



Entered on Docket
July 23, 2008

Hon. Mike K. Nakagawa
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT

DISTRICT OF NEVADA

In re)

CONTROL ELECTRONICS, INC.,)

Debtor.)

Case No. BK-S-07-12425-MKN

Chapter 11

Date: July 16, 2008

Time: 9:30 a.m.

**MEMORANDUM DECISION ON EMERGENCY MOTION FOR DECLARATION
THAT AUTOMATIC STAY DOES NOT APPLY**

The Emergency Motion for Declaration that Automatic Stay Does Not Apply, brought by creditor GBH Holdings-Rainbow-Sahara, LLC, was heard on July 16, 2008. The appearances of counsel were noted on the record. After arguments were presented, the matter was taken under submission.

BACKGROUND¹

Control Electronics, Inc. (“Debtor”) filed a voluntary Chapter 11 petition for reorganization on April 30, 2007. Its schedules indicate that as of the petition date, it owned furniture inventory in a retail showroom located at 2350 South Rainbow Boulevard in Las Vegas as well as inventory in a warehouse located at 5150 South Decatur Boulevard. Debtor’s

¹ In the text and footnotes of this Memorandum Decision, all references to “Section” shall be to provisions of the Bankruptcy Code appearing in Title 11 of the United States Code unless otherwise indicated. All references to “Rule” shall be to provisions of the Federal Rules of Bankruptcy Procedure unless otherwise indicated.

1 Schedule "B" also indicated that additional furniture inventory is or was stored at another
2 warehouse located at 4225 Fidus Drive.

3 Previous proceedings in this bankruptcy case were conducted with respect to Debtor's
4 dispute regarding a sublease for the warehouse space at Decatur Boulevard. Debtor's dispute
5 with the master tenant, Goldway Enterprises, Inc., was settled on or about June 21, 2007, and an
6 order approving that settlement was entered on August 22, 2007. (Dkt# 76)

7 On July 25, 2007, GHB Holdings, Inc., the landlord for the retail showroom on Rainbow
8 Boulevard, filed a motion for relief from stay and for payment of rent. (Dkt# 63) Debtor filed
9 written opposition (Dkt# 68) and GHB filed a reply. (Dkt# 69) On October 16, 2007, the Court
10 entered an Order Modifying Automatic Stay ("Order"). (Dkt# 142) The Court determined that
11 the parties' relationship should be treated as a month-to-month tenancy guided by the terms of a
12 previous written lease between the parties. The Court further concluded that cause under Section
13 362(d)(1) had been established by virtue of the Debtor's breach of the terms of the month-to-
14 month lease and the absence of monthly operating reports showing the Debtor's ability to
15 become current on the rental payments. The Court further found that relief from stay under
16 Section 362(d)(2) was appropriate because the Debtor has no equity in the Rainbow Boulevard
17 premises and had not demonstrated a reasonable possibility of confirming a Chapter 11 plan
18 within a reasonable amount of time. The Order therefore modified the automatic stay so as to
19 require the Debtor to cure all post-petition rent arrearages no later than October 1, 2007.² In the
20 event the Debtor failed to cure the subject arrearages, the Order authorized GHB to obtain, on an
21 ex parte basis, immediate relief from stay to pursue unlawful detainer proceedings in state court.

22 There is no dispute that the payment and other defaults addressed by the Order were
23 satisfied by the October 1, 2007 deadline. Thereafter, the Debtor and GHB apparently operated
24 under the terms of the month-to-mouth lease until an irreparable breakdown occurred in the
25

26 ² The Order also required the Debtor to discontinue use of the parking lot to conduct
27 retail sales.

1 parties' relationship in approximately May 2008. When the Debtor failed to pay the May rent, it
2 was served with a Five-Day Notice to Pay Rent or Quit the Premises ("Five-Day Notice").
3 Debtor filed opposition asserting that it had attempted to pay the May rent but that GHB refused
4 its proposed manner of payment. Debtor also argued that GHB's initiation of unlawful detainer
5 proceedings was precluded by the automatic stay. A summary eviction proceeding was held
6 before the Justice Court of Las Vegas Township on May 20, 2008. After additional briefing was
7 submitted by the parties, the Justice Court issued an order on June 9, 2008, staying any further
8 proceedings in the unlawful detainer proceeding until the Bankruptcy Court permits GHB to
9 proceed.

