UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK

In Re:

JOHN RIVA,

Debtor.

BK. NO. 90-21609

DECISION AND ORDER

BACKGROUND

On August 1, 1990, the debtors, John Riva ("Riva"), Riva Development Corporation ("Riva Development") and Riva Management Corporation ("Riva Management") each filed separate voluntary petitions initiating Chapter 11 cases. The debtors operate there Burger King restaurants in the Rochester, New York area. These restaurants are located at 750 West Ridge Road ("Ridge Road"), Midtown Plaza ("Midtown") and 1100 Jefferson Road ("Jefferson Road").

At the time of the filing of the petitions on August 1, 1990, Riva, individually, was the holder of franchise agreements from Burger King Corporation ("Burger King") covering the Midtown and Jefferson Road locations. As to the Ridge Road location, Riva had previously assumed from a former operator both a restaurant franchise agreement and a sublease of the premises which had been entered into with Burger King. The assumed franchise agreement and sublease, after several extensions, appear to have terminated on March 19, 1990. (This decision will not determine the existing legal relationship between Riva and Burger King as to the Ridge Road location.)

By the end of February 1991 Riva was $70, 617.58 in arrears in post-petition payments due to Burger King for royalties, advertising and base and percentage rent for the Ridge Road location. Riva claims the primary reason for this was an overall loss of revenue resulting when a December, 1990 fire at the Jefferson Road location, the largest volume location, caused the restaurant to close until April 22, 1991. By motion dated March 1, 1991 Burger King sought an order: 1) directing Riva to assume or reject the franchise agreements for Midtown and Jefferson Road, and requiring that all post-petition arrearages be immediately paid if the agreements were assumed; 2) directing that Riva immediately pay all post-petition arrearages due in connection with the Ridge Road location, or in

the alternative that Burger King be allowed to regain possession of the premises; and 3) requiring that if Riva assumed the franchise agreements and cured the post-petition arrearages at Ridge Road, he make future monthly payments when due or the agreements would be deemed automatically rejected.

On March 25, 1991, an order was entered by the Honorable Edward D. Hayes. who retired on January 2, 1992, which: 1) required that Riva pay Burger King $5,000 per week on each and every Monday commencing on the earlier of May 6 or the first Monday after the Jefferson Road store reopened until the $70,617.58 in post-petition arrearages were paid in full; 2) required that all invoices issued by Burger King to Riva for charges accruing after March 1, 1991 be paid timely in accordance with the terms of the agreements between the parties; and 3) provided that "if the Debtor fails to make any of the payments required by this Order, each of the Debtor's two franchise agreements, the franchise-at-will agreements and the lease-at-will shall be deemed rejected upon the date of said default and Burger King Corporation shall be free to take whatever steps are necessary to regain possession of the premises utilized by the Debtor and the equipment and materials owned by Burger King Corporation and used by the Debtor pursuant to the franchise agreements and/or lease, without further order of this Court."

There is no dispute that at no time between March 25, 1991 and December 20, 1991 was Riva ever in full compliance with the terms of the Court's March 25, 1991 order, or that between March 25, 1991 and December 20, 1991 Burger King accepted payments from Riva, including payments for charges incurred after March 25, 1991 which were late, in some case as much as 193 days late.

After a July 10, 1991 telephone conference among Raymond L. Miolla, Jr., senior attorney at Burger King ("Miolla"), Riva and counsel for Riva and Burger King and a July 22, 1991 telephone conference among Miolla and counsel for Burger King and Riva, Miolla forwarded a letter to counsel for Riva. This July 22, 1991 letter states that the purpose of the letter is to confirm the discussions during the July 22, 1991 telephone conference to the effect that various things which

Burger King required Riva to do, as outlined in the July 10, 1991 telephone conference, had not been completed, including a requirement that Riva continue to make weekly payments of $1,500 against pre-petition arrearages and that he remain current on post-petition charges. The July 22, 1991 letter from Burger King to Riva's attorneys also states that "Based on the foregoing, any offer by Burger King Corporation to waive or restructure its rights under the order obtained by the Bankruptcy Court on March 25, 1991, is hereby withdrawn and Burger King Corporation reserves all rights under said order. No delay by Burger King Corporation in exercising those rights shall constitute a waiver thereof. Burger King Corporation is currently examining its options, and will contact the landlords for the restaurants in which your client is located in an effort to determine what disposition of the property will occur should the bankruptcy proceedings be converted to a Chapter 7 proceeding."

