

FACING THE ISSUES®

Legal Briefs from the Attorneys of
Mackall, Crouse & Moore, PLC

Creditors' Corner

Wednesday, July 1, 2009
Volume 9, Number 6

2009 ECONOMIC STIMULUS ACT CREATES COLLATERAL FOR LENDERS

The “American Recovery and Reinvestment Act of 2009” (the “Act”) legislated many changes in tax law. Interestingly enough, one of these changes creates an opportunity for lenders to improve their collateral position with borrowers. While many security agreements grant a security interest in tax refunds, those that do not should be amended and here is why.

Prior to the Act net operating losses (“NOLs”) could be carried back two years before the year of the loss and carried forward twenty years after the year of the loss. For tax years beginning in 2008, the Act grants a look-back of five years, as far as 2003, for small businesses with gross receipts of \$15 million or less. Individuals with losses from ownership interests in sole proprietorships, rentals, LLCs, LLPs and S-Corps may thus be able to obtain tax refunds even though the entity itself cannot obtain a refund. C-Corps that previously paid taxes may be eligible.

Practice Pointer: Lenders should make sure that borrowers or guarantors collateralize their obligations to the lender with tax refunds particularly where there are now big operating losses. The attorneys at MCM can assist in document review or properly draft the necessary security agreement clauses.

BANKRUPTCY COURT GRANTS ADMINISTRATIVE CLAIM FOR POST-PETITION RENT ON NON-RESIDENTIAL LEASE

Section 365(d)(3) of the Bankruptcy Code requires a trustee or a Chapter 11 debtor in possession to perform all obligations under an unexpired non-residential lease until the lease is rejected for a period of up to sixty days. In *Roehrich v. Burival (In re Burival)*, No. 08-6026 (8th Cir. BAP, June 4, 2009), a crop land lease required debtor to make his final bi-annual rental payment of \$90,799.33, which became due only two days after his bankruptcy. The debtor in possession was legally responsible for payment of the full amount to the landlord, even though the payment related to pre-petition usage of the property for the prior six months. The Court held that the debtor is responsible for rental payments becoming due in the sixty days, even if that obligation accrued prior to the sixty days. *(continued)*

If the landlord is not paid it may file an administrative claim for the amount owed under Section 503(b) (1). The administrative claim will require payment in full or else the debtor cannot likely confirm a plan of reorganization. The critical aspect of the Court's holding is that landlords can claim the administrative claim without first establishing that the rent obligation "was an actual and necessary cost or expense of preserving the bankruptcy estate," as is required for many other administrative claims. While this case involved a crop land lease, the Court's analysis of Section 365(d)(3) equally applies to all unexpired non-residential leases in bankruptcy.

Practice Pointer: The court's ruling provides a powerful benefit for a landlord and a severe detriment for a tenant. A landlord facing a tenant in bankruptcy should always consult with experienced bankruptcy counsel in order to maximize its remedies under the Bankruptcy Code. A failure to properly file an administrative claim would waive any ability to make the claim. The landlord should also consult with experienced bankruptcy counsel if issues arise with the lease and a bankruptcy trustee. MCM routinely advises commercial landlords in bankruptcy-related issues.

SOPHISTICATED LENDERS CANNOT BENEFIT FROM EQUITABLE SUBROGATION

Lenders advancing funds to satisfy a prior mortgage cannot generally benefit from the rule of equitable subrogation and take priority from the recording date of the mortgage that has been satisfied. This issue arises in cases where lenders fail to properly or timely record their mortgage and another mortgagee records its interest in the interim.

In *Citizens State Bank v. Raven Trading Partners, Inc.*, A08-1560 (Minn. Ct. App. 2009), Citizens State Bank ("Citizens") advanced funds which satisfied and discharged two prior mortgages and received a new mortgage on the subject property. Citizens' mortgage was not properly recorded until 80 days after the closing, because the mortgage registration tax was not properly calculated and other delays occurred which Citizens did not explain. Raven recorded a mortgage between the date the Citizens mortgage was signed and when it was recorded, without notice of Citizens' mortgage. The District Court found that Citizens could step into the priority of the two mortgages it paid off (and ahead of Raven's mortgage), under the doctrine of equitable subrogation. The Court of Appeals reversed the District Court, and held that Citizens Bank could not be equitably subrogated ahead of Raven because its failure to timely record its mortgage was not a justifiable or excusable mistake. The court held that a professional lender, such as a bank, is subject to a higher standard for purposes of equitable subrogation. *(continued)*

Practice Pointer: A lender should always make sure its mortgages are timely and properly recorded. The attorneys at MCM regularly assist our bank clients with proper procedures and documentation to perfect mortgage liens. The attorneys at MCM have also extensive experience in litigating the issue of equitable subrogation.

If you have any questions, please call one of the attorneys in our MCM Creditors' Remedies group:

Timothy D. Moratzka
(612) 305-1456
tdm@mcmlaw.com

Robert S. Lee
(612) 305-1448
rsl@mcmlaw.com

Stacy A. Woods
(612) 305-1409
saw@mcmlaw.com

Andrew P. Moratzka
(612) 305-1418
apm@mcmlaw.com

Allen E. Christy, Jr.
(612) 305-1490
aec@mcmlaw.com

Patrick C. Summers
(612) 305-1473
pcs@mcmlaw.com

Matthew A. Anderson
(612) 305-1401
maa@mcmlaw.com

Mychal A. Bruggeman
(612) 305-1478
mab@mcmlaw.com

"MCM has prepared these materials for informational purposes only and not as legal advice or **recommendations for specific situations**. Receipt of this information does not create an attorney-client relationship. You should not act upon this information without seeking professional counsel **for specific legal guidance.**" If you do not wish to receive future newsletters from Mackall, Crouse & Moore, please email mcmlaw@mcmlaw.com with the subject of Unsubscribe.

IMPORTANT NOTICE: Any tax information contained in this email or its attachments is not intended, and cannot be used by the taxpayer or any other person, to avoid any civil or criminal tax penalties which the Internal Revenue Service or another governmental agency may impose on the taxpayer or any other person for acting in reliance upon information contained in this email or its attachments.



1400 AT&T Tower · 901 Marquette Avenue · Minneapolis, MN 55402

Telephone: 612.305.1400 · Fax: 612.305.1414

E-mail: mcmlaw@mcmlaw.com · Web: www.mcmlaw.com