State of New Hampshire Supreme Court

NO. 99-317

2000 TERM

AUGUST SESSION

TILTON ASSOCIATES a/k/a TILTON PLAZA ASSOCIATES, L.P

v.

TILTON VARIETY, INC. d/b/a BEN FRANKLIN CRAFTS

RULE 7 APPEAL FROM FINAL DECISION OF FRANKLIN DISTRICT COURT

BRIEF OF DEFENDANT, BEN FRANKLIN CRAFTS

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QUESTIONS PRESENTED

1. Did the Franklin District Court properly grant the defendant Ben Franklin Crafts's motion to dismiss because the meaning of terms of a lease between it and its landlord had been fully litigated and decided by the federal bankruptcy court?

STATEMENT OF FACTS AND STATEMENT OF THE CASE

This case arose in the context of a commercial landlord and tenant lease dispute, but has its roots in two earlier federal bankruptcy court decisions.

I. Landlord and Tenant Dispute

The plaintiff, Tilton Associates, owns and manages the Town Line Plaza shopping center on Route 3 in Tilton, New Hampshire. The defendant, Tilton Variety, Inc., leases a store in the shopping center called Ben Franklin Crafts.

The lease between the parties, originally executed in 1976, contains a clause giving the tenant a discount on its rent in the event the anchor store ceased operation. The A&P supermarket was the anchor store, but it closed its doors in April, 1992. In 1993 Ben Franklin invoked the clause and abated its rent pursuant to it.

The original lease was for 15 years, but contains an option allowing the tenant to renew it for 5 years at a time. The lease was renewed in 1991 subject to the abated rent. In 1995 Ben Franklin again notified its landlord that it would renew the lease and that it intended to continue paying the abated amount. The landlord objected, claiming that the lease did not allow the abatement to continue into successive option periods.

In September 1998, the landlord served Ben Franklin with a Notice to Quit based on the non-payment of the abated portion of the rent. Had this case gone to trial, the Franklin District Court would have decided it in large part on the interpretation of the option and abatement clauses, and whether they allow Ben Franklin to continue abating its rent.

II. New Jersey Federal Bankruptcy Court Litigation

Several years ago, Tilton Plaza Associates, the landlord in this case, went bankrupt. The matter was litigated in and resolved by the United States Bankruptcy Court for the District of New Jersey.

In bankruptcy, leases are considered a type of executory contract which must be either assumed or rejected by the bankruptcy estate. 11 U.S.C. §§ 365(a) & (f). If a lease is assumed, it can be assigned to a party if there are appropriate assurances that the party will pay the rent. *See*, COLLIER ON BANKRUPTCY, ¶ 365.05[5][a] (15th ed. 1996).

During the litigation, Tilton Plaza vigorously contested the assignment of the lease to Ben Franklin on the grounds that the lease's option clause did not allow Ben Franklin to continue abating its rent. The matter was fully litigated, with Tilton Plaza filing a 5-page complaint and a 24-page memorandum of law expressing its position. COMPLAINT (June 24, 1997), *Appx. to N.O.A.* at 27-31; MEMO OF LAW (Sept. 15, 1997), *Appx. to N.O.A.* at 27-31.

The complaint was signed by "Carol Knowlton, Esq.," who is identified as "Attorneys for the Debtor, Tilton Plaza Associates, L.P." COMPLAINT, *Appx. to N.O.A.* at 27-31.

III. Illinois Federal Bankruptcy Court Decision

Ben Franklin, the tenant in this case, also went bankrupt. That bankruptcy was heard by the United States Bankruptcy Court for the Northern District of Illinois. The bankruptcy trustee filed a motion to assume the lease and to assign it to the tenant in this case. In its order, the Illinois court said: "it appearing that good and sufficient notice of the Motion [to assume and assign] having been provided by the Trustee to the case Service List and *to Carol Knowlton, counsel for Tilton Plaza Associates, L.P. (the 'Landlord')*." ORDER GRANTING TRUSTEE'S MOTION FOR AUTHORITY TO ASSUME AND ASSIGN LEASE FOR TILTON, NEW HAMPSHIRE PROPERTY (Feb. 18, 1996), *Appx. to N.O.A.* at 21 (emphasis added).

