

IN THE UNITED STATES BANKRUPTCY COURT FOR THE  
EASTERN DISTRICT OF TENNESSEE

In re

APPALACHIAN STAR VENTURES,	)	
INC., d/b/a APPALACHIAN	)	Case No. 93-35224
LEASING, INC., d/b/a	)	Chapter 11
APPALACHIAN AVIATION, INC.,	)	
d/b/a APPALACHIAN FLYING	)	
SERVICES, INC.	)	
	)	
Debtor.	)	

M E M O R A N D U M

This matter came before the court for hearing on March 15, 1994, upon the (1) motion of the Tri-City Airport Commission ("TCAC") for relief from the automatic stay pursuant to 11 U.S.C. § 362(d) to terminate a lease agreement between it and Appalachian Aviation, Inc.;<sup>1</sup> and (2) Debtor's motion to assume the lease agreement pursuant to 11 U.S.C. § 365(a). For the reasons set forth below, the court concludes that this matter should be set over for further hearing on June 6, 1994, at 1:30 p.m in the bankruptcy courtroom, Downtown Centre Courthouse, Market Street, Johnson City, Tennessee. The following constitutes findings of fact and conclusions of law as required by FED. R. BANKR. P. 7052. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A)(G) and (M).

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<sup>1</sup>Appalachian Star Ventures, Inc. is the parent corporation of its wholly-owned subsidiaries, Appalachian Leasing, Inc., Appalachian Aviation, Inc., and Appalachian Flying Services, Inc., all of which will be collectively referred to herein as the "Debtor."

I.

TCAC is a commission established by the Tennessee cities of Bristol, Johnson City and Kingsport, the city of Bristol, Virginia, and the Tennessee counties of Sullivan and Washington, for the purpose of operating the Tri-City Regional Airport (the "Airport"). The principal place of business of the Debtor is located at the Airport where it conducts a fixed-based operation. On October 16, 1979, TCAC and the Debtor entered into a lease agreement (the "Lease"), whereby Debtor agreed to lease from TCAC certain commercial property at the Airport consisting of hangers, buildings, ramps and other paved and unpaved areas for a period of 20 years commencing April 1, 1980, and ending March 31, 2000. Under the terms of the Lease, rent for the leased premises was calculated on a square footage basis for the particular area leased with general adjustments based on cost of living increases in accordance with the Consumer Price Index along with specified graduated increases for one of the hangers.

In conjunction with its fixed-based operation, the Debtor operates a fuel storage facility at the Airport pursuant to a lease agreement between Appalachian Flying Service, Inc. and TCAC dated June 1, 1977 (the "Fuel Farm Lease"). The Fuel Farm Lease expired by its own terms prior to the bankruptcy filing, but the Debtor continues to lease the facility on a month to month basis. In early 1989, a fuel spill occurred at the facility. The Debtor has been working with the Tennessee Department of Environment and

Conservation to clean up the soil contamination caused by the spill, but has not had the funds necessary to complete the cleanup.

In late 1991, the Debtor began experiencing financial difficulties due in part to a general decline in the aviation business. Soon thereafter, the Debtor approached TCAC and requested a reduction in its rent. The parties began a series of discussions regarding the Debtor's financial situation, adjustments in the rent and other modifications to the Lease, and the construction of a new fuel farm for the Debtor. Beginning in July 1993, the Debtor ceased all payments to TCAC, as its financial difficulties reached the point where it could no longer make rent payments to TCAC and pay its other expenses. By December 1993, when Debtor was six months behind in its payments to TCAC, the parties reached a stalemate in negotiations concerning the appropriate adjustments to the rent under the Lease, and Debtor advised TCAC that it was unable to cure the rental arrearage or complete the cleanup at the fuel storage facility. Thereupon, TCAC notified the Debtor that it intended to terminate the Lease as of December 31, 1993. The Lease termination was forestalled by the Debtor's filing of this Chapter 11 case on December 30, 1993.

