UNITED STATES BANKRUPTCY COURT
DISTRICT OF MAINE

In re: MONTREAL MAINE & ATLANTIC RAILWAY, LTD. Debtor.	Bk. No. 13-10670 Chapter 11

ESTATE REPRESENTATIVE'S REPLY IN SUPPORT OF *AMENDED* OBJECTION TO PROOFS OF CLAIM FILED BY CENTER BEAM FLATCAR COMPANY ON THE BASIS THAT (A) CLAIM 116-1 IS DUPLICATIVE OF CLAIM 116-2 AND (B) CERTAIN OF THE AMOUNTS ASSERTED IN CLAIM 116-2 ARE UNENFORCEABLE UNDER THE BANKRUPTCY CODE

Robert J. Keach, the estate representative (the "Estate Representative") of the post-effective date estate of Montreal Maine & Atlantic Railway, Ltd. ("MMA" or the "Debtor"),[1] hereby files this reply (the "Reply") in support of the *Trustee's Amended Objection to Proofs of Claim Filed by Center Beam Flatcar Company on the Basis that (A) Claim 116-1 is Duplicative of Claim 116-2 and (B) Certain of the Amounts Asserted in Claim 116-2 Are Unenforceable Against the Debtor* [D.E. 2025] (the "Amended Objection")[2] and in reply to Center Beam's response to the Amended Objection [D.E. 2066] (the "Response"):

INTRODUCTION

1. In light of Center Beam's Response, the only unresolved issue raised in the Estate Representative's Amended Objection is whether Center Beam is entitled to a general unsecured claim in the amount of $83,403.23 (Center Beam has acknowledged that it is not entitled to an administrative expense claim for that amount, *see* Resp. ¶ 15) (the "Disputed

[1] In accordance with the *Trustee's Chapter 11 Plan of Liquidation, dated July 15, 2015 (As Amended on October 8, 2015)* [D.E. 1822] (the "Plan"), upon the Effective Date of the Plan (which occurred on December 22, 2015, *see* D.E. 1927), Robert J. Keach became the Estate Representative of the Post-Effective Date Estate (as defined in the Plan). *See* Plan § 6.1(a).

[2] Capitalized terms not defined in this Reply shall have the meanings ascribed in the Amended Objection.

Claim"). The Order authorizing the rejection of the Lease already set the Petition Date as the effective date for rejection of the Lease and thus for calculation of rejection damages, yet the Disputed Claim represents post-petition amounts asserted to be owing under the Lease. Moreover, rejection damages comprise only those damages calculable on the day before the petition date, and any post-petition damages asserted must qualify for administrative expense status (and Center Beam acknowledges that the Disputed Claim does not so qualify). The Estate Representative thus submits this Reply in further support of his contention that the Disputed Claim (which is only a portion of Center Beam's total asserted general unsecured claim) should be disallowed.

REPLY

A. Center Beam's Request for the Disputed Claim Is an Impermissible Collateral Attack on the Rejection Order

2. As set forth in the Amended Objection, the Order authorized rejection of the Lease *nunc pro tunc* to the Petition Date. *See* D.E. 421. The rejection of the Lease was thus effective—and Center Beam's rejection damages were cut off—as of the Petition Date. To permit Center Beam to assert a rejection damages claim that includes damages which accrued after the effective date of the rejection would be to eviscerate the *nunc pro tunc* relief awarded. The time for Center Beam to have taken issue with the effective date of the Lease rejection was in connection with entry of the Order, which is now *res judicata*. As Center Beam is collaterally estopped from attacking the Order, the Disputed Claim should be disallowed.

B. The Bankruptcy Code Limits Rejection Damages to Those Calculable on the Day Before the Petition Date

3. Even putting aside this Court's Order, which made the Lease rejection effective as of the Petition Date, the Bankruptcy Code limits rejection damages to those calculable on the day before the filing of the petition (which is—perhaps not coincidentally—consistent with the

