No.: 21-56264, Appealed from No. 2:20-cv-10656--FLA

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In re

HAWKEYE ENTERTAINMENT, LLC,

Debtor.

SMART CAPITAL INVESTMENTS I, LLC, SMART CAPITAL INVESTMENTS II, LLC, SMART CAPITAL INVESTMENTS III, LLC, SMART CAPITAL INVESTMENTS IV, LLC, AND SMART CAPITAL INVESTMENTS V, LLC,

APPELLANTS,

vs.

HAWKEYE ENTERTAINMENT, LLC, AND W.E.R.M. INVESTMENTS, LLC,

APPELLEE.

Appeal From The United States District Court for the Central District of California, Western Division, Case No. 2:20-cv-10656-FLA

APPELLEE'S ANSWERING BRIEF

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Bankruptcy Procedure 8012(b) and Federal Rule of Appellate Procedure 26.1, Appellee Hawkeye Entertainment, LLC, certifies that it is a privately held California limited liability company and has no parent corporation, subsidiaries, or affiliates that have issued shares to the public.

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I. INTRODUCTION

Appellant devotes approximately one-third of its brief trying to transform findings of fact into a legal issue about "materiality". Its effort is to obfuscate its failure at trial to meet a predetermined burden of proof regarding alleged "defaults". It is also an effort to obscure the Bankruptcy Court's finding that its witnesses lacked credibility. The materiality issue is nothing more than a discrete secondary justification of the Bankruptcy Court connected to one specific finding of no rental default in one post-petition month. It was in minor facet of thorough findings of fact and conclusions of law resulting from a five-day trial. It is the quintessential red herring.

Assuming *arguendo* that materiality was incorrectly relied upon by the Bankruptcy Court in finding no rental default occurred, such error is harmless due to the rent payment actually being paid prior to assumption, together with the Bankruptcy Court finding of no default, material or otherwise.

Furthermore, as will be elucidated more fully below, Appellant's legal analysis is flawed. In arguing materiality may not be considered in a 11 U.S.C. §365(b) motion to assume, Appellant overlooks well-established legal authority that a Bankruptcy Court is to look to the contract terms and state law to determine whether default exists.

II. SUMMARY OF ARGUMENT

A preliminary overview of three areas will simplify discussion and focus on "what" is of primary significance in this appeal. Without such focus, there are two dangers. First, clarity of occurrences below becomes obscured in unnecessarily tangled, highly technical, and largely irrelevant argument. Second, the briefs simply talk past one another, without addressing clearly and specifically the issues before this Court.

A. What Was Factually Proven.

The first area of focus is on what was factually proven, or more correctly not proven, in the Bankruptcy Court trial on Appellee's motion to assume the lease. At the close of that contested trial, no default was proved by Appellant. This factual determination was then sustained by the District Court, applying what all agree is the correct "clearly erroneous" standard. The language of 11 U.S.C. §365(b)(1), as well as the legislative history of the subsection requires before anything else, at the time of assumption there must exist a proven default, properly noticed pursuant to the lease, and not cured.

Appellant was properly tasked with an initial burden to make *prima facie* showing through credible evidence of this foundational prerequisite. *In re Harris Management Co., Inc.,* 791 F.2d 1412, 1414 (9th Cir. 1986); *In re Rachels Industries, Inc.,* 109 B.R. 797, 802-803 (Bankr. W.D. TN 1990). Prior to the

contested trial, Appellant requested and was granted the full panoply of discovery. At trial, Appellant presented evidence and witnesses it alone deemed relevant. At the conclusion of trial and prior to making its decision, the Bankruptcy Court considered the totality of the evidentiary presentation, including that described as "likely immaterial or contrived" (ER – 28) together with witness testimony whose credibility on key matters was questioned by the Court. (ER – 29). The Court concluded upon the evidence admitted and giving it the weight to which it was entitled, that at the time of assumption no default (irrespective of any qualifier) existed. (ER – 29 –30). It was not "what had happened" that controlled. It was the then state of facts.

The consequence of failing to establish the foundational factual prerequisite was, and is, clear from a natural reading of 11 U.S.C. §365(b)(1), which for over 20-years has been without substantial dispute. Absent an established default under the unexpired lease, Appellee had no obligation to address or prove any elements of 11 U.S.C. §365(b)(1). *In re Rachels Industries, Inc., supra*, 109 B.R. at 802-803; *In re Natco Industries, Inc*. 54 B.R. 436, 440-441 (Bankr. S.D. NY 1985). Since the Bankruptcy Court found Appellant failed to meet its *prima facie* factual burden, the arguments and voluminous case law presented in the Opening Brief, while interesting in the abstract, are inapposite.

