NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re:	BAP No. CC-04-1287-PaBK
	BAP No. CC-04-1300-PaBK
EL TORO MATERIALS COMPANY, INC.,	(cross appeals)
Debtor.	Bk. No. SA 02-18913-RA
	Adv. No. SA 03-01486-RA
EL TORO MATERIALS COMPANY, INC.,	
Appellant,	
v.	**MEMORANDUM**[1]
SADDLEBACK VALLEY COMMUNITY CHURCH; UNITED STATES TRUSTEE; KAREN SUE NAYLOR, Trustee,	
Appellees.	

Argued and Submitted on February 23, 2005
at Los Angeles, California

Filed - July 8, 2005

Appeal from the United States Bankruptcy Court
for the Central District of California

Honorable Robert W. Alberts, Bankruptcy Judge, Presiding

Before: PAPPAS,[2] BRANDT and KLEIN, Bankruptcy Judges.

[1] This disposition is not appropriate for publication and may not be cited to or by the courts of this circuit except when relevant under the doctrines of law of the case, res judicata, or collateral estoppel. See 9th Cir. BAP Rule 8013-1.

[2] Hon. Jim D. Pappas, Bankruptcy Judge for the District of Idaho, sitting by designation.

Debtor rejected a real property lease in its chapter 11 case.[3] The lessor filed a proof of claim for $23 million in damages. Through an adversary proceeding, Debtor objected to the lessor's claim and sought to recover money damages from the lessor for its alleged prepetition breach of the lease. The lessor asserted counterclaims under several different theories, including nuisance, waste, and trespass, all premised upon the same conduct by Debtor.

On Debtor's motion for partial summary judgment, the bankruptcy court decided that the lessor's claims for nuisance and waste were not subject to the cap on a lessor's claim for breach damages under 11 U.S.C. § 502(b)(6). It also dismissed the lessor's trespass claim. Debtor timely appealed the bankruptcy court's application of § 502(b)(6), and the lessor cross-appealed dismissal of its trespass counterclaim.

We REVERSE the decisions of the bankruptcy court and REMAND.

I. FACTS

As early as the 1960s, the predecessor-in-interest to Debtor El Toro Materials Co., Inc. ("El Toro") conducted sand and gravel mining operations on leased property in Orange County, California. By the late 1970s, El Toro took over control of the operation.

The leased property was owned, at least as of the 1980s, by Baker Ranch Properties ("Baker Ranch"). On November 1, 1988,

---

[3] Absent contrary indication, all section and chapter references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1330. "Rule" references are to the Federal Rules of Bankruptcy Procedure, and "FRCP" references are to the Federal Rules of Civil Procedure.

Baker Ranch and El Toro executed a lease agreement with a term of ten years and seven months. This lengthy document comprehensively detailed El Toro's rights and duties as to the leased property. Among the terms relevant to this appeal, the lease provided:

> [ARTICLE] 9.01 Throughout the term of this Lease, El Toro, at its sole cost and expense, shall promptly comply with all present and future laws, ordinances, orders, rules, regulations and requirements of all federal, state, county and municipal governments, departments, commissions, boards and offices, including, but not limited to the conditions set forth in all existing permits.
>
> . . . .
>
> [ARTICLE] 10.01 El Toro shall have the right to use the Premises only for the following:
>
> (a) Subject to the conditions set forth in all applicable government permits, the removal from the Premises of rock, sand, gravel, and fill materials . . . .
>
> . . . .
>
> (e) The storage of materials procured from or off the Premises which are used in conjunction with [the permitted mining operations described in the lease].
>
> . . . .
>
> [ARTICLE] 10.05 As additional consideration for [Baker Ranch] entering into this Lease, El Toro shall conduct all of its operations in a workmanlike manner in accordance with sound engineering and mining principals and practice, though Lessor hereby acknowledges that El Toro does not have an engineer on the Premises at all times, and consistent with the reshaping of the Premises as follows:
>
> (a) The Premises shall be restored to as near as practical with the grade as outlined in El Toro's Reclamation Plan granted by the County of Orange . . . and the finished grade as set forth in El Toro's Grading Permit . . . or as said Grading Permit is later amended with the written consent of Lessor.
>
> . . . .
>
> (c) All settlement ponds and debris deposits will be removed from the Premises prior to the termination of the

> term, except as same are necessary to complete El Toro's operations within the term of the Lease, which remaining ponds and deposits shall be removed no later than four (4) months following the date of termination.
>
> . . . .
>
> ARTICLE 23 SURRENDER - END OF THE TERM
>
> On the expiration or other termination of the term of this Lease . . . El Toro shall quit and surrender the Premises to Lessor, in good order and condition, as set forth in Section 10.05 hereinabove, free and clear of lettings, subtenancies and occupancies and of all liens and encumbrances other than those if any, created by lessor.

El Toro and Baker Ranch executed an amendment to the lease on the same day they executed the lease. This amendment provided Baker Ranch with the right to bifurcate the lease into two separate leases in connection with a division of the property into two separate lots and a sale or transfer of either lot. The amendment further specified that, upon bifurcation of the property into Plots 1 and 2, the lease would continue in effect with the fee owners of either plot.

On June 20, 1997, appellee Saddleback Valley Community Church ("SVCC") and El Toro executed a conditional amendment to El Toro's 1988 lease with Baker Ranch in anticipation of SVCC's purchase of Plot 1. At the time, SVCC owned other property adjoining the Baker Ranch property. One of the proposed modifications between SVCC and El Toro extended El Toro's lease term indefinitely, subject to termination by either party upon two years' notice. SVCC purchased Plot 1 (approximately forty acres) from Baker Ranch in 1999, and in December 2001 it gave El Toro notice of its intent to terminate the lease.