After a hearing, the Illinois court found that no arrearage existed with regard to the lease and that adequate assurances existed for continued payment of rent. The court thus approved the assumption and assignment of the lease to the tenant here.

IV. Collateral Estoppel

After it was served with a Notice to Quit in the current case, Ben Franklin filed a motion to dismiss on the grounds that the meaning of the lease terms, which ostensibly would be decided in the landlord/tenant case, had been resolved by the bankruptcy courts and that further litigation of them was, therefore, collaterally estopped. MOTION TO DISMISS, *Appx. to N.O.A.* at 9.

There was a procedural wrinkle, however. After Ben Franklin's motion to dismiss, *id.*, the landlord objected. PLAINTIFF'S OBJECTION TO MOTION TO DISMISS, *Appx. to N.O.A.* at 13. By leave of the court, Ben Franklin supplemented its first motion with a second motion to dismiss, to which it appended the various bankruptcy court documents showing collateral estoppel. MOTION TO DISMISS, *Appx. to N.O.A.* at 18. The landlord filed no objection. Based on

these pleadings, the court dismissed the matter. ORDER, *Appx. to N.O.A.* at 56. The landlord then filed a motion to reconsider, in which it alleged that the court had erred procedurally in dismissing the case because the landlord believed it had additional time to file its objection. PLAINTIFF'S MOTION TO RECONSIDER ORDER OF DISMISSAL, *Appx. to N.O.A.* at 57. The landlord simultaneously filed its objection to the defendant's second motion to dismiss. PLAINTIFF'S OBJECTION T DEFENDANT'S SECOND MOTION TO DISMISS, *Appx. to N.O.A.* at 63. In it, the landlord addressed the collateral estoppel issue. It claimed that it had had no notice of the Illinois bankruptcy court proceeding, and alleged that collateral estoppel does not apply to assumption and assignment proceedings. The Franklin District Court denied the motion for reconsideration, and noted that it did so based on the application of collateral estoppel. ORDER, *Appx. to N.O.A.* at 70.

The landlord filed this appeal.

SUMMARY OF ARGUMENT

The defendant, Ben Franklin Crafts, first argues that the bankruptcy court heard and decided the meaning of lease terms, and that its construction of them was appropriately given collateral estoppel effect by the Franklin District Court. The defendant points out that the plaintiff landlord has presented no viable argument or authority to the contrary.

Ben Franklin then argues that despite an appearance of procedural error, the District Court made clear that it based its decision on the substance of the party's pleadings, and if there was error it was harmless.

ARGUMENT

I. Collateral Estoppel Applies to this Case Because the Bankruptcy Court Heard and Decided the Meaning of the Lease Terms in a Proceeding in Which the Matter was Fully Litigated

Collateral estoppel applies in this case because the issue before the Franklin District Court – the construction of the option and abatement clauses – was heard and decided by the federal bankruptcy court.

The landlord claims, however, that collateral estoppel does not apply because the proceeding in the bankruptcy court was to determine assumption and assignment, and that type of determination cannot have estoppel effect. For this conclusion, the landlord cites *Grossman v. Murray*, 141 N.H. 265 (1996).

In *Grossman* this Court found that neither *res judicata* nor collateral estoppel applied to the defendant's counterclaim that it had the right of first refusal to buy a piece of property. The Court ruled that while *res judicata* and collateral estoppel generally apply to the decisions of the federal bankruptcy court, bankruptcy court "contested matter" proceedings do not automatically bar re-litigation of an issue. The Court held that the counterclaims were not barred because the underlying issues had not nor could have been raised in the bankruptcy court.

Grossman correctly points out that "contested matter" proceedings, as distinguished from "adversary proceedings," are "generally designed for the adjudication of simple issues, often on an expedited basis." *Grossman*, 141 N.H. at 270 (quotations omitted). The difference between the two are the formality of the procedural rules. Proceedings to determine assumption of an executory contract are generally contested matters, but the bankruptcy court may employ the more formal rules if the issues are complex or contentious. COLLIER ON BANKRUPTCY, ¶

9014.05 (15th ed. 1996).