B. Application of *In re Cochise College Park*.

The second focus centers on the Bankruptcy Court's straight-forward application of Ninth Circuit law existing for almost 39-years, and which for at least 33-years has been approvingly relied upon by this and other circuits, once again without substantial dispute.[1] To the extent the term "materiality" was discussed by the courts below, it was not done in the context of adding additional or different requirements to the Bankruptcy Code on issues unique to federal law. It was done in the context of the substantive issues of the consequences of a failure to perform, whether a default exists, and whether it rose to the required level of "materiality" by looking at applicable state law. *In re Cochise College Park*, 703 F.2d 1339, 1348 (9th Cir. 1982)

The logical terminus of Appellant's approach seems that if, at the time of assumption, there was a discarded peanut butter and jelly sandwich lying in a parking lot, and the lease required parking lot maintenance, assumption would be

[1] Among others, Ninth Circuit Court of Appeals decisions *In re Rega Properties, Ltd.,* 894 F.2d 1136, 1139 (9th Cir. 1990), *In re Wegner*, 839 F.2d 533 (9th Cir. 1988), and *Lindsay v. Beneficial Reinsurance Co. (In re Lindsay),* 59 F.3d 942, 948 (9th Cir. 1995); Ninth Circuit Bankruptcy Court decisions *In re Filipino Cmty. Ctr., Inc.,* 2019 Bankr. LEXIS 3028 (Bankr. HI 2019), *Pearce v. Woodfield (In re Woodfield),* 602 B.R. 747, 760 (Bankr. OR. 2019), *Carruth v. Eutsler (In re Eutsler),* 585 B.R. 231, 236 (BAP 9th Cir. 2017), *Ulrich v. Schian Walker, P.L.C. (In re Boates),* 551 B.R. 428, 434 (BAP 9th Cir. 2016), *In re Hertz*, 539 B.R. 434, 439 (Bankr. C.D. CA 2015), *In re Henke*, 84 B.R. 693, 698 (Bankr. MT 1988); Third Circuit Court of Appeals decision *Enterprise Energy Corp. v. United States (In re Columbia Gas Sys.),* 50 F.3d 233, 239 (3rd Cir. 1995); Fourth Circuit Court of Appeals decision *Gloria Mfg. Corp. v. International Ladies' Garment Workers' Union*, 734 F.2d 1020, 1021 (4th Cir. 1984).

prohibited unless the tenant went through a mechanical application of each of the 11 U.S.C. §365(b)(1) elements. Appellant would require the Bankruptcy Court to disregard what state law had to say about the peanut butter and jelly sandwich, or whether its presence had any legal significance. Absolute mechanical application would be required for "anything." While the absurdity of a discarded peanut butter and jelly sandwich triggering §365(b)(1) elements should be obvious, the only way one avoids that absurdity is to consider "materiality", the exact opposite of what Appellant seeks. Appellant advocates the discard of state law considerations in favor of a never-ending "anything and anything" Alice in Wonderland Rabbit-Hole, with or without reasonable notice to the tenant. This terminus was the precise "moving target" about which the Bankruptcy Court had legitimate concern, and about which it requested but did not receive an adequate proffer to avoid (SER – 23), to avoid a situation where the landlord is doing nothing more than "piling on." (ER – 28 –29).

It is for this precise reason *In re Cochise College Park, supra,* has well-placed practical and legal import, as well as general acceptance. The courts below, using the peanut butter and jelly sandwich example, did not conclude one was in the parking lot at the time of assumption. What they did was to use logic and common sense, then consider and give weight utilizing applicable state law to separate, once again using the words of the Bankruptcy Court, meaningful matters

from those "likely immaterial or contrived." (ER – 28). Appellant's own case citation, *In re Senior Care Ctrs., LLC*, 607 B.R. 580, 588-589 (Bankr. N.D. TX 2019), contrary to supporting Appellant's position, is consistent with this bedrock principle, facilitating a debtor's effort to reorganize its affairs. The Courts below neither created nor adopted a new legal standard, nor did they inject equitable considerations into the analysis. What each did was simply take this Court's practical and longstanding guidance, apply it to the evidence before them, and use common sense.

C. Speculative Prejudice.

The third focus centers on the spurious and speculative "stripped rights" argument. Simply stated, despite having the ability to do so, Appellant neither made, nor now makes, any reasonable presentation of actual prejudice. At best it argues harmless error.

