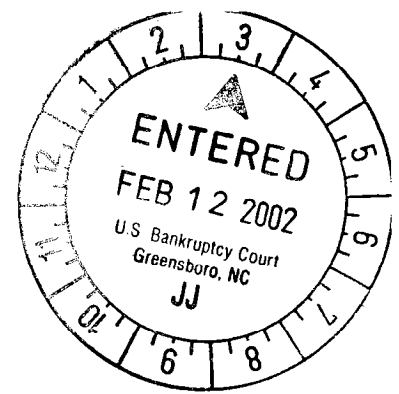


UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION



IN RE:)
)
Convenience USA, Inc., et al.,) Case No. 01-81478 through
) 01-81489 (Administratively
Debtors.) Consolidated)
)

MEMORANDUM OPINION

These cases came before the court on February 7, 2002, for hearing upon the Motion of Debtors to Reject Certain Unexpired Non-Residential Real Estate Property Leases ("the Motion"). John A. Northen and Richard M. Hutson, II appeared on behalf of the Debtors, Alan D. McInnes appeared on behalf of U.S. Restaurant Properties, Inc. and six related limited liability companies who are landlords under the lease referred to in the Motion (hereinafter referred to collectively as "USRP"), John H. Small appeared on behalf of LaSalle Bank National Association and Diane P. Furr appeared on behalf of the Committee of Unsecured Creditors. Having considered the Motion, the objection filed on behalf of USRP and the evidence offered by the parties, the findings of the court pursuant to Bankruptcy Rules 9014 and 7052 are hereinafter set forth.

MATTER BEFORE THE COURT

The Motion was filed pursuant to § 365 of the Bankruptcy Code under which a trustee or Chapter 11 debtor, subject to the court's approval, may assume or reject an unexpired lease of the debtor. Under the lease referred to in the Motion, Debtors leased from the

six landlords named in the lease 27 convenience stores for an initial lease term of 20 years. The Debtors seek to reject the lease only as to six of the leased properties. USRP objects to the motion, arguing that the Debtors must assume or reject the lease as a whole. The issue presented is whether the Debtors may reject the lease as to only six of the leased properties or whether the Debtors must assume or reject the lease as a whole.

FACTS

Debtor Convenience USA, Inc. ("Convenience USA") is a consolidator of convenience stores in the southeastern region of the United States and currently operates over 200 such stores. The stores generally sell gasoline, lottery tickets, money orders, food items and other convenience merchandise. The stores are owned and operated through entities which are subsidiaries or affiliates of Convenience USA. These subsidiaries and affiliates are the other debtors in this case. The subsidiaries and affiliates of Convenience USA were formed in connection with acquisitions of existing chains of convenience stores from various third parties over a period of approximately two years, from March 5, 1998 through January of 2000.

In the process of acquiring chains of convenience stores from various third parties, Convenience USA became aware that Gant Oil Company ("Gant Oil") operated a chain of 28 convenience stores located in North Carolina and was interested in selling its

business. Gant Oil owned some of the 28 locations, leased some store locations from unrelated third parties and leased the remaining properties from related third parties ("the Gant Entities").

In March of 1999 Convenience USA formed Gant Acquisition, LLC ("Gant Acquisition") for the purpose of acquiring various assets involved in the Gant Oil business and engaged in negotiations with the Gant Entities for the acquisition of the Gant Oil business. The Gant Entities were interested in minimizing the income taxes related to the sale of the Gant Oil business, including the real property owned or leased by them. In order to reduce the tax obligations of the Gant Entities, Convenience USA, Gant Acquisition and the Gant Entities agreed to a structure for the acquisition of the Gant Oil business assets by Gant Acquisition under which Gant Acquisition agreed to buy the inventory, certain equipment and certain other business assets from the Gant Entities for \$2,164,000.00 plus the cost of the inventory. In addition, the Gant Entities agreed to transfer 27 parcels of real estate with improvement and equipment to U.S. Properties Operating L.P. ("USRP Operating") or its assigns for the purchase price of \$13,075,000.00 and USRP Operating, in turn, was to lease the 27 properties to Gant Acquisition with an annual base rent that was the product of 11.375% multiplied by the sum of the purchase price of the 27 properties plus the expenses incurred by USRP in purchasing the 27

properties.¹ Asset purchase agreements were entered into in May of 1999 and the deal was closed in July of 1999, at which time Gant Acquisition acquired the inventory, equipment and other business assets from the Gant Entities, Gant Entities closed the sale of the 27 convenience stores to USRP Operating and, pursuant to a lease document known as the Energy Lease, the 27 convenience stores were leased to Gant Acquisition by six different lessors who were the assigns of USRP Operating.

