

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

In re: :
: :
421 WILLOW CORPORATION :
t/a THE ELECTRIC FACTORY :
: :
Debtor. : Misc. No. 03-182

MEMORANDUM AND ORDER

J. M. KELLY, J.

OCTOBER , 2003

Presently before the Court is a Debtor's Motion for Stay Pending Appeal of the Bankruptcy Court's Orders of September 12, 2003 and Request for Expedited Hearing filed by Debtor 421 Willow Corporation t/a The Electric Factory ("Willow"), the opposition thereto filed by Callowhill Center Associates ("Callowhill") and Willow's Memorandum of Points and Authorities. Willow seeks a stay of the September 12, 2003 Orders of the United States Bankruptcy Court for the Eastern District of Pennsylvania, which dismissed Willow's adversary proceeding against Callowhill and lifted the automatic stay to permit Callowhill to reclaim its realty. The Bankruptcy Court's factual findings are not in dispute. For the following reasons, Willow's Motion for Stay and Request for Expedited Hearing is **DENIED**.

I. BACKGROUND

A. The Lease

On March 28, 1995, Willow entered into a commercial Agreement of Lease (the "Lease") with Callowhill to lease

property located at 421 North 7th Street, Philadelphia, Pennsylvania (the "Leased Premises"). The Lease was a commercial contract that permitted Willow the right to promote, advertise and exhibit live music performances at the Leased Premises, a venue known as The Electric Factory. The Lease contained language restricting the right of Willow to assign or sublet the Leased Premises without the prior written consent of Callowhill.

On February 28, 2000, Willow's principals and SFX Entertainment, Inc. ("SFX") executed a Stock Purchase Agreement ("SPA"), pursuant to which certain of Willow's affiliates, together with certain other assets, would be conveyed to SFX, including prompt transfer of Willow's Lease with Callowhill. Following execution of the SPA, Willow informed Callowhill that it desired to assign the Lease to SFX, but Callowhill denied the request.

B. The Pennsylvania State Court Proceedings

When Callowhill refused to consent to the proposed assignment, Willow initiated two suits, which were consolidated, in the Court of Common Pleas of Philadelphia County (the "State Court Action"), seeking, among other things, a declaration that Callowhill had breached the Lease by failing to approve the requested assignment to SFX. See 421 Willow Corp. and SFX Entertainment, Inc. v. Callowhill Center Assocs., May Term, 2001,

Nos. 1848 and 1851 (Pa. Comm. Pleas Ct., filed May 18, 2001).

Callowhill counterclaimed seeking, among other things, that the Court of Common Pleas declare the Lease terminated.

On February 18, 2003, Callowhill filed a Motion for Summary Judgment in the State Court Action and, following oral argument held on May 13, 2003, the Court of Common Pleas issued an Order on May 23, 2003 granting Callowhill's requests for relief. The Honorable Gene Cohen ("Judge Cohen") determined that Willow breached, and was in default of, the Lease and that the Lease was terminated. 421 Willow Corp. v. Callowhill Center Assocs., May Term 2001, Nos. 1848 and 1851, slip. op. at 7 (Pa. Comm. Pleas Ct., May 23, 2003.) Specifically, Judge Cohen determined that, since Callowhill did not consent to any transfer of rights to SFX, Willow breached the Lease when the SPA was executed, which granted SFX the right to manage and operate the Leased Premises, resulting in a de facto assignment of the Lease. Id. at 4-6. Judge Cohen concluded that since "Willow has both assigned the Lease to SFX and allowed SFX entities to use the Leased Premises without the consent of Callowhill," an event of default had occurred and Callowhill was "entitled to terminate the Lease as a result." Id. at 7.

On June 10, 2003, Willow's Motion for Reconsideration of the May 23, 2003 Order and Opinion was denied by Judge Cohen. On that same day, Willow filed its Bankruptcy Petition (the

"Petition") with the United States Bankruptcy Court for the Eastern District of Pennsylvania.