It is a serious accusation to claim any court has caused a litigant prejudice. Appellant fails to present even a small modicum of what rights were stripped, and even more significantly, any meaningful prejudice suffered thereby. Nothing more than hyperbole is presented. The claimed deprivation and prejudice cannot involve a single late rent payment since evidence established that at the time of the assumption all rent payments (and any late fees) had already been made. The claim cannot relate to an insurance certificate, since the Bankruptcy Court factually

found no violation of insurance requirements had occurred. (ER – 79 – 83). The claim cannot relate to an estoppel certificate, especially since the Bankruptcy Court also found that Appellant never even requested a signed estoppel certificate. (ER – 86). What was presented for signature contained materially false and misleading statements, and, making matters worse, Appellant made up facts that were directly contradicted by the evidence and the Bankruptcy Court's findings in efforts to find a breach of Sections 18.1 or 18.3 of the Lease. (ER – 83). When Appellee corrected and submitted edits, Appellant *non voleva palare*. (ER – 83). It is unpersuasive for Appellant to advance that it is prejudiced because it lost an "ability" to force another to commit lender fraud. (ER – 83). Further, Appellant admits that its lender required Appellee to execute an estoppel certificate that exceeded the requirements of the Lease. (SER – 14 – 19).

Respectfully, some amount of common sense should be applied before undertaking a deep dive into abstract legal theories raised by Appellant. The lower courts committed no clear error in finding Appellant factually failed to prove default. The lower courts correctly applied consistent and long-standing Ninth Circuit guidance. There is not a scintilla of proffered facts that even remotely demonstrates rights were taken or prejudice inflicted. No error is present and the Bankruptcy Court's ruling, and the District Court's affirmance of such ruling, should be upheld.

III. STATEMENT OF FACTS

A. Background

Appellee ("Debtor") commenced this bankruptcy case by filing a Voluntary Petition under Chapter 11 of the Bankruptcy Code on August 21, 2019. The filing protected its most valuable asset, a Lease Agreement dated July 17, 2009, as modified by the First Amendment to Lease Agreement dated August 19, 2014, and any and all options and extensions thereunder and related thereto (collectively the "Lease"). (ER – 165-207). The Lease was between (i) Lessor, Smart Capital Investments I, LLC, a California limited liability company, Smart Capital Investments II, LLC, a California limited liability company, Smart Capital Investments III, LLC, a California limited liability company, Smart Capital Investments IV, LLC, a California limited liability company, and Smart Capital Investments V, LLC, a California limited liability company, as successor-in-interest to New Vision Horizon, LLC (successor-in-interest to Pax America Development, LLC) (collectively "Landlord") and (ii) Debtor. The Lease involved portions of the real property commonly known as the Pacific Stock Exchange Building, and located at 618 South Spring Street, Los Angeles, California (the "Premises").

Debtor was entitled to use the first four floors and a portion of the basement of the Premises. It subleased the Premises to a related company, W.E.R.M.

Investments, LLC ("WERM"). WERM operated a popular and highly successful entertainment venue from the Premises.

B. The Alleged Default

On August 5, 2019, without warning or prior notice the Landlord delivered a letter alleging various nonmonetary defaults. The letter lacked specificity as to the exact nature of such defaults but nonetheless demanded cure within a 15-days (the "Default Letter"). (SER – 38 – 40)

Having been unable to obtain specificity from the Landlord despite repeated attempts, on August 19, 2019, the Debtor served its written response to the Landlord's contentions. (SER – 45 – 48). As part of the response, and despite the Debtor's categorical disagreement with the Landlord's claims and contentions contained in the Default Letter, the Debtor notified the Landlord that it had complied with the Landlord's demands. *Id*. Despite its disagreement with each and every allegation contained in the Default Letter, the Debtor tried to reason with the Landlord and promptly notified the Landlord of this in writing. *Id*. Nevertheless, the Landlord refused to acknowledge the Debtor's efforts to resolve the situation and simply issued a Three-Day Notice. (SER – 41 – 44).

Prior to the April 2020 rent payment being due, Debtor filed a motion with the bankruptcy court, requesting that due to the COVID pandemic shutdowns of WERM's business operations that began in March 2020, and while it explored

whether the City of Los Angeles moratorium of rent payment applied to the Premises, that it be granted permission to defer rent. The Bankruptcy Court denied the motion. (ER – 29 – 30). Rent was thereafter paid. Prior to the contested trial on the assumption motion, all fees related to the April rent were also paid. (ER – 30).