The preclusive effect of prior judgments is determined on a case by case basis. *Hallisey v. DECA Corp.*, 140 N.H. 443, 445 (1995). The record here does not reveal what type of proceeding was held by the bankruptcy court. It is clear, however, that the construction of the option and abatement clause in this case were fully litigated – the landlord itself filed a filed a 5-page complaint and a 24-page memorandum of law on the issue. Thus, while simple issues decided in contested matter proceedings should not be given collateral estoppel effect in accord with *Grossman*, when the issues were well litigated in the bankruptcy court, a party should be estopped from revisiting them. *C.f. M.A. Crowley Trucking v. Moyers*, 140 N.H. 190 (1995).

The landlord also cites a second circuit bankruptcy appeal, *In re Orion Picture's Corp. v. Showtime Networks*, 4 F.3d 1095 (2d Cir. 1993), for the proposition that a bankruptcy court decision on assumption of an executory contract cannot have subsequent collateral estoppel effects. The landlord's argument is that a bankruptcy court makes its assumption decision in its "business judgment" role, and not in its legal role.

Not only did the *Orion* court assert this without citation, but the landlord here misconstrues the *Orion* dicta.

It is clear that a bankruptcy court makes a decision about the assumption of an executory contract based on its best business sense. But in this case *nobody* is claiming estoppel based on the bankruptcy court's assumption decision. Rather, Ben Franklin is relying on the bankruptcy court's legal conclusions regarding the construction of lease terms. The bankruptcy court in this case *first* construed the lease to mean that the abatement provision applies during the option period, and *then* determined that (that being so) it was a good business decision to assume and

assign the lease to Ben Franklin. If Ben Franklin was before this Court claiming collateral estoppel effect of the bankruptcy court's assumption and assignment decision itself, the landlord here might have a cogent *Orion*-based argument. But because Ben Franklin is relying solely on the bankruptcy court's legal judgment, and not its business judgment, the *Orion* logic does not apply.

The *Orion* court said as much in the passage quoted by the landlord:

> "[I]t is important to keep in mind that the bankruptcy court's 'business judgment' in *deciding a motion to assume* is just that – a judgment of the sort a businessman would make. In no way is *this decision* a formal ruling on the underlying disputed issues, and thus will receive no collateral estoppel effect.

Orion, 4 F.3d at 1099 (emphasis added). The words "this decision" refers to "deciding a motion to assume," not to outstanding disputed issues.

The other cases cited by the landlord are not helpful. They are all bankruptcy cases that do not require application of collateral estoppel, and all merely cite *Orion* with no further authority or argument for the landlord's position. *See In re Gateway Apparel, Inc.*, 210 B.R. 567, 570 (Bkrtcy. E.D. Mo. 1997); *In re Gucci*, 193 B.R. 411, 414-15 (S.D. N.Y. 1996); *Big Rivers Elec. Corp. v. Green River Coal Co., Inc.*, 182 B.R. 751, 756 (W.D. Ky. 1995).

Courts have recognized the need to give collateral estoppel effect to the bankruptcy court's determination of issues. *See In re Dibert, Bancroft & Ross Co.*, 117 F.3d 160, 179 (5th Cir. 1997) (collateral estoppel bared re-litigation of "essentially identical" issue decided by bankruptcy court's order of sale); *In re PCH Associates*, 949 F.2d 585 (2d Cir. 1991) (collateral estoppel not applied because bankruptcy court made plain in its order determining assumption of executory contract that it was not deciding issue being later litigated); *Puett v. McCannon*, 358

S.E.2d 300 (Ga. App. 1987) (collateral estoppel not applied because issue being later litigated was not in dispute in the bankruptcy court's determination of assumption of the lease); *Atiyeh v. Bear*, 690 A.2d 1245 (Pa. Super. 1997) (collateral estoppel applied because the bankruptcy court had determined in a proceeding to determine assumption of executory contract that the party had breached the contract); *Adams v. Wilhite*, 636 S.W.2d 851 (Tex.App. 1982) (collateral estoppel applied because same issue determined by bankruptcy court).