On December 20, 1991 the attorneys for Burger King sent out a Notice That Certain Leases and Agreements are Deemed Rejected. This Notice advised that the franchise agreements, the franchise-at-will agreement and the lease-at will between Riva and Burger King are "deemed rejected by reason of Debtor's failure to make all of the payments required" by the Court's March 25, 1991 order.

In conversations which occurred between counsel after the December notice was received, Riva learned that Burger King had entered into a contract to enter into new franchise agreements with another entity and that Burger King would not consent to Riva selling or assigning to anyone his rights under the prior agreements with Burger King that had been deemed rejected.

After receiving the December 20, 1991 notice Riva, by his attorneys, offered to immediately bring all post-petition payments due to Burger King current. At that time, the amount required was $21,730.97. Because it would have been required to waive its deemed rejected position regarding its relationships with Riva, Burger King chose not to accept the amount offered.

By motion dated January 13, 1992 and returnable February 3, 1992, Burger King moved to convert Riva's Chapter 11 case to a Chapter 7 liquidation case. One of the reasons why Burger King

alleged that the case should be converted was the fact that on December 20, 1991 Burger King confirmed that the lease and franchise agreements with the debtor were deemed rejected pursuant to the terms of the March 25, 1991 Bankruptcy Court order. In his response to the motion to convert, on the issue of whether the agreements with Burger King were in fact deemed rejected, Riva alleged that by its conduct Burger King were in fact deemed rejected, Riva alleged that by its conduct Burger King is estopped to enforce and in fact has waived any rights under the March 25, 1991 order to deem the agreements rejected by reason of Riva's payment defaults.

By motion dated January 24, 1992 and returnable February 3, 1992, Carrols Corporation ("Carrols"), a major unsecured creditors as a supplier to the restaurants in nine different states, moved for the appointment of a Chapter 11 trustee.

By motion dated January 24, 1992, and returnable February 3, 1992, William Burns, the landlord of the Jefferson Road premises, moved for an order rejecting the Jefferson Road lease and for relief from the automatic stay on the grounds that Riva was in default under his lease by reason of being in default of his franchise agreement with Burger King based on Burger King's December 20, 1991 notice.

Thereafter, the motions to convert, for the appointment of a trustee and for the rejection of the Jefferson Road lease were adjourned to February 4, 1992. At that time a comprehensive case scheduling order was granted by the Court. The pending motions were adjourned to February 18, 1992, at which time a hearing was scheduled for March 31, 1992 to take testimony and evidence on the issue of whether the relationships between Riva and Burger King had been properly deemed rejected pursuant to the Court's March 25, 1991 order and/or whether on equitable grounds the Court would refuse to allow the enforcement of any such rejection.

At the March 31, 1992 hearing the Court heard the testimony of Riva, Miolla, and Robin Wright, the finance manager for Riva Development.

DISCUSSION

From the extensive pleadings before the Court in connection with the motions for conversion, the appointment of a trustee and rejection of the Jefferson Road lease, it is clear that the pending Chapter 11 cases were not progressing as quickly as they might have. It is also clear that Burger King may very well have been justified in its obvious frustration with this lack of progress, some of the things that Riva or his attorney were or were not doing and Riva's apparent perceived lack of attention to the relationship between himself and Burger King in connection with the overall plan process and reorganization. It is also clear, however, that Riva's three Burger King restaurants were being well run in terms of quality control, cleanliness and customer satisfaction, and that a three-location unit, the operations since July 1991, after the Jefferson Road location had reopened, were profitable and as going concerns had significant value. At the hearing, Riva testified that, based on his percentage of sale analysis, as applied to the particular facts and circumstances of each location as ongoing operations his three Burger King restaurants could have a going concern value of in excess of $1,750,000 (Jefferson Road $1,000,000; Ridge Road - $350,000; and Midtown - $400,000).

The March 25, 1991 order of the Bankruptcy Court, as consented to by Riva's attorneys, is self-executing and does not provide for a notice of default, cure period or other recourse to the Bankruptcy Court in the event of a default, even a technical or minor default. The order provides that if the debtor fails to make any of the payments required by the order, each of the debtor's agreements shall be deemed rejected upon the date of said default. From the pleadings before the Court and the testimony at the hearing, if appears that the parties did not believe or intend that the order would be literally or strictly construed.