C. No Defaults Established

The Bankruptcy Court found that at the time of assumption, no default existed. The Bankruptcy Court pointed out that despite the Landlord knowing about alleged issues for many years prior to 2019, on June 6, 2019, Landlord self-certified that the Debtor was not in default and no Lease defaults existed. (SER – 36 – 37). In discovery and under penalty of perjury the Landlord affirmed the June 6, 2019, statement on August 27, 2020, and at trial on October 15, 2020. (SER – 6 – 13); (SER – 31 – 34); (SER – 36 – 37). Based in part on this self-certification which Landlord attempted to impeach at trial, the Court found the Landlord lacked credibility. (ER – 66).

IV. STANDARD OF REVIEW

This Court has discretion to review both the Bankruptcy Court's decision and the District Court's confirmation. *Sherman v. SEC (In re Sherman)*, 441 F.3d 794, 812-13 (9th Cir. 2006); *Ardmor Vending Co. v. Kim (In re Kim),* 130 F.3d 863, 864 (9th Cir. 1997).

Only conclusions of law are reviewed *de novo*. *In re Arizona Appetito's*

Stores, Inc., 893 F.2d 216, 218 (9th Cir. 1989) (citing *Sea Harvest Corp. v. Rivera Land Co*., 868 F.2d 1077, 1078 (9th. Cir 1989). While the Supreme Court has stated that when a *de novo* review is compelled, no form of appellate deference is acceptable, it has also acknowledged an efficient and sensitive appellate court will consider the trial court's analysis as well as any expertise possessed by the trial court. *Salve Regina College v. Russell*, 499 U.S. 225, 230-232 (1991).

The general standard of review governing factual findings is set forth in *Federal. Rules of Civil Procedure 52 (a*). That Rule provides, in pertinent part, that findings of fact, whether based on oral or other evidence, "must not be set aside unless clearly erroneous". A reviewing court must give due regard to the trial court's opportunity to judge the witnesses' credibility. *Federal. Rules of Civil Procedure 52 (a)(6).*

It is not incumbent on an appellee to persuade the reviewing court that a lower court's findings of fact are correct. Appellants bear the sole burden to establish findings of fact it specifies are clearly erroneous. *Pacific Queen Fisheries v. Symes*, 307 F.2d 700, 707 (9th Cir. 1962). The evidence is viewed in the light most favorable to the party who prevailed in the lower court, giving that party the benefit of all inferences reasonably drawn from the evidence. *Id*. at 707; *accord*, *United States v. Alaska S.S. Co.,* 491 F.2d 1147, 1151 (9th Cir. 1974) and *Komie v. Buehler Corp.,* 449 F.2d 644, 647 (9th Cir. 1971).

The presumption of correctness applies both in assessing conflicting testimony, as well as documentary evidence and factual inferences drawn from undisputed facts. *Constructora Maza, Inc. v. Banco de Ponce*, 616 F.2d 573 (1st Cir. 1980). Such findings will not be disturbed on appeal unless the reviewing court, considering all the evidence, can conclude the trial court erred as a matter of law. *Seven Up Co. v. Cheer Up Sales Co*., 148 F.2d 909 (8th Cir. 1945). Where a trier of fact infers that a witness has made false material statements, unless clearly erroneous, that finding of lack of credibility must stand. *United States Anchor Mortgage. Corp.*, 711 F.3d 745 (7th Cir. 2013).

The United States Supreme Court has held the clearly erroneous standard does not allow a reviewing court to reverse the trial court's finding of fact simply because it would have decided the case differently. Rather, if the trial court's account of the evidence is plausible considering the record viewed in its entirety, the finding of fact stands even if the reviewing court would have weighed the evidence differently. When there are two permissible views of the evidence, a trial court's choice between them cannot be "clearly erroneous." *Anderson v. Bessemer City,* 470 U.S. 564, 573-574 (1985), *accord*, *Cooper v. Harris*, 137 S. Ct. 1455, 1468 (2017), *U.S. Bank N.A. v. Vill at Lakeridge (In re Lakeridge, LLC),* 814 F.3d 993, 1002 (9th Cir. 2016), *Yim v. Chaffee (In re Chaffee)*, 2017 Bankr. LEXIS 723 (9th Cir. BAP 2017), and *Chou v. Brody (In re Brody)* 2017 Bankr. LEXIS 696 (9th

Cir. BAP 2017).

