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Matter In Bankruptcy?

[Executory Contracts -- What Are They And Why Do They Matter In Bankruptcy?](#)

Posted on July 18, 2006 by [Bob Eisenbach](#)

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If you start talking to a bankruptcy lawyer, before long you'll probably hear them use the term "executory contract." Often they'll act as though people use the term everyday. The truth is that bankruptcy lawyers are just about the only lawyers – much less business people -- who ever talk about executory contracts. (I confess I do it too, but there's a really good reason.)

So what is an executory contract? The concept is fairly simple. It's a contract between a debtor and another party under which both sides still have important performance remaining. Put another way, if either side stopped performing the contract it would be an actual breach of contract.

Examples of executory contracts (and some common reasons why they might be executory) include:

- Real estate leases (tenant has to pay rent/landlord has to provide space)
- Equipment leases (lessee has to pay rent/lessor has to provide equipment)
- Development contracts (development work required/payment required on milestones), and
- Licenses to intellectual property (licensee can use only within scope of license/licensor must refrain from suing for licensed uses).

Having cleared up the definition, the next question is why executory contracts seem to matter so much in bankruptcy. (The debtor even has to list them separately in its [bankruptcy schedules](#).)

The short answer is that they are treated differently from general unsecured claims in three important ways.

- *First*, a debtor (or a bankruptcy trustee) gets to decide whether to agree to perform or refuse to perform its obligations under an executory contract. In bankruptcy parlance, agreeing to perform translates to "assumption" of the contract and refusing to perform translates to "rejection" of the contract.

- *Second*, while the debtor is thinking about what to do, you – the non-debtor party to an executory contract – have to keep on performing as if no bankruptcy had been filed. (You do have some options if this puts a burden on your business but you will need an attorney to help you sort them out.)
- *Third*, if the debtor assumes the executory contract – here’s the good news -- the debtor has to pay (“cure”) in full any payment or other defaults and show that it can actually perform in the future too. If the debtor wants to assume and assign the executory contract to someone else, commonly a buyer of its assets, at a minimum the debtor has to cure any defaults and the buyer has to show that it can actually perform under the contract in the future.

Except for commercial real property leases (which are treated differently -- stay tuned for another post on that topic), executory contracts must be assumed or rejected within 60 days of the filing of the bankruptcy petition in a Chapter 7 liquidation case and prior to the time a plan of reorganization is confirmed in a Chapter 11 case. The bankruptcy court can change these deadlines but otherwise these dates apply.

Be forewarned: The specific bankruptcy rules governing executory contracts are complex. If you think your agreement may be an executory contract, to protect your rights be sure to get advice from a bankruptcy attorney as soon as the debtor files bankruptcy.