10 On June 13, 2008, GHB filed the instant motion ("Emergency Motion") seeking a
11 declaration that the automatic stay does not apply to its unlawful detainer efforts. (Dkt# 232)³ It
12 contends that the Debtor terminated the month-to-month tenancy in early May and refused to pay
13 the required rent. Based on the asserted termination, GHB argues that Section 362(b)(10)
14 exempts from the automatic stay its efforts to evict the Debtor from the Rainbow Boulevard
15 premises. On July 9, 2008, Debtor filed written opposition (Dkt# 243) accompanied by a
16 declaration of its principal, Israel Salei (Dkt# 244). A reply brief was filed by GHB (Dkt# 246).
17 On July 16, 2008, the parties presented oral argument and the matter was submitted for decision.

18 DISCUSSION

19 After the Five-Day Notice was issued, Debtor made two payments to GHB in the full
20 amount of a monthly payment under the month-to-month arrangement. GHB does not dispute
21 receipt of the payments, but indicates that they were applied to the amounts owing for June and
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23 ³ Although the Emergency Motion was filed on June 13, 2008, along with an application
24 for order shortening time (Dkt# 233), the request for order shortening time was not accompanied
25 by an attorney information sheet under Local Rule 9006(a) indicating counsel's effort to obtain
26 consent from opposing counsel to having the matter heard on an expedited basis. The
27 information sheet was filed on June 27, 2008, but indicated that opposing counsel had not been
28 contacted until June 26, 2008. (Dkt# 237) An order shortening time was not entered until June
30, 2008, scheduling the Emergency Motion to be heard on July 16, 2008. (Dkt# 238)

1 July, leaving the May rent unpaid. Debtor contends that the two payments should have been
2 applied to May and June and as a result, Debtor is simply late at worst on its July payment.

3 In connection with the alleged termination of the month-to-month tenancy, GHB has
4 offered as proof a letter dated 05-05-2008 from Israel Salei, the Debtor's president, addressed to
5 Lawrence Goldberg, who apparently is a principal of GHB. See Exhibit "B" attached to
6 Emergency Motion.⁴ Based on that missive and Debtor's subsequent conduct, GHB argues that
7 the Debtor terminated the month-to-month tenancy and is improperly refusing to pay the May
8 rent.⁵

9 At the hearing, Debtor objected to the admission of the 05-05-2008 letter, arguing that it
10 is a privileged settlement communication. Under the Federal Rules of Evidence, evidence of
11 conduct or statements made in compromise negotiations regarding a claim is not admissible
12 "when offered to prove liability for, invalidity of, or amount of a claim that was disputed as to
13 validity or amount..." Fed.R.Evid. 408(a)(2). In the instant case, the 05-05-2008 letter is
14 offered by GHB as evidence that the month-to-month tenancy was terminated by the Debtor. It
15 is not being offered as to the validity of GHB's claim for May rent or of the amount owed since
16 neither element is disputed. Thus, Debtor's objection to admission of the letter is without merit.
17 No argument has been made that Exhibit "B" is not a true and accurate copy of the letter or that
18 it otherwise lacks foundation.

19 Admission of the 05-05-2008 letter, however, is not determinative of either parties'
20 position. GHB's argument that the Debtor terminated its tenancy based on the letter, as well as
21 the Debtor's conduct, is belied by at least two undisputed facts: (1) Debtor has not vacated the
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23 ⁴ The same Exhibit "B" is attached to the Affidavit of Kammy Bridge that was filed in
24 connection with GHB's application for order shortening time. (Dkt# 233) Apparently, GHB had
25 intended to attach the same affidavit to its Emergency Motion as Exhibit "1" thereto.

26 ⁵ At the hearing, GHB's counsel could not and did not suggest that the Justice Court had
27 ever ruled that the month-to-month lease had been terminated on the basis of the 05-05-2008
28 letter.

1 premises and (2) Debtor has made, and GHB has accepted, two subsequent monthly rent
2 payments. As previously noted, the parties differ as to whether the two payments have been or
3 should have been applied to the May and June rent, or to the June and July rent.

4 Insofar as GHB is seeking a declaration that the automatic stay does not apply to its
5 unlawful detainer efforts, such a declaration cannot be granted by way of the present motion.
6 Bankruptcy Rule 7001(7) provides that a proceeding to obtain an injunction or other equitable
7 relief requires the commencement of an adversary proceeding and Bankruptcy Rule 7001(9)
8 provides that a proceeding to obtain a declaratory judgment for such relief also requires an
9 adversary proceeding. In connection with a prior motion for a similar declaration brought by
10 creditor DLC Holdings, LLC (Dkt# 82), the Court previously ruled that an adversary proceeding
11 would be required for declaratory relief to be provided. The Court reaches the same conclusion
12 with respect to the instant motion by GHB.

