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UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO

U.S. BANKRUPTCY COURT
ALBUQUERQUE, NM

In re

FURR'S SUPERMARKETS, INC.,

Case No. 11-01-10779-SA

Chapter 11

Debtor.

**Response to Objections to Debtor's
Separate Treatment of Certain Equipment Leases**

The Debtor seeks to separately assume or reject certain equipment lease schedules. Each schedule is separately executed and related to the lease of specific equipment. The Debtor's rent obligation under each schedule is plainly set forth and each schedule has slightly different terms. The obligations under each schedule are interrelated only in the loose sense that each schedule involves the lease of equipment from one party: Finova Capital Corporation.¹ Nonetheless, Finova has objected to the Debtor's proposed treatment of its leases.

The United States Supreme Court has explained that "[w]hether a number of promises constitute one contract or more than one is to be determined by inquiring 'whether the parties assented to all the promises as a single whole, so that there would have been no bargain whatsoever, if any promise or set of promises were

¹ MDFC Equipment Leasing has conceded that the Debtor may separately assume or reject its leases on a schedule by schedule basis, and the Debtor has reached an agreement with the other equipment lessors.

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struck out."² Finova does not argue that "there would have been no bargain whatsoever" if any single schedule was not part of the parties' transactions.³

In fact, each schedule has all the terms needed to be deemed an independent contract under the only Court of Appeals opinion to address this issue. Accordingly, the Court should overrule the Finova Objection and rule that each equipment lease is comprised of several independent agreements, each of which the Debtor may separately assume and assign, or reject.

1. *Integration Clauses Are Inapposite*

Finova points to the integration clauses in the agreements to support its argument that the parties "plainly" intended a single agreement. But integration clauses simply define the scope of the parties' agreement, and limit the documents a court may consider when interpreting that agreement.⁴ Integration clauses thus have no bearing on whether a particular agreement is, in fact, comprised of several distinct contractual obligations.⁵

² *United States v. Bethlehem Steel Corp.*, 315 U.S. 289, 298 (1942) (quoting Williston on Contracts at §§ 863).

³ As discussed below, Finova's cross-default provisions are plainly unenforceable in Chapter 11.

⁴ E. ALLAN FARNSWORTH, *CONTRACTS* § 7.3, at 436 (3d. ed. 1999).

⁵ *In re Plitt Amusement Co. of Washington Inc.*, 233 B.R. 837, 846 (Bankr. C.D. Ca. 1999) ("The purpose of an integration clause of this type is to

(continued...)

2. *Under A Proper Application of Gardinier, the Schedules are Distinct Agreements*

In *Gardinier*, the Eleventh Circuit found two contracts in a single written agreement: one for the sale of real property, the other to pay a broker in connection with that sale.⁶ The court developed a three-part test that has become the standard for determining the separateness of related agreements.⁷

Under this test, a court should consider (i) whether the nature and purpose of the obligations differ, (ii) whether the consideration for the obligations is separate and distinct, and (iii) whether the obligations of the parties are interrelated. Long before the development of the *Gardinier* test, the second factor – "separate and distinct" consideration – was recognized as the most important factor in determining whether a contract is divisible.⁸

⁵ (...continued)
prevent the introduction of parol evidence of other agreements not contained in a particular instrument. This is a wholly separate issue from whether the various instruments constitute a single agreement for the purposes of assumption or rejection. Thus this provision is irrelevant to the dispute before the court.").

⁶ *In re Gardinier*, 831 F.2d 974 (11th Cir. 1987).

⁷ *See In re Pollock*, 139 B.R. 938, 940 (B.A.P. 9th Cir. 1992).

⁸ *See, e.g., Bianchi Bros., Inc. v. Gendron*, 198 N.E. 767, 770 (Mass. 1935) ("An important factor in the determination of the question is whether the consideration is stated to be given for each part as a separate unit or whether there is a single consideration covering the various parts.")

The Finova equipment schedules at issue meet each element of the *Gardinier* test, and are therefore properly treated as separate agreements. First, the nature of each schedule is inherently different, as each schedule relates to a distinct set of leased equipment. Similarly, the Debtor's obligations under each schedule are distinct, as each schedule sets forth different terms and conditions for the lease.⁹ Second, the consideration for the obligations under each schedules is separate and distinct. Each schedule separately indicates the monthly rent due for the equipment set forth on that schedules. Finally, the obligations under the schedules are not interrelated. Indeed, Finova's equipment schedules were separately executed at various times between January 1997 and November 1999, undermining any argument that the obligations were dependant on each other.

