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The Impact of Amended RPAPL §749(3) on Commercial Tenant Bankruptcies

With the deletion of just a few words from RPAPL §749(3), the 2019 amendment opens the door for tenant-debtors to assume leases even after a pre-bankruptcy warrant of eviction has been issued, without the need for the tenant to first vacate the warrant of eviction.

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A recent decision in the Chapter 11 case of *Payam*, 642 B.R. 365 (Bankr. S.D.N.Y. Aug. 10, 2022) by Chief Judge Martin Glenn of the U.S. Bankruptcy Court for the Southern District of New York highlights the significant impact that a 2019 amendment to the New York Real Property and Procedures Law (RPAPL) will have on future disputes in bankruptcy cases where the tenant files for bankruptcy after the issuance of a warrant of eviction but before its execution. With the deletion of just a few words from RPAPL §749(3), the 2019 amendment opens the door for tenant-debtors to assume leases even after a pre-bankruptcy warrant of eviction has been issued, without the need for the tenant to first vacate the warrant of eviction.

The 2019 Amendment

Before the amendment, RPAPL §749(3) provided that "[t]he issuing of a warrant for the removal of a tenant cancels the agreement under which the person removed held the premises, *and annuls the relation of landlord and tenant*, but nothing contained herein shall deprive the court of the power to vacate such warrant for good cause shown prior to the execution thereof." RPAPL §749(3) (2018) (emphasis added). Under the prior version of the statute, the issuance of a warrant of eviction terminated the landlord-tenant relationship. This legal proposition was uniformly recognized by both New York state and bankruptcy courts. See, e.g., *In re Éclair Bakery Ltd.*, 255 B.R. 121, 136 (Bankr. S.D.N.Y. 2000); *In re Touloumis*, 170 B.R. 825, 829 (Bankr. S.D.N.Y. 1994); *Lazy Acres Park v. Ferretti*, 118 A.D.3d 1406, 1407 (4th Dep't 2014); *Fisk Bldg. Assocs. v. Shimazaki II*, 76 A.D.3d 468, 469 (1st Dep't 2010); *Stepping Stones Assocs. v. Seymour*, 48 A.D.3d 581, 584 (2d Dep't 2008); see also *In re Super Nova 330 v. Gazes*, 693 F.3d 138, 142 (2d Cir. 2012)

("Under New York law, … while the issuance of a warrant of eviction cancels any existing lease and seemingly terminates the landlord-tenant relationship, the tenant, in fact, retains a residual interest in the lease until the execution of the warrant."). In the bankruptcy context, the termination of the leasehold interest under RPAPL §749(3) meant that there was no lease for the tenant to assume. See *In re Éclair Bakery Ltd.*, 255 B.R. at 136 (noting that, where issuance of warrant of eviction terminates lease, "the filing of a bankruptcy case does not revive the lease"); *In re W.A.S. Food Serv.*, 49 B.R. 969, 972 (Bankr. S.D.N.Y. 1985) (where a warrant of eviction has been issued "the mere potentiality of a restoration of the landlord tenant relationship through vacatur of the warrant of eviction does not vest the debtor with a sufficient interest in the leased property to allow assumption and assignment of the lease") (citations omitted). The debtor would need to vacate the warrant in order to resurrect the lease.

Although a terminated lease may not be assumed in bankruptcy, the tenant-debtor's possessory interest in the leasehold is protected by the automatic stay that is triggered by the commencement of a bankruptcy case pursuant to §362 of the Bankruptcy Code. See *In re Sweet N Sour 7th Ave.*, 431 B.R. 63, 67 (Bankr. S.D.N.Y. 2010) ("[I]f a debtor remains in possession after the issuance of a warrant, the debtor retains an equitable possessory interest in the leasehold sufficient to trigger the protection of the bankruptcy automatic stay."); *In re Éclair Bakery Ltd.*, 255 B.R. at 133 (automatic stay applies to lease where state court enters a warrant of eviction, and stays its application). A landlord seeking to complete the eviction of the tenant-debtor is therefore required to first seek relief in the bankruptcy court to vacate the automatic stay in order to proceed. In pre-2019 RPAPL amendment bankruptcy cases addressing lift stay motions filed by landlords seeking to proceed with tenant evictions where a warrant of eviction had issued, bankruptcy courts have looked to whether there is a reasonable possibility that the state court would vacate the warrant of eviction. See, e.g., *In re Griggsby*, 404 B.R. 83, 93 (Bankr. S.D.N.Y. 2009) (noting that "[t]he prepetition issuance of a warrant may provide 'cause' to terminate the automatic stay pursuant to §362(d)(1)," and finding cause to vacate the stay because debtor "failed to show grounds upon which the Civil Court would vacate the warrant of eviction"); *In re Syndicom*, 268 B.R. 26, 46 (Bankr. S.D.N.Y. 2001) (granting landlord relief from stay because there was no pending state court proceeding to vacate the warrant of eviction, and

debtor did not show reasonable possibility that the state courts would vacate the warrant of eviction based on prior state court decision denying even a stay of eviction); *In re Éclair Bakery Ltd.*, 255 B.R. at 136 (granting landlord stay relief to remove debtor from possession of premises and noting that "where state court litigation is not pending or in the cards, or where the debtor has failed to show any basis for a belief that the state court will grant relief, the prepetition termination of the landlord-tenant relationship will at least normally provide cause for relief from the stay").