There is no rigid rule about what standard of review to apply to mixed questions. *Ornelas v. United States*, 517 U.S. 690, 701 (1966) (Scalia, J dissenting). Deferential review of mixed questions of law and fact is warranted when it appears that the trial court is in a "better position" to decide the issue in question. *Salve Regina College, supra*, 499 U.S. at 233. For any of the issues Appellant claims are "mixed," this Court should consider the Bankruptcy Court's unique expertise, as well as the Bankruptcy Judge's extensive involvement in Appellee's specific bankruptcy matter (including previous motions and evidence submitted by both Appellee and Appellant therein) when evaluating whether the Bankruptcy Court was in a better position to evaluate, and whether some appropriate amount of deference is warranted. See, *Salve Regina College v. Russell*, *supra*, 499 U.S. 225, 230-232.

V. ARGUMENT

A. No Default Existed At The Time Of Assumption

A debtor's ability to assume is one of the most basic reorganization tools available under the Bankruptcy Code. The provisions of 11 U.S.C. §365(b) become applicable only if "there has been a *default* in . . . an unexpired lease of the debtor . . ." 11 U.S.C. § 365(b)(1) (emphasis added). The relevant time snapshot is the time of assumption, since §365(b)(1)(A) specifically requires cure, or adequate

assurance of future cure, to occur at that statutorily referenced time. Appellant has the initial burden of proving the alleged default and that defaults have been properly noticed. *In re Rachels Indus., Inc.*, 109 B.R. 797, 802 (Bankr. W.D. TN 1990). Uncured non-monetary defaults prevent assumption only if the defaults are material, or they cause substantial economic detriment. *In re Vent Alarm Corp*., 2016 Bankr. Lexis 1725, *4 (Bankr. PR 2016). If defaults are established by proof, the burden shifts to the debtor to cure or provide adequate assurance of prompt cure and provide adequate assurance of future performance. *In re Rachels Indus., Inc.*, *supra*.

Appellant describes these "defaults" as failure to pay rent, failure to sign an estoppel certificate, failure to carry insurance, allowing the premises to be used for an improper purpose, and serving alcohol on the first floor of the premises. As to each the Court considered the evidence submitted by Appellant, and it was found lacking. (ER – 32 – 52).

Appellant spends some time addressing the single post-petition rent payment, so a brief discussion seems in order. At the same time, Appellant cannot dispute the simple fact that prior to trial and at the time of assumption, no rent under the Lease was either due or owing. (ER – 30). The Court found that at trial Appellee had paid the April 2020 rent as well as paying an associated late fee. (ER – 29 – 32). So, at that time of assumption there was nothing to cure. Appellant

failed to prove it provided the requisite notice of late payment required by the Lease. As noted by the Court, the purported late payment occurred at the height of the Covid pandemic and during the period a motion was pending before the Bankruptcy Court to permit Appellee to avail itself of the emergency City rent relief. Hence, at least as to rent at the time of the assumption there was no "default". To the extent "materiality" was discussed or considered by the Court (assuming arguendo materiality might be inapplicable under §365(b)), since the Landlord was already whole any alleged error would therefore be harmless.

Contrary to what Appellant has represented, the Bankruptcy Court found: "[r]eally a default *does not* exist at this time, because the lease provides for the payment of the rent late, as long as the late fees are paid." (emphasis added) (ER – 30). The Court went on to explain the basis for its finding, stating that "…at the time when the rent was due, there was a motion…to excuse the April rent at the time, and the COVID shutdown and the lockdowns had just started at the end of March, and there was a legitimate question that needed to be analyzed at the time, whether the [Los Angeles] city's moratorium on payment of rent due to COVID income loss applied in this situation or not." (ER – 30). The Court then stated it "did rule that it didn't apply, that the force majeure clause of the lease overcame the city's special order, but I don't think it's an exaggeration to say everyone was fairly confused and not operating at top speed in early April of this year, and we

started sorting things out and figuring normal business practices a few weeks after that, really, at the earliest." (ER – 30).

B. Statutory Construction

If default at the time of assumption is absent, statutory construction plays no role. Attempting to circumvent the factual void, Appellant however argues the Bankruptcy Court committed error when, for purposes of legitimacy, it implicitly reviewed objections to assumption based upon actual weight. Appellant appears to argue that "any means any", and therefore logic, common sense, or state law is apocrypha. The argument fails to appreciate that some concept of materiality is inextricably woven into the very fabric of §365(b) when assumption is used as a legitimate tool to assist a debtor in its reorganization.