When these cases were filed on May 21, 2001, the Debtors were still leasing the 27 stores and have continued to do so. However, the six stores identified in the Motion have continued to operate at a loss since these cases were filed. The Debtors' efforts to improve the profitability of the six stores have not been successful and the six stores in question do not generate sufficient income to cover the rent or other expenses related to the operation of the six stores. As a result, the Debtors are sustaining substantial losses at the six stores. The Debtors have concluded that these losses cannot be stemmed and Debtors therefore wish to reject the lease of the six stores and close the six stores in order to avoid further losses to the estate.

DISCUSSION

The general rule is that in order for a contract to be assumed

¹The 28th store was to be leased by Gant Acquisition directly from the existing landlord.

or rejected under § 365 of the Bankruptcy Code, the contract must be assumed or rejected in its entirety. See Stewart Title v. Old Republic Nat. Title, 83 F.3d 735, 741 (5th Cir. 1996). However, where a contract, though contained in a single document, is divisible into several different agreements, some of the divisible agreements may be assumed or rejected under § 365 without assuming or rejecting the entire contract. See id.; In re Gardinier, Inc., 831 F.2d 974 (11th Cir. 1987); In re Holly's, Inc., 140 B.R. 643, 681 (Bankr. W.D. Mich. 1992); In re Cutter's, Inc., 104 B.R. 886, 889 (Bankr. M.D. Tenn. 1989).

The parties in the present case are in sharp disagreement regarding the status of the Energy Lease. USRP contends that the Energy Lease is a single, indivisible agreement which must be assumed or rejected in its entirety. The Debtors argue that the Energy Lease is a divisible contract and that the lease of each of the 27 leased properties is an executory agreement, divisible from the Energy Lease as a whole, that may be rejected by the Debtors without rejecting the leases of the other properties described in the Energy Lease.

The conflicting contentions of the parties involve their rights under the Energy Lease. Determination of contract or property rights by the bankruptcy courts ordinarily is controlled by state law. See Butner v. United States, 440 U.S. 48, 54, 99 S. Ct. 914, 917-18, 59 L.Ed.2d 136 (1979). Usually, the law of the

forum state is controlling. However, in the present case, paragraph 18.15 of the Energy Lease provides that the lease shall be governed by the laws of the State of Texas. In the Fourth Circuit, a bankruptcy court must apply the conflicts of law rules of the forum state in determining which state's law to apply in making determinations of property rights in the assets of a bankruptcy estate. See In re Merritt Dredging Co., Inc., 839 F.2d 203 (4th Cir. 1988). This rule requires resort to North Carolina conflicts of law rules to determine which body of state law is controlling in determining the issues regarding the interpretation of the Energy Lease.

The general rule in North Carolina is that a choice of law or forum selection clause in a contract is enforceable unless it is shown that the clause was the product of fraud or unequal bargaining power or that enforcement of the clause would be unfair or unreasonable. See Bell Atlantic Tricon Leasing Corp. v. Johnnie's Garbage Serv., Inc., 113 N.C. App. 476, 439 S.E.2d 221 (1994). In the present case, involving a contract negotiated by experienced business people, no such showing has been made. The court therefore will apply Texas law in accordance with the choice of law provision in the Energy Lease.

A. Application of Texas Law.

The concept of divisible contracts is recognized under Texas law. See In re Payless Cashways, Inc., 230 B.R. 120, 135 (8th Cir.