Prior to the lease expiring under the two-year notice

provision of the modification agreement, on October 18, 2002, SVCC gave El Toro a "Thirty (30) Day Notice to Perform or Quit." This notice alleges that El Toro had violated Articles 9.01 and 23 of the 1988 lease by stockpiling waste material generated in its sand mining operation. SVCC demanded that El Toro remove or dispose of the waste material within thirty days, vacate Plot 1, or face legal action.

El Toro filed for protection under chapter 11 of the Bankruptcy Code on November 18, 2002.[4] SVCC filed a proof of claim for $23 million in El Toro's bankruptcy case. According to the proof of claim, the basis for SVCC's claim is that El Toro stockpiled approximately 650,000 cubic yards of mining byproducts on its property; the amount of the claim was derived from cost estimates SVCC received to remove the waste material.[5] SVCC's claim also references unspecified future damage it may incur due

---

[4] A chapter 11 trustee was appointed in the Chapter 11 case on October 1, 2003. However, the record does not disclose the circumstances precipitating this event, nor do the parties suggest they are relevant to the appeal or cross-appeal.

[5] At oral argument, counsel for El Toro represented that the waste material at issue is not a "hazardous material." It is, counsel suggests, "fill" material. While SVCC refers to the stockpile in its briefing as "goo," or more specifically, as water-saturated clay resulting from El Toro's sand-washing operation, rubble and debris, we presume the nature of the material is not particularly pertinent to the issues on appeal, but rather, it is the existence of and amount in the stockpile that concern SVCC.

In addition, we note SVCC's dispute with El Toro also involved, at least initially, certain equipment and other personal property El Toro left behind on Plot 1. Counsel for El Toro informed the Panel that the trustee had sold these items prior to oral argument. Presumably, that sale effectively settled any dispute regarding the equipment, and so the Panel will focus only on the stockpiled material, as have the parties.

to delays in its ability to develop Plot 1, and the possibility of subsequently amending its proof of claim to assert an administrative claim for El Toro's postpetition "unauthorized operations . . . and the delay in the development" of Plot 1.

On January 24, 2003, El Toro and SVCC filed a stipulation in the bankruptcy case. This stipulation provided El Toro would reject the lease, effective upon the bankruptcy court's order approving the stipulation, but remain in possession of Plot 1 until April 30, 2003. El Toro was required to pay rent during this extension, which allowed it to make a more orderly departure. The bankruptcy court entered an order approving the stipulation on January 27, 2003. El Toro vacated the premises on the designated date but did not remove the residue.

El Toro objected to SVCC's claim, and it filed a complaint against SVCC on April 25, 2003, initiating the adversary proceeding from which this appeal and cross-appeal arise. The bankruptcy court consolidated El Toro's objection to SVCC's proof of claim and the adversary proceeding in an order dated October 24, 2003.

In its complaint, El Toro alleged, inter alia, that SVCC breached the lease agreement and interfered with El Toro's relationship with its subtenants and with its plan to shift its operation to Plot 2. SVCC answered and asserted counterclaims against El Toro for, as relevant to this appeal, breach of the lease, and state law claims for waste, nuisance, and trespass.

All four of SVCC's counterclaims were premised, in whole or in part, on El Toro's stockpiling of mining byproducts on Plot 1. In particular, the trespass claim focused on El Toro's

postpetition, post-rejection failure to remove the stockpiled mining waste. Specific to this claim, SVCC identified its damages as including the cost of removing the stockpiled material and restoring Plot 1 as detailed in a reclamation plan. In its prayer for relief, SVCC also requested that the bankruptcy court issue an injunction requiring El Toro to remove the mining waste and any other property it had left behind on the leased property.

On November 3, 2004, El Toro filed a motion for partial summary adjudication in which it asked the bankruptcy court to apply the § 502(b)(6)[6] cap on claims of a lessor for damages to both SVCC's proof of claim and to its counterclaims in the adversary proceeding; to dismiss SVCC's counterclaim for interference with prospective economic advantage; and to dismiss SVCC's request for injunctive relief requiring it to remove the mining waste.

---

[6] This Code provision states that, upon objection to a claim, the bankruptcy court

> shall determine the amount of such claim as of the date of the filing of the petition, and shall allow such claim in lawful currency of the United States in such amount, except to the extent that—
>
> . . . .
>
> (6) if such claim is the claim of a lessor for damages resulting from the termination of a lease of real property, such claim exceeds—
>
> (A) the rent reserved by such lease, without acceleration, for the greater of one year, or 15 percent, not to exceed three years, of the remaining term of such lease, following the earlier of—
>
> (i) the date of the filing of the petition; and
>
> (ii) the date on which such lessor repossessed, or the lessee surrendered, the leased property; plus
>
> (B) any unpaid rent due under such lease, without acceleration, on the earlier of such dates[.]

In its opposition papers, SVCC made a number of arguments, including one urging that its trespass claim should not be dismissed. El Toro filed a reply brief, and in a footnote, it argued that since El Toro was in rightful possession of Plot 1 prior to lease rejection, it could not be liable for trespass.

The bankruptcy court granted El Toro's motion in part. It held:

> (1) All of SVCC's claims for damage due to the Debtor's nonperformance under the lease, including damages for breach of the lease covenants, are limited by the cap in § 502(b)(6) of the bankruptcy Code as damages resulting from "termination" of the subject lease.
>
> (2) However, SVCC's claims for damages arising from "tortious illegal acts (specifically, those for nuisance and waste)" are not limited by the cap.
>
> (3) Debtor's motion for partial summary judgment was granted as to SVCC's counterclaim for trespass.
>
> (4) Debtor's motion for partial summary judgment was granted as to SVCC's claim for injunctive relief.

