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14
15 UNITED STATES BANKRUPTCY COURT
16 FOR THE NORTHERN DISTRICT OF CALIFORNIA
17

18 In re

19 HOWREY LLP,

20 Debtor.
21
22

Case No. 11-31376 DM

Chapter 11

**CHAPTER 11 TRUSTEE'S
OBJECTION TO MOTION OF
HINES REIT 321 NORTH CLARK
STREET, LLC'S MOTION FOR
ADMINISTRATIVE EXPENSE**

23 Date: January 11, 2012

24 Time: 1:30 p.m.

25 Ctrm: 22nd Floor

U.S. Bankruptcy Court

235 Pine Street

San Francisco, California
26

1 Allan B. Diamond, chapter 11 trustee for the estate of Howrey LLP (the “Trustee”), files
2 his objection to the Motion of Hines REIT 321 North Clark Street, LLC (“Hines”) for Allowance
3 and Immediate Payment of Administrative Expense Claims Pursuant to 11 U.S.C. § 365(d)(3) or,
4 in the Alternative, Pursuant to 11 U.S.C. § 503(b)(1) (the “Motion”) and, in support thereof,
5 respectfully represents as follows:

6
7 **PRELIMINARY STATEMENT**

8 1. Although Bankruptcy Code § 365(d)(3) has been widely applied to require timely
9 payment of post-petition rent on non-residential leases, the statute is completely silent on the
10 appropriate remedy for a Debtor’s failure to timely make those payments. Rather, the remedy,
11 including the timing of the payment of a § 365(d)(3) administrative expense claim, is left to the
12 sole discretion of the bankruptcy court.

13 2. Prior to the Trustee’s appointment, the Debtor entered into an agreement to reject
14 the Lease (defined below) and vacate the premises. Although it appears that § 365(d)(3) required
15 the Debtor to timely pay Hines for post-petition rent that became due before the Lease was
16 rejected, the Debtor did not make that payment. After the expiration of almost 6 months
17 following rejection, Hines now seeks entry of an order compelling the Trustee to immediately
18 pay Hine’s asserted § 365(d)(3) administrative expense claim.

19 3. While the Trustee is sympathetic to Hines’ position, the reality is that this estate
20 has very limited financial resources at this time, thus warranting the indefinite postponement of
21 the payment of any allowed § 365(d)(3) claim. As discussed below, this estate faces
22 administrative expense claims not only from Hines but from other former landlords as well. If
23 allowed as filed, the landlord claims alone would completely exhaust the estate’s current cash
24 assets. Moreover, the estate’s cash is subject to Citibank’s asserted cash collateral lien claims,
25 and Citibank has not agreed to any carve-outs or special accommodations for the benefit of the
26 Debtor’s former landlords. For all of these reasons, should Hines demonstrate its entitlement to

1 a § 365(d)(3) claim to the Court’s satisfaction, the Trustee seeks entry of an order postponing
2 payment of such claim until it is determined that this estate is administratively solvent.

3 **BACKGROUND**

4
5 4. On April 11, 2011 (the “Commencement Date”), a chapter 7 involuntary petition
6 was filed against Howrey LLP by L.A. Best Photocopies, Inc., Kent Daniels and Associates, Inc.,
7 and Advanced Discovery LLC.

8 5. On June 6, 2011, Howrey LLP (the “Debtor”) filed its *Ex Parte Consent to Entry*
9 *of Order for Relief and Motion to Convert Debtor’s Case to Chapter 11* and the Court entered its
10 *Order for Relief and Converting Case to One Under Chapter 11* (the “Order for Relief”) on the
11 same date.

12 6. Following entry of the Order for Relief, the Debtor operated its business and
13 managed its assets as a debtor in possession.

14 7. On September 15, 2011, Citibank, N.A. (“Citibank”) filed its *Motion for Entry of*
15 *an Order Converting the Debtor’s Chapter 11 Case to a Case Under Chapter 7 of the*
16 *Bankruptcy Code, or, In the Alternative, Appointing a Chapter 11 Trustee*. On September 22,
17 2011, the Court entered its *Order Approving Citibank, N.A.’s Motion to Appoint a Chapter 11*
18 *Trustee*.

19 8. On October 7, 2011, the United States Trustee for the Northern District of
20 California (the “U.S. Trustee”) appointed the Trustee as the chapter 11 trustee for the estate of
21 Howrey LLP, which appointment was approved by an order of this Court dated October 12, 2011
22 Thereafter, the Trustee satisfied all of the conditions set forth in Bankruptcy Code § 322, and the
23 Trustee is now serving as chapter 11 Trustee for the Debtor’s chapter 11 estate pursuant to §
24 1104 of the Bankruptcy Code.