TCAC filed its motion for relief from the automatic stay on January 12, 1994, less than two weeks after the commencement of this case. That motion came before the court for a preliminary hearing on January 25, 1994. As a result of the hearing, the parties entered into an agreed order on February 3, 1994, which provided that a final hearing on TCAC's motion would be held on

March 15, 1994, along with any motion filed by the Debtor pursuant to 11 U.S.C. § 365(a) to assume the Lease. The parties also agreed that in the interim the Debtor would pay TCAC the sum of \$10,000.00 per month in postpetition rent without TCAC waiving its right to subsequently seek additional amounts due under the Lease in excess of the \$10,000.00 monthly rental payments.

The agreed order further provided that on or before February 24, 1994, the Debtor would submit to TCAC a commitment from a lending institution or other third-party setting forth terms and conditions under which sufficient credit would be advanced to the Debtor to cure the rental arrearage due under the Lease and to fund the environmental cleanup. As contemplated, the Debtor moved to assume the Lease on February 25, 1994, and the Debtor made the agreed \$10,000.00 monthly rental payments in February and March.

## II.

11 U.S.C. § 362(d) provides that:

On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay-

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest; or

(2) with respect to a stay of an act against property under subsection (a) of this section, if-

(A) the debtor does not have an equity in such

property; and

- (B) such property is not necessary to an effective reorganization.

It is undisputed that at the time this case was filed, the Debtor was in default under the terms of the Lease and owed TCAC for rent payments from July through December 1993, totalling \$81,474.13. TCAC contends that it is entitled to relief from the stay under § 362(d)(1) for cause and under § 362(d)(2) because the Debtor has no equity in the Lease and the Lease is not necessary for the Debtor's reorganization since the Debtor allegedly does not have the financial means to reorganize. TCAC points out that in order to reorganize, the Debtor must assume the Lease because it has no other place to conduct its fixed-base operation than at the Airport. For the Debtor to assume the lease under § 365(b)(1) of the Bankruptcy Code,<sup>2</sup> it must, *inter alia*, cure the default or

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<sup>2</sup>11 U.S.C. § 365(b)(1) provides:

If there has been a default in an executory contract or unexpired lease of the debtor, the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee--

- (A) cures, or provides adequate assurance that the trustee will promptly cure, such default;
- (B) compensates, or provides adequate assurance that the trustee will promptly compensate, a party other than the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default; and
- (C) provides adequate assurance of future performance under such contract or lease.

provide adequate assurance that it will promptly cure the default at the time of the assumption. In addition, the Debtor must "provide adequate assurance of future performance" under the Lease. TCAC alleges and presented proof in support thereof that the Debtor does not have the ability to do either.

In defense to TCAC's motion for relief from stay, the Debtor admits that it is technically in default under the terms of the Lease. The Debtor contends, however, that it is in default only because the rental provisions of the Lease are illegal under both federal and state law. Under federal law, all leases or contracts entered into by TCAC are subject to certain "assurances" required to be given by airports to the Secretary of Transportation under the Airport and Airway Improvement Act of 1982, 49 U.S.C. app. § 2210 (1993). These assurances require, *inter alia*, that "each fixed-based operator be subject to the same rates, fees, rentals, and other charges as are uniformly applicable to all other fixed-based operators making the same or similar uses of such airport utilizing the same or similar facilities." 49 U.S.C. app. § 2210(a)(1)(B).

Under Tennessee law, airport charges, rentals and fees must "be reasonable and uniform for the same class of privilege or service." TENN. CODE ANN. § 42-5-110(a)(2) (1993).<sup>3</sup> The Debtor

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<sup>3</sup>"In each case, the municipality may establish the terms and conditions and fix the charges, rentals or fees for the privileges, uses or services, use of buildings or structures which shall be reasonable and uniform for the same class of privilege or service and shall be established with due regard to the property and improvements used and the expenses of operation to the municipality." TENN. CODE ANN. § 42-5-110(a)(2) (1993).