At the hearing, Riva testified that in conversations at the time of Burger King's March 1991 motion when he expressed concern about the ability to meet the requirement that the debtor pay $5,000 per week towards the arrearages and keep current, there were statements by Miolla that "we

will work it out." In the Memorandum of Law submitted in support of Burger King's motion to convert, it states "in the first instance, BKC has recognized from the start that Chapter 11 proceedings are equitable in nature. There is no way that BKC could expect or did expect that it would be able to sustain a deemed rejected status to the franchise agreements merely as a result of one or a few tardy payments. Thus, there was an effort to work with the debtor after (as well as before) March 25, 1991." (Burger King's conversion motion at 9.) From the foregoing and the testimony at the hearing, this Court concludes that the provisions of the March 25, 1991 order of the Bankruptcy Court were intended by the parties to be a best efforts goal for the repayment to Burger King of the pre-March 1, 1991 post-petition arrearages and the subsequent charges that would become due to Burger King from Riva during the course of the Chapter 11 proceedings.

Undisputed testimony at the hearing on March 31, 1991 indicates that at not time between March 25, 1991 and December 20, 1991 was Riva in compliance with the Court's March 25, 1991 order. In fact it was not until late June 1991 that Miolla, who testified that he had insisted on the self-executing provision of the order, first focused on Riva being in default. It is also clear from the testimony that at no time, despite Burger King's knowledge or Riva's payment defaults, did Burger King ever give Riva specific notice of a time within which he could or must cure any payment defaults and bring himself into compliance with the order. In addition, at no time between March 25, 1991 and December 20, 1991 was Riva advised that because of his failure to make the payments as required by the order that his various agreements with Burger King had been "deemed rejected" in accordance with the provisions of the order. Although various "messages" of frustration, displeasure, non-waiver, and unclear statements that Burger King was going to do something about finding replacement franchisees were delivered in the telephone conferences of July 10 and July 22, Burger King's July 22, 1991 letter and in a conversation between Miolla and Riva in November of 1991, Burger King continued to accept late payments from Riva without ever giving him a specific notice of default and a time within which to cure existing payment defaults.

From the pleadings of the parties in connection with the pending motions and the testimony on March 31, it appears that Burger King was less than straight forward with Riva, not about its frustrations with his overall progress in the Chapter 11 and Riva's failure to establish a good working relationship with Burger King in the plan and reorganization process (Burger King was very clear about that), but with respect to its true intentions regarding: 1) attempting to find replacement franchisees to which it would issue new franchises directly, essentially preventing Riva and his creditors from realizing any or at least fair value for the restaurants as going concerns; and 2) defaulting Riva for nonpayment and deeming the relationships with Burger King rejected without ever clearly advising him that Burger King was at some future time going to insist on strict performance under the March 25, 1991 order, and giving him an opportunity to bring all postpetition arrearages current before that time.

This Court is aware of the importance of enforcing the provisions of the Court's own orders and of not discouraging creditors from dealing fairly and in good faith with debtors attempting to reorganize, and even in some cases not having those creditors insist on absolute strict performance without having to fear that they will waive their rights. However, based on the facts and circumstances of this case, it is clear that Burger King prior to July 22, 1991 intended to and did by its conduct waive its rights to strict performance of the payment terms of the Court's March 25, 1991 order. Thereafter, except for its July 22, 1991 letter, Burger King continued exactly as before to accept late payments, and did not in good faith dealing take any clear and specific act prior to December 20, 1991 sufficient to put Riva on notice that it would require strict performance under the order after a reasonable opportunity to cure any defaults which had occurred during the period when it had waived strict performance. Certainly Burger King's July 22, 1991 letter did not do this.

A waiver is the intentional relinquishment of a known right which may be accomplished by express agreement or by such conduct or failure to act as to evince an intent not to claim the proposed advantage. Gerald R. Hadden v. Consolidated Edison Company of New York, Inc., 45