C. The United States Bankruptcy Court Proceedings

On June 26, 2003, Callowhill filed a motion to dismiss Willow's Petition or, in the alternative, for relief from the automatic stay to proceed against Willow under state law. On July 3, 2003, Willow filed an Adversary Complaint against Callowhill, alleging that Judge Cohen's May 12, 2003 Order declaring the Lease terminated was a preferential and/or fraudulent transfer under 11 U.S.C. §§ 547 and 548 of the Bankruptcy Code,¹ and could be avoided by Willow in the

¹ Bankruptcy Code Section 547(b) provides:

- (b) Except as provided in subsection (c) of this section, the trustee may avoid any transfer of an interest of the debtor in property--
- (1) to or for the benefit of a creditor;
 - (2) for or on account of an antecedent debt owed by the debtor before such transfer was made;
 - (3) made while the debtor was insolvent;
 - (4) made--
 - (A) on or within 90 days before the date of the filing of the petition; or
 - (B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and
 - (5) that enables such creditor to receive more than such creditor would receive if--
 - (A) the case were a case under chapter 7 of this title [11 U.S.C. §§ 701 et seq.];
 - (B) the transfer had not been made; and
 - (C) such creditor received payment of such debt to the extent provided by the provisions of this title [11 U.S.C. §§ 101 et seq.].

bankruptcy proceedings.

Following an initial hearing on the motion for relief from stay, on July 25, 2003, the Honorable Stephen Raslavich ("Judge Raslavich") issued an Order finding that, pursuant to the Rooker-Feldman doctrine,² the Bankruptcy Court was barred from reviewing the state court decision declaring the Lease terminated. In re 421 Willow Corp., Bankr. No. 03-18978, slip op. at 7 (Bankr. E.D. Pa. July 25, 2003). Judge Raslavich also ordered that a further

11 U.S.C. § 547(b).

Bankruptcy Code Section 548(a)(1)(B) provides:

(a) (1) The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within one year before the date of the filing of the petition, if the debtor voluntarily or involuntarily--

. . . .
(B) (i) received less than a reasonably equivalent value in exchange for such transfer or obligation; and
(ii) (I) was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation;
(II) was engaged in business or a transaction, or was about to engage in business or a transaction, for which any property remaining with the debtor was an unreasonably small capital; or
(III) intended to incur, or believed that the debtor would incur, debts that would be beyond the debtor's ability to pay as such debts matured.

11 U.S.C. § 548(a)(1)(B).

² Under the Rooker-Feldman doctrine, federal courts may not overturn state court decisions or evaluate claims that are "inextricably intertwined" with the state court's decision. See District of Columbia Court of Appeals v. Feldman, 460 U.S. 462 (1983); Rooker v. Fidelity Trust Co., 263 U.S. 413 (1923).

evidentiary hearing be held on August 14, 2003 regarding Callowhill's motion for relief from stay.

On August 6, 2003, Callowhill filed a motion to dismiss Willow's Adversary Complaint, positing that the specific language of 11 U.S.C. § 365(c)(3)³ dictated that a debtor in possession cannot assume or assign an executory contract where the same had been terminated under applicable nonbankruptcy law prior to the commencement of the case, and that this specific provision trumped the more general language regarding "transfers" of interests subject to avoidance under 11 U.S.C. §§ 547 and 548, as contended by Willow.

On September 12, 2003, Judge Raslavich granted Callowhill's motion to dismiss Willow's Adversary Complaint and granted Callowhill relief from the automatic stay, permitting Callowhill to proceed against Willow under state law for repossession of the Leased Premises. See 421 Willow Corp. v. Callowhill Center Assoc., Advs. No. 03-732 slip op. (Bankr. E.D. Pa. Sept. 12, 2003). Significantly, Judge Raslavich found that pursuant to the Rooker-Feldman doctrine, the Bankruptcy Court was "without jurisdiction to entertain questions of whether the lease in question has or has not been terminated, or whether the Common

³ Section 365(c)(3) provides that the trustee may not assume or assign any executory contract or unexpired lease of the debtor if "such lease is of nonresidential real property and has been terminated under applicable nonbankruptcy law prior to the order for relief." 11 U.S.C. § 365(c)(3).

Pleas Court erred in evaluating the evidence which led it to declare the lease terminated." Id. at 5-6. With respect to Willow's Adversary Complaint, relying on the precedent from this Circuit, Judge Raslavich found that Willow had failed to state a claim. Id. at 10-13. Since the Lease was terminated and could not be revived through the adversary proceeding, Judge Raslavich granted Callowhill's request for permission to retake the Leased Premises. Id. at 14-15.