alleges that the rent charged by TCAC under the Lease violates the federal assurances and state law because the other fixed-based operator at the airport, Tri-City Aviation, pays less rent than Debtor even though their facilities are roughly equal, and because the rent on one of the hangers leased by the Debtor is higher than the current fair market rental. Debtor maintains that as a third-party beneficiary to the federal and state statutes or otherwise, it has a claim against TCAC for its alleged failure to comply with the federal and state requirements. Debtor admits that no actual adversary proceeding asserting these claims has been filed, but alleges that one is contemplated in the near future. It is the position of the Debtor that despite the lack of a pending action, TCAC's alleged failure to comply with the federal assurances and Tennessee law constitutes a defense to TCAC's motion for relief from stay.

### III.

The legislative history to 11 U.S.C. § 362 indicates that hearings on relief from the automatic stay are not the appropriate time for deciding collateral issues such as counterclaims and affirmative defenses, although the court may consider potential counterclaims in ruling on the motion as long as there is no adjudication of the merits of the counterclaim. *Madison National Bank v. Chiapelli*, 131 B.R. 354, 358 (E.D. Mich. 1991); *In re Compass Van & Storage Corp.*, 61 B.R. 230, 234 (Bankr. E.D.N.Y. 1986); *In re Pappas*, 55 B.R. 658, 660 (Bankr. D. Mass. 1985); *In re*

*Tally Well Service, Inc.*, 45 B.R. 149, 151 (Bankr. E.D. Mich. 1984), citing S. REP. No. 95-989, 95th Cong., 2d Sess. 55 (1978) reprinted in 1978 U.S.C.C.A.N. 5841.<sup>4</sup> A debtor may defeat a creditor's motion for relief through probative evidence to the court's satisfaction that the debtor will likely prevail in its action against the creditor. See *In re Compass Van & Storage Corp.*, 61 B.R. at 234, citing *In re Dennison*, 50 B.R. 950, 955 (Bankr. E.D. Pa. 1985). Accordingly, the court will consider the merits of Debtor's claim against TCAC only to aid it in determining whether the pending motion for relief should be granted or denied.<sup>5</sup> As a result, the court's consideration of the issues

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<sup>4</sup>The legislative history to § 362 states that "[t]he action commenced by the party seeking relief from the stay is referred to as a motion to make it clear that at the expedited hearing under subsection (e), and at hearings on relief from the stay, the only issue will be lack of adequate protection, the debtor's equity in the property, and the necessity of the property to an effective reorganization of the debtor, or the existence of other cause for relief from the stay. This hearing will not be the appropriate time in which to bring in other issues, such as counterclaims against the creditor, which, although relevant to the question of the amount of the debt, concern largely collateral or unrelated matters ... Those counterclaims are not to be handled in the summary fashion that the preliminary hearing under this provision will be. Rather, they will be the subject of more complete proceedings by the trustee to recover property of the estate or to object to the allowance of a claim. However, this would not preclude the party seeking continuance of the stay from presenting evidence on the existence of claims which the court may consider in exercising its discretion. What is precluded is a determination of such collateral claims on the merits of the hearing." S. REP. No. 95-989, 95th Cong., 2d Sess. 55 (1978) reprinted in 1978 U.S.C.C.A.N. 5841.

<sup>5</sup>The same limitations on the full adjudication of the merits of counterclaims apply in the context of a motion to assume an executory contract or lease. A motion to assume should be considered a summary proceeding; it is not the time or place for a

(continued ... )

regarding the Debtor's claim against TCAC is not dispositive or intended to be *res judicata*.

The court initially notes that even though the Debtor has indicated that it intends to file an action against TCAC in the near future, its right to do so is far from clear. As Debtor concedes, the law is well settled in the Sixth Circuit that no private right of action exists under 49 U.S.C. app. § 2210 for violation of the federal assurances. See *Northwest Airlines, Inc. v. County of Kent, Mich.*, 955 F.2d 1054 (6th Cir. 1992), *aff'd*, 114 S. Ct. 855 (1994). The Debtor maintains, however, that it may bring an action by way of 42 U.S.C. § 1983 even though no direct action is available under § 2210.