Order). As set forth in Center Beam's Response, "[p]ursuant to § 365(g), 'the rejection of an executory contract or unexpired lease of the debtor constitutes a breach of such contract or lease . . . ***immediately before the date of the filing of the petition*** . . . .'" *See* Resp. ¶ 19 (emphasis added). Accordingly, rejection "damages are to be determined on the last business day before the petition is filed." In re Enron Corp., 354 B.R. 652, 659 (S.D.N.Y. 2006); *see also* In re Aslan, 909 F.2d 367, 371 (9th Cir. 1990) ("We agree with the district court and hold that when the debtor secures rejection of a non-assumed executory contract under section 365(g)(1), ***the date of breach is the day immediately prior to the filing of the bankruptcy petition***.") (emphasis added). Importantly, Bankruptcy Code sections 365(g)(1) and 502(g) prescribe that the *amount* of rejection damages—and not just the prepetition character of the claim—is fixed as of the day before the petition is filed. *See* Enron, 354 B.R. at 657 ("Congress understood 'determining' a claim to involve the mathematical calculation of the claim amount and not [just] fixing the type of claim."); Aslan, 909 F.2d at 369, 372 (affirming the district court holding that "the relevant date of breach, and therefore the date at which to value . . . damages, was the date immediately preceding the petition for bankruptcy."). Rejection damages are thus limited to those that would have been calculable on the day before a bankruptcy petition is filed. *See* 11 U.S.C. §§ 365(g), 502(g)(1); Enron, 354 B.R. at 659; Aslan, 909 F.2d at 371.

4. In its Response, Center Beam quotes a provision of the Lease[3], stating "[u]pon a breach by the Debtor, '[t]he Owner shall be entitled to collect and receive any and all rents and other amounts that under the terms of this lease that [sic] may then be due or that have accrued to the date of such delivery to Owner . . . .'" *See* Resp. ¶ 20; Lease ¶ 15, p. 6 (the "Default Damages Provision"). Center Beam thus appears to argue (without explicitly doing so—the Default Damages Provision is not again referenced in the Response) that the Disputed Claim

[3] The Lease is attached to the Response as Exhibit A.

results from the Default Damages Provision triggered by the Debtor' breach, which was deemed to occur on the day before the Petition Date in accordance with Bankruptcy Code sections 365(g)(1) and 502(g).[4]

5. Because the Bankruptcy Code ordains the day before the petition date as the date for calculation of rejection damages, damages that might have been triggered under state law at a later date are necessarily excluded from that calculation. The facts of Enron are illustrative. In Enron, the debtor continued selling electricity to a counterparty postpetition under the terms of an executory contract. 354 B.R. at 654. But when the price of electricity rose above that set forth in the contract, the debtor rejected it. Id. The counterparty filed a claim for rejection damages, calculating the damages based on the market electricity price at the time of the rejection, and justifying the calculation on the basis that the contract itself provided for calculation of damages based on the actual economic loss *at the time of the breach*. Id. The debtor objected, arguing that the plain language of Bankruptcy Code section 502(g)[5] required that rejection damages be calculated as of the day before the filing of the bankruptcy petition (not the date on which the contract was rejected, despite the language of the contract). Id. at 654. Although calculating damages as of the day before the petition date meant that the counterparty's rejection damages were greatly reduced (due to the increase in electricity price since the petition date which prompted the rejection), the bankruptcy court agreed with the debtor and the district court affirmed. Id. at 654, 660.

6. Here, as in Enron, despite the fact that state law might have awarded the non-breaching counterparty damages under the terms of the contract calculated as of—or accruing

[4] To the extent that Center Beam argues that the Default Damages Provision was triggered upon the Debtor's bankruptcy filing, it constitutes an unenforceable *ipso facto* clause, and any claim asserted to be flowing therefrom is thus likewise unenforceable. *See* 11 U.S.C. § 365(e)(1).

[5] At the time of the Enron decision, new Bankruptcy Code section 562 had been enacted but the parties agreed it was inapplicable because the claim at issue arose prior to its adoption. Id. at 657.

through—a later date, the Bankruptcy Code is explicit: damages are limited to those calculable as of the day before the petition date. On the day before the Petition Date, the Default Damages Provision had not been triggered, and thus no claim is awardable in connection therewith under Bankruptcy Code sections 365(g)(1) and 502(g). Claim 116-2 must thus be reduced by the amount of the Disputed Claim asserted to be flowing from the Default Damages Provision.