N.y.Sd 466, 469, 410 N.Y.S.2d 274, 382 N.E.2d 1136 (1978). Waiver is always a matter of intent. In re Willow Cafeterias, Inc., 95 F.2d 306, 309 (2nd Cir. 1938), cert. denied sub nom., Willow Cafeterias, Inc. v. 650 Madison Avenue Corp., 304 U.S. 567 (1938). While the intent to waive may be inferred from the acceptance of payments under certain circumstances, acceptance itself does not establish waiver as a matter of law. If there is a course of conduct of accepting late payments, there has to be notice of an intent to require strict compliance before terminating. Palmer and Singer Manufacturing Co. v. Barney Estate Co., 149 A.D. 136, 137, 133 N.Y.S. 876, 879 (1st Dept. 1912); see In re Delta Hotel of Syracuse, 10 B.R. 585, 597 (Bankr. N.D.N.Y. 1981). In Delta Hotel, the bankruptcy court found that a waiver had occurred in a similar factual situation where lessors had accepted late payments numerous times and never gave notice that they were going to demand strict compliance with the lease before they terminated the lease. 10 B.R. at 597. To the contrary, in In re Family Showtime Theatres, Inc., 72 B.R. 38, 43 (Bankr. E.D.N.Y. 1987), the court decided that there was no waiver since the lessor did give clear notice of termination of the sublease and when it granted extensions of time to negotiate and accepted rent payments the lessor expressly reserved its right to claim that the lease was terminated.

The Court after listening to the testimony of Miolla and Riva with respect to the July 10, 1991 and November 1991 telephone conversations, reviewing the Burger King letter of July 22, 1991, which although it contains non-waiver language does not contain clear language affording an opportunity to cure and insisting on strict performance thereafter, and confirming from the testimony and the exhibits regarding payments, Burger King's continuing acceptance of late payments throughout the period between March 25, 1991 and December 20, 1991, after each of the above contacts, can only conclude that Burger King by its total conduct waived its rights to insist upon strict performance of the payment terms of the March 25, 1991 order.

In this case, Riva has also argued that Burger King should be equitably estopped from being able to enforce the deemed rejected provision of the March 25, 1991 order. Under New York law,

the essential elements required which relate to the party to be estopped are:

(1) conduct which amounts to false representation or concealment of material facts or which gives the impression that the facts are otherwise than as asserted,

(2) intention or expectation that such conduct would be relied upon by the other party,

(3) actual and constructive knowledge of the real facts, The elements relating to the party asserting the estoppel; defense are:

(4) lack of knowledge of the real facts,

(5) reliance on the conduct of the party to be estopped, and

(6) action based thereon resulting in a prejudicial change of position.

In re Delta Motor Hotel of Syracuse, 10 B.R. 585, 598 (Bankr. N.D.N.Y. 1981). In addition, it must be shown that the party asserting the estoppel defense acted in good faith.

In this matter there is no allegation that Riva did not act in good faith with respect to the payments to Burger King, and the testimony given and the exhibits produced at the hearing establish the following facts concerning Burger King, the party to be estopped:

(1) Burger King did not promptly seek to enforce or insist upon strict compliance with the provisions of the March 25, 1991 order. Although Burger King knew that Riva had not at any time fully complied with the order for the period of March 25 to December 20, 1991, until December 20, 1991 it never clearly stated that Riva was in default and that it would deem the various relationships with Riva rejected. Furthermore, after the July 22, 1991 letter, Burger King, while it was accepting late payments, never advised Riva that it was negotiating for new franchise agreements with the Kessler Group, a local group which owns and/or operates a number of other Burger King restaurants in the Rochester area, and would deem the Riva relationships rejected only when it had entered into a contract for new franchise agreements. Even if Riva had cured the defaults after the contract with the Kessler Group was entered into in late November, Burger King, because of its contract with the Kessler Group, might have declared the Riva relationships deemed rejected at some date prior to the

date it entered into the contract with the Kessler Group. This course of conduct of continuing to accept late payments concealed the fact that Burger King was negotiating for new franchise agreements which would not allow Riva and his creditors to realize on the value of his restaurants, and failed to give Riva clear notice that his relationships with Burger King might be terminated for failure to strictly comply with the payment provisions of the March 25, 1991 order;

(2) An expectation that such conduct of accepting late payments could be relied on by Riva appears clear. Burger King accepted late payments after the March 25, 1991 order and continued to accept late payments after the July 10 and July 22, 1991 conversations, the July 22, 1991 letter of Burger King and the November, 1991 conversation of Miolla and Riva without giving notice to Riva that the late payments would result in a claim that the relationship he had with Burger King had been deemed rejected; and

(3) Burger King was always aware that the payments it was accepting were late and that it had not given Riva a clear notice of default and an opportunity to cure the late payment defaults so as to be able to prevent a deemed rejection and possibly preserve the going concern value of his restaurants, or at least not lose them as a result of the late payments.