BAP 1999) (discussing Texas law), aff'd 203 F.3d 1081 (8th Cir. 1999). Under Texas law, there is no one test or criterion that is determinative as to whether a contract is entire or divisible. See Johnson v. Walker, 824 S.W.2d 184, 187 (Tex. App. - Ft. Worth 1991); St. John v. Barker, 638 S.W.2d 239, 243 (Tex. App. 1982); Chapman v. Tyler Bank & Trust Co., 396 S.W.2d 143, 146 (Tex. Civ. App. - Tyler 1965). The determination of whether a contract is divisible depends primarily upon the intent of the parties, the subject matter of the agreement and the conduct of the parties. See Walker, 824 S.W.2d at 187; St. John, 638 S.W.2d at 243; Chapman, 396 S.W.2d at 146-47. "The intention of the parties as determined by the language used in a contract is controlling in determining whether the contract is severable or is entire and indivisible." Blackstock v. Gribble, 312 S.W.2d 289, 292-293 (Tex. Civ. App. - Eastland 1958). A frequently used test under Texas law to determine the divisibility of a contract is whether the consideration for the agreement is apportionable, and it generally is held that a contract is divisible where the part to be performed by one party consists of several distinct and separate items and the price to be paid by the other party is apportioned to each item. See Walker, 824 S.W.2d at 187; Click v. Seale, 519 S.W.2d 913, 918 (Tex. Civ. App. - Austin 1975); Chapman, 396 S.W.2d at 146-147. Single assent to a whole transaction involving several parts indicates that a contract is entire. However, the mere fact

that agreements are embraced in one instrument will not make the writing entire and indivisible. See Click, 519 S.W.2d at 918. "In the end, the intent of the parties, as demonstrated by the language used, is controlling." In re Payless Cashways, Inc., 230 B.R. at 135.

1. Intent of the Parties

In the present case, the Energy Lease, of course, is a single instrument in which there apparently was single assent by the multiple parties to the lease. However, as the foregoing authorities make clear, this circumstance, standing alone, does not end the inquiry and make the agreement entire and indivisible. See Click, 519 S.W.2d at 918. The other circumstances of the case must be considered and under Texas law, the factor that weighs most heavily in deciding whether the Energy Lease is an entire contract or is divisible, is the intent of the parties as reflected in the provisions of the Energy Lease.

From an examination of the lease provisions, the court is satisfied that the intent of the parties in this case was to have a contract in which the lease of the various leased properties would be divisible. Such intent is reflected in several provisions of the Energy Lease, particularly those provisions dealing with the transfer of leased properties during the term of the lease and the provisions dealing with allocation of the rent.

Paragraph 18.2 of the Energy Lease, dealing with the transfer

of a leased property by the landlord, and paragraph 18.24, entitled "Separate Lease Agreements," strongly reflect an intent that the lease be divisible with respect to the various leased properties. Under these provisions, the landlord has the unfettered right to sell or otherwise transfer any number of the leased properties at any time during the lease term. In such event, the Energy Lease requires the tenant to enter into a new lease with the transferee or new owner of the property being sold or transferred, and the Energy Lease continues in effect as to the remaining leased properties, except that the rent payable under the Energy Lease is reduced by the amount of the rent allocated under the lease to the property being sold or transferred. The effect of these provisions is that the property that is transferred is severed from the Energy Lease and becomes subject to a new lease with a new landlord, while the Energy Lease remains in effect as to the other leased properties, which reflects that the Energy Lease is a divisible contract. In fact, the lease has to be divisible in order for the landlord to be able to sell leased properties and still have the lease continue into effect as to the remaining properties. While paragraph 18.25 of the Energy Lease gives the tenant an option to purchase any leased property proposed for sale, such an option is entirely consistent with the Energy Lease being divisible because if the tenant exercises the option, one of the leased properties is severed from the Energy Lease and transferred to the tenant without

affecting the lease of the remaining leased properties.

Paragraph 1.8 of the lease is the "Rent Reduction Amount" provision and also is strongly indicative of an intent to have a divisible contract. This provision, together with Exhibit G of the lease, provides for the apportionment of the rent and the assignment of specific amounts of rent to each of the 27 leased properties. This provision provides the mechanism for determining the amount of the rent reduction that is to occur when there is a division of the Energy Lease as a result of the sale or destruction of one or more leased properties. The amount of the reduction is the product of (i) total Base Rent (described in Exhibit D) prior to any reduction multiplied by (ii) the ratio of (A) the purchase price allocated pursuant to Exhibit G to the Building with respect to which the Rent Reduction Amount is calculated, divided by (B) the aggregate purchase price allocations for each of the buildings. USRP's argument that the lease does not provide for an apportionment of the base rent under the lease ignores the foregoing terms of the Energy Lease, as well as the conduct of the parties following the execution of the lease. In actuality, the inclusion in the Energy Lease of provisions permitting the landlords to sell leased properties during the lease term and providing for the termination of the lease as to destroyed properties necessitated that the parties adopt a mechanism for adjusting the rent. Such a mechanism is contained in paragraph 1.8