D. Request to Bankruptcy Court for Stay Pending Appeal

On September 17, 2003, Willow filed with the Bankruptcy Court a motion for stay while it appealed that Court's September 12, 2003 Orders to the District Court. Following an expedited hearing held on September 23, 2003, the Bankruptcy Court denied Willow's request for the stay based upon its analysis that it was unlikely that Willow would prevail on the merits of its appeal. The Bankruptcy Court also considered the public policy embodied in the Bankruptcy Code that a landlord be permitted to repossess realty under a lease that terminated prepetition. At the conclusion of the hearing, however, Callowhill agreed that it would temporarily refrain from proceeding with repossession while Willow appealed to this Court for a stay.⁴ In re 421 Willow

⁴ On September 18, 2003, Willow filed a second Motion for Reconsideration in the State Court Action seeking the state court's reconsideration of its determination that the Lease had

Corp., Bankr. No. 03-18978 (Bankr. E.D. Pa. Sept. 24, 2003)
(amended order granting temporary stay for debtor to present
request for stay to district court).

E. Request to District Court for Stay Pending Appeal

On September 23, 2003, Willow filed in this Court the instant Motion for Stay Pending Appeal of the Bankruptcy Court's Orders of September 12, 2003. Callowhill filed its opposition on September 26, 2003, and Willow filed its Memorandum of Points and Authorities on October 7, 2003. We address Willow's request below.

II. STANDARD OF REVIEW

Federal Bankruptcy Rule 8005 sets forth the standards for issuance of a stay pending appeals from orders, judgments or decrees by the Bankruptcy Courts:

A motion for a stay of the judgment, order, or decree of a bankruptcy judge, for approval of a supersedeas bond, or for other relief pending appeal must ordinarily be presented to the bankruptcy judge in the first instance. Notwithstanding Rule 7062 but subject to the power of the district court and the bankruptcy appellate panel reserved hereinafter, the bankruptcy judge may suspend or order the continuation of other proceedings in the case under the Code or make any other appropriate order during the pendency of an appeal on such terms as will protect the rights of all parties in interest. A motion for such relief, or for modification or termination of relief granted by a

been terminated, as well as a stay and an immediate appeal.

bankruptcy judge, may be made to the district court or the bankruptcy appellate panel, but the motion shall show why the relief, modification, or termination was not obtained from the bankruptcy judge. The district court or the bankruptcy appellate panel may condition the relief it grants under this rule on the filing of a bond or other appropriate security with the bankruptcy court

U.S.C.S. Bankr. R. 8005; In re Blackwell, 162 B.R. 117, 119 (E.D. Pa. 1993).

The test for the appropriateness of the stay is the same as that for a preliminary injunction and, thus, the movant must establish all four of the following elements: (1) a strong likelihood of success on the merits of the appeal; (2) that the movant will suffer substantial irreparable injury if the stay is denied; (3) that substantial harm will not be suffered by other parties if the stay is granted; and (4) that issuance of the stay would not involve harm to the public interest. In re Blackwell, 162 B.R. at 119; In re Mediterranean Associates, L.P., No. Civ. A. 93-MC-304, 1993 U.S. Dist. LEXIS 18356 at *3-*4 (E.D. Pa. Dec. 29, 1993).

III. DISCUSSION

A. Likelihood of Success on the Merits of the Appeal

Willow contends that prepetition termination of the Lease may be avoided pursuant to the avoidance provisions contained in Bankruptcy Code Sections 547 and 548, which govern preferences and constructive fraud, respectively, in setting aside the Lease

termination. Avoidance of the termination requires this Court to accept that a prepetition termination of the Lease constitutes a "transfer," since Sections 547 and 548 apply only when a "transfer" has occurred.⁵ However, decisions from the courts in this Circuit have addressed this very issue to find that lawful prepetition termination of a contract or lease agreement does not constitute a transfer, with each case reasoning that an overbroad reading of the "transfer" language within the meaning of Bankruptcy Code Sections 547 and 548 would conflict with the specific language of Bankruptcy Code Section 365. See e.g., In re Coast Cities Truck Sales, Inc., 147 B.R. 674, 677-78 (D.N.J. 1992), aff'd without opinion, 5 F.3d 1488 (3d Cir. 1993); In re Egyptian Brothers Donut, Inc., 190 B.R. 26, 29 (Bankr. N.J. 1995). See also, In re LiTenda Mortgage Corp., 246 B.R. 185, 191, aff'd without opinion, 276 F.3d 578 (3d Cir. 2001).

