessor to demonstrate the legitimacy of the expenses and that the use of the property benefited the estate. However, after the first 60 days, such a showing is not required under the holding of *In re Russell Cave*, and accordingly, lessors would be entitled to rent claims whether or not the equipment is used for the debtor's benefit.

The effect of *In re Russell Cave* is that debtors cannot obtain a "free ride" for the use of leased property in the first 60 days of a bankruptcy case. The debtors may take 60 days to determine what leases they will assume or reject without paying rent; however, to the extent the estate benefits from the use of leased equipment, rent must be paid.

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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