The testimony and the exhibits produced at the hearing establish the following facts concerning Riva, the party asserting the estoppel:

(1) Riva lacked knowledge of Burger King's real intentions regarding his continuing late payments and its efforts to find new franchisees who would not pay Riva or his estate for the going concern value of his restaurants;

(2) Reliance by Riva is self-evident. Riva testified at the hearing that he thought that he could be fully current in his payments to Burger King by the end of December 1991, and that if he did so he would be able to continue to operate his restaurants pursuant to a confirmed plan, if the plan was otherwise acceptable to Burger King and his creditors, but that his relationships with Burger King would not be deemed rejected based on the late payments which Burger King kept

accepting; and

(3) Riva continued to make late payments rather than bring all post petition amounts due completely current, which he may have been able to do, as was demonstrated in December of 1991 when his attorneys attempted to bring all amounts due current. Because Burger King failed to ever given him clear notice of default and its intentions to require strict performance without an opportunity to cure within a reasonable time, and based on its acceptance of late payments until the December 20, 1991 notice, Riva believed that he had until the end of December to become current.

Based on the foregoing, and since there is no question that Riva was acting in good faith as to the payments due to Burger King, Burger King is equitably estopped from being able to enforce the deemed rejected provision of the March 25, 1991 order based on Riva's late payments.

Forfeitures are not favored in equity. Palmer & Singer Mfg. Co. v. Barney Estate Co., 149 App. Div. 136, 137, 133 N.Y.S. 876, 879 (1st Dept. 1912). Bankruptcy courts will refuse to enforce them in appropriate circumstances. This is particularly true when enforcement would result in a loss of a substantial asset, and especially when it is the most paramount asset of a debtor and one which is necessary to the ultimate repayment of the debtor's creditors. Delta Motor Hotel of Syracuse, Inc., 10 B.R. 585 (Bankr. N.D.N.Y. 1981).

As affirmed by Carroll's, which owns and/or operates 165 Burger King locations, the Jefferson Road, Midtown and Ridge Road locations can generate sufficient cash flow and profits to pay all of the creditors of Riva, Riva Development and Riva Management 100% of the amounts owed them over a period of from between three to five years, while also maintaining a valuable asset for Riva and continue to serve the community well. It is clear that the locations have higher than average customer satisfaction ratings, and therefore enhance the Burger King reputation.

Although Burger King claims that in reliance on the March 25, 1991 order and its July 22, 1991 letter indicating that it was not waiving any of its rights under the order, it then proceeded to negotiate for and enter into a contract for replacement franchise agreements with the Kessler Group,

and thus would be prejudiced if the Riva-Burger King relationships were not deemed rejected, it is clear that Burger King was on less than solid ground in believing that, based on its conduct and the facts and circumstances of this case, the Court would deem its relationships with Riva to have been terminated by reason of the payment defaults under the March 25, 1991 order. Since the restaurants were being well operated from the public's perspective, and in a profitable manner, although Burger King may have been frustrated with the progress of the Chapter 11 case, there certainly was no urgency to find a replacement franchisee. Before entering into its agreements with the Kessler Group, Burger King could easily have brought its motion to convert and/or for the Court to determine that by reason of defaults the agreements had been deemed rejected. Moreover, it does not appear that Burger King's change in position is really prejudicial. As the Court understands the contract with the Kessler Group it is contingent upon, among other things, the Kessler Group being able to come into Bankruptcy Court and obtain the debtors' equipment at the locations and/or assignments of the leases at the Jefferson Road an Midtown locations. Certainly if the now filed plans of each of the debtors are confirmed and the leases assumed as part of the plans, these events will never occur, the contingency will not be satisfies and the contract with the Kessler Group will not be binding on Burger King. Also as a existing franchisee, it is doubtful that the Kessler Group would have or seek damages against Burger King for any breach if this Court finds that the Riva-Burger King relationships have not been deemed rejected or refuses to enforce such rejection.

For this Court to allow the forfeiture of the Riva-Burger King relationships, which have the potential to pay creditors in full, would be truly inequitable.

CONCLUSION

Based upon all of the facts and circumstances of this case, the Court holds that Burger King has waived its rights to and is equitably estopped from deeming rejected its relationships with Riva by reason of his failure to make the required payments in accordance with the provisions of this

Court's March 25, 1991 order. Moreover, in the exercise of this Court's equitable powers, on the facts and circumstances of this case, it refuses to allow the enforcement of any such rejection and forfeiture of these relationships which would result in substantial and unnecessary prejudice to the debtors' creditors.

IT IS SO ORDERED.

/s/
HON. JOHN C. NINFO, II
U.S. BANKRUPTCY COURT JUDGE

Dated: April 6, 1992