The availability of § 1983 action as an avenue of relief for violations of § 2210 is an issue that has not been decided by the Sixth Circuit Court of Appeals or any other circuit court. However, of the lower courts that have considered the issue, all but one have determined that § 1983 is not available. See *Northwest Jet Center, Ltd. v. Lehigh-Northampton Airport Authority*, 767 F. Supp. 672 (E.D. Pa. 1991); *Rocky Mountain Airways, Inc. v. Pitkin County*, 674 F. Supp. 312 (D. Colo. 1987); *Hillman Flying Service v. City of Roanoke*, 652 F. Supp. 1142 (W.D. Va. 1987),

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( ... continued)

prolonged discovery or a lengthy trial with disputed issues. *In re Orion Pictures Corp.*, 4 F.3d 1095, 1098-99 (2nd. Cir. 1993), *petition for cert. filed*, 62 U.S.L.W. 3555 (Jan. 31, 1994); *In re Docktor Pet Ctr., Inc.*, 144 B.R. 14, 16 (Bankr. D. Mass. 1992); *In re L.T. Ruth Coal Company, Inc.*, 66 B.R. 753 (Bankr. E.D. Ky 1986).

*aff'd*, 846 F.2d 71 (4th Cir. 1988); *Norwood Aviation v. Boston Metro. Airport*, 1988 WESTLAW 148779 (D. Mass. 1988 memo. op.). But see *New York Airlines, Inc. v. Dukes County*, 623 F. Supp. 1435 (D. Mass. 1985). The Debtor urges the court to adopt the reasoning of *New York Airlines, Inc. v. Dukes County*, the one decision that has held there is a right of action under § 1983. However, the court finds the majority approach the better reasoned one.

By its terms, § 1983 gives a cause of action to every person within the jurisdiction of the United States who, under color of state regulation, is deprived of any rights secured by "the Constitution and laws of the United States." Although stated broadly, § 1983 does not provide a means of enforcing every federal statute. If Congress foreclosed private enforcement when it enacted the statute in question or if the statute is not of "the kind" that creates enforceable rights under § 1983, then the statute does not provide a private right of action enforceable under § 1983. *Middlesex County Sewerage Authority v. National Sea Clammers Association*, 453 U.S. 1, 101 S. Ct. 2615 (1981); *Pennhurst State School & Hospital v. Halderman*, 451 U.S. 1, 101 S. Ct. 1531 (1981).

With regard to the former, Congress will be found to have foreclosed a § 1983 remedy when the federal statute itself provides other remedial devices or creates its own comprehensive enforcement scheme. *Middlesex County Sewerage Authority v. National Sea Clammers Association*, 453 U.S. at 19-20, 101 S. Ct. at 2512-2513. With regard to the latter, the U. S. Supreme Court has given little

guidance as to the relevant criteria to be employed in determining whether a federal statute is of "the kind" that creates rights enforceable under § 1983. *Rocky Mountain Airways, Inc. v. Pitkin*, 674 F. Supp. at 317-318. It has, however, appeared to draw a distinction between those kinds of statutes such as 49 U.S.C. app. § 2210 whereby federal funds are disbursed to states upon the condition that the state provide adequate "assurances" of some sort to the federal government, reasoning that the typical remedy for state noncompliance with such federally mandated conditions is not a private cause of action for noncompliance, but rather action by the federal government to terminate payment of funds to the state. *Pennhurst State School & Hospital v. Halderman*, 451 U.S. at 28, note 21, 101 S. Ct. at 1545, note 21. See also *Rocky Mtn. Airways, Inc. v. Pitkin*, 674 F. Supp. at 317.

