UNITED STATES BANKRUPTCY COURT
FOR THE MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION

IN RE:	)	
	)	
Convenience USA, Inc., et al.,	)	Case Nos. 01-81478 through 01-81489
	)	
Debtors.	)	
	)	

MEMORANDUM OPINION

These cases came before the court on May 19, 2003, for hearing upon the restated claim of U.S. Restaurant Properties, Inc., U.S. Restaurant Properties Operating, L.P., USRP (Gant 1), LLC, USRP (Gant 2), LLC, USRP (Gant 3), LLC, USRP (Gant 4), LLC, USRP (Gant 5), LLC, and USRP (Gant 6), LLC (collectively "USRP") for amounts due for assumption of leases under § 365(b) of the Bankruptcy Code (the "Restated Claim"). William B. Sullivan appeared on behalf of USRP, John A, Northen appeared on behalf of the Debtors and John H. Small and Gary W. Marsh appeared on behalf of LaSalle Bank National Association.

JURISDICTION

The court has jurisdiction over the subject matter of this proceeding pursuant to 28 U.S.C. §§ 151, 157 and 1334, and the General Order of Reference entered by the United States District Court for the Middle District of North Carolina on August 15, 1984. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A),(M) and (O) which this court may hear and determine pursuant to 28 U.S.C. § 157(b)(1).

FACTUAL BACKGROUND

On May 21, 2001 (the "Petition Date"), each of the Debtors filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code. When these cases were filed, the convenience stores operated by the Debtors included 27 stores located in North Carolina which the Debtors leased from USRP pursuant to an Energy Lease dated as of July of 1999 (the "Energy Lease").

During the pendency of these cases the Debtors sought, over the objection of USRP, to assume and assign the leases for 15 of the 27 stores subject to the Energy Lease and to reject the leases for the remaining 12 stores. By orders entered on February 12, 2002, October 21, 2002, and February 12, 2003, this court ruled that: (1) the Energy Lease is divisible into separate leases for each of the 27 stores; (2) the Debtors may assume the leases for 15 of the USRP stores (the "USRP Core Leases"); and (3) the Debtors may reject the leases for the remaining 12 USRP stores (the "USRP Non-Core Stores").

On December 19, 2002, the Debtors filed their Amended Joint Plan of Reorganization under Chapter 11 (the "Plan") and their Amended Joint Disclosure Statement for Debtors' Plan of Reorganization. The Plan as proposed by the Debtors provided for the 15 USRP Core Leases to be assumed by the Debtors and assigned to an entity known as EXPREZIT! Convenience Stores North Carolina, LLC.

Over the objections of USRP, Debtors' Amended Joint Disclosure Statement was approved and an order was entered fixing the time for filing acceptances or rejections of the Plan and scheduling a confirmation hearing. USRP objected to the confirmation of the Plan and opposed confirmation at the confirmation hearing. The court overruled the objections to confirmation of the Plan and an order was entered on February 12, 2003, confirming the Plan, including the provisions providing for assumption and assignment of the 15 USRP Core Leases (the "Confirmation Order") The Confirmation Order also provided for the filing of claims or notices of amounts due or claimed to be due for or in connection with the assumption and assignment of leases and executory contracts and required that any party claiming any amounts due under § 365(b) with respect to the assumption and assignment of real estate leases, equipment leases and executory contracts to be assumed and assigned by the Debtors under the Plan file and serve a claim within 10 days after service of the Confirmation Order on such persons.

USRP's initial claim was filed on February 24, 2003, and included $9,536.63 for property taxes which USRP asserted were due under the USRP Core Leases and $192,217.03 for fees and expenses incurred by USRP. On April 4, 2003, USRP filed a supplement to its claim which added additional fees to the claim and increased the total amount of the USRP claim to $230,652.40. However, on

April 18, 2003, USRP filed the Restated Claim which is now before the court. The Restated Claim supercedes and replaces the earlier claims filed by USRP.

The Restated Claim is in the amount of $72,034.36 and consists entirely of fees and expenses allegedly incurred by LTSRP since these cases were filed.[1] The fees and expenses claimed by USRP consist of $32,782.04 paid to Arthur E. Nienhueser, II for $27,900.00 of consulting fees and $4,882.04 for reimbursement of expenses and $39,656.32 paid to its attorneys in this case, Womble, Carlyle Sandridge & Rice, PLLC, for $38,834.50 of attorneys' fees and $821.82 for reimbursement of expenses. USRP asserts that payment of the $72,034.36 is required under § 365(b)(1)(A) to cure defaults under the USRP Core Leases as well as under § 365(b)(1)(B) as pecuniary losses resulting from defaults under the USRP Core Leases. On March 5, 2003, the Debtors objected to the Restated Claim asserting that no fees and expenses were owed under the USRP Core Leases, that no default had occurred under the leases and that no amount was required to be paid to USRP under either § 365(b)(1)(A) or § 365(b)(1)(B) in order for the USRP Core Leases to be assumed and assigned under the Plan.

