

Abingdon, Virginia. The lease was originally entered into on December 22, 1992, by Aetna Life Insurance Company (“Aetna”) as landlord and Helig-Meyers Furniture Company (“Helig-Meyers”) as tenant. Double K Properties, L.L.C. (“DKP”) later became the landlord in place of Aetna and Aaron Rents, Inc. (“Aaron”) purchased its interest as tenant in the lease when Helig-Meyers liquidated its assets during Chapter 11 bankruptcy proceedings. The lease provided Helig-Meyers with the right to extend the lease past the original term at its option (the “Extension Option”). DKP contends that because the Extension Option was made personal to Helig-Meyers, Aaron has no right to exercise it. In its Complaint, DKP seeks a declaration from the court in that regard as well as an injunction preventing Aaron from remaining on the premises because the original lease term has expired. Aaron has filed a counterclaim seeking a declaration that it is entitled to exercise the option. Both parties have filed motions for summary judgment.¹ The motions have been briefed and argued and are now ripe for decision.²

Section 2 of the lease provides for a lease term of ten years commencing on May 14, 1993. Section 9 sets forth the Extension Option as follows:

¹ Aaron additionally filed a Motion to Transfer Venue, but has withdrawn that motion.

² Jurisdiction of this court exists pursuant to diversity of citizenship and amount in controversy. *See* 28 U.S.C.A. § 1332(a) (West 1993 & Supp. 2002).

Tenant shall have the right to extend the Term for Two (2) successive periods of Five (5) years each The right set forth in this Section 9 shall be a personal right of Tenant, and . . . shall not inure to the benefit of Tenant's successors or assigns, except for successors or assigns approved by Landlord in accordance with the provisions of Section 22 (D) hereof.

Section 22(D) of the lease specifies three situations in which a successor or assign may exercise the Extension Option, none of which apply here. Aaron agrees that it has no right to exercise the Extension Option under the express provisions of the lease. Instead, Aaron argues that the Bankruptcy Code renders the "personal right" limitation unenforceable, enabling it to exercise the Extension Option.

II

Summary judgment is appropriate when there is "no genuine issue of material fact," given the parties' burdens of proof at trial. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986); *see* Fed. R. Civ. P. 56(c). There are no disputed factual issues in this case but only a question of law as to the effect of the relevant provisions of the Bankruptcy Code on the Extension Option. Accordingly, summary judgment is appropriate.

Section 365 of the Bankruptcy Code applies when a debtor, such as Helig-Meyers, assigns or sells an unexpired lease of real property during bankruptcy

proceedings. *See* 11 U.S.C.A. § 365 (West 1993 & Supp. 2003). This section was added as part of the Bankruptcy Reform Act of 1978 and voids certain contract and lease provisions in order to “assist[] a debtor in its rehabilitation or liquidation effort.” *In re David Orgell, Inc.*, 117 B.R. 574, 576 (Bankr. C.D. Cal. 1990) (citing H.R. Rep. No. 595, 95th Cong., 1st Sess. 349 (1977)). While 365(f)(1) specifically invalidates anti-assignment clauses that completely prevent a debtor from assigning contracts or leases, 365(f)(3) more broadly invalidates any lease or contract provision “which burdens the debtor’s ability to make an effective assignment by modifying . . . [the lease] so that the assignee receives a different agreement than the debtor had.” *Id.* In particular, the section provides that

[n]otwithstanding a provision in an executory contract or unexpired lease of the debtor . . . that terminates or *modifies* . . . such contract or lease or a right or obligation under such contract or lease on account of an assignment of such contract or lease, such contract, lease, right, or obligation may not be terminated or *modified* under such provision because of the assumption or assignment of the contract or lease by the trustee.

11 U.S.C.A. § 365(f)(3) (emphasis added).

The lease at issue expressly provides that the Extension Option is “personal” to Helig-Meyers and is not available to “successors or assigns,” except under certain circumstances that are not present here. While this provision does not constitute an express anti-assignment clause rendered unenforceable by 365(f)(1), it does “modify”

the lease “on account of assignment,” bringing it within the ambit of the broader 365(f)(3).

In *David Orgell, Inc.* the court invalidated a lease provision that increased rent upon assignment, noting that the provision was “clearly designed to alter the basic terms of the lease if the . . . debtor should ever transfer the lease.” 117 B.R. at 577. Similarly, the lease provision here, if enforced, alters the potential length of the lease once transferred from Helig-Meyers, because Aaron would not have the option to extend the lease. This is clearly “a different agreement” than Helig-Meyers had at the time it signed the lease. “Such a result is contrary to section 365(f)(3) and the Congressional policy that supports it.” *Id.*

Courts have also used 365(f) to invalidate lease provisions that are “designed to impede a tenant’s ability to assign an . . . unexpired lease by . . . imposing economic impediments to assignment.” *In re Office Prods. of Am., Inc.*, 136 B.R. 992, 997 (Bankr. W.D. Tex. 1992). The present lease provision, if enforced, would impose an economic impediment to assignment because without the benefit of the Extension Option, the lease obviously would be less attractive to potential purchasers. This is especially true because Helig-Meyers sold the lease in July of 2001, less than two years before the original lease was set to expire. A lease provision that turns a potential twelve-year lease into a two-year lease upon assignment is clearly an

“economic impediment” to the debtor. Accordingly, I find that section 365(f)(3) of the Bankruptcy Code renders unenforceable³ the “personal right” language in Section 9 of the lease, enabling Aaron to exercise the Extension Option.⁴

DKP also asserts that, even if 365(f)(3) applies, Aaron waived its ability to assert rights under 365(f)(3) because it did not ask the bankruptcy court to adjudicate this issue at the time of sale. However, Aaron likely did not ask for such adjudication because the Sale Order, pursuant to which Aaron purchased the lease, quite clearly invoked 365(f) by expressly stating that “[a]ny . . . termination or recapture rights under the Leases, arising from sale and assignment of the Lease, are of no force and effect, null and void, and unenforceable pursuant to Section[] 365(f)(1) of the Bankruptcy Code.” (Sale Order ¶ 16.) It also provides that “[n]o section of any lease which purports to prohibit, restrict, or condition the assignment of that Lease to Purchaser shall have any force or effect.” (Sale Order ¶ J.)

³ The provision is merely unenforceable against Aaron, not void. Aaron concedes that the provision would be applicable if Aaron were to assign the lease.

⁴ DKP also relies on 365(b)(3)(C), which provides that when the lease assigned or assumed is a shopping center lease, the assignee is subject to *all* of the lease provisions. DKP argues that this prevents invalidation of any lease provision under 365(f). “However, Section 365(b)(3) is not meant to be read in isolation,” but rather “in conjunction with the section that it cross-references, Section 365(f).” *In re Rickel Home Ctrs, Inc.*, 240 B.R. 826, 831 (D. Del. 1998) (invalidating several lease provisions under 365(f) despite fact that lease was for shopping center space).

Traditional waiver principles apply in the bankruptcy context, placing the burden of proof on the party asserting the defense, and requiring proof that a “party voluntarily or intentionally relinquishe[d] a known claim right.” *Devan v. Simon DeBartolo Group, L.P. (In re Merry-Go-Round Enters., Inc.)*, 180 F.3d 149, 159 (4th Cir. 1999) (internal citation omitted). Given the clear language in the Sale Order, I do not find that Aaron “voluntarily or intentionally relinquished” any right under section 365(f).

III

For these reasons, I will grant summary judgment in favor of the defendant. A separate judgment consistent with this opinion will be entered forthwith.

DATED: July 14, 2003

United States District Judge