25 9. Prior to the Commencement Date, the Debtor and Hines entered into a non-
26 residential office lease dated April 20, 2002 (the “Lease”) providing for the Debtor’s use and

1 occupancy of office space located at 321 North Clark Street, Suites 3300, 3400, and 3500,
2 Chicago, IL 60610 (the "Leased Space"). Pursuant to its terms, the Lease was set to expire on
3 February 28, 2017.¹

4 10. Effective April 15, 2011, the Debtor and Hines entered into that certain Lease
5 Possession Termination and Surrender Agreement (the "Lease Termination Agreement")
6 pursuant to which the Debtor and Hines agreed that the Debtor would vacate and surrender the
7 Leased Space as of April 15, 2011.

8 11. On June 6, 2011, the Debtor filed a motion seeking this Court's authority to reject
9 the Lease [Dkt. No. 63] (the "Rejection Motion"). On June 21, 2011, the Court entered an order
10 granting the Rejection Motion, and providing that the Lease was deemed rejected as of "the
11 earlier of the date of the [Rejection] Motion or any earlier termination of the particular
12 Unexpired Lease" See Order dated June 21, 2011 [Dkt. No. 115] (the "Rejection Order").
13 Accordingly, the Lease was rejected as of April 15, 2011 (the "Rejection Date").

14 12. On December 14, 2011, Hines filed the Motion, seeking immediate payment of
15 \$28,911.67 as an administrative expense which Hines contends arose between the
16 Commencement Date and the Rejection Date.

17 JURISDICTION AND VENUE

18 13. This Court has subject matter jurisdiction to consider and determine this matter
19 pursuant to 28 U.S.C. § 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b). Venue
20 is proper before this Court pursuant to 28 U.S.C. §§ 1408 and 1409.

21 OBJECTION

22 14. While the Trustee concedes that 11 U.S.C. § 365(d)(3) entitles Hines to an
23 administrative expense claim to the extent the amount of such claim is proven by Hines, the
24 timing of payment is expressly within this Court's discretion. See *In re Silver State Helicopters*,

25 _____
26 ¹ Because Hines attached copies of the Lease and related documents to the Motion, and in light of the documents' length, the Trustee is not attaching additional copies to this Response.

1 *LLC*, 566 F.3d 1177 (9th Cir. 2009) (holding that the timing of payment of a § 365(d)(3) claim is
2 “fully within the discretion of the bankruptcy court . . .”). For the reasons discussed below, the
3 Court should exercise its discretion to postpone payment of any administrative expense claim to
4 Hines until it becomes evident that there are, or will be, sufficient assets in this estate to accord
5 the same treatment to all § 365(d)(3) administrative expense claims.

6 15. The Debtor’s estate presently holds extremely limited resources (approximately
7 \$2.6 million in cash), yet it faces § 365(d)(3) expense claims in excess of \$10 million, including
8 a claim from the Debtor’s former Washington D.C. landlord who, like Hines, is seeking
9 immediate payment of an administrative expense claim for allegedly unpaid rent. According to
10 the Washington D.C. landlord, its administrative expense claim is in excess of \$10.9 million.
11 *See* Request of Warner Investments L.P. for Payment of Administrative Rent and Gap Period
12 Rent [Dkt. No. 399]². While the Trustee disputes the amount of those other administrative
13 expense claims, if allowed, they may be entitled to the same priority and payment treatment as
14 Hines’ present administrative expense claim. As such, ordering immediate payment of the
15 Hines’ claim – even though it is for a relatively small amount – may subject this estate to
16 demands for immediate payment of other administrative claims for which there are currently
17 insufficient estate assets.

18 16. Although the Trustee believes that there will ultimately be sufficient estate assets
19 to satisfy all allowed administrative claims in full, there can be no certainty until the remainder
20 of the Debtor’s assets are liquidated, accounts receivable collection efforts are substantially
21 concluded, and the Debtor’s litigation assets are adjudicated or resolved. In the short time since
22 his appointment, the Trustee has been diligently getting up to speed and developing a strategy to
23 generate the largest possible estate for satisfaction of all claims, and the Trustee believes that he
24 will be ultimately successful in achieving that result. Nevertheless, until that result is obtained, it
25

26 ² Warner Investment’s motion is set for hearing on January 27, 2012, the same date as a pre-trial conference
in the Debtor’s adversary proceeding against Warner Investments, adversary proceeding no. 11-03170.

1 would be premature to order immediate payment to one particular administrative expense
2 creditor to the possible detriment and prejudice of other administrative creditors.

