UNITED STATES BANKRUPTCY COURT
For the Southern District of Iowa

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| In the Matter of | : | |
| | : | Case No. 90-3112-C H |
| FITNESS WORLD WEST, INC., | : | |
| | : | Chapter 11 |
| Debtor. | : | |

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**ORDER--GRANTING MOTION FOR RELIEF FROM STAY**

A hearing was held on January 22, 1991, on the creditor's motion for relief from stay. James L. Spellman and Martin E. Spellman appeared on behalf of the creditor and Ronald L. Hansel appeared on behalf of the Debtor. At the conclusion of the hearing, the court took the matter under advisement and now considers it fully submitted.

This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(G). The Court, upon review of the motion, resistance, evidence submitted and arguments of counsel, now enters its findings and conclusions pursuant to Fed. R. Bankr. P. 7052.

**FINDINGS OF FACT**

1. On September 11, 1986, Fitness World West, Inc. (Debtor) and Dr. Paul From (creditor) entered into a lease agreement. The parties signed an amendment to the lease agreement on September 16, 1987.

2. On October 16, 1990, the creditor sent the debtor a notice of default and intent to terminate lease. The notice was sent by certified mail and it indicated the debtor was in default for failure to pay the monthly rent due by October 15, 1990. The notice stated the Debtor had 10 days to cure the default and if the default was not cured it was the landlord's intention to terminate the lease and take possession of the property.

3. A three-day notice to quit was served on the debtor on November 13, 1990, and another three-day notice to quit was sent to the Debtor by certified mail on November 16, 1990. Other than the form of delivery, the only difference between the two notices appears to be that the latter notice incorrectly refers to the Debtor's address as 2100 Westown Parkway. However, both the exhibit attached to the notice and the receipt for certified mail refer to the correct local address which is 3200 Westown Parkway.

4. On November 16, 1990, Debtor was served with a notice of termination of tenancy and demand for rent. The notice stated the creditor had terminated the Debtor's tenancy of the premises as of November 1, 1990.

5. On November 21, 1990, the creditor filed a petition for forcible entry and detainer in the Iowa District Court for Polk County.

6. The trial court decree dated December 5, 1990, and

filed at 8:12 a.m. on December 6, 1990, ordered the Debtor to vacate the premises with execution for possession to issue immediately. The Court found the Debtor had breached the terms of the lease by failing to make timely rental payments, the lease had been terminated and the debtor had continued in possession and was holding over after termination of the lease.

7. A warrant of removal and forcible entry and detainer was filed on December 6, 1990, at 8:12 a.m. The warrant ordered the Polk County Sheriff to execute the court's judgment and remove the Debtor from the premises and put the creditor in possession.

8. At 9:48 a.m. on December 6, 1990, the Debtor filed a Chapter 11 petition with the bankruptcy court.

9. On December 11, 1990, the creditor filed a motion for relief from stay seeking to proceed under the Iowa District Court judgment with execution for possession of the premises. As alternative relief the creditor requested that the debtor be required to provide him with adequate protection for the value of his interest in the property. Debtor subsequently resisted the motion.

10. The Debtor filed a notice of appeal from the decision of the Iowa District Court on January 3, 1991. An appeal bond was filed on January 7, 1991.

11. Article III section 4 of the lease agreement

prohibits the tenant from setting off any obligations of the landlord against the tenant's payments of rent. Article XV Section 1 provides the nonpayment of rent is grounds for terminating the lease.

## CONCLUSIONS OF LAW

Relief from stay is governed by 11 U.S.C. § 362(d) and may be granted:

> (1) for cause, including the lack of adequate protection of an interest in property of such party in interest; or
>
> (2) with respect to a stay of an act against property under subsection (a) of this section, if--
>
> (A) the debtor does not have an equity in such property; and
>
> (B) such property is not necessary to an effective reorganization.

The creditor asserts the debtor-in-possession could not assume or assign the lease of the nonresidential real property because it was terminated under state law prior to entry of the order for relief. See 11 U.S.C. § 365(c)(3). The creditor contends that since the lease was terminated and the Debtor no longer has an interest in the leasehold "cause" exists for granting relief from stay. The Debtor claims the lease was not terminated as it was entitled to a credit for overpayments pertaining to common areas and taxes and it had made all rental payments.

State law governs whether a lease has terminated pre-petition. See In re Emilio Cavallini, Ltd., 112 B.R. 73, 76 (Bankr. S.D.N.Y. 1990); In re Mako, Inc., 102 B.R. 814, 817 (Bankr. E.D. Okla. 1988); In re Memphis - Friday's Associates, 88 B.R. 830, 834 (Bankr. W.D. Tenn. 1988). A lease agreement which is validly terminated pursuant to state law may not be resurrected by filing a bankruptcy petition. In re Hickory Point Indus., Inc., 83 B.R. 805, 806 (M.D. Fla. 1988); In re Santos Borrero, 75 B.R. 141, 142 (Bankr. D. P.R. 1987); In re Trang, 58 B.R. 183, 189 (Bankr. S.D. Tex. 1985); In re Horn & Hardart Baking Co., 19 B.R. 597, 598 (Bankr. E.D. Pa. 1982). A court may not revive a terminated lease simply because it is important or essential to a debtor's reorganization efforts. See Mako, 102 B.R. at 818; In re Crabb, 48 B.R. 165, 168 (Bankr. D. Mass. 1985); In re Bricker, 43 B.R. 344, 348 (Bankr. D. Ariz. 1984); In re Maxwell, 40 B.R. 231, 238 (N.D. Ill. 1984).

