

Dated: March 7, 2012



U.S. BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

Charles G. Case, II
Charles G. Case, II, Bankruptcy Judge

In re:

**MOUNTAINSIDE FITNESS CENTERS
OF GILBERT, LLC; FIREBIRD
INVESTMENT CO.; and
MOUNTAINSIDE FITNESS CENTERS
OF ARVADA, LLC,
Debtors.**

) In Chapter 11 proceedings.
) Case No.: 2:10-bk-23734-CGC
)
) UNDER ADVISEMENT DECISION
) REGARDING GRASSER INVESTMENTS,
) LLC'S STANDING TO FILE A PROOF OF
) CLAIM
)
)

I. Introduction

As has been the case with many matters of late, this case is before the Court as a result of the current economic crisis. A debtor entered into a verbal real property lease with a landlord who subsequently assigned all rights in the lease to a bank in consideration for a loan. When the debtor filed for bankruptcy, the landlord filed a proof of claim for amounts due under the verbal lease. However, the landlord's assignment and the various contractual provisions in connection therewith presented significant issues that affect the landlord's ability to recover monies due under the verbal lease. For this reason, Debtor, Firebird Investment Co. ("Firebird"), now asks the Court to disallow Grasser Investments, LLC's ("GILLC") proof of claim arguing that GILLC lacks standing to file a proof of claim because GILLC assigned all its rights it had under the alleged verbal lease to Wells Fargo.

II. Background and Facts

This dispute centers upon an alleged oral real property lease ("Verbal Lease") between landlord GILLC and tenant Firebird for commercial property owned by GILLC known as Gilbert Commons ("Property"). GILLC assigned the Verbal Lease to Wells Fargo Bank, N.A. ("Wells Fargo") on May 21, 2008 as consideration for a construction

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3 loan (“Loan”) for \$18,703,000. The Loan was secured by a Construction Deed of Trust
4 with Absolute Assignment of Leases and Rents, Security Agreement and Fixture Filing
5 (“Deed of Trust”) which contained an assignment provision whereby GILLC irrevocably
6 assigned to Wells Fargo all of GILLC’s right, title and interest in the Property, as well as
7 all licenses and agreements relating to the Property. The assignment was non-contingent,
8 absolute and could be exercised without possession of the Property.

9 After GILLC defaulted on its obligations to Wells Fargo under the Deed of Trust,
10 both parties stipulated to the appointment of a receiver for the property in November
11 2010. Wells Fargo and Firebird settled issues regarding both the written and Verbal
12 Lease under a First Amended Settlement and Release Agreement (“Settlement
13 Agreement”). A key provision of the Settlement Agreement is that Wells Fargo
14 discharged any claims which it may have had against Firebird under the Verbal Lease.

15 GILLC filed a proof of claim for \$103,087 based on the Verbal Lease on January
16 25, 2011. Firebird objected, arguing first that GILLC’s claim should be disallowed
17 because it is based on the Verbal Lease, which violates the statute of frauds. Second,
18 even if the Verbal Lease was valid, GILLC has no standing to pursue its legal rights
19 because it assigned all right, title, and interest in the Property to Wells Fargo pursuant to
20 the Deed of Trust, thereby making Wells Fargo the real party in interest. Finally,
21 Firebird notes that the Deed of Trust granted GILLC a revocable license to collect lease
22 payments, so long as GILLC was not in default. Therefore, the moment GILLC
23 defaulted on its obligation to Wells Fargo, the license was revoked terminating any
24 interest GILLC had in the Property.

25 **III. Analysis**

26 A party filing a proof of claim has the burden to establish that it has standing to
27 do so. In re Minbatiwalla, 424 B.R. 104, 111 (Bankr. S.D.N.Y. 2010). The standing
28 provisions of the Bankruptcy Code are liberally interpreted and are designed to allow a
party to appear as long as it has a direct stake in the litigation under particular
circumstances. Id. at 109. Federal courts may only exercise jurisdiction over a litigant

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3 when the litigant meets both constitutional and prudential standing requirements. Veal v.
4 Am. Home Mortg. Servicing, Inc. (In re Veal), 450 B.R. 897, 906 (B.A.P. 9th Cir. 2011).