Appellant cites numerous cases, but its argument primarily relies upon language appearing in *Stevens v. Whitmore (In re Stevens)*, 15 F.4th 1214 (9th Cir. 2021), and *In re Senior Care Ctrs., LLC*, 607 B.R. 580, 588-589 (Bankr. N.D. TX 2019). Respectfully, neither case supports the argument as presented. In addition, authority cited in the *Senior Care Ctrs.* is strikingly aligned to that of the Bankruptcy Court below.

When dealing with a term not specifically defined by the Bankruptcy Code, a fundamental difference exists between the process unique to a bankruptcy case processing through the bankruptcy system, from the impact on substantive legal

rights and duties. Far from error, the Bankruptcy Court below simply followed long-standing, commonly understood, and consistently applied Ninth Circuit law.

1. *Stevens v. Whitmore* (In re Stevens) is Inapposite.

The *Stevens* decision dealt with a specific unique bankruptcy procedural issue. Reading more into the decision or attempting to apply its reasoning outside of that issue is inappropriate.

The narrow question resolved by *Stevens* was whether, under 11 U.S.C. §554(c), asset abandonment occurred if a debtor failed to make a literal entry on a specific form, a form that could be amended at any time prior to case closure pursuant to Bankruptcy Rule 1009(a). If the literal entry was required on the specific form, and entry had not occurred by case closure, did "abandonment" (as specifically defined by the Code) occur? Or did the trustee have power found in the Bankruptcy Code to, in a reopened proceeding, take possession of the asset, or its proceeds. 15 F.4th at 1215-1216. This very narrow issue involved pure administrative bankruptcy rule and process. To resolve this administrative issue, the *Stevens* court looked at 11 U.S.C. §554(c) and the specific language in adjoining 11 U.S.C. §512(a). Applying the grammatical use rule, it not unexpectedly concluded "scheduled" meant black words literally appearing on the correct white paper "schedule"[2] (quoting with

[2] The *Stevens* opinion pointed out that the Federal Rules of Bankruptcy procedure "routinely distinguish between the bankruptcy petition itself, bankruptcy schedules, the SOFA, and other documents", citing as an example Rule 1007. 15

approval *Jeffrey v. Desmond*, 70 F.3d 183, 186 (1st Cir. 1995) [property to be properly abandoned must be formally scheduled], and *Vreugdenhill v. Navistar Int'l Transp. Corp*., 950 F., 2d. 524, 526 (8th Cir. 1991) [a trustee's knowledge of property is insufficient- for the claim to be abandoned pursuant to §554(a), it must be scheduled]). 15 F.4th at 1218; see also, *FCC v. AT&T Inc.,* 562 U.S. 397, 402 (2011). *Stevens* did not address substantive legal rights. It simply resolved a unique procedural bankruptcy issue. It cannot be read independent of the context in which the issue was considered.

2. When Addressing Default and §365, Bankruptcy Courts Are Permitted to Look to State and Common Law.

Setting aside the absence of proven factual default, before this Court are not issues of "unique bankruptcy procedures" but the "substantive application of law to determine legal rights". When the Bankruptcy Code specifically does not prohibit looking at applicable state and common law that impacts the substantive rights of the parties, may it be used by the Bankruptcy Court to decide those issues? Far from being in error, the approach used followed commonly understood and consistently applied Ninth Circuit law existing in an unrefined state for over 39-years. Appellant does not argue that the courts below incorrectly applied state law. What it argues is that they were prohibited from doing so.

F.4th at 1218.

In the Ninth Circuit, and within the context of 11 U.S.C. §365(b)(1), (i) the legal consequences of failure to comply with contract terms are determined under state law, (ii) the legal consequences of one party's failure to perform obligations under a contract is an issue of state contract law, (iii) while principles of contract law may have some state-to-state similarities, when they vary a bankruptcy court should apply the specific contract law of the state in which the bankruptcy court sits, and (iv) whether the failure to perform gives rise to a "material breach", are all resolved using state law. *In re Cochise College Park, supra*, 703 F.2d 1339, 1348, fn. 4. As shown above, the *Cochise College Park* analysis does not stand alone. Whether due to practical considerations, common sense, or legitimate concern that unscrupulous creditors will use immaterial or contrived claims to circumvent the Code's intent to allow a debtor to restructure its affairs, when resolving a §365(b) motion, on an ordinary, consistent, and predictable basis Bankruptcy Courts routinely look to state law on the critical issues of materiality, substantive rights, and consequences. It is that about which Appellant complains. Instead of using state contract law, Appellant would substitute the established rule that has worked, and worked well, with a case-by-case subjective evaluation, using Black's Law Dictionary or "ordinary usage" as the only guide.