Although the judgment did not dispose of all of the claims raised in the adversary proceeding, the bankruptcy court certified it as a final order pursuant to FRCP 54(b), applicable via Rule 7054.

After the bankruptcy court denied their respective motions for reconsideration, El Toro and SVCC each timely appealed the judgment. El Toro seeks review of the bankruptcy court's decision concerning application of the § 502(b)(6) cap; SVCC appeals dismissal of its trespass claim.[7]

---

[7] As the two appeals were identified as cross-appeals, the BAP clerk issued a cross-appeal briefing schedule, with which the parties have complied. On January 31, 2005, El Toro filed an "Additional Citation of a Relevant Decision" with a cite to K-4, Inc. v. Midway Engineered Wood Prods., Inc. (In re Treesource Indus., Inc.), 363 F.3d 994 (9th Cir. 2004).

II. JURISDICTION

The bankruptcy court had jurisdiction via 28 U.S.C. § 1334 and § 157(b)(1) and (b)(2)(B). We have jurisdiction on appeal under 28 U.S.C. § 158(c).

III. ISSUES

A. Whether the bankruptcy court erred in concluding that SVCC's counterclaims against El Toro under state law for waste and nuisance, premised upon conduct by El Toro that also constituted a breach the parties' lease agreement, were not subject to the damage cap in § 502(b)(6).

B. Whether the bankruptcy court erred in granting summary judgment to El Toro dismissing SVCC's counterclaim for trespass.

IV. STANDARD OF REVIEW

The Panel reviews the grant or denial of summary judgment de novo. Prestige Ltd. P'ship-Concord v. E. Bay Car Wash Partners (In re Prestige Ltd. P'ship-Concord), 234 F.3d 1108, 1114 (9th Cir. 2000) (addressing denial of summary judgment); Captain Blythers, Inc. v. Thompson (In re Captain Blythers, Inc.), 311 B.R. 530, 534 (9th Cir. BAP 2004) (addressing grant of summary judgment). Viewing the evidence in the light most favorable to the nonmoving party, the Panel must determine whether there are any genuine issues of material fact and whether the trial court correctly applied relevant substantive law. In re Captain Blythers, Inc., 311 B.R. at 534. The bankruptcy court's interpretation of the Bankruptcy Code is also reviewed de novo. Id.

V. DISCUSSION

A. Does the § 502(b)(6) cap limit damages resulting from a debtor's conduct that violates the terms of the lease, but is also actionable under state tort law?

Because SVCC's nuisance and waste claims are based upon El Toro's failure to remove the mining residue from the leased property, conduct that SVCC in its proof of claim concedes constitutes a violation of the lease, we conclude that the § 502(b)(6) cap on a lessor's damages applies. Our conclusion is based upon the language of the Bankruptcy Code, the interpretations previously given this provision by this Panel, and, importantly, is required by the critical undisputed facts of this case.

1. The Language of the Code.

As always, our examination of the scope of the statutory cap on damage claims begins with the words of the statute. The critical language here is that part of § 502(b)(6) that applies a cap to "the claim of a lessor for damages resulting from the termination of a lease of real property . . . ."

This language is simple enough and is not ambiguous. The Code applies the cap to a lessor's claim for "damages." The words in the statute do not distinguish between a lessor's claims founded upon contract, tort, statute or some other legal basis. If the lessor holds a claim for "damages," the claim is capped. All kinds of damages claims are logically included within the reach of the cap. As a result, under a plain reading of the statute, there is no reason to infer a limitation on the type of damages a lessor may recover under the statute.

It is also significant that later, in the same subsection of

the Code, in constructing the formula for calculating the amount of the cap in each case, Congress refers to "the rent reserved" and to "any unpaid rent." 11 U.S.C. § 502(b)(6)(A), (B). See Koons Buick Pontiac GMC, Inc. v. Nigh, 125 S. Ct. 460, 466-67 (2004) (instructing that statutory construction is a "holistic endeavor" and that perceived ambiguity may be clarified by reading one statute in the light of the remainder of the statutory scheme). By using these more specific terms, presumably Congress intended there be a difference between rendering all the lessor's "damages," which are subject to the cap, and those kinds of damages used to calculate the actual amount of the cap in each case, using a formula based on "rent." See Kuske v. McSheridan (In re McSheridan), 184 B.R. 91, 96-100 (9th Cir. BAP 1995) (establishing a three-part test for determining which components of a lessor's claim constitute "rent reserved" for purposes of § 502(b)(6)(A)). We must assume that if Congress intended that the reach of the cap be limited solely to claims for "rent," or that the nature of the damage claim be limited at all, Congress would have expressly said so in the statute.

Instead, the only limitation in the damage cap is that the lessor's claim be one "resulting from the termination of a lease." In other words, to come within the cap, the lessee's failure to perform the lease must be the "cause in fact" of the lessor's damages. This language requiring a causal connection between the lessee's conduct and the lessor's damages does not require that the damages be based on breach of the lease, nor does it exclude damages claimed for state common law torts based

upon the debtor's conduct in violating the lease, if that conduct in fact caused the damages.

A broad reading of the scope of the cap on lessor damages is consistent with its purpose. As the Panel has previously observed, the statutory limit on a lessor's claim was intended by Congress to "[prevent] landlords from receiving a windfall as a result of the filing of the bankruptcy petition [by the lessee]." McSheridan, 184 B.R. at 97. Indeed, the cap reflects a balancing of interests struck by Congress by allowing a lessor "to be paid a reasonable sum without unfairly diluting or squeezing out other creditors." Redback Networks, Inc. v. Mayan Networks Corp. (In re Mayan Networks Corp.), 306 B.R. 295, 306 (9th Cir. BAP 2004) (Klein, J., concurring).