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[1] According to the Restated Claim, no property taxes were included in the Restated Claim because the $9,536.63 of property taxes included in the previous claim were paid in full by the Debtors following the confirmation hearing.

DISCUSSION

The language of § 365(b)(1)(A) and (B) makes it clear that no amount is due thereunder unless there has been a default under the executory contract or unexpired lease sought to be assumed. The pertinent language of § 365(b)(1)(A) and (B) provides that "[i]f there has been a default in an executory contract or unexpired lease of the debtor, the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee (A) cures . . . such default and (B) compensates a party other the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default." (Emphasis supplied). Thus, in the absence of a default by the debtor with respect to the executory contract or unexpired leased that is being assumed, there is no obligation to pay any amount under either § 365(b)(1)(A) or under § 365(b)(1)(B). See 3 COLLIER ON BANKRUPTCY ¶ 365.05[1] (15th ed. rev. 2003) ("By its terms, section 365(b) applies only when there has been a default. If there has been no default, the trustee or debtor need not comply with the cure, compensation, and adequate assurance requirements of section 365(b)."). See also In re Shangra-La. Inc., 167 F.3d 843, 849 (4th Cir. 1999) (attorneys' fees following a default are recoverable under § 365(b)(1)(B) "if such monies were expended as the result of a default under the contract or lease between the parties and are recoverable under the contract and applicable state

law.").

As a party seeking the recovery of fees and expenses pursuant to § 365(b)(1), USRP has the stance of a plaintiff in a contested matter and therefore has the burden of proving its entitlement to the amounts sought. See In re Joshua Slocum, Ltd., 103 B.R. 601, 605 (Bankr. E.D. Pa. 1989). In order to satisfy its burden of proof, USRP was required to prove all elements of the compensation and damages sought by a preponderance of the evidence. See id. The elements which must be proven by LJSRP include the defaults alleged by USRP as the basis for its claim.

USRP asserts that there were three defaults by the Debtors under the USRP Core Leases consisting of: (1) failure to pay real and personal property taxes; (2) failure to pay USRP for the consulting fees and expenses that it paid to Mr. Nienhueser; and (3) failure to pay LJSRP for the attorneys' fees and expenses it incurred with respect to those objections and issues on which it had success concerning enforcement of its rights. Neither of these alleged defaults was established by USRP. The taxes were promptly paid when properly presented to the Debtors and therefore may not serve as the basis for claiming a default. No default having occurred under the Energy Lease prior to USRP incurring the consulting and attorney fees and expenses, Debtors had no obligation under the Energy Lease to reimburse USRP for such fees and expenses. The failure to pay the fees and expenses therefore

was not a default that is required to be cured under § 365(b)(1)(A), nor do such fees and expenses constitute a pecuniary loss resulting from a default for purposes of § 365(b)(1)(B).

A. No Default From The Property Taxes.

According to the original USRP claim, the default involving property taxes involved $9,536.63 of property taxes that were delinquent when the claim was filed on February 24, 2003. Although these taxes had not been paid when the claim was filed, the evidence did not establish that the failure of the Debtors to pay the taxes prior to February 24, 2003, constituted a default under the Energy Lease. Under the Energy Lease the tax bills were sent to USRP by the taxing authorities. Since the bills were going to USRP, the Energy Lease required USRP to then send the bills to the Debtors so that the Debtors would be aware of the taxes and could pay the tax bills. In that regard, paragraph 5.1 of the Energy Lease specifically required USRP to "forward copies of all tax bills within fifteen (15) days after Landlord's receipt thereof." There was no evidence that the tax bills in question were ever furnished to the Debtors prior to the claim being filed in February of 2003, although the tax bills apparently were received by USRP months before February of 2003. Additionally, paragraph 17 of the Energy Lease, which defines what constitutes a default under the Lease, provides that a failure by the tenant to pay monetary sums

due under the lease is a default "where such failure continues for ten (10) days after written notice by Landlord to Tenant. . ." There likewise was no evidence that USRP provided written notice of the $9,536.63 of taxes prior to the filing of its claim in February of 2003. Once the claim was filed, it is undisputed that the taxes were immediately paid by the Debtors. Based upon the foregoing, the court concludes that no default was established by USRP with respect to the $9,536.63 of property taxes that initially were included in the USRP claim. Moreover, even if the failure to pay the taxes until after the USRP claim was filed could be considered a default, which is not the case, it is clear that any such default was cured before the hearing on the USRP claim because it is undisputed that the taxes were paid in full prior to the hearing. Hence, there is no default to be cured pursuant to § 365(b)(1)(A). Nor is there any basis for a claim under § 365(B)(1)(B) because there was no showing by USRP that any of the attorney or consulting fees claimed by USRP were incurred in connection with the collection of the property taxes.