which specifically sets forth a formula for allocating the base rent among the 27 properties. Moreover, following the execution of the Energy Lease, the parties agreed upon a schedule (page 2 of Debtors' Exhibit No. B) which specifically and on a property-by-property basis detailed the amount of the annual and monthly rent allocated to each of the 27 properties. Under Texas law, a circumstance that weighs very heavily in finding that a contract is divisible is if the part of the contract to be performed by one party consists of several separate items and the price to be paid by the other party is apportioned to each item. See Walker, 824 S.W.2d at 187; Click, 591 S.W.2d at 918; Chapman, 396 S.W.2d at 146-47. This is precisely what occurred in the present case--the landlords agreed to lease to the Debtors 27 separate and distinct properties and the parties allocated the rent among the various properties on both an annual and monthly basis.

There are other provisions that reflect an intent to have a divisible contract. Under paragraph 14.0 of the lease, if one of the leased properties is condemned, the entire lease is not terminated. Instead, the lease provides for the lease of the condemned property to be severed from the Energy Lease and for the lease to continue in effect as to the other leased properties. A similar division occurs in the event of the destruction of a building on a leased property. Under paragraph 13.0 of the lease, if one of the stores is damaged beyond repair, the lease terminates

as to that leased property. This occurs without affecting the lease of the other leased properties except that under paragraph 1.8 the rent payable under the Energy Lease is apportioned and reduced by the amount of rent that was being paid for the leased property that was destroyed.

In arguing that these provisions do not reflect an intent that the Energy Lease be divisible, USRP contends that in adopting such provisions the parties were merely recognizing possible contingencies and dealing with them. While this may be true, it does not follow that these provisions do not reflect an intent that the lease be divisible. With respect to each of the contingencies, the parties had two choices. The parties could have elected to provide in the lease that if one of the leased properties were sold, condemned or destroyed, the entire lease would terminate. Presumably, the parties would have made this election if the economic realities had dictated such a resolution upon the loss of one or more of the leased properties. The parties did not elect such a provision. Instead, the parties elected to have a contract under which the lease of some of the properties may be terminated without affecting the continuing lease of the remaining properties. Choosing such terms reflects an intent to have a divisible contract.

Another provision of the Energy Lease reflecting the intent of the parties that the Energy Lease be divisible is paragraph 18.23

dealing with "Landlord Obligation." This provision recites that each of the six separate landlords named in the lease "is leasing its respective premises, as identified on Exhibit A, to tenant on a several, and not joint and several basis." Under this provision, none of the six landlords named in the lease is responsible for a default on the part of any other landlord and, in the event of a default by one landlord, the intent and effect of the provision is that the leases of the defaulting landlord would be severed from the Energy Lease and the Energy Lease would continue in effect as to the leased properties owned by the other landlords.

In concluding that the parties intended that the Energy Lease be divisible, the court also has considered Paragraph 17 of the Energy Lease, which deals with default. In the event of a default, paragraph 17.2(b) permits the landlord to terminate the tenant's right to possession "of one or more (including all)" of the leased properties. This provision also permits a division of the lease by permitting the landlord to terminate any number of the leased properties, while leaving the lease in effect as to the remaining properties. This provision was characterized during the evidence as a "cross default" clause. As such, it is argued that the provision is inconsistent with an intent that the contract be divisible. To the extent that the default provisions are inconsistent with an intent that the lease be divisible, such provisions are insufficient to outweigh the other provisions of the

lease which weigh more heavily in favor of a finding of an intent that the lease be divisible. Accordingly, the court concludes that it was the intent of the parties that the Energy Lease be divisible.

2. Subject Matter of the Agreement

The second prong to be considered under Texas law in deciding whether a contract is divisible is the subject matter of the agreement. A finding that the subject matter of the contract is such that the contract can be divided into two or more separate agreements that can be performed independent of each other weighs in favor of a finding that the contract is divisible.