The conundrum Appellant urges is probably best shown by analyzing the other decision it advances, *In re Senior Care Ctrs., LLC*, 607 B.R. 580, 588-589

(Bankr. N.D. TX 2019). Appellant cites *Senior Care Ctrs.* for the proposition "materiality is not a factor under §365". A careful review of the cited authority indicates otherwise.

Senior Care Ctrs. involved debtors who had failed to pay rent in the month the bankruptcy case was filed (607 B.R. 580, at 588). Apparently as of the date of the Memorandum Opinion and Order on the assumption motion, the *rent remained unpaid*. The debtors proposed to prospectively cure on the effective date of their plan of reorganization. *Id*., at 588. Contrary to Appellant's assertion, that materiality is never relevant, it simply was not relevant to the facts existing in that case. The Bankruptcy Court's actual statement was "… The court disagrees with the notion that materiality *is a factor here*… But even assuming that §365(b)(1) is only triggered by "material" defaults… *failure to pay rent should be considered a material breach*." *Id*., at 588 [emphasis added]. As support, the Bankruptcy Court cited *In re Joshua Slocum*, 922 F.2d 1081 (3rd Cir. 1990) as authority for the conclusion that unpaid rent as of the assumption was a "material" breach. *Id*., at 588, fn. 21. Without requiring a deep dive, if at the time of assumption rent remains unpaid, *under those circumstances* a material default occurs. Contrary to the overly broad argument, *Senior Care Ctrs.* supports the proposition that materiality is an appropriate area for examination.

Since *Senior Care Ctrs*. stands for the proposition that failure to pay rent is

material and rent remaining unpaid at the time of assumption is a default, any discussion by the judge in that case of no relationship between materiality and §365 is nothing more than gratuitous *dicta*. At the same time, a simple review of *Joshua Slocum* undermines any argument that materiality may not be considered by a bankruptcy court.

Joshua Slocum involved a motion to assume pursuant to 11 U.S.C. §365(b)(3). The decision invests a fair amount of analysis discussing what might be "materially and economically significant" to parties to a lease. 922 F.2d at 1092. Looking outside the Bankruptcy Code, including using "logic and simple common sense", *Joshua Slocum* discusses materiality as that which goes to the very heart of a contract. *Id*. And discussing another term undefined by the Bankruptcy Code (a "shopping center") but the definition of which impacts substantive rights, *Joshua Slocum* instructs that proper definition is left to "case-by-case interpretation", including reviewing secondary sources (such as Collier on Bankruptcy) and other case decisions. *Id*. at 1086, citing *In re Goldblatt Brothers, Inc.,* 766 F.2d 1136, 1140 (7th Cir. 1985). To overstate the obvious, not only is materiality a proper subject for consideration. It is also a very common one.

3. Material v. Non-Material

Since the Bankruptcy Court did not find a default under the Lease, this Court's analysis should end here. Nonetheless, even in if the Court was to consider

whether a default must be material or not, governing Ninth Circuit law supports the Bankruptcy Court decision. *In re Cochise College Park*, 703 F.2d 1339 (9th Cir. 1983).

California case law has long held that when a landlord seeks to declare a forfeiture of the lease,[3] the breach must be "material," "substantial," or "total." Since at least 1928, California law has been clear that - the law abhors lease forfeitures. *Feder v. Wreden Packing & Provision Co*., 89 Cal.App. 665, 673 (1928); see also, *Keating v. Preston*, 42 Cal.App.2d 110, 115 (1940) ("Unless the lease specifically limits the use of the property to a particular purpose, or that restriction is necessarily inferred from the language which is employed, the lease may not be forfeited on account of the mere use of the property for another purpose even though that be an illegal use prohibited by statute, for the reason that forfeitures of leases are not favored by the law."). Appellee's argument, without any legislative history or case law support, is apparently that 11 U.S.C. §365(b) vitiates 100 years of fundamental California public policy as well as the plain and unambiguous language of the Lease.

As long determined in California, whether a particular breach will give a plaintiff landlord the right to declare a forfeiture is based on materiality. *NIVO 1*

[3] The Notice of Default, the 3-Day Notice, and the practical result of Landlord's efforts to prevent Appellee from assuming the Lease, all had the same common goal- eliminating Debtor as a tenant.