Obviously, the cap becomes important only when a lessor's damages recoverable under state law exceed the amount of the cap as calculated under the statute.[8] When it operates, the cap effectively denies a landlord payment of a claim otherwise

---

[8] Given the procedural status of this action, it would be speculative for the Panel to assume SVCC will prevail on the merits of its claims against El Toro. The issue here is, assuming SVCC holds valid claims against El Toro under its different theories, whether the amount of those claims would be capped. We are somewhat concerned that we are asked to decide an issue of law that may, or may not, be implicated in the final analysis. We acknowledge, though, SVCC's proof of claim alleges El Toro owes it "in excess of $23 million," an amount that would clearly exceed any cap calculated under § 502(b)(6). Therefore, resolving the legal question as to the applicability of § 502(b)(6) to SVCC's counterclaims will materially aid the bankruptcy court on remand. In addition, we understand the bankruptcy court has certified its decision as a final judgment under FRCP 54(b), applicable here via Rule 7054. See Dawson v. Washington Mut. Bank (In re Dawson), 390 F.3d 1139, 1145-46 (9th Cir. 2004) (considering similar factors in assessing appellate jurisdiction).

enforceable under state law. But the § 502(b)(6) cap is not remarkable in that regard. Through many provisions of the Code,[9] Congress has decided which creditor claims are to be paid, or not, in bankruptcy cases, or as in this case, how much creditors can recover. In adopting the § 502(b)(6) cap, Congress has exercised its judgment about the policies embodied in the Code. Because policy is implicated, the bankruptcy courts, in enforcing the Code, cannot appropriately alter the outcome, even if the results in a particular case may seem harsh. See Lamie v. United States Tr., 540 U.S. 526, 542 (2004).

In summary, the language of § 506(b)(6) cannot be read to exclude from the scope of the lessor's damages cap claims based on state tort law when the same conduct giving rise to those claims also amounts to a breach of the lease.

2. BAP Precedent.

The decisional law in this Circuit also counsels against any attempts to limit the broad scope of § 502(b)(6). In 1995, in a thoughtful analysis, the panel in McSheridan gave us clear guidance concerning the scope of the § 502(b)(6) cap. In that case, the BAP was asked to decide whether, upon rejection of a commercial real property lease in a bankruptcy case, a lessor's

---

[9] See, e.g., 11 U.S.C. §§ 502(b)(7) (capping the claim of an employee for damages resulting from the termination of an employment contract); 502(e)(1) (disallowing claims for reimbursement or contribution under certain conditions); 507(a)(3) (capping the amount of a priority claim for wages, salaries, or commissions) (to be re-codified as § 507(a)(4) under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 212, 119 Stat. 23, 51).

claims for unpaid utilities, repair and maintenance costs, expenses for replacement of an air conditioning system and the roof of the leased premises, and for insurance costs, all came within the cap. Although these were all charges that the lease required the lessee to bear, because they were not "rent reserved," the debtors objected to allowance of the lessor's claim. To resolve the dispute, the panel was required to decide whether these sorts of charges came within the scope of the § 502(b)(6) cap, and if so, how the amount of the cap should be calculated. The panel concluded that all the expenses claimed by the lessor came within the cap, and remanded the case to the bankruptcy court to decide, under a new test developed by the panel, the amount of the cap.

Admittedly, in McSheridan, the lessor did not argue, nor did the panel address, whether the tenant had committed one or more torts. Nor was there any claim made by the lessor in that case that the costs it sought to recover resulted from the debtor's violation of local government environmental or land-use regulations or ordinances. Instead, the lessor claimed the costs could be recovered based upon the lease.

Because of this, it may be tempting to distinguish, or putting it more bluntly, to disregard, the panel's decision as dicta in the face of the facts and arguments made in this appeal. It would be unwise, however, to read McSheridan so narrowly. In resolving the issues, the McSheridan panel decided how to interpret the same provisions of § 502(b)(6) that are at issue here. Its interpretive approach was essential to its holding. And in its reading of the Code, the McSheridan panel rejected the

very same interpretation offered, and authorities cited, by SVCC.

More specifically, the McSheridan panel discussed the decision of the bankruptcy court in In re Atlantic Container Corp., 133 B.R. 980 (Bankr. N.D. Ill. 1991), a decision relied upon by the lessor in this case. In Atlantic Container, the bankruptcy court held that a lessor's claim for repair and maintenance costs under the lease resulting from the lessee's physical neglect and damage to the leased property was not capped by § 502(b)(6) because the

> phrase "damages resulting from the termination of the lease" does not seem to contemplate the type of damages being sought here. The phrase suggests that § 502(b)(6) is intended to limit only those damages which the lessor would have avoided but for the lease termination. Any damages caused to the Premises by the Debtor's failure to fulfill its repair and maintenance obligations are unrelated to the termination of the lease.

McSheridan, 184 B.R. at 100 (quoting Atlantic Container Corp., 133 B.R. at 987). Because the damages caused by the lessee to the leased premises in Atlantic Container were not "prospective" and "had nothing to do with the long-term nature of the lease," the bankruptcy court concluded the cap should not apply.

McSheridan also carefully considered the bankruptcy court's decision in In re Bob's Sea Ray Boats, Inc., 143 B.R. 229 (Bankr. D.N.D. 1992). There, the lessor sought to recover not only unpaid rent, but asserted claims for damages inflicted on the premises by the lessee-debtor, and for the lessee's wrongful removal of light fixtures from the leased property's parking lot. Relying upon Atlantic Container, the bankruptcy court refused to apply the § 502(b)(6) cap to the claims for damage to the premises and removal of the lights because the cap "does not

address damages wholly collateral to the termination event—such things as waste, destruction or removal of leasehold property." 143 B.R. at 231.