The type of agreement involved in the present case, of course, is a lease. The subject matter of a lease is the property that is dealt with in the lease. In the present case, that subject matter consists of 27 separate and distinct convenience stores located in 18 different cities and scattered over a wide area of North Carolina. The Energy Lease deals with the various properties in the same way, imposing the same lease terms upon each location, except for the amount of rent allocated to the various locations. There is nothing in the evidence or in the Energy Lease that suggests that the various stores cannot be operated separately and independently of each other in accordance with the provisions of the lease. It thus appears from the nature of the properties and the terms of the Energy Lease that the Energy Lease can be divided

into separate and independent leases for one or more of the properties. The subject matter aspect of the test for determining whether a contract is divisible therefore weighs in favor of a finding that the Energy Lease is a divisible contract.

3. Conduct of the Parties

The third point of focus under Texas law in determining whether a contract is divisible is the conduct of the parties. USRP points out that following the execution of the Energy Lease, the Debtors paid the rent under the lease by means of a single payment that was wire transferred into a sweep account that USRP was required to maintain for its lender. USRP argues that this method of payment reflects that there was no allocation of the rent among the various leased properties. However, the evidence also showed that following the execution of the lease the parties followed through with the provisions of the Energy Lease calling for an allocation of the rent and generated a schedule that incorporated both components of the "base rent" (i.e., the \$13,075,000.00 cost of the properties and the amount of the expenses incurred by USRP in purchasing the properties) and which specifically set forth an allocation of the annual and monthly rent for each of the 27 properties. With such an allocation in place, making a single payment into the sweep account had little significance since such payments could be allocated at any time using an allocation that was in place for just such purpose. The

court therefore concludes that the conduct of the parties also favors a finding that the Energy Lease is divisible.

In summary, having considered the intent of the parties, the subject matter of the Energy Lease and the conduct of the parties the court finds and concludes that the Energy Lease is a divisible contract such that each of the 27 leased properties may be regarded as the subject of a separate executory contract that stands on its own and may be dealt with separate and apart from the other leased properties.

B. Application of Bankruptcy Law

While state law is controlling on the issue of whether the Energy Lease is divisible, the rejection or assumption of executory contracts or unexpired leases pursuant to § 365 of the Bankruptcy Code is governed solely by federal law. See Otto Preminger Films, Ltd. v. Qintex Entm't, Inc., 950 F.2d 1492, 1495 (9th Cir. 1991); In re Wheeling-Pittsburgh Steel Corp., 54 B.R. 772, 779 (Bankr. W.D. Pa. 1985). Section 365 was intended to permit a DIP to pick and choose among the debtor's executory contracts and unexpired leases and to assume those which are beneficial to the estate and to reject those that are not beneficial. It having been determined in the present case that the Energy Lease is divisible into separate leases, the issue of whether the Debtors may reject six of those unexpired leases at this time is a matter of federal law involving the application of

§ 365.

1. Effect of Default Provisions

As noted above, paragraph 17.2(b), in effect, is a cross-default clause, since it purports to permit the landlords to terminate all of the leases based upon a default with respect to only one of the leased properties. USRP argues that the default provisions have the effect of inextricably intertwining the leases in such a fashion that the Debtors cannot reject less than the entire Energy Lease. In the bankruptcy context, it is well established that cross-default provisions do not integrate executory contracts or unexpired leases that otherwise are separate or severable. See In re Plitt Amusement Co. of Washington, Inc., 233 B.R. 837, 847 (Bankr. C.D. Cal. 1999). Moreover, cross-default provisions are unenforceable in bankruptcy where they would restrict the debtor's ability to fully utilize the provisions of § 365 with respect to an executory contract or unexpired lease. See In re Sanshoe Worldwide Corp., 139 B.R. 585, 597 (S.D.N.Y. 1992); In re Braniff, Inc., 118 B.R. 819, 845 (Bankr. M.D. Fla. 1989). The permissible limitations on the ability of a DIP to assume and assign executory contracts or unexpired leases under § 365 are found in § 365(c). Any contractual restriction on assignment under § 365 other than those specified in § 365(c) is invalidated by § 365(f). Thus, where a debtor is a party to a number of unexpired leases, cross-default clauses that would serve to prevent the

debtor from assuming some of the leases without assuming the others at the same time are unenforceable under § 365(f). See In re Sambo's Rests., Inc., 24 B.R. 755, 757-58 (Bankr. C.D. Cal. 1982).