Bankruptcy Code Section 365(c)(3) provides that a debtor in possession may not assume or assign an executory contract or unexpired lease where the same has been terminated under applicable nonbankruptcy law prior to the commencement of the case:

(c) The trustee may not assume or assign any executory

⁵ A "transfer" is defined by § 101(54) of the Bankruptcy Code as "every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property" 11 U.S.C. § 101(54).

contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if--

. . . .
(3) such lease of nonresidential real property has been terminated under applicable nonbankruptcy law prior to the order for relief

11 U.S.C. § 365(c)(3).

The relationship between Section 365 and Sections 547 and 548 can be explained as follows:

The structure of the Bankruptcy Code reflects this understanding of the difference between the loss of rights under an executory contract and other transfers of property. A separate section (11 U.S.C. § 365) governs the treatment of executory contracts. It would be anomalous, to say the least, to expect that the drafters of a generally thrifty codification of the bankruptcy law would devote a substantial section of the Code to the subject of assumption or rejection of executory contracts and unexpired leases, while at the same time allowing a portion of that subject to spill over into the section governing fraudulent transfers and obligations A statute should be construed as a harmonious whole. This is even truer of a Code. The general language of § 548 must be read harmoniously with the rest of the Code, including § 365 (and § 108) in order to preserve the legislative intent.

In re Egyptian Brothers, 190 B.R. at 30 (quoting In re Jermoo's, Inc., 38 B.R. 197, 204 (Bankr. W.D. Wisc. 1984)). These sections must be interpreted together, in accordance with the established rule of statutory construction that the specific provision of a statute supersedes a general provision of the same statute:

To follow [In re] Harvey [Company, Inc., 68 Bankr. 851 (Bankr. D. Mass. 1987)] would require the court to ignore clear statutory language and congressional intent for treatment of terminated nonresidential leases as expressed in § 365(c)(3). "[I]t is a commonplace of statutory construction that the specific

governs the general" Morales v. Trans World Airlines, Inc., 504 U.S. 374, 384 (1992). . . .
Section 365(c)(3), dealing expressly with nonresidential leases terminated prior to the bankruptcy filing, is a more specific section of the Bankruptcy Code than the provisions of § 548(a) for the avoidance of fraudulent transfers generally. Thus, the principles of statutory construction require that meaning and effect be given to § 365(c)(3), which must be applied instead of § 548(a) to the extent the two statutes are inconsistent

Id. at 31 (quoting In re Haines, 178 B.R. 471, 475 (Bankr. W.D. Mo. 1995)). As a result, the Court in Egyptian Brothers found that, while the "literal definition" of the term "transfer" encompassed termination of the agreements, "its application in Code §§ 547 or 548 so as to avoid the terminations is not consistent with the statutory framework." Id.

Significant policy considerations are implicated when a debtor is permitted to reinstate an otherwise valid prepetition termination of an executory contract: "The implications of a contrary finding would render virtually every validly terminated executory contract revivable by a debtor by simply initiating bankruptcy proceedings. Such a holding is not only unwarranted, but contrary to the intent of the drafters of the code." In re Coast Cities, 147 B.R. at 678. See also, In re Egyptian Brothers, 190 B.R. at 31; In re Haines, 178 B.R. 471 (Bankr. W.D. Mo. 1995). The Court in Egyptian Brothers agreed with these policy considerations, and credited the Court's comments in Haines, which examined the commercial consequences of earlier

cases that had arrived at a contrary conclusion:

The avoidance of non-collusive prepetition lease terminations as fraudulent transfers presents significant policy consideration. Strict application of cases such as Harvey and In re Queen City Grain, Inc. [51 Bankr. 722 (Bankr. S.D. Ohio 1985)], would make it impossible to settle rights in real property. Under the ruling in Harvey, landlords cannot rely on a state court judgment for termination of the lease and possession of the premises, but must wait until the statute of limitations on fraudulent transfer actions has passed. As one authority concluded, "the Harvey decision . . . will introduce a significant degree of uncertainty into the termination of leases and the transfer, mortgaging, and insurance of property that has been the subject of a lease termination."