5 **A. Constitutional Standing**

6 Constitutional standing requires an injury-in-fact, caused by the defendant's
7 conduct, which the requested relief will likely redress. Id. GILLC suffered an injury-in-
8 fact when it was unable to collect rent under the Verbal Lease. This injury was caused by
9 Firebird, who was the tenant and had an obligation to pay rent to GILLC pursuant to the
10 Verbal Lease. Allowing GILLC's proof of claim would redress GILLC's harm by giving
11 it the opportunity to collect from Firebird. Thus, GILLC meets the requirements for
12 constitutional standing.

13 **B. Prudential Standing**

14 Apart from constitutional standing, a party must also have prudential standing,
15 which consists of judicially self-imposed limits on the exercise of federal jurisdiction.
16 Veal, 450 B.R. at 906-07. See Sprint Comm. Co., L.P. v. APCC Servs., Inc., 554 U.S.
17 269, 289 (2008); Elk Grove Unified School Dist. v. Newdow, 542 U.S. 1, 11-12 (2004).
18 Federal Rule of Civil Procedure 17¹ expounds on these limits by requiring any action to
19 be prosecuted by a real party in interest. See Fed. R. Civ. P. 17(a)(1). The real party in
20 interest doctrine melds procedural and substantive law and ensures that the party bringing
21 the action has rights that can be vindicated by proving the elements of the claim for relief
22 asserted. Veal, 450 B.R. at 908. Analysis of the real party in interest doctrine requires a
23 determination of the applicable substantive law as it is that law which defines and
24 specifies the wrong, the parties aggrieved, and the redress they may receive. Id.

25 Because the real party in interest doctrine requires consideration of the
26 substantive law at issue, Bankruptcy Rule 3001(b), which governs filing of proofs of
27 claims, controls the prudential standing analysis. Only a creditor or the creditor's
28 authorized agent is eligible to file a proof of claim. See Fed. R. Bankr. P. 3001(b);

¹ Federal Rule of Civil Procedure 17 is applicable in bankruptcy proceedings by Federal Rule of Bankruptcy Procedure 7017. See Fed. R. Bankr. P. 7017.

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3 Minbatiwalla, 424 at 108-09. A creditor is an entity that has a claim against a debtor that
4 arose before the petition was filed. See 11 U.S.C. § 101(10)(A); Minbatiwalla, 424 B.R.
5 at 108-09. A claim is a right to payment, including a right to payment for breach of
6 performance, if such breach gives right to payment. See 11 U.S.C. § 101(5)(A) and (B);
7 Minbatiwalla, 424 B.R. at 108-09. Pursuant to Bankruptcy Rule 3001(b), GILLC will
8 have standing to file a proof of claim against Firebird if GILLC had a claim before
9 Firebird filed for bankruptcy. Here, the only way GILLC could have a claim is through
10 the Verbal Lease. Thus, if GILLC’s assignment of the Verbal Lease to Wells Fargo
11 terminated all interest GILLC had in the Verbal Lease and the Property, then GILLC
12 does not have standing to file a proof of claim.

13 Because the lease is a contract, Arizona contract law is implicated. Under
14 Arizona law, contracts are read as a whole, giving effect to the main purpose of the
15 contract, and interpreting the contract so as to make it effective and reasonable. See
16 Phelps Dodge Corp. v. Brown, 540 P.2d 651, 653 (Ariz. 1975); Kinter v. Wolfe, 426 P.2d
17 798, 802 (Ariz. 1967); Hamberlin v. Townsend, 261 P.2d 1003, 1006 (Ariz. 1953); Chu
18 v. Ronstadt, 498 P.2d 560, 563 (Ariz. Ct. App. 1972); see also 3 Williston on Contracts
19 §§ 618-626 (1961). The effectiveness of an assignment of rents is determined with
20 reference to the instrument creating the assignment; such effectiveness can be either
21 before, upon, or after a default. Scottsdale, 159 B.R. at 299-300. A “present and
22 absolute assignment” creates an immediate interest in both present and future rents. Id.
23 at 300.

24 According to the Deed of Trust, GILLC irrevocably assigned to Wells Fargo all
25 present and future interests in the Property². This assignment was a “present and absolute
26 assignment” Deed of Trust at 3. Because the Deed of Trust created the assignment,

27 ² The Deed of Trust assignment provision reads in pertinent part:

28 [GILLC] hereby irrevocably assigns to [Wells Fargo] interest in . . . all
present and future leases of the Property . . . all licenses and agreements
relating to the . . . Property . . . now existing or entered into after the date
hereof . . . and . . . the rents . . . and profits of the Property, including . . .
all amounts payable and all rights and benefits accruing to [GILLC] . . .