The McSheridan panel declined to follow the approach of Atlantic Container Corp. or Bob's Sea Ray Boats. Instead, the panel opted for a broad interpretation of the scope of the cap. It noted that a broad cap fulfills the purpose of discharging the debtor from suits based upon violation of the lease and fixes the liability of the lessee. McSheridan, 184 B.R. at 101. The panel also noted that § 502(b)(6) must be read in concert with other provisions of the Code, including § 365(d)(3) (requiring the debtor to perform a lease only until it is assumed or rejected), § 365(g) (deeming rejection a breach of the lease), and § 502(g) (providing that a lease rejection claim is to be treated as a prepetition claim). Doing so, the panel observed:

> [R]ejection of the lease results in the breach of each and every provision of the lease, including covenants, and § 502(b)(6) is intended to limit the lessor's damages resulting from that rejection. The damages are those resulting from nonperformance of the debtor's obligations under the lease.

184 B.R. 102.[10]

The holding in McSheridan was not limited to its facts, nor did it depend upon the precise type of damages being asserted by the lessor. Fairly read, the holding of McSheridan was, as

---

[10] In a slightly different context, Judge Klein has expressed that § 502(b)(6) "is not ambiguous when one considers interrelated provisions [of the Code]" and that "[w]hat looks like ambiguity when § 502(b)(6) is viewed in isolation is clarified by other Bankruptcy Code provisions." In re Mayan Networks Corp., 306 B.R. at 303-04 (Klein, J., concurring).

stated in the panel's opinion, that "all damages due to nonperformance [by the lessee of the lease] are encompassed by [the § 502(b)(6) cap]." Id. To accept SVCC's arguments in this case, which are founded upon the same cases considered and rejected by the panel, would imply a limitation not found in the language of the Code, and it would require us to modify the McSheridan approach to interpreting this statute, which we are unwilling to do. As McSheridan made clear, "all damages" flowing from the debtor-lessee's conduct constituting "nonperformance" of the lease are capped by § 506(b)(6).

3. The Undisputed Material Facts.

Finally, the facts of this appeal compel reversal of the bankruptcy court's grant of summary judgment to SVCC concerning the damages cap. Though SVCC has invited us to do so, we cannot ignore these important undisputed facts. When they are considered, it becomes clear that any claims that SVCC could assert for damages for nuisance or waste based on El Toro's conduct in this case would also constitute a breach of the covenants of the parties' lease.

Before discussing those facts, it is important to recognize an issue we need not decide — whether there could ever be a situation in which a lessor should be allowed to assert a state law tort claim against its lessee that would be excluded from the § 502(b)(6) cap. In this regard, the analogies offered by SVCC in its briefing are inapt. This is not a case, as SVCC's approach suggests, where one party commits an intentional tort (or even a crime) against another while those parties, as a matter of coincidence, occupy the status of tenant and landlord.

Those are not our facts.

Here, we need only determine whether a lessor's claim for damages caused by a lessee's acts, which acts also constitute a breach of its lease, should be excluded from the reach of the § 502(b)(6) cap, simply because those same acts may constitute a state law tort, or because those acts also violate a state or local regulation or ordinance. When the issue is properly framed, it is apparent that if the cap is not applied, SVCC will succeed in a classic end-run around the will of Congress.

It is undisputed that El Toro (or its predecessor) had occupied and used the property in question since the 1960's, most recently pursuant to a 1988 written real property lease with SVCC's predecessor. That lengthy document comprehensively details El Toro's rights and duties as to the leased property. It is also important to recognize it was a long-term lease; its original term would not have expired until 1999. And in connection with SVCC's acquisition of the property, SVCC and El Toro agreed to extend the term of the lease indefinitely and to allow that it could be terminated only upon two years' notice.

Some of the lease terms that are critical in this appeal include:

– El Toro was allowed by the lease to mine and remove rock, sand, gravel and fill materials from the land. This provision contemplated that El Toro would wash sand from excavated materials, a process that created the "goo," "residue" or "debris" involved in this case.

– Incident to its operations, El Toro was authorized by the lease to store materials it mined from the land on the leased

premises. Fairly read, this provision authorizes El Toro to stockpile the residue.

– El Toro committed to remove "debris deposits" from the leased premises "no later than four (4) months following the date of termination [of the lease]." This provision reflects the parties' understanding that, upon termination of the lease, there may be stockpiles of residue remaining on the leased premises.

– In conducting its business operations on the leased property, El Toro promised to comply with all applicable federal, state and local laws, regulations and ordinances.

– And El Toro agreed to restore the grade of the leased premises, and to "rehabilitate" the property, so as to comply with a reclamation plan that had been approved by the county.

SVCC did not succeed to the lessor's interest under the lease until 1997. In other words, El Toro had been operating under the terms of the lease, mining material from the leased land, washing out saleable sand, and producing and storing residue clay on the property, for nearly a decade prior to SVCC's succession to Baker Ranch's interest under the El Toro lease. SVCC was presumably aware and approved of the nature of El Toro's operations, since in connection with acquiring the lease, SVCC agreed to an indefinite extension of the lease with El Toro. El Toro apparently continued in its use of the property in this fashion for several years after SVCC became its neighbor and landlord.

It was not until October 2002 that SVCC gave El Toro a written notice that it intended to forfeit the lease. In that notice, SVCC alleged that El Toro had breached the lease. In

particular, SVCC relied upon provisions of the lease requiring El Toro to comply with local laws, ordinances and regulations, and it contended El Toro had failed to do so because certain local laws allegedly required it to "regularly remove" the clay residue it was stockpiling on the property. SVCC also alleged in the notice that El Toro breached the lease terms requiring it to restore the property to conditions described in the county's reclamation plan, although the lease provides that this duty does not arise until expiration or termination of the lease.