C. Center Beam is Not Entitled to Damages Incurred After Rejection Unless Such Damages Qualify for Administrative Expense Status

7. Center Beam goes on to assert that "[s]ince the rejected Lease is deemed to have been breached immediately before the date of the filing of the petition" (the Estate Representative agrees with this first clause), "Center Beam has an unsecured, prepetition claim for the amount due in lease payments *until the time that the rail cars were returned to Center Beam*, which amount totals $83,403.23." Resp. ¶ 21 (emphasis added).[6] As an initial matter, the Estate Representative does not follow this logic. But taking the second clause on its own, Center Beam appears to put forth a different justification for the asserted $83,403.23 general unsecured claim from the one implied in Response ¶ 20: that it is entitled to damages under the rejected Lease not—as prescribed by the Bankruptcy Code—until the effective date of such rejection, but instead until the property subject to the rejected Lease is returned.

8. But Center Beam cannot argue that the Disputed Claim both fits within Bankruptcy Code sections 365(g) and 502(g)(1) as arising "before the date of the filing of the petition" *and* argue that the claim arose during the period between when the Lease was rejected (the Petition Date) and when the cars subject to the Lease were returned (which would

[6] Center Beam also adds that adopting the Estate Representative's position would "mean that parties are precluded from recovering prepetition lease rejection damages, which is contrary to the Bankruptcy Code and case law." Resp. ¶ 23. But the Estate Representative explicitly did not challenge any of Center Beam's pre-petition lease rejection damages. *See* Amended Obj. ¶ 11 (parsing the asserted claim into pre- and post-petition components, and not challenging any pre-petition amounts). The Estate Representative takes issue only with damages Center Beam has calculated as accruing *after the effective date of this Court's order approving the rejection of the Lease.*

necessarily mean the claim arose post-petition). As set forth above, if the basis for the Disputed Claim is the Default Damages Provision, the Default Damages Provision had not been triggered as of the day before the Petition Date, and any damages flowing therefrom could thus not have qualified as rejection damages under Bankruptcy Code sections 365(g) and 502(g)(1).

9. If the basis for the Disputed Claim is instead that the return of the rail cars is the relevant event for assessment of rejection damages—as opposed to the effective date of the Order authorizing rejection of the Lease, this argument is inconsistent with applicable law. *See* In re Trak Auto Corp., 277 B.R. 655, 665 (Bankr. E.D. Va. 2002) ("[T]he effective date of rejection provided in the [relevant] order will govern. The issue of rejection does not turn on when the debtor turns the keys over to the landlord but is a matter of court order . . . ."). While the Trak Auto Court did go on to acknowledge that "when a debtor remains on the premises after the effective date of rejection[,] that debtor is [not] absolved for charges that accrue post-rejection," id., such "charges that accrue after the date of rejection and while the debtor remains in possession . . . fall under § 503(b) . . . ," id. at 666; *see also* In re Ames Dep't Stores, Inc., 306 B.R. 43, 62 n.67 (Bankr. S.D.N.Y. 2004) ("[T]o the extent [a claim] would be recoverable[] after rejection, ***it would not be under section 365(d)(3), whose obligations, as discussed above, end on rejection***. It would rather be based on a benefit to the estate, to be analyzed under section 503(b)(1).") (emphasis added).[7]

10. Center Beam has already acknowledged that the estate received no benefit corresponding to the asserted $83,403.23 claim. *See* Resp. ¶ 15. The claim thus cannot merit administrative status. *See* 11 U.S.C. § 503(B) (conferring administrative expense status upon "the actual, necessary costs and expenses of preserving the estate . . . ."). The Disputed Claim

[7] Bankruptcy Code section 365(d)(3) deals with leases of non-residential real property, but this analysis is equally applicable to Bankruptcy Code section 365(d)(5), which deals with leases of personal property.

thus qualifies neither as one for rejection damages or for an administrative expense status, and must be disallowed.

CONCLUSION

WHEREFORE, for the reasons set forth herein, the Estate Representative requests that the Court enter an order, substantially in the form annexed hereto, pursuant to section 502 of the Bankruptcy Code, Bankruptcy Rule 3007 and Local Rule 3007-1, (i) sustaining this Amended Objection; (ii) disallowing Claim 116-1 in its entirety, (iii) disallowing the Disputed Claim asserted in Claim 116-2 in its entirety and reducing Claim 116-2 in like amount, and (iv) granting such other and further relief as may be just.

Dated: April 1, 2016

ROBERT J. KEACH, ESTATE REPRESENTATIVE OF THE POST-EFFECTIVE DATE ESTATE OF MONTREAL MAINE & ATLANTIC RAILWAY, LTD.

By his attorneys:

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