Although the Sixth Circuit has yet to decide the issue of whether a person may indirectly bring a private cause of action under § 2210 by means of § 1983, the Sixth Circuit's holding in *Northwest Airlines* that there is no direct private right of action under § 2210 was based on the observation that § 2210 establishes its own administrative enforcement scheme, the existence of which is inconsistent with a private right of action. See *Northwest Airlines v. County of Kent*, 955 F.2d at 1058-59. Because the Sixth Circuit has determined that § 2210's own administrative enforcement scheme indicates Congress' intent that there be no private right of action under § 2210, this court concludes that the Sixth Circuit would similarly find that a 1983 remedy is foreclosed because of §

2210's administrative enforcement scheme.

The Debtor's ability to maintain an action for TCAC's alleged violation of Tennessee state law, specifically the requirement in TENN. CODE ANN. § 42-5-110(a)(2) that municipalities fix rentals and fees at municipal airports on a reasonable and uniform basis, is also uncertain. Apparently, no Tennessee court has considered the issue of whether this statute may be enforced by a private right of action and the court has been unable to locate cases from any other jurisdictions construing similar state statutes. A leading Tennessee treatise instructs that "to infer a private right of action not otherwise authorized by statute, the existence of such cause of action must be consistent with the evident legislative intent and with the effectuation of the purposes intended to be served by the statute." 1 TENN. JURIS. ACTIONS § 10 (1983). The court agrees with Debtor that it would appear that § 42-5-110(a)(2) was enacted not only for the benefit of the public, but also for the benefit of entities like the Debtor who are charged fees and rentals by municipal airports. A provision which requires certain fees to be "reasonable and uniform" almost certainly was intended to benefit those who were to be charged these fees.

The court is not convinced, however, that it is sufficiently likely that the Debtor would prevail on the merits in an action asserting that the fees and rentals charged by TCAC under the Lease violate § 42-5-110(a)(2). With the exception of the charges to the Debtor for the west hanger, the evidence establishes that TCAC's fees and charges applicable to Tri-City Aviation are substantially

similar to those charged to Debtor. The rates paid by Debtor and Tri-City Aviation are identical for paved and unpaved areas per square foot per year and both leases are adjusted every three years based on cost of living increases as established by the Consumer Price Index. Tri-City Aviation is charged \$.68 per square foot for each of its hangers and Debtor is charged \$.68 per square foot for the east hanger. The major difference is in respect to the west hanger occupied by Debtor which has a current rental rate of \$4.11 per square foot, a rate more than twice the \$1.50 per square foot which an expert testified was a fair market rate for the hanger.

TENN. CODE ANN. § 42-5-110(a)(2) does not mandate the same rent to all fixed-based operators. Instead, the statute requires that the rentals be reasonable and uniform "for the same class of privileges or service" and that they are to be established "with due regard to the property and improvements used and the expenses of operation to the municipality." The rentals charged to Debtor for the west hanger are different than those charged Tri-City Aviation because the services furnished are different. Unlike Tri-City Aviation which provided its own buildings with its own funds, the west hanger was constructed by TCAC for the Debtor in 1979 at a total cost of \$785,000.00, with \$475,000.00 of the funds being paid by TCAC and the balance provided by a state grant. The lease payments on this hanger were designed to allow TCAC to recoup its cash outlay plus a 14% rate of return. To accommodate the Debtor, the rents were set artificially low in the initial years of the Lease with step increases of \$2,700.00 per year such that by the

end of the term the Debtor would be paying artificially higher rent payments. However, over the term of the Lease, the rental payments would average out to an appropriate rental payment. As a result of the step increases and the cost of living increases, the present rentals on the west hanger are substantially higher than market.

There is no evidence, however, that the Lease when executed in 1979 was unfair or unreasonable or that the capitalization rate was not in line with the market rate. The high rates now being paid by the Debtor are the result of the repayment scheme worked out by the Debtor and TCAC in 1979, including the step increases and cost of living increases rather than the result of a scheme or conspiracy to discriminate against the Debtor. Granted, the Debtor is paying higher than the market rate at the present time, but the Debtor paid lower than market rate during the initial years of the Lease. This court is not convinced that TENN. CODE ANN. § 42-5-110 does not allow a municipality to recover its costs and a reasonable rate of return when it expends funds on behalf of a tenant or that it does not permit a municipality to charge different rates to fixed-based operators who provide their own buildings. In fact, the express language of the statute provides that the rates are to be established based on the services provided and the cost to the municipality.