Deed of Trust at 3.

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3 the effectiveness of the assignment will be determined in reference to the Deed of Trust.
4 The Deed of Trust contains clear language referencing the assignment as present and
5 absolute; thus the assignment gave Wells Fargo an immediate interest in present and
6 future rents under the Verbal Lease. Therefore, the assignment completely transferred
7 *any* rights GILLC had to Wells Fargo.

8 GILLC argues that, notwithstanding the assignment, it has standing to file a proof
9 of claim because under the terms of the Deed of Trust Wells Fargo granted GILLC a
10 revocable license to collect payments under the Verbal Lease. The Deed of Trust grants
11 GILLC a revocable license to collect and retain payments until default, in which case the
12 license is immediately revoked.³ GILLC is currently over 800 days in default and owes
13 Wells Fargo over \$18,000,000. See Super. Ct. of Maricopa Cnty. Min. Entry at 3, ECF
14 226-2. Therefore, whatever rights that were extended to GILLC under the license no
15 longer exist as GILLC's license was automatically revoked when it defaulted on its
16 obligations.

17 GILLC also argues that regardless of the revocable license provision, its proof of
18 claim is clearly an allowed for and authorized action under the defense provision of the
19 Deed of Trust to protect, preserve, and defend the Property. The Deed of Trust allows
20 GILLC, at its sole expense, to protect Wells Fargo's and GILLC's rights of the Property.⁴
21 This provision, standing alone, confers upon GILLC the right to take any action to defend
22 the Property against adverse claims. However, pursuant to Arizona law, contracts are
23 interpreted as a whole, and an interpretation keeping provisions consistent with each
24 other is always preferred. Viewing the contract as a whole, it is apparent that GILLC and

25 ³ The Deed of Trust revocable license provision reads in pertinent part:

26 [Wells Fargo] confers upon [GILLC] a revocable license . . . to collect and
27 retain the [p]ayments as they become due and payable, until the
28 occurrence of a [d]efault Upon a [d]efault, the [l]icense shall be
automatically revoked and [b]eneficiary may collect and apply the
[p]ayments . . . without notice and without taking possession of the
Property.

Deed of Trust at 4.

⁴ The Deed of Trust defense provision reads in pertinent part: “[GILLC] shall protect, preserve and defend the Property[,] . . . the security . . . and rights of [Wells Fargo] and [GILLC] against all adverse claims, or the filing of any action or proceeding” Deed of Trust at 7.

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3 Wells Fargo intended for the Deed of Trust to assign all of GILLC's rights under the
4 Verbal Lease to Wells Fargo while also granting GILLC a revocable license to continue
5 to collect rent from the Property. The revocable license is clear: upon GILLC's default,
6 all the privileges granted to it under the license will automatically expire. Thus, the only
7 interpretation of the defense provision consistent with the general intent of the entire
8 Deed of Trust is that upon GILLC's default, the revocable license expired, causing
9 GILLC to lose its rights under the defense provision.

10 **I. Conclusion**

11 Although GILLC has constitutional standing, it lacks prudential standing to file
12 its proof of claim because it assigned its rights in the Verbal Lease, which was the basis
13 upon which GILLC filed its proof of claim, to Wells Fargo under the Deed of Trust.
14 While the Deed of Trust conferred a revocable license to GILLC allowing it to collect
15 payments under the Verbal Lease, this license was automatically revoked when GILLC
16 defaulted on its obligations to Wells Fargo. Similarly, the defense provision allowing
17 GILLC to preserve, protect and defend the Property expired when GILLC defaulted on
18 its obligations to Wells Fargo, revoking its license. Because GILLC does not have
19 prudential standing, it is not a real party in interest in this proceeding, and is not able to
20 file a proof of claim.

21 **So ordered.**

22 Dated: March 7, 2012.

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26 CHARLES G. CASE II
27 UNITED STATES BANKRUPTCY JUDGE

28 COPY of the foregoing mailed by the BNC and/or
sent by auto-generated mail to:

All creditors and interested parties.