In the present case, because the Energy Lease is divisible, the Debtor in effect is a party to 27 separate unexpired leases. If given effect, the cross-default provisions in this case would prevent the Debtors from utilizing the provisions of § 365 to reject some of those leases, while reserving the decision whether to reject or to assume and assign the remaining leases to a later time. If the cross-default provisions were permitted to operate in such a fashion they would have the effect of foreclosing the ability of the Debtors possibly to assume and assign the other 21 leases pursuant to § 365. Such a result is contrary to § 365(f) and is not permissible under bankruptcy law. It follows that the default provisions in the present case do not limit the ability of the Debtors to reject six of the leases at this time, while leaving to another day the decision whether to reject the remaining leases or whether to assume and assign them in accordance with the provisions of § 365.

2. Standard Applicable to Motion to Reject

The standard to be applied in this case in determining whether the Debtors' decision to reject should be approved is the business judgment standard or test. See Lubrizol Enters, Inc. v. Richmond Metal Finishers, Inc., 756 F.2d 1043, 1047 (4th Cir. 1985). Where

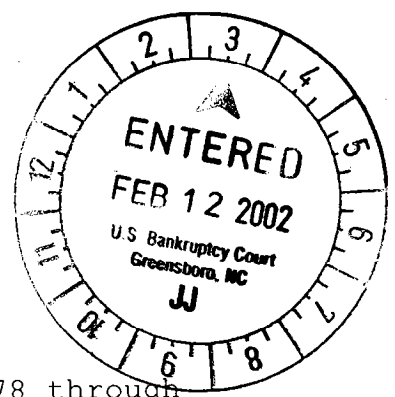
the debtor's decision to reject an executory contract represents an exercise of sound business judgment, the decision should be approved by the court. The Debtors have sustained continuing losses from the operation of the stores located on the properties referred to in the Motion despite efforts to improve operations at the stores. There is no market for the stores at the current rental rates for the properties and unless the stores are closed the Debtors will continue to sustain significant losses at each location. Under these circumstances, Debtors' decision to close the stores in order to avoid further losses to the estate represents an exercise of sound business judgment. Accordingly, the Motion should be granted and the rejection sought by Debtors should be approved. A separate order so providing will be entered contemporaneously with the filing of this memorandum opinion.

This 12th day of February, 2002.

William L. Stocks

WILLIAM L. STOCKS
United States Bankruptcy Judge

UNITED STATE BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION



IN RE:)
)
Convenience USA, Inc., et al.,) Case No. 01-81478 through
) 01-81489 (Administratively
Debtors.) Consolidated)
)

ORDER

In accordance with the memorandum opinion filed contemporaneously herewith, it is ORDERED, ADJUDGED AND DECREED as follows:

(1) The Motion of Debtors to Reject Certain Unexpired Non-Residential Real Estate Leases is granted and the rejection by Debtors of the unexpired leases of the properties listed on attached Exhibit A is approved;

(2) Such rejection shall be effective as of January 31, 2002, provided that the Debtors vacate the premises listed on Exhibit A by February 14, 2002; and

(3) The lessors listed on Exhibit A shall have 60 days from the date of this order within which to file any claims for damages based upon Debtors' rejection pursuant to this order.

This 12th day of February, 2002.

William L. Stocks

WILLIAM L. STOCKS
United States Bankruptcy Judge

Store No.	Address	Lessor
810	648 Waughtown Street Winston-Salem, NC	USRP (Gant 2), LLC
812	1078 Cedar Point Blvd. Swansboro, NC	USRP (Gant 2), LLC
815	4862 Arendell Street Morehead City, NC	USRP (Gant 3), LLC
818	150 Highway 70W Havelock, NC	USRP (Gant 3), LLC
830	1310 Live Oak Street Beaufort, NC	USRP (Gant 5), LLC
832	1915 West Webb Avenue Burlington, NC	USRP (Gant 5), LLC