There was also testimony at the hearing indicating that Tri-City Aviation's location resulted in it getting more traffic, and that Tri-City Aviation had an above-ground fuel storage tank which was more appealing to airlines while Debtor had an underground tank

which presented potential environmental problems. However, the location does not appear to be the result of any grand design by TCAC to discriminate against Debtor. With respect to the fuel tank farm, Tri-City Aviation built a new tank farm in 1991, and it appears that TCAC was in the process of having one built for the Debtor at the time this case was filed.

Although the Debtor agrees that it is not appropriate for this court to adjudicate the merits of its claim against TCAC in the context of these summary proceedings, the Debtor does assert that the court should take its claim into consideration to reduce the prepetition arrearages owed to TCAC to a reasonable amount in order to conform to the requirement of the federal assurances and state law that the rates be reasonable. It is Debtor's position that the court has the ability to make such alterations pursuant to its equity powers. However, the court does not agree that its powers are that broad and far-reaching.

This court has no authority to modify leases or executory contracts. See *In re SCCC Associates II Ltd. Partnership*, 158 B.R. 1004, 1015 (Bankr. N.D. Cal. 1993); *In re McDaniel*, 89 B.R. 861, 863 (Bankr. E.D. Wash. 1988); *Matter of Lauderdale Motorcar Corp.*, 35 B.R. 544, 548-549 (Bankr. S.D. Fla. 1983); *In re TSW Stores of Nanuet, Inc.*, 34 B.R. 299, 304 (Bankr. S.D.N.Y. 1983). Nor can a debtor pick and choose the portions of the contract it considers profitable, while rejecting any burden it considers onerous; a lease must be assumed or rejected by the debtor in its entirety. *N.L.R.B. v. Bildisco and Bildisco*, 465 U.S. 513, 531-32, 104 S. Ct.

1188, 1199 (1984); *In re Downtown Properties, Inc.*, 162 B.R. 244, 247 (Bankr. W.D. Mo. 1993); *In re Plum Run Service Corp.*, 159 B.R. 496, 498 (Bankr. S.D. Ohio 1993).

The Debtor maintains that because the Lease is allegedly illegal, the court can refuse to enforce the Lease to the extent of its illegality. However, it is clear under state law that in the event of an illegal contract, the relief available to the injured party is the nonenforcement of the contract. *See Lambert v. Home Federal Savings & Loan*, 481 S.W.2d 770 (Tenn. 1972); *State of Tennessee v. Heath*, 806 S.W.2d 535 (Tenn. App. 1990), *perm. to app. denied*, (Tenn. 1991). There is no authority for this court to rewrite the Lease to make it legal and then force it upon the parties.<sup>6</sup> *See Bob Pearsall Motors Inc. v. Regal Chrysler-Plymouth, Inc.*, 521 S.W.2d 578, 580 (Tenn. 1975) (courts are precluded from creating new contract for the parties).

Of course, if the Lease were in actuality a series of separate or divisible agreements such that any illegal portions could be separated from the legal portions, the Debtor would have the option of assuming the divisible legal agreements and rejecting the divisible illegal ones. *See In re Plumb Run Service Corp.*, 159 B.R. at 498. However, in this case the amount of the rent is the

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<sup>6</sup>It appears that Tennessee courts have carved out an exception for the judicial modification of non-compete covenants in employment contracts where such covenants are found to be reasonably necessary to protect the employer's interest without imposing undue hardship on the employee and if the public interest is not adversely affected. This so-called rule of reasonableness is uniquely peculiar to covenants not to compete and has no applicability here. *See Central Adjustment Bureau, Inc. v. Ingram*, 678 S.W. 2d 28, 36 (Tenn. 1984).

very heart of the Lease. There is no way to separate alleged illegal rent from the remainder of the Lease.