3 17. When faced with similar questions about an estate's administrative solvency,
4 courts routinely exercise their discretion to delay payment of § 365(d)(3) claims. For example,
5 in *In re LPM Corporation*, the Ninth Circuit Court of Appeals was asked to reverse a bankruptcy
6 court's holding that § 365(d)(3) claims are not entitled to priority over other administrative
7 expense claims. 300 F.3d 1134, 1137 (9th. Cir. 2002). Instead, the Ninth Circuit held that had
8 Congress intended § 365(d)(3) claims to hold super-priority status entitling them to payment
9 before other administrative claims, it would have made that clear in the plain language of §
10 365(d)(3). *Id.* at 1138. Accordingly, the Court affirmed the bankruptcy court's decision that "§
11 365(d)(3) is devoid of any grant of a superiority and it is inappropriate to imply such a remedy
12 simply because [the landlord] acted promptly." *Id.* 1138, *affirming In re LMP Corporation*, 253
13 B.R. 914, 919 (Bankr. S.D. Cal. 2000).

14 18. That result is entirely consistent with how other bankruptcy courts in this district
15 and beyond have resolved the issue. For example, this Court has previously declined to order
16 immediate payment of § 365(d)(3) claims when faced with a potentially administratively
17 insolvent estate. *In re Daisey/Cadnetix, Inc.*, 126 B.R. 87, 91 (Bankr. N.D. Cal. 1991); *In re*
18 *National Refractories & Minerals Corp.*, 297 B.R. 614, 616 (Bankr. N.D. Cal. 2003). Courts
19 outside of this district have likewise reached the same result. *See, e.g., In re Tandem Group,*
20 *Inc.*, 61 B.R. 738, 742 (Bankr. C.D. Cal. 1986) (§ 365(d)(3) is entitled to no greater priority than
21 other expenses of administration); *In re Microvideo Learning Systems*, 254 B.R. 90, 92-93
22 (holding that § 365(d)(3) does not give a landlord priority over other administrative expense
23 claims); *In re Pudgie's Development of NY, Inc.*, 239 B.R. 688, 695-96 (same).

24 19. Moreover, even if the estate had sufficient cash on hand to immediately pay all
25 asserted § 365(d)(3) claims (which it does not), that cash is subject to Citibank's asserted cash
26 collateral liens. None of the cash collateral budgets contain any provisions for payment of §

1 365(d)(3) administrative expenses, and Hines has not argued that its asserted § 365(d)(3) claim is
2 entitled to priority over Citibank's asserted secured claims and liens. Thus, even were Hines or
3 any other § 365(d)(3) administrative creditor allowed immediate payment of its asserted claim,
4 the Trustee would be unable to pay those claims because the estate has no cash that is not
5 encumbered by Citibank's asserted liens.

6 **CONCLUSION**

7 20. For the reasons stated, it is respectfully submitted that payment of any allowed §
8 365(d)(3) claims should be postponed pending the Trustee's determination that this estate is
9 administratively solvent, or further order of the Court.

10
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21 Dated: December 28, 2011

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1 CERTIFICATE OF SERVICE

2 I, the undersigned, declare:

3 I am employed in the City of Oakland, County of Alameda, California. I am over the age
4 of 18 years and not a party to this action. My business address is 1970 Broadway, Suite 225,
5 Oakland, California 94612.

6 On December 28, 2011, I served or caused to be served a true and correct copy of the
7 following document(s):

8 **CHAPTER 11 TRUSTEE'S OBJECTION TO MOTION OF HINES REIT 321
9 NORTH CLARK STREET, LLC'S MOTION FOR ADMINISTRATIVE
10 EXPENSE**

11 in the manner described below addressed as follows:

12 **X Mail:** By mailing said document(s) in an envelope and depositing the sealed envelope with
13 the United States Postal Service with postage fully prepaid, addressed as follows:

14 SEE ATTACHED SERVICE LIST

15 **X Via-Electronic Mail (CM/ECF):** Said document(s) and transmission of the Notification
16 of Electronic Filing by the Clerk to a Registered Participant(s), addressed as follows:

17 SEE ATTACHED SERVICE LIST

18 **X Via-Email Transmission:** By transmitting via-electronic mail the above listed
19 document(s) to the email address(es) as set forth below on this date:

20 SEE ATTACHED SERVICE LIST

21 I declare under penalty of perjury under the laws of the State of California that the
22 foregoing is true and correct and that this declaration was executed on December 28, 2011, at
23 Oakland, California.
24
25
26

/s/ Gail A. Michael

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