LLC v. Antunez, *supra*, 217 Cal.App.4th Supp 1 at 5. And as more clearly set forth by the California Court of Appeal in *Superior Motels, Inc. v. Rinn Motor Hotels, Inc*., 195 Cal.App.3d 1032 (1987), at 1051:

> "The law sensibly recognizes that although every instance of noncompliance with a contract's terms constitutes a breach, not every breach justifies treating the contract as terminated. (See 4 Corbin on Contracts (1951) § 943, pp. 806-807; Farnsworth, Contracts (1982) §§ 8.15-8.16, pp. 607-613; Murray on Contracts (2d rev. ed. 1974) § 167, pp. 322-327; 11 Williston on Contracts (3d ed. 1968) § 1292, pp. 8-9.) Following the lead of the Restatements of Contracts, *California courts allow termination only if the breach can be classified as "material," "substantial," or "total."* (See *Coughlin* v. *Blair* (1953) 41 Cal.2d 587, 598-599 [262 P.2d 305]; *Sackett* v. *Spindler* (1967) 248 Cal.App.2d 220, 229 [56 Cal.Rptr. 435]; *Story* v. *San Rafael Military Academy* (1960) 179 Cal.App.2d 416, 417 [3 Cal.Rptr. 847]; *Budget Way etc. Laundry* v. *Simon* (1957) 151 Cal.App.2d 476, 480-481 [311 P.2d 591]; *Asso. Lathing*

> *etc. Co.* v. *Louis C. Dunn, Inc*. (1955) 135 Cal.App.2d 40, 50-51 [286 P.2d 825]; *Smith* v. *Empire Sanitary Dist*. (1954) 127 Cal.App.2d 63, 72-73 [273 P.2d 37].)"
>
> (*Emphasis added*)

Whether a breach is so material as to constitute cause to terminate a contract is ordinarily a question for the trier of fact. *Whitney Inv. Co. v. Westview Dev. Co*., 273 Cal.App.2d 594, 601 (1969) (citing the California Supreme Court decision, *Gold Min. & Water Co.* v. *Swinerton*, 23 Cal.2d 19, 28 (1943)). Applying California law, a finding that a breach is not "material" is reviewed under the substantial evidence standard (*Brown v. Grimes*, 192 Cal.App.4th 265, 279 (2011)), that is whether a reasonable trier of fact could have made such a finding based upon the whole record. *Kuhn v. Department of General Services*, 22 Cal.App.4th 1627, 1633 (1994).

What is "material" is not without some reasonable standards, but it is also not formalistic. As explained by former Supreme Court Justice Benjamin Cardozo in *Jacobs & Young, Inc. v. Kent*, 230 N.Y. 239 (1921), at 243-244:

> "The courts never say that one who makes a contract fills the measure of his duty by less than full performance. They do say, however, that an omission, both trivial and innocent, will sometimes be atoned for by allowance of

the resulting damage, and will not always be the breach of a condition to be followed by a forfeiture [citations omitted] … Where the line is to be drawn between the important and the trivial cannot be settled by a formula. 'In the nature of the case precise boundaries are impossible' (2 Williston on Contracts, sec. 841). The same omission may take on one aspect or another according to its setting. Substitution of equivalents may not have the same significance in fields of art on the one side and in those of mere utility on the other. Nowhere will change be tolerated, however, if it is so dominant or pervasive as in any real or substantial measure to frustrate the purpose of the contract [citation omitted] … The question is one of degree, to be answered, if there is doubt, by the triers of the facts [citation omitted]. … We must weigh the purpose to be served, the desire to be gratified, the excuse for deviation from the letter, the cruelty of enforced adherence. … This is merely to say that the law will be slow to impute the purpose, in the silence of the parties, where the significance of the

default is grievously out of proportion to the oppression of the forfeiture."

VI. CONCLUSION

For the reasons stated above, Appellee respectfully submits the Bankruptcy Court order approving the assumption, and the District Court's affirmance of the same, be upheld.

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CERTIFICATE OF COMPLIANCE WITH FEDERAL RULE OF APPELLATE PROCEDURE 32 AND NINTH CIRCUIT RULE 32-1(a)

The foregoing Appellee Answering Brief complies with Ninth Circuit Rule 32-1(a) and contains 5921 words according to the word-processing system used to prepare the brief, excluding the items exempted by Fed. R. App. P. 32(f). The brief's type size and typeface comply with Fed. R. App. P. 32(a)(5) and (6). I certify that this brief complies with the word limit of Cir. R. 32-1. It was prepared using Microsoft Word 365 in 14-point Times Roman font, a proportionally spaced typeface.

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FOR THE NINTH CIRCUIT

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