Finally, the Debtor urges the court to consider the prospect that the prepetition claim of TCAC for the rental arrearage may be equitably subordinated to the claims of the Debtor's other creditors. A debtor may interpose the defense of equitable subordination to a motion for relief from stay. See *In re Poughkeepsie Hotel Associates Joint Venture*, 132 B.R. 287, 292-293 (Bankr. S.D.N.Y. 1991). While the sufficiency of such a defense may be considered, it is likewise not appropriate for the court to adjudicate the merits of equitable subordination in the context of a motion for relief from stay. *Id.*

Establishing the defense of equitable subordination requires proof that the non-insider claimant was engaged in gross misconduct tantamount to fraud which resulted in injury to the debtor's creditors or which conferred an unfair advantage on the claimant. See *In re Baker & Getty Financial, Inc.*, 974 F.2d 712, 717-718 (6th Cir. 1992). Here, the Debtor has not offered any evidence that TCAC engaged in any misconduct tantamount to fraud. Accordingly, the defense of equitable subordination is insufficient.

The court having also concluded that TCAC's alleged failure to comply with the federal assurances and Tennessee law does not constitute a sufficient basis for denying TCAC's motion for relief from the automatic stay, the court must consider whether granting of the motion is appropriate. As noted previously, TCAC maintains that Debtor does not have the financial means to reorganize.

Debtor's ability to reorganize, indeed its very existence, depends upon its assumption of the Lease. Thus, the court must determine whether the prerequisites for assumption under § 365(b) have been established, *i.e.*, the prompt cure or adequate assurance of a prompt cure of any and all defaults under the Lease and adequate assurance of future performance under the Lease. The Debtor has the burden of proof on these issues. *See In re Rachels Industries, Inc.*, 109 B.R. 797, 802 (Bankr. W.D. Tenn. 1990). *See also* 11 U.S.C. § 362(g)(2).

The defaults in the Lease, which Debtor must cure before it can assume the Lease, are the \$81,474.13 in prepetition arrearage and the completion of the fuel spill cleanup. Although the Debtor is negotiating with the Tennessee Department of Environment and Conservation to reduce the funds needed by Debtor to complete the cleanup, at the present there has been no reduction and the balance required is \$60,000.00. Thus, the Debtor will need funds totaling \$141,474.13 to cure the prepetition Lease defaults.

As evidence of its ability to cure the defaults, the Debtor introduced a letter from Richlands National Bank (the "Bank"), dated February 11, 1994, wherein the Bank agrees to loan Debtor the sum of \$60,000.00 subject to certain terms and conditions including the renegotiation of a long-term lease between TCAC and the Debtor at a substantially reduced rent. Obviously, this commitment falls far short of the funds needed by Debtor to cure the Lease defaults and the Debtor has reached no agreement with TCAC as to future rent reductions. In deference to the Debtor, however, it has not known

the exact amount needed to cure the defaults until this court's ruling regarding the Debtor's potential counterclaims and affirmative defenses.

To establish that Debtor has the ability to meet its future lease obligations, Mike Bales, president and majority stockholder of the Debtor, testified that since the commencement of its Chapter 11 case, the Debtor has been able to pay all of its current operating expenses (although it was unclear from Mr. Bales' testimony whether this included full payments to the Bank), and that it has cut its expenses by \$3,000.00 per month through a reduction of the monthly payment to the Bank from \$14,000.00 to \$11,000.00. Mr. Bales also testified that from the beginning of this calendar year through the end of February, the Debtor has had a \$7,000.00 profit which compares favorably with the same time period in 1993 when the Debtor suffered a \$30,000.00 loss. It was the opinion of Mr. Bales that the Debtor was approaching its best months, March through September, and that the Debtor would be able to meet its debt service in the future based on pro formas prepared by Mr. Bales. Mr. Bales admitted on cross-examination that his confidence that the Debtor would be able to fund the plan was based on speculation, but stated that it was speculation based on his 15 years of experience. Neither the pro formas mentioned by Mr. Bales, nor the Debtor's current financial statements were introduced at the hearing.