Iowa law provides termination of leases can be made contractual. Gendler Stone Products Co. v. Laub, 179 N.W.2d 628, 631 (Iowa 1970). Parties may, and frequently do, include in leases certain provisions giving an election and method for cancellation. Id.

Article XV of the lease agreement at issue in this case provides the landlord may terminate the lease upon the failure of the tenant to pay an installment of rent when due provided

the tenant has not remedied the default within 10 days. The creditor gave the debtor a notice of default and intent to terminate lease on October 16, 1990. When the Debtor did not cure the default within 10 days, the creditor had a three-day notice to quit and a notice of termination of tenancy served on the Debtor.

The notices served on the Debtor manifested the creditor's clear and unequivocal intent to terminate the lease. See Jack Morwitz Co. Management v. Walker, 429 N.W.2d 127, 130 (Iowa 1988) (termination in the context of a residential lease). After the Debtor had failed to cure the default within the time allowed by the lease, the creditor filed a petition for forcible entry and detainer which is a remedy provided by Iowa law when a lessee holds over after the termination of a lease. Iowa Code § 648.1(2) (1989).

The district court for Polk County held a trial on the petition for forcible entry and detainer and found the Debtor had breached the terms of the lease by failing to make timely rental payments. The Court found the Debtor was properly served with a notice to terminate the tenancy and notices to quit. The Court found the lease had been terminated and the Debtor had continued in possession holding over after termination of the lease. The Debtor was ordered to vacate the premises and a warrant of removal and forcible entry and detainer was issued.

A federal court must give full faith and credit to the records and judicial proceedings of any state. 28 U.S.C. § 1738. The state trial court held a trial on whether the lease was terminated and the creditor asserts that decision should bar further relitigation of the issue by this court. See generally, In re Neville, 118 B.R. 14, 17 (Bankr. E.D.N.Y. 1990), (a state court judgment terminating a lease and awarding possession to the landlord has preclusive effect in the bankruptcy context and a bankruptcy court should not undertake an independent review of issues previously decided in the state court).

The Debtor, however, has appealed the decision of the district court and claims it has no res judicata effect while on appeal. "The question whether the pendency of an appeal from a judgment destroys its effect as res judicata is governed by the law of the sovereign whose court has rendered the judgment." 21 Federal Procedure, L.Ed. § 51:191 (1984). Thus, where a prior judgment was rendered in a state court, the law of the state is binding on the federal courts as to the finality of the state judgment pending appeal therefrom. Id. The general rule according res judicata effect to a judgment notwithstanding a pending appeal is inapplicable when the proceeding on review is de novo. Id.

While Iowa case law suggests a ruling is res judicata while on appeal, Johnson v. Ward, 265 N.W.2d 746, 749 (Iowa

1978); Shaw v. Addison, 236 Iowa 720, 727, 18 N.W.2d 796, 800 (1945), the Eighth Circuit has indicated a state court judgment on appeal is not given preclusive effect if it is subject to de novo review. See Silent Automatic Sales Corp. v. Stayton, 45 F.2d 476, 477 (1930); Ransom v. City of Pierre, 101 F. 665, 669 (8th Cir. 1900). An action for forcible entry and detainer is an equitable action subject to de novo review. Roshek Realty Co. v. Roshek Bros. Co., 249 Iowa 349, ___ 87 N.W.2d 8, 10 (1957); Iowa R. App. P. 4.

Rather than determine the preclusive effect of an Iowa equity action pending appeal, this Court has reviewed the evidence and exhibits submitted and concludes, that apart from any preclusive effect the state district court judgment may have, the evidentiary record before this court indicates the lease was terminated due to the Debtor's nonpayment of rent. The lease terminated prior to the filing of the Debtor's bankruptcy petition. The Debtor no longer had any interest in the leasehold at the time the petition was filed and this constitutes "cause" for granting relief from the stay under § 362(d)(1). See In re Pagoda Int'l, Inc., 26 B.R. 18, 20 (Bankr. D. Md. 1982).

IT IS HEREBY ORDERED that the parties' lease agreement was terminated under Iowa law prior to the filing of Debtor's bankruptcy petition and the creditor is entitled to relief from the stay in order to proceed under the judgment of the

Iowa District Court for Polk County with execution of the warrant of removal for possession of the premises.

Dated this 4th day of March, 1991.

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Russell J. Hill
U.S. Bankruptcy Judge