13 In the alternative, GHB has requested relief from the automatic stay to pursue its
14 unlawful detainer action pursuant to Sections 362(d)(1) and 362(d)(2).⁶ Upon a showing of
15 “cause”, the automatic stay may be terminated, annulled, modified or conditioned as ordered by
16 the bankruptcy court. See 11 U.S.C. § 362(d)(1). Relief also may be granted if the debtor has no
17 equity in the subject property and the property is not necessary to an effective reorganization of
18 the debtor. See 11 U.S.C. § 362(d)(2). A property is “necessary to an effective reorganization”
19 if a debtor demonstrates that there is a “reasonable possibility of a successful reorganization
20 within a reasonable amount of time.” See United Savings Association of Texas v. Timbers of
21 Inwood Forest Associates, Ltd. (In re Timbers of Inwood Forest), 484 U.S. 365, 376, 108 S.Ct.
22 626, 633 (1988); In re Jordan, 2008 WL 2705187 at *16 (Bkrcty.D.Idaho July 1, 2008); In re A

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24
25 ⁶ At the hearing, Debtor argued that GHB had not complied with meet and confer
26 requirement under Local Rule 4001(a)(3) prior to filing a motion requesting relief from stay.
27 Debtor also argued that no information sheet had been provided as required by Local Rule
28 4001(a)(2)(B). Neither objection was raised in Debtor’s written opposition, however, and the
Emergency Motion clearly requests relief from stay in the alternative.

1 Partners, LLC, 344 B.R. 114, 126 (Bkrtcy. E.D.Cal. 2006). The party requesting relief from the
2 automatic stay has the burden of proof on any issues regarding the debtor's equity in any
3 property that is the subject of the request, while the debtor or opponent has the burden of proof
4 on all other issues. See 11 U.S.C. § 362(g)(2).

5 In connection with GHB's prior motion, the Court concluded that cause under Section
6 362(d)(1) had been established by virtue of the Debtor's then breach of the terms of the month-
7 to-month tenancy and the absence of monthly operating reports showing the Debtor's ability to
8 become current on the rental payments. The Court further found that relief from stay under
9 Section 362(d)(2) was appropriate because the Debtor has no equity in the leased premises and
10 had not demonstrated a reasonable possibility of confirming a Chapter 11 plan within a
11 reasonable amount of time.

12 Since the time the Court entered the prior Order, the Debtor has cured the payment
13 breaches that were the subject of that Order, but admittedly has failed to make at least one rental
14 payment regardless of how its two payments after May 2008 are applied. While the Debtor now
15 has filed its monthly operating reports, the Debtor recently has sought relief from an order
16 allowing attorney's fees to GHB, on grounds that it does not have sufficient funds on hand to pay
17 the fees awarded and to continue operations.⁷ As evidence in support of that argument, Debtor
18 offered a declaration from its principal (Dkt# 239) attesting that the Debtor had enough cash on
19 hand to pay the July rent on the Rainbow Boulevard premises and postpetition taxes owed to the
20 Internal Revenue Service, but insufficient funds to satisfy GHB's allowed attorney's fees. Under
21 these circumstances, the record indicates that the Debtor is in no appreciably better position now
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23 ⁷ Debtor's Motion to Alter or Amend Order Granting Motion for Attorney's Fees (Dkt#
24 221) was heard on July 2, 2008. The order granting attorney's fees to GHB (Dkt# 215) had been
25 entered on May 14, 2008 and required the Debtor to pay \$10,089.16 within 10 days of entry of
26 that order. In its motion for relief from that order, Debtor asserted that it did not have sufficient
27 funds to pay the amount ordered and still have sufficient funds to operate for the remainder of
the month. An oral ruling was issued on July 16, 2008, that granted the Debtor an additional 30
days to pay the full amount of the fee award.

1 than it was when the prior Order was entered. Thus, cause for relief from stay under Section
2 362(d)(1) exists.

3 Since the time the Court entered the prior Order, the Debtor has filed a proposed plan of
4 reorganization (Dkt# 121) and a proposed disclosure statement (Dkt# 120), but has not moved
5 forward with the confirmation process. It did obtain approval of the disclosure statement on
6 October 29, 2007, but has never submitted an order approving the disclosure statement or
7 scheduling a hearing on plan confirmation. At a status hearing held at the Debtor's request on
8 July 2, 2008, the Debtor represented that the original disclosure statement underestimated the
9 priority administrative claims of creditors Goldway Enterprises, GHB Holdings, DG Associates,
10 and DLC Holdings.⁸ A deadline of August 15, 2008, has been established for the Debtor to file
11 an amended plan of reorganization and an amended disclosure statement that takes into account
12 the significantly greater amount of priority administrative expenses that have been incurred by
13 the Debtor.