To counter Debtor's assertion that it could meet its current obligations, TCAC offered into evidence the Debtor's financial

statements for the years 1989 through 1992, which show that the Debtor suffered a loss in each of those years, with a loss in 1989 of \$31,515.00, a loss in 1990 of \$69,127.00, a loss in 1991 of \$36,993.00 and a loss for 1992 of \$158,140.00. TCAC also introduced Debtor's financial statement as of September 30, 1993, which showed a net loss of \$72,000.00 if the Debtor's monthly debt service to the Bank had been paid, which it had not. TCAC's director of finance, Kathy Smith, testified that from a review of the Debtor's financial statements and its financial ratios, she saw no way for the Debtor to make its Lease payments.

In order to meet the directive of § 362(d)(2)(B) that the property a debtor seeks to retain is necessary for an effective reorganization, the United States Supreme Court has stated that a debtor must establish that there is a "reasonable possibility of a successful reorganization within a reasonable time." *United States Savings Association of Texas v. Timbers of Inwood Forest Associates, Ltd.*, 484 U.S. 365, 376, 108 S. Ct. 626, 633 (1988). The Supreme Court noted in *Timbers* that this burden requires a less detailed showing during the four months in which a debtor is given the exclusive right to put together a plan, see 11 U.S.C. § 1121(b) and (c)(2), but that even then § 362(d)(2) relief is appropriate if there is "no realistic prospect of effective reorganization." *Id.*

In this case, the Debtor is still in its exclusivity period, having been in this Chapter 11 less than four months. While the evidence offered by the Debtor that it can reorganize is not substantial, it is not so insignificant to suggest that the Debtor

has no realistic prospect of reorganizing. Now that the court has established the amounts needed to cure the defaults, the court finds it appropriate to give the Debtor the opportunity to demonstrate that it can promptly cure the Lease defaults and provide adequate assurance of its future performance in light of the court's ruling. This conclusion is supported by the following findings: a debtor should be given every opportunity to establish its ability to reorganize during the early stages of its case; the Debtor is current in its postpetition obligations; and the Bank has indicated its desire to back the Debtor's reorganization efforts as shown by its reduction of Debtor's interest rate and monthly payment and the Bank's offer to finance at least a portion of the funds needed to cure the Lease defaults. Finally, and most importantly, Debtor should be given an additional opportunity to establish that it can assume the Lease because the effect upon the Debtor if TCAC is granted relief from the stay would be catastrophic while there is no prejudice to TCAC by a short delay; TCAC is now receiving postpetition rental payments, although admittedly in a smaller amount than it is entitled to under the Lease.

The court does want to emphasize to the Debtor, however, that it must meet all the requirements of assumption set forth in § 365(b). The court will not entertain any proposals that contemplate an extended period of time to cure the default. Section 365(d) requires that the Debtor "at the time of assumption of ... Lease" cure or provide adequate assurance that it will

"promptly" cure the default. (emphasis supplied). As noted in the article entitled *Contractual Cure in Bankruptcy* in THE AMERICAN BANKRUPTCY LAW JOURNAL, "in the case of real estate leases ... courts will almost universally require that any pecuniary default be cured at or prior to the time the contract is assumed." Richard L. Epling, *Contractual Cure in Bankruptcy*, 61 AM. BANKR. L. J., Winter 1987, at 74 (1987).

In accordance with the directives of the Court set forth above, this matter is continued until June 6, 1994, for a determination as to whether the prerequisites to Debtor's assumption of the Lease set forth in § 365(b) have been met. If the Debtor is unable to establish these requirements at the continued hearing, TCAC's motion for relief will be granted.

ENTER: April 13, 1994

BY THE COURT

A handwritten signature in cursive script, appearing to read "Marcia Phillips Parsons".

MARCIA PHILLIPS PARSONS  
UNITED STATES BANKRUPTCY JUDGE