B. No Default From Nonpayment of the Consulting and Attorney Fees and Expenses.

In support of its contention that Debtors are obligated to pay USRP's fees and expenses, USRP argues that "Debtors breached the Energy Lease by virtue of their bankruptcy filing" and that Debtors' bankruptcy filing constituted 'a default that triggers the remedy contained in paragraph 17.2(b) that requires the subsequent

payment of attorneys' fees related to the bankruptcy filing."" This argument raises two issues: does section 17.2(b) of the Energy Lease call for the payment of attorneys [or consulting fees and expenses] based solely upon the filing of a bankruptcy case and, if so, is such a provision enforceable against a chapter 11 debtor-in-possession seeking to assume an executory contract or unexpired lease under § 365 of the Bankruptcy Code? The consideration of these issues begins with an examination of the Energy Lease and the specific provisions of section 17 thereof. The caption for section 17 reflects that it deals with default and remedies upon default.' Section 17.1 defines what constitutes a material default under the Lease and contains four subparagraphs. Section 17.2 then describes remedies that are available upon the occurrence of default. The language relied upon by USRP is contained in the following portion of Section 17.2:

> 17.2 Remedies. In the event of any such material default or breach by Tenant, Landlord may, at any time thereafter, without limiting Landlord in the exercise of any right or remedy at law or in equity which Landlord may have by reason of such default or breach:
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> (a) Maintain this Lease in full force and effect and recover the rent and other monetary charges as they become due, without terminating Tenant's right to possession irrespective of whether Tenant shall have

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[2]USRP's Memorandum in Support of Its Claim for Amounts Due as Required for Assumption of Leases Under Section 365(b), p. 5.

'The caption reads "DEFAULTS, REMEDIES".

abandoned any Leased Property. In the event Landlord elects not to terminate the Lease, Landlord shall have the right to attempt to relet all or any portion of any Leased Property at such rent and upon such conditions and for such a term, and to do all acts necessary to maintain or preserve any Leased Property as Landlord deems reasonable and necessary without electing to terminate the Lease, including removal of all persons and property from each Leased Property;

(b) Terminate Tenants right to possession of one or more (including all) of all Leased Property by any lawful means, in which case this Lease shall terminate with respect to such Leased Property (collectively the 'Terminated Leased Property') and Tenant shall immediately surrender possession of the Terminated Leased Property to the Landlord. In such event Landlord shall be entitled to recover possession of the Terminated Leased Property from Tenant and those claiming through or under Tenant, and Landlord may continue the operations at the Leased Property itself or through an affiliate, and Tenant hereby assigns to Landlord its interest in the following as security for Tenant's obligation hereunder: Tenant's interest in any trade name used by Tenant in the operations at the Leased Property. Such termination of this Lease and repossession of the Terminated Leased Property shall be without prejudice to any remedies which Landlord might otherwise have for arrears of rent or for a prior breach of the provisions of this Lease. In case of such termination, Tenant shall indemnify Landlord against all costs and expenses and loss of rent (loss of rent for the Terminated Leased Property shall be determined in accordance with Exhibit D) Items of expense for which Tenant shall indemnify Landlord shall include the costs and expenses incurred in collecting amounts due from Tenant under this Lease (including attorneys' fees, litigation expenses and the like); the damages incurred by Landlord by reason of Tenant's default, including, the cost of recovering possession

> of the Terminated Premises, expenses of reletting including necessary repairs of the Leased Property; and all Landlord's other reasonable expenditure proximately caused by the termination. All sums due in respect of the foregoing shall be due and payable immediately upon notice from Landlord that a cost or expense has been incurred without regard to whether the cost or expense was incurred before or after the termination of this Lease. In the event proceedings are brought under the Bankruptcy Code, including proceedings brought by Landlord which relate in any way to this Lease including, without limitation, proceedings for the termination, assumption o r assignment thereof, or proceedings to secure adequate protection for Landlord or proceedings involving objections to the allowance of Landlord's claim, then Landlord shall be paid, in addition to any and all amounts due Landlord pursuant to the terms of this Lease, such further amount as shall be sufficient to cover all costs and expenses incurred by Landlord with respect to the proceeding, which costs and expenses shall include the reasonable compensation, costs, expenses, disbursements and advances of Landlord, its agents and attorneys.