El Toro's response to SVCC's notice was to seek chapter 11 relief, and in that bankruptcy case, to reject the lease. In its proof of claim, SVCC recites the same lease provisions referenced in the notice it had given to El Toro, and alleges its damages are based upon breach of the lease. It seeks recovery of in excess of $23 million to "[remove] the debris and deleterious material stockpiled by the debtor in violation of the permits, Reclamation Plan, and Lease . . . ."[11]

Based upon this record, it appears clear that SVCC's claim is based upon El Toro's storage of, and failure to remove, the residue from the leased premises, allegedly in violation of county rules and ordinances. Nor is there any question, at least in SVCC's view, that El Toro's conduct is expressly prohibited by

---

[11] There is no indication in the record that SVCC has ever amended its proof of claim to show that, in addition to breach of the lease, SVCC seeks to recover against El Toro for state law torts or for El Toro's violations of local law. Apparently the first mention in the bankruptcy court record of SVCC's contention that it is asserting claims for other than breach of the lease is in SVCC's answer and amended counterclaim filed in the adversary proceeding from which this appeal originated.

the various provisions of the parties' lease cited above.[12] Again, contrary to SVCC's assertions, this is not a case involving a lessee's commission of a tort against another person who, coincidentally, happens to be the tortfeasor's landlord. Instead, the facts more closely resemble the Atlantic Container and Bob's Sea Ray Boats cases, where the debtor-lessee had committed lease violations (such as neglecting the premises, or "stealing" light fixtures) that may have also given rise to state law tort claims for nuisance, waste, trespass, and although not alleged here, perhaps conversion.

Simply put, the undisputed facts in this appeal show the same conduct that SVCC alleges constitutes nuisance and waste in this case also constitutes a breach of the lease.

4. Based upon the statute, case law, and facts of this case, the damage cap in § 502(b)(6) applies to SVCC's counterclaims arising under state tort law.

El Toro's rejection of the lease in its bankruptcy case is deemed as a matter of bankruptcy law to constitute a breach of that lease immediately before the date of the filing of the

---

[12] It is disconcerting that SVCC, which purchased adjoining property and the lessor's ownership interest more than ten years after El Toro began its business on the leased land, could recover, years later, under state tort law for El Toro's continuing activities. It is also unclear whether SVCC, as a private party, has standing to enforce state or local mining laws and regulations. The bankruptcy court rejected El Toro's standing arguments because it failed to provide legal support for them. Although the court's reaction to such a lackadaisical approach is understandable, on remand the bankruptcy court is reminded that "federal courts are under an independent obligation to examine their own jurisdiction, and standing 'is perhaps the most important of [the jurisdictional] doctrines.'". FW/PBS, Inc. v. City of Dallas, 493 U.S. 215, 231 (1990) (quoting Allen v. Wright, 468 U.S. 737, 750 (1984)).

petition. 11 U.S.C. § 365(g)(1). As a result, SVCC's claim against El Toro for failure to remove the residue stockpile is a prepetition claim. 11 U.S.C. § 502(g); K-4, Inc. v. Midway Engineered Wood Prods., Inc. (In re Treesource Indus., Inc.), 363 F.3d 994, 998 (9th Cir. 2004).

The § 502(b)(6) damage cap should apply because SVCC's claim against El Toro for its alleged failure to comply with local laws and to remove the residue stockpile is one for damages resulting from El Toro's rejection (i.e., the breach) of the lease. That El Toro's acts may also give rise to claims by SVCC founded on state law tort does not matter.

The language of § 502(b)(6) is broad and includes all claims by a lessor for "damages," provided those claims result from termination of the lease. Sound precedent from this panel instructs that the lease cap applies to all damages flowing from a breach of the covenants of a lease, and not just to claims for unpaid "rent." That same case law rejects the approach taken by other courts, and invoked by SVCC here, that the cap does not apply to "collateral" claims for infliction of damages to the leased premises or for conversion of leasehold improvements and furnishings. And finally, the notice SVCC gave to El Toro, and the proof of claim filed in El Toro's bankruptcy case, both establish that SVCC's claim is for conduct constituting a breach of the lease.

The bankruptcy court erred when it decided that any claims SVCC can assert for nuisance or waste under state law are excepted from the § 502(b)(6) cap. We reverse that decision.

B. Did the bankruptcy court err in dismissing SVCC's trespass claim?

SVCC argues in its cross-appeal that the bankruptcy court erred procedurally in dismissing its counterclaim for trespass. It complains that El Toro did not request such relief in its motion and the issue was raised so late in the proceedings that it did not have adequate notice its trespass claim had been called into question. Alternatively, SVCC argues the bankruptcy court misapplied the law regarding the merits of its trespass action.

1. Did the court commit procedural error?

A trial court generally may not grant summary judgment on a claim when a party has not requested it, Kelly v. Arriba Soft Corp., 336 F.3d 811, 822 (9th Cir. 2003), unless the opposing party has had a full and fair opportunity to ventilate the issues involved in the motion. United States v. Grayson, 879 F.2d 620, 625 (9th Cir. 1989). In this case, SVCC requested injunctive relief to remedy El Toro's alleged trespass based on El Toro's post-rejection failure to remove the residue. El Toro moved for summary judgment arguing equitable relief was not available to SVCC, a contention which surely put the trespass claim in the spotlight. Apparently SVCC perceived that El Toro's motion for summary judgment placed its trespass claim in jeopardy because, in its opposition papers, SVCC argued its trespass claim should proceed to trial. Apparently, SVCC's contentions prompted El Toro to include in its reply brief a more direct attack on the substance of the trespass claim, as opposed to just the remedy sought, albeit in a footnote.