II. Collateral Estoppel Applies to this Case Because the Bankruptcy Court Heard and Decided the Meaning of the Lease Terms in a Proceeding in Which the Landlord was Notified

The landlord claims that it was not notified of the proceeding in which the bankruptcy court construed the lease terms.

The bankruptcy court order specifically noted that the landlord's attorney was given "good and sufficient notice." ORDER GRANTING TRUSTEE'S MOTION FOR AUTHORITY TO ASSUME AND ASSIGN LEASE FOR TILTON, NEW HAMPSHIRE PROPERTY (Feb. 18, 1996), *Appx. to N.O.A.* at 21 (emphasis added).

Accordingly, the landlord's claim is impossible to substantiate. Collateral estoppel should be applied, and the issues should not be re-litigated in this proceeding.

III. Ben Franklin Met the Elements of Collateral Estoppel

> "In order for collateral estoppel to apply, . . . the following elements must be satisfied: (1) the issue subject to estoppel must be identical in each action; (2) the first action must have resolved the issue finally on the merits; (3) the party to be estopped must have appeared in the first action or have been in privity with someone who did; (4) the party to be estopped must have had a full and fair opportunity to litigate the issue; and (5) the finding must have been essential to the first judgment."

Farm Family Mutual Ins. Co. v. Peck, ___ N.H. ___ (decided June 16, 1999).

Ben Franklin has met the elements of collateral estoppel. The issues in this case are the same as that resolved by the bankruptcy court after the landlord fully litigated them, the parties are the same, and the bankruptcy court's construction of the lease terms was essential to its judgment.

Accordingly, the elements of collateral estoppel have been met, and the landlord here has provided no argument or authority against the Franklin District Court's decision to give the bankruptcy court's order collateral estoppel effect. Its decision must, therefore, be affirmed.

IV. The District Court Based its Decision on the Substance of the Parties' Collateral Estoppel Arguments, Making the Landlord's Procedural Argument Moot

The landlord did not object to Ben Franklin's motion to dismiss. Litigants have ten days in which to object to such motions. DIST.CT.R. 1.8 D. If a party makes no objection, "that party shall be deemed to have waived a hearing and the court may act" on the motion. *Id.* In this case, the landlord did not object to Ben Franklin's motion, and the court was entitled to grant the motion to dismiss on procedural grounds alone.

Nonetheless, the landlord makes a procedural claim that the district court erred in that "it may well have disregarded" the landlord's objection to the plaintiff's second motion to dismiss. *Plaintiff's Br.* at 8.

The landlord filed the objection on April 22, 1999. The district court issued its order on April 30, 1999. Because the order makes reference to the matters contained in it, it must be presumed that the court had in hand the landlord's objection. In the last sentence of its order, the court made clear that its decision was based, not on the procedural issues, but on application of the doctrine of collateral estoppel. ORDER, *Appx. to N.O.A.* at 70 ("This Court granted the Defendant's Motion based on supporting documents to the Motion and adopted the Defendant's position that the Doctrine of Collateral Estoppel applies.").

Several previous sentences in the order chide the landlord for misreading the district court rules. Those sentences express the court's displeasure at what it apparently considered sloppy practice, and are probably intended to instruct the litigant and its attorney on the correct interpretation of the rules. But those sentences have no legal effect, and the court made plain that it did not base its decision on any procedural defect. If the court made a procedural error, it is

thus harmless. *See Semprini v. Railroad*, 87 N.H. 279, 281 (1935) (court's ruling harmless when it had no legal effect and did not result in any finding of fact or ruling of law).

CONCLUSION

Ben Franklin has met the elements of collateral estoppel, and the landlord has failed to present any argument or authority to undermine them. Accordingly, the district court's order should be affirmed.

Respectfully submitted,

Ben Franklin Crafts
By its Attorney,

Law Office of Joshua L. Gordon

Dated: August 8, 2000

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REQUEST FOR ORAL ARGUMENT AND CERTIFICATION

Counsel for Ben Franklin requests that Attorney Charles W. Chandler be allowed 15 minutes for oral argument.

I hereby certify that on August 8, 2000, copies of the foregoing will be forwarded to Arthur G. Green, Esq.; and to Glenn A. Perlow, Esq.

Dated: August 8, 2000

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