(Emphasis supplied). As reflected above, the language relied upon by USRP is a part of section 17.2 of the Lease. Section 17.2 sets forth remedies which are available "[i]n the event of any such material default or breach by the Tenant . ." The provision relied upon by USRP follows this language and is a part of the remedies which are available to the Landlord in the event one of the material defaults described in section 17.1 occurs. The only event of default described in section 17.1 which has occurred in this case is described in section 17.1(d) and consist of "the filing by or against Tenant of a petition to have Tenant adjudged

a bankrupt, or of a petition for reorganization or arrangement under any law relating to bankruptcy ." However, under § 365(b)(2)(B) such a default is not a default for purposes of § 365(b)(1).[4] Hence, there is no requirement to cure such a default nor to compensate for any pecuniary damages resulting from such a default. Confronted with this reality, USRP does not argue that the bankruptcy filing was a default, but instead argues that it was a trigger for the remedy contained in the language contained in section 17.2(b) of the Energy Lease and that upon the filing of the bankruptcy the Debtors became obligated to pay fees pursuant to section 17.2(b) even though no default had occurred under the Lease (other than the unenforceable ipso facto default under section 17.1(d) which is ignored by USRP). LJSRP argues that such a result is apparent from reading the language of section 17.2 "on its face." The court disagrees. USRP's argument focuses only upon the selected language from section 17.2(b) and ignores other language contained in section 17. As noted earlier, section 17.2 sets forth remedies which are available to the Landlord 'in the event of" a material default by the Tenant. The language selected by USRP from section 17.2(b) is a part of one of the remedies that is available in the event of a material default. USRP presented no basis

[4]Section 365(b)(2)(B) provides that "Paragraph (1) of this subsection does not apply to a default that is a breach of a provision relating to . the commencement of a case under this title . ."

legally or factually for ignoring the plain language of section 17.1 and the fact that the recovery of fees is a part of the remedies that become available if a material default occurs. To the extent that it can be argued that the wording and location of the language contained in section 17.2(b) creates an ambiguity, USRP offered no evidence that the parties intended that in the event any proceedings were brought under the Bankruptcy Code (including proceedings brought by USRP relating to the Lease), USRP would have an unlimited right to recover any fees and expenses that it incurred with respect to the proceeding without regard to whether the Tenant defaulted under the Lease. The statement in USRP's memorandum that the language in section 17.2(b) that is relied upon by USRP is "slightly indented and therefore apparently added to section 17.2(b)" is nothing more than speculation which is not supported by any evidence and which has no probative value in determining the meaning of section 17 of the Energy Lease. In fact, USRP presented no evidence of how the provision got into the Lease or that the Tenant ever agreed that no default was required in order for USRP to recover fees and expenses despite the fact that the recovery of such fees and expenses is listed as one of the remedies available in the event of a default by the Tenant. For the foregoing reasons, the court rejects USRP's argument that it is entitled to recover the fees and expenses of its consultant and its attorneys under section 17.2(b) of the Lease solely as a result of

the Debtors' bankruptcy filing and without regard to whether Debtors' defaulted under the Lease.

Even if section 17.2(b) could be read as being applicable solely as a result of a bankruptcy filing, as contended by USRP, USRP nonetheless would not be entitled to recover fees and expenses under section 17.2(b) because, if interpreted as contended by USRP, section 17.2(b) runs afoul of § 365(e) of the Bankruptcy Code and is rendered inoperative.

Section 365(e)(1)(B) provides as follows:

> Notwithstanding a provision in an executory contract or unexpired lease, or in applicable law, an executory contract or unexpired lease of the debtor may not be terminated or modified, and any right or obligation under such contract or lease may not be terminated or modified, at any time after the commencement of the case solely because of a provision in such contract or lease that is conditioned on the commencement of a case under this title. .