190 B.R. at 31 (quoting Haines, 178 B.R. at 475). See also In re LiTenda Mortgage Corp., 246 B.R. at 191 ("Possession of expired rights is the equivalent of the possession of no rights. When a termination is pursuant to the terms of a contract, there is no transfer.").

Indeed, the only cases in this Circuit squarely addressing the interplay between the Bankruptcy Code's avoidance powers in Sections 547 and 548 and a debtor in possession's restriction under Section 365(c)(3) have demonstrated that a prepetition termination of a nonresidential lease cannot be avoided by the more general provisions of Sections 547 and 548. For these reasons, we find that Willow cannot demonstrate that there exists a strong likelihood of success on the merits of the appeal.

B. Application of the Rooker-Feldman Doctrine

Under the Rooker-Feldman doctrine, lower federal courts lack subject-matter jurisdiction to engage in appellate review of state court determinations that are "inextricably intertwined with the state court's [decision] in a judicial proceeding." District of Columbia Court of Appeals v. Feldman, 460 U.S. 462, 483 n.16 (1983); see also Rooker v. Fidelity Trust Co., 263 U.S. 413 (1923).

In this case, Willow raised before the Bankruptcy Court and this Court, the same claim that was raised and disposed of in state court, specifically, a determination as to Willow's leasehold interest in the realty owned by Callowhill. On May 23, 2003, the Court of Common Pleas rendered judgment in the matter, finding that Willow breached the Lease and that, due to its default, the Lease was declared terminated. On June 10, 2003, the same day that Willow filed its Bankruptcy Petition with the Bankruptcy Court, the Court of Common Pleas denied Willow's Motion for Reconsideration of its May 23, 2003 Order. Since assertion of jurisdiction over Willow's claim would require this Court to decide an issue that is "inextricably intertwined" with the Pennsylvania state court's decision, and the Rooker-Feldman doctrine instructs that the only courts empowered to review for error are the appellate Pennsylvania courts and, ultimately, the United States Supreme Court, to hold that Willow would likely

succeed on the merits of its appeal to avoid the prepetition Lease termination would effectively impermissibly reverse the state court decision. See Port Auth. Police Benevolent Ass'n, Inc. v. Port Auth. of New York and New Jersey Police Dep't, 973 F.2d 169, 177 (3d Cir. 1992).⁶

IV. CONCLUSION

For the foregoing reasons, this Court finds that Willow is unable to demonstrate a likelihood of success on the merits of the appeal of the Bankruptcy Court's September 12, 2003 Orders and that, pursuant to the Rooker-Feldman doctrine, this Court is nevertheless precluded from review of the Pennsylvania state court proceedings terminating the Lease that is at issue in this request for a stay pending appeal. Accordingly, Willow's Motion for Stay Pending Appeal and Request for Expedited Hearing is **DENIED.**

⁶ Willow's contention that the Rooker-Feldman doctrine does not apply to state court interlocutory orders is also without merit. Rooker-Feldman precludes review of decisions of the lower state courts, even those decisions that are interlocutory in nature. Port Auth. Police Benevolent Ass'n, 973 F.2d at 177-78.

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

In re: :
: :
421 WILLOW CORPORATION :
t/a THE ELECTRIC FACTORY :
: :
Debtor. : Misc. No. 03-182

O R D E R

AND NOW, this day of October, 2003, in consideration of the Debtor's Motion for Stay Pending Appeal of the Bankruptcy Court's Orders of September 12, 2003 and Request for Expedited Hearing (Doc. No. 1) filed by Debtor 421 Willow Corporation t/a The Electric Factory ("Willow"), the opposition thereto (Doc. No. 2) filed by Callowhill Center Associates, and Willow's Memorandum of Points and Authorities (Doc. No. 3), **IT IS ORDERED** that Willow's Motion for Stay Pending Appeal and Request for Expedited Hearing is **DENIED**.

BY THE COURT:

JAMES MCGIRR KELLY, J.