On this record, we are persuaded that the bankruptcy court afforded SVCC a "full and fair opportunity to ventilate" its position before it ruled on the validity of SVCC's trespass claim. SVCC submitted to the court its arguments why its trespass claim should be allowed to go forward. Since SVCC was fairly heard, the bankruptcy court did not commit a procedural error in granting summary judgment.

2. Did the bankruptcy court incorrectly apply state law?

The bankruptcy court did not discuss its basis for dismissing SVCC's trespass claim. Rather, it simply agreed with El Toro's contention that "trespass will not lie under the facts of this case." El Toro had argued that because it had been in rightful possession of the property prior to termination of the lease, it could not be liable for trespass under California law because its actions were not "an invasion of the interest in the exclusive possession of land," citing Capogeannis v. Superior Court, 15 Cal. Rptr. 2d 796, 799 (1993). SVCC contends that El Toro's post-rejection failure to remove the residue and equipment constitutes a wrongful occupation of Plot 1, and that the bankruptcy court erred in summarily dismissing its trespass claim because the uncontroverted evidence established trespass. In the alternative, SVCC argues that there are issues of material fact with respect to this cause of action.

Trespass is "an unlawful interference with the possession of property." Mangini v. Aerojet-Gen. Corp., 281 Cal. Rptr. 827, 837 (Cal. Ct. App. 1991).

> A trespass may be committed by the continued presence on the land of a structure, chattel, or other thing which the actor or his predecessor in legal interest

> has placed on the land
> (a) with the consent of the person then in possession of the land, if the actor fails to remove it after the consent has been effectively terminated, or
> (b) pursuant to a privilege conferred on the actor irrespective of the possessor's consent, if the actor fails to remove it after the privilege has been terminated, by the accomplishment of its purpose or otherwise.

Restatement (Second) of Torts § 160 (1965). See also Mangini, 281 Cal. Rptr. at 837. California case law supports the proposition that a holdover tenant may be liable to a landlord for trespass. Fragomeno v. Ins. Co. of the W., 255 Cal. Rptr. 111, 115-17 (Cal. Ct. App. 1989), overruled on other grounds by Vandenberg v. Superior Court, 88 Cal. Rptr. 2d 366 (Cal. 1999); Peter Kiewit Sons' Co. v. Richmond Redevelopment Agency, 223 Cal. Rptr. 728, 734 (Cal. Ct. App. 1986); Stephens v. Perry, 184 Cal. Rptr. 701, 706 n.4 (Cal. Ct. App. 1982).

In light of these authorities, that El Toro was in lawful possession of Plot 1 prior to termination of the lease does not necessarily preclude SVCC's trespass claim targeting El Toro's failure to remove its property (i.e., the "goo") when it surrendered the premises. In this respect, the bankruptcy court's dismissal of the trespass claim was erroneous and must be reversed.

On remand, the bankruptcy court must also address several questions we do not reach. Of course, while SVCC may proceed on its trespass counterclaim, we express no opinion on the merits of that claim. Moreover, if SVCC prevails on more than one of its counterclaims, the bankruptcy court, prior to applying the § 502(b)(6) cap, may be required to analyze the damages available to SVCC under each theory and to reconcile the result in light of

the prohibition under California law against double recovery. See McCall v. Four Star Music Co., 59 Cal. Rptr. 2d 829, 831 (Cal. Ct. App. 1996) (discussing rule against double recovery); Stoiber v. Honeychuck, 162 Cal. Rptr. 194, 209 (Cal. Ct. App. 1980).

And the parties have raised yet another issue that we cannot fully resolve. El Toro argues that California law prohibits a party from recovering in tort if the allegedly tortious conduct is covered by the terms of a contract (i.e., a lease). As a general principle, El Toro's argument correctly reflects the law. JRS Prods., Inc. v. Matsushita Elec. Corp. of Am., 8 Cal. Rptr. 3d 840, 849 (Cal. Ct. App. 2004) ("a party to a contract cannot recover damages in tort for breach of contract"). But the same conduct that constitutes breach of a contract may also amount to an actionable tort if the conduct violates a duty that is independent of the contract and arises from principles of tort law. Erlich v. Menezes, 981 P.2d 978, 983 (Cal. 1999). Because the bankruptcy court did not reach this issue, we will not address it either.

However, while the trespass claim must be remanded for trial, it is proper on this record for us to conclude that if SVCC prevails in recovering an award of money damages against El Toro,[13] any damages awarded to SVCC would be subject to the cap in § 502(b)(6). This conclusion results from the analysis above

[13] This presumes SVCC forgoes its claim for equitable relief since SVCC did not appeal the bankruptcy court's ruling that it is not entitled to an injunction because it has an adequate remedy at law.

regarding SVCC's counterclaims for nuisance and waste. Because SVCC's trespass claim against El Toro stems from the lessee's failure to remove the stockpile at lease termination, a clear violation of the terms of the parties' lease, the cap applies.

And even though El Toro's alleged failure to remove the residue results from its conduct during the bankruptcy case, SVCC's trespass damages would nonetheless constitute a nonadministrative, prepetition claim. In Treesource Indus., the Ninth Circuit addressed whether a lessor's claim for the debtor/lessee's failure to restore leased property to its pre-lease condition upon termination should be considered a prepetition or postpetition claim. 363 F.3d at 995–96 (considering administrative expense priority under § 503). The lease required the debtor to remove, upon termination, all improvements it made during the term of the lease, including footings, floors, and foundations, and to regrade the land to its natural contours. Id. at 996. The debtor failed to remove a concrete slab upon rejection of the lease. Although the lessor in Treesource Indus. did not assert a trespass claim, the court provided a straightforward analysis. Because the debtor's obligation to restore the leased property was triggered, under the terms of the lease, upon its "termination or expiration," and because the debtor's rejection of the lease terminated it, the lessor's claim for the debtor's failure to remove the concrete slab was a prepetition claim. Id. at 998.