14 Notwithstanding the deadline for the amended plan and disclosure statement to be filed, it
15 is clear that the Debtor has had the protection of the automatic stay for nearly 15 months and has
16 not materially advanced its reorganization efforts for the past 9 months. Debtor's asserted lack
17 of current resources to satisfy the attorney's fees awarded to GHB militates against a present
18 finding of a reasonable possibility of being able to confirm a plan. Confirmation requires that all
19 allowed administrative claims to be satisfied on the effective date of the proposed plan. See 11
20 U.S.C. § 1129(a)(9).⁹ If the Debtor cannot pay the attorney's fees that were awarded back in
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22 ⁸ The Goldway Enterprises, Inc. claim was estimated to be \$15,000 rather than the
23 \$29,936.60 that was allowed, the GHB Holdings claim for attorneys fees claim was estimated at
24 \$1,500 instead of the \$10,089.16 that was allowed, the DG Associates, LLC claim for a super-
25 priority administrative expenses was estimated at \$5,000 and the parties reached agreement at
26 the amount of \$5,384.48, and the DLC Holdings' administrative rent claim was estimated at
27 \$10,800 when it currently is seeking in excess of \$30,000.

28 ⁹ Section 1129(a)(9) requires that holders of claims allowed under Sections 507(a)(2) be
paid in cash on the effective date of a Chapter 11 plan, unless the holder of the claim agrees

1 December 2007, there is little basis in the record to infer that it will have the cash available to
2 pay all allowed administrative claims on the effective date of a confirmed plan. While the
3 Debtor might be able to present evidence at plan confirmation of its ability to satisfy all of the
4 requirements under Section 1129, the current record is insufficient to establish a reasonable
5 possibility of a successful reorganization. Thus, as it concluded in connection with GHB's prior
6 motion for relief from stay, the Court again concludes that the Debtor has failed to meet its
7 burden of showing that the Rainbow Boulevard premises are necessary to an effective
8 reorganization within the meaning of Section 362(d)(2).

9 Under the circumstances, a modification of the automatic stay is warranted. The Debtor
10 will have until the close of business on July 31, 2008, to cure any arrearages on its month-to-
11 month tenancy with GHB for the retail premises located on Rainbow Boulevard. These amounts
12 are separate and apart from the attorney's fees previously allowed and awarded to GHB in this
13 proceeding. In the event Debtor fails to cure the arrearages and is not current on all outstanding
14 rental obligations by July 31, 2008, GHB may request an ex parte order granting immediate
15 relief from stay to proceed with its remedies under state law, including the commencement of
16 unlawful detainer proceedings, if appropriate, and the disposition of any personal property
17 remaining on the premises, including inventory, in accordance with applicable nonbankruptcy
18 law. The ex parte order may be obtained by submission of an affidavit attesting to the Debtor's
19 failure to cure the arrearages along with a proposed order.

20 In the event that the Debtor cures the existing arrearages as of July 31, 2008, but defaults
21 on its obligations under the month-to-month arrangement thereafter, GHB may obtain an order

22 _____
23 otherwise. Claims encompassed by Sections 507(a)(2) include administrative expenses allowed
24 under Section 503(b). Administrative expenses allowed under Section 503(b) include actual,
25 necessary costs and expenses of preserving the bankruptcy estate. It is well-established that the
26 administrative expenses allowed under Section 503(b) include a debtor-in-possession's rental
27 and related obligations for premises occupied during the Chapter 11 case. See generally, Alan N.
Resnick & Henry J. Sommer, 4 Collier on Bankruptcy, ¶ 503.06[6] (15th edition revised 2008).
See, e.g., Burlington Northern Railroad Co. v. Dant & Russell, Inc. (In re Dant & Russell), 853
F.2d 700, 707 (9th Cir. 1988).

1 granting relief from stay as provided above upon submission of an affidavit or declaration and a
2 proposed order.

3 In the event that the Debtor cures the existing arrearages as of July 31, 2008, but either
4 party elects to terminate the month-to-month tenancy in accordance with applicable state law,
5 then either party may obtain an order granting relief from stay to do so upon submission of an
6 affidavit or declaration and a proposed order.

7 **CONCLUSION**

8 For the reasons stated above, GHB's Emergency Motion for Declaration that Automatic
9 Stay Does Not Apply will be denied, but its alternative request for relief from automatic stay will
10 be granted. A separate order has been entered concurrently herewith.

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