The 2019 amendment to RPAPL §749(3) fundamentally changes the analysis. The current version of the statute provides that "[n]othing contained herein shall deprive the court of the power to stay or vacate such warrant for good cause shown prior to the execution thereof, or to restore the tenant to possession subsequent to execution of the warrant." RPAPL §749(3) (2019). The statutory language providing that the issuance of the warrant of eviction "annuls the relation of landlord and tenant" has been deleted. *Payam* is the first published bankruptcy court decision to address the post-2019 amended RPAPL §749(3). The *Payam* court provides clear guidance on how practitioners can expect lift stay litigation between landlords and tenant-debtors to unfold.

The Procedural Posture of 'Payam'

In *Payam*, the debtor operated a restaurant under a commercial lease with its landlord at the leased premises. Following the occurrence of certain defaults, the landlord commenced a holdover proceeding in New York Civil Court. In addition to non-monetary defaults relied upon in the holdover petition, the tenant had not paid monthly rent to the landlord since March 2020 despite receipt of two PPP loans, and rental arrears had ballooned to approximately $800,000. In the holdover proceeding, the landlord and tenant entered into a stipulation pursuant to which the tenant agreed, among other things, (1) to the state court's entry of a final judgment of possession and issuance of a warrant of eviction, with execution thereon stayed until June 1, 2022, and (2) to waive any defenses to, or seek to extend or further stay, the execution of the warrant of eviction. Despite the terms of the stipulation, the tenant refused to vacate the premises and instead filed an order to show cause with the state court seeking to extend the stay of the execution of the warrant of eviction. The state court declined to enter the order to show

cause, and the tenant filed its Chapter 11 case before the marshal could execute the warrant of eviction.

In the bankruptcy case, the landlord sought relief from the automatic stay to proceed with execution on the warrant of eviction against the tenant-debtor. The debtor did not file an objection to the landlord's motion. The bankruptcy court granted the landlord's motion and indicated in its order vacating the stay that it would issue a subsequent written opinion explaining its reasons for granting relief, because "the Motion raises important issues concerning the analysis of motions for relief from stay in cases involving nonresidential leases where New York courts have issued judgments of possession and warrants of eviction before Chapter 11 petitions are filed." *Payam*, at 366. As it turns out, the important issue alluded to by the bankruptcy court in its order, and discussed in the *Payam* decision, is the 2019 amendment to RPAPL §749(3), an amendment that the court noted "has seemingly gone unnoticed." Id. at 370. The bankruptcy court noted that multiple New York state courts in post-amendment cases have continued to (erroneously) enunciate the "well-settled" principle that a warrant of eviction terminates the landlord-tenant relationship. Id. (citing *McKinney Supplemental Practice Commentary* (Supp. 2021)).

How the 2019 Amendment Changes the Analysis

In *Payam*, the bankruptcy court offered a candid assessment of a tenant-debtor's chances at assuming a lease that was subject to the issuance of a warrant of eviction before the amendment: "The *best* outcome for the debtor was the automatic stay remaining in place while the debtor returned to state court seeking to have the warrant of eviction vacated and the lease reinstated—often a long shot at best." Id. at 367. According to the *Payam* court, "the amendment to RPAPL §749(3) changes the analysis. The analysis today is much simpler as it is now unnecessary for the bankruptcy court to find an equitable possessory interest because the statute does not terminate the leasehold rights upon the issuance of the warrant of eviction." Id. at 370. As a result, the bankruptcy court predicted that lift stay motions in this context will "focus on the usual bankruptcy law issues concerning stay relief (typically adequate protection) without the debtor having to return to state court to vacate the warrant of eviction." Id. at 367. Indeed, in its own decision, the *Payam* court did not analyze whether the debtor would be able to vacate the

warrant of eviction, but concluded that the landlord had clearly established cause for relief from stay on the grounds that (1) the debtor was not performing its post-bankruptcy obligations under the lease as required by the Bankruptcy Code, nor had it sought to extend the time to do so, (2) the debtor did not provide adequate protection to the landlord, and (3) the debtor would not be able to cure the substantial defaults under the lease, including payment of the approximately $800,000 in rent arrearages.

The *Payam* court also hinted at a more significant impact of the amendment to RPAPL §749(3) on tenant-debtor bankruptcy cases. Because the issuance of the warrant of eviction no longer terminates the leasehold, the lease may be assumed even after a warrant of eviction has issued, as long as the debtor satisfies the requirements for assumption under §365 of the Bankruptcy Code. *Payam*, at 367. Thus, bankruptcy now provides a better option for tenants near the end of an adversely-resolved holdover proceeding, an option that was not previously available (as a practical matter) because vacating a warrant of eviction was a "long shot at best." With the change in the statute, if the lease is not terminated before the bankruptcy filing, the question for a tenant-debtor becomes not whether there is a basis to vacate a warrant of eviction, but whether it can comply with the Bankruptcy Code's requirements for assumption of a lease. Counsel representing landlords and tenants alike cannot ignore the 2019-amendment to RPAPL §749(3). The relevant legal analysis (and the attendant legal advice that clients can expect to receive) has changed substantially.

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