Under § 365(e), a clause in an executory contract providing for the termination or modification of the contract which is conditioned on the debtor's insolvency, the commencement of a bankruptcy case or the appointment of a receiver or custodian, is inoperative in a bankruptcy case. See In re Metrobility Optical Svs., Inc., 268 B.R. 326, 329 (Bankr. D.N.H. 2001) ("Section 365(e) invalidates ipso facto clauses in executory contracts and unexpired leases."); In re Child World, Inc., 161 B.R. 349, 354 (Bankr. S.D.N.Y. 1993). See generally 3 COLLIER ON BANKRUPTCY ¶ 365.07 (15th ed.

rev. 2003). The language of section 17.2(b) relied upon by USRP provides that "in the event bankruptcy proceedings are filed, the Landlord shall be paid, in addition to any and all amounts due Landlord pursuant to the terms of this lease, such further amount as shall be sufficient to cover all costs and expenses incurred by landlord with respect to the proceeding. ." Clearly, the operative effect of this provision is conditioned upon the commencement of a bankruptcy proceeding. The effect of the provision in the event a bankruptcy proceeding is filed, is to impose upon the Tenant a "further amount" in addition to "any and all amounts due Landlord pursuant to the terms of the lease" solely because the proceeding is filed. The "further amount" due as a result of the bankruptcy filing is the amount of the fees and expenses incurred by the Landlord during the bankruptcy proceeding. In purporting to impose this new and additional liability on the Tenant, the provision clearly modifies the obligation of the Debtors under the Energy Lease by the addition of the new liability for fees and expenses incurred during the bankruptcy proceeding. As such, the provision is an ipso facto clause which falls within the prohibition contained in § 365(e)(1)(B) and is rendered inoperative.

Although USRP did not rely upon section 18.14 of the Energy

Lease in claiming the right to recover attorneys' fees', the court has considered whether USRP has a claim for the recovery of attorneys' fees under that provision. Section 18.14 of the Energy Lease is entitled "Costs of Suit" and provides as follows:

> If Tenant or Landlord shall bring any action for any relief against the other, declaratory or otherwise, arising out of this Lease, including any suit by Landlord for the recovery of rent or possession of any Leased property, the prevailing party shall be entitled to an award of its reasonable attorneys' fees and costs. Such fees and costs shall include those fees and costs incurred at trial, on appeal, or in any bankruptcy proceeding.

Clearly, USRP is not entitled to recover any attorneys' fees under this provision. Under section 18.14, it is the "prevailing party" that is given the right to recover attorneys's fees in those proceedings to which section 18.14 is applicable. Even if it is assumed that section 18.14 is applicable with respect to the Chapter 11 cases filed by the Debtors, it is clear that USRP in no sense could be regarded as the "prevailing party" for purposes of

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[5] In fact, USRP argued that section 18.14 is not applicable in this case because it applies only where one of the parties brings an action for relief against the other arising out of the Energy Lease, and "neither the Debtors nor USRP brought an action for relief against the other arising out of the Energy Lease." On the other hand, the Debtors argued that section 18.14 is applicable to the various disputes and contested matters involving the Debtors and USRP that arose during these cases, that the Debtors were the prevailing party with respect to such matters and that Debtors therefore would be entitled to claim their attorneys' fees as a setoff defense.

section 18.14. Instead, the record reflects that as between the Debtors and USRP, the Debtors were the prevailing party in these cases. This is true whether the prevailing party determination is made on the basis of the number of matters in which the Debtors prevailed or the significance of the matters in which the Debtors prevailed. The disputed matters involving the Debtors and USRP included (a) the determination of whether the Energy Lease was severable; (b) the Debtors' request to reject 12 of the 27 stores leased from USRP; (c) the Debtors' request to abandon the underground storage tanks and the underground storage tank systems at sites where the USRP leases have been rejected; (d) the Debtors' request to assume and assign to EXPREZIT! the leases for the 15 USRP core stores; (e) confirmation of the Debtors' amended joint plan of reorganization; and (f) USRP's request to stay the confirmation order. These matters are by far the most significant matters involving the USRP leases that were in dispute during these Chapter 11 cases and the Debtors prevailed in all such matters. While there were some disputes during these cases involving the Debtors and USRP in which USRP prevailed, such disputes were few in number and of much less significance than the disputes in which USRP prevailed. More importantly, the attorneys' fees incurred by the Debtors with respect to the disputed matters in which they prevailed greatly exceed USRP's fees for any matters in which USRP could be regarded as the prevailing party and Debtors' fees as

prevailing party therefore would cancel out any claim by USRP under section 18.14. In summary, whether the disputed matters involving the Debtors and USRP are viewed on the basis of the number of matters in which the Debtors prevailed or on the basis of the importance of the matters in which the Debtors prevailed, the Debtors rather than USRP must be regarded as the prevailing party. It follows that USRP would have no claim for attorneys' fees under section 18.14 that would have to be paid or cured under either § 365(b)(1)(A) or § 365(b)(1)(B) of the Bankruptcy Code.

CONCLUSION

For the foregoing reasons, an order shall be entered denying and disallowing the Restated Claim of USRP in toto.

This 8 day of December, 2003.

William L. Stocks

WILLIAM L. STOCKS
United States Bankruptcy Judge