Atlantic Computer Systems, where the court considered an equipment lease under *Gardinier*, and refused to allow the debtor to separately reject one part of that lease, does not support the argument that the Debtor may not separately assign or reject the schedules.¹⁰ *Atlantic Computer Systems* involved the debtor's attempt to separate a "Flexlease" from an equipment schedule and master lease. Unlike the

⁹ For example, the schedules are indexed at different percentages above the applicable Treasury Note. See ¶ 6 ("Indexing") of each schedule.

¹⁰ See *Pieco, Inc. v. Atlantic Computer Systems, Inc. (In re Atlantic Computer Systems, Inc.)*, 173 B.R. 844 (S.D.N.Y.1994).

present case, the Flexlease applied to the very same equipment covered by the equipment schedule, and the debtor owed no distinct consideration under the Flexlease.

Importantly, the court noted that

it is clear to the Court that all thirteen of the lease documents – the Master Lease, the six Equipment Schedules, and the six Flexleases cannot be considered all to comprise one single agreement. At best, from Picco's perspective, there are six single agreements, each consisting of the Master Lease and one Equipment Schedule and that Equipment Schedule's correspondingly numbered Flexlease.¹¹

In short, the *Atlantic Computer Systems* court's analysis is entirely consistent with the Debtor's proposed treatment of the Finova equipment schedules.

3. *Finova's Cross Default Clauses Are Unenforceable*

It is well-settled that, in the bankruptcy context, cross-default provisions are impermissible restrictions on assumption and assignment.¹² Accordingly, these provisions are unenforceable and will not consolidate related agreements for purposes of assumption or rejection under section 365.¹³

¹¹ *Id.* at 849.

¹² *See, e.g., In re Plitt Amusement Co. of Washington Inc.*, 233 B.R. 837, 847 (Bankr. C.D. Ca. 1999) (collecting cases); *In re Wheeling-Pittsburgh Steel Corporation*, 54 B.R. 772, 777-79 (Bankr. W.D.Pa. 1985) (where enforcement of the cross-default provision would conflict with the debtor's ability to assume the contract, the provision will not be enforced).

¹³ *See EBG Midtown South Corp. v. McLaren/Hart Environmental Engineering*
(continued...)

In *Sambo's Restaurants, Inc.*,¹⁴ the leading case on cross-default provisions, each store lease had a cross-default provision that tied to a master agreement which, the landlord argued, had to be assumed or rejected as a whole. The bankruptcy court permitted the debtor to reject two of ten restaurant leases, and reserve decision on the remainder. Thus, Finova's argument that, as a result of the cross-default provision, the Debtor must cure all defaults – even if the Debtor intends to reject a particular schedule – is without merit.

The *Kopel* decision,¹⁵ cited by Finova in support of its argument, does not contradict this conclusion. That court recognized that "cross-default provisions are inherently suspect."¹⁶ The court concluded, however, that the agreements at issue – all executed as part of the sale of a business – were so interlaced that they were, effectively, one agreement and enforcement of the cross-default provision would not offend the policies of the Bankruptcy Code.

¹³ (...continued)
Corp. (In re Sanshoe Worldwide Corp.), 139 B.R. 585, 597 (S.D.N.Y. 1992),
aff'd, 993 F.2d 300 (2d Cir. 1993); *Braniff, Inc. v. GPA Group PLC (In re*
Braniff, Inc.), 118 B.R. 819, 845 (Bankr. M.D. Fla 1990).

¹⁴ *In re Sambo's Restaurants, Inc.*, 24 B.R. 755 (Bankr. C.D. Cal. 1982)

¹⁵ *Kopel v. Campanile (In re Kopel)*, 232 B.R. 57 (Bankr. E.D.N.Y. 1999).

¹⁶ *Id.* at 64.

The court expressly distinguished the case from one, such as the present matter, where "the non-debtor party seeks enforcement of a cross-default provision in an effort to extract priority payments under an unrelated agreement."¹⁷ The court's holding means that a creditor must establish that the agreements in question are interrelated before a cross-default provision will be enforced. Finova's attempt to use the cross-default provision to connect otherwise unrelated agreement must therefore fail under *Kopel*.

Conclusion

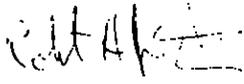
For the foregoing reasons the Debtor asserts that it may properly assume and assign, or reject, each of the Equipment Leases.

Dated: Los Angeles, California
August 24, 2001

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¹⁷ *Id.* at 65.