That same logic applies with equal force to the facts here. El Toro's obligation to vacate Plot 1 and restore the property as detailed in the reclamation plan was triggered, under ARTICLE 23,

upon the lease's expiration or termination. El Toro's rejection of the lease terminated it. The termination gave rise to El Toro's obligation to remove the mining waste, a corollary of which is El Toro's liability under state trespass law for its failure to do so. Viewed this way, any harm SVCC suffers as a result of the stockpiled waste, regardless of the legal theory employed, is a result of the termination of the lease, is a prepetition claim, and is therefore subject to the damage cap in § 502(b)(6).

VI. CONCLUSION

The bankruptcy court erred in deciding that SVCC's nuisance and waste claims were not limited by the cap on lease termination damages in § 506(b)(6). The bankruptcy court also erred by dismissing SVCC's trespass claim. The decision of the bankruptcy court is REVERSED and this adversary proceeding is REMANDED to the bankruptcy court for further proceedings consistent with this opinion.

BRANDT, Bankruptcy Judge, concurring:

Confined by our prior authority, In re McSheridan, 184 B.R. 91 (9th Cir. BAP 1995), I reluctantly concur, but I find the reasoning of In re Atlantic Container Corp., 133 B.R. 980 (Bankr. N.D. Ill. 1991) and In re Bob's Sea Ray Boats, Inc., 143 B.R. 229 (Bankr. D.N.D. 1992), more persuasive.

I disagree that the language of the statute is plain, and in this case, the result is potentially very harsh. Further, it is

perverse: to enforce tenants' guarantees of lease obligations other than those ordinarily understood by business folk to be "rent" in state proceedings, or security for those guarantees, a lease must make breaches of those obligations defaults. But then if the tenant becomes a debtor in bankruptcy, an expansive interpretation of the cap of 11 U.S.C. § 506(c) vitiates the perfectly reasonable protections so bargained for. It is also ironic that, were El Toro a trespasser, SVCC's claim would not be limited by the cap. Finally, I see no principled distinction between violations of covenants to comply with environmental laws and violation of covenants not to engage in tortious or criminal conduct — all of those obligations arise independently of the landlord-tenant relationship.

Were I free to follow the contrary authority, I would do so.

KLEIN, Bankruptcy Judge, concurring in result:

I reluctantly concur in the result and share Judge Brandt's concerns. My doubts are substantive and procedural.

I assume, for purposes of analysis, that McSheridan controls, even though that decision did not deal with a bargained-for restore-the-premises post-expiration obligation. Our McSheridan panel dealt with how to determine whether particular expenses, not expressly denominated as "rent," nevertheless qualified as "rent reserved by" a so-called "triple-net" lease and rejected arguments that non-rent expenses might be recovered on a tort theory.

A

While I agree that re-branding contractual obligations as "torts" is not a promising strategy for eluding the § 502(b)(6) cap, thinking about the problem head-on as a matter of contract gives pause.

I am not confident that a bargained-for contractual restore-the-premises obligation following the end of a lease by either expiration or termination is necessarily subsumed by § 502(b)(6). It may, instead, be an independently cognizable obligation. The language of the statute appears to include a causation requirement linked to termination of a lease ("damages resulting from the termination of a lease of real property"). A contractual restore-the-premises obligation that applies regardless of whether the lease terminates or merely expires arguably is an obligation that does not "result from" termination.

As noted in the majority opinion, the § 502(b)(6) cap reflects a balancing of interests struck by Congress by allowing a lessor a reasonable sum without unfairly diluting or squeezing out other creditors by virtue of the common-law measure of damages that permits a landlord to obtain, subject to a duty of mitigation, the full balance of rent owed under the lease. In a functional sense, the cap amounts to a conclusive presumption, as between landlord and estate, that the landlord will have fully mitigated all future lost-rent damages once it receives the amount of the cap.

A restore-the-premises obligation does not fit comfortably within either the language or the policy of § 502(b)(6). Hence,

it may be doubted that the second half of the McSheridan analysis, which appears to say that all sums owed pursuant to a lease contract following lease termination are subsumed by the capped rent claim, would survive scrutiny by the court of appeals. McSheridan, 184 B.R. at 100-02.

If the lease had expired by its terms before the bankruptcy case was filed, it is doubtful that § 502(b)(6) would cap the full restoration obligation under a lease contract. Similarly, if the lease were to expire by its terms within one year after the filing of the petition, it is not clear that the cap would impair the contractual restoration obligation. If these doubts are meritorious, then it arguably ought not to matter that the lease was terminated prematurely.

B

As a matter of procedure, the trial court's certification of finality pursuant to Federal Rule of Civil Procedure 54(b), as incorporated by Federal Rule of Bankruptcy Procedure 7054(a), directing entry of judgment makes the judgment that was rendered on partial summary judgment final and immediately appealable. 28 U.S.C. § 158(a)(1).

Nevertheless, there is reason for caution. This appeal appears to be inextricably intertwined with numerous other as-yet unresolved facets of the larger dispute between the parties. It appears that, in reality, it was the landlord who did the terminating. Each party continues to have claims against the other. There may be issues of setoff and other complications that add up to create a settlement imperative.

The consequence of all this is that, while we must exercise jurisdiction, the circumstances are inherently interlocutory. Our ruling may be more advisory than definitive. I am reluctant to make definitive determinations in speculative circumstances about a very complex problem.

Hence, I CONCUR IN THE RESULT.