

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW HAMPSHIRE**

In re:

Bk. No. 01-10700-JMD
Chapter 11

Clarkeies Market, L.L.C.,
Debtor

Clarkeies Market, L.L.C.
Movant

v.

Objections to Claims Nos. 71,
78 and 82

Associated Grocers of New England, Inc. and
Associated Lease Corp.,
Respondents

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MEMORANDUM OPINION

I. INTRODUCTION

On April 10, 2003, the Court held a hearing on the second group of issues involved in the Objection by Debtor to Proof of Claim and Amended Proof of Claim of Associated Grocers of New England, Inc. ("AGNE") (POC 71 and 82) (Doc. No. 266) and the Objection by Debtor to Proof of Claim of Associated Lease Corp. ("ALC") (POC 78) (Doc. No. 270). This second group of issues involves the determination of a valuation date for the stock of AGNE held by the Debtor

and the application of the value of such stock to various obligations of the Debtor to AGNE pursuant to three agreements pledging the stock as collateral. The findings and rulings in this Memorandum Opinion, by agreement of the parties, are necessary, but preliminary, issues to be resolved prior to a final evidentiary hearing on the Debtor's objections to the claims of AGNE and ALC. Accordingly, the findings and rulings in this Memorandum Opinion are interlocutory and shall not be considered final until this Court enters an order determining the allowed claims of AGNE and ALC.

This Court has jurisdiction of the subject matter and the parties pursuant to 28 U.S.C. §§ 1334 and 157(a) and the "Standing Order of Referral of Title 11 Proceedings to the United States Bankruptcy Court for the District of New Hampshire," dated January 18, 1994 (DiClerico, C.J.). This is a core proceeding in accordance with 28 U.S.C. § 157(b).

II. FACTS

The parties stipulated in writing (Doc. No. 519), and on the record, that the documents submitted as Exhibits 1 through 14 were admitted into evidence. The parties also stipulated and agreed upon the three possible valuation dates (the petition date, the hearing date or the confirmation date) and the value, or method of determining the value, of the Class A and Class B stock of AGNE on those dates (Doc. No. 518). At the hearing, the Court heard the arguments of counsel and testimony from the principals of the Debtor and two officers of AGNE.

The Debtor's relationship with AGNE began on March 7, 1997 when the Debtor borrowed \$200,000.00 from AGNE under the terms of a promissory note (the "1997 Note"). See Exhibit 1. In connection with the 1997 Note the Debtor also executed an agreement whereby it pledged any and all stock in AGNE owned by the Debtor and granted a security interest in any patronage

refunds or other distributions due to the Debtor from AGNE as security for its obligations under the agreement and the other Loan Documents (the “1997 Member Agreement”). See Exhibit 4. Under the 1997 Member Agreement the term “Loan Documents” was defined to include the 1997 Note, the security agreement executed in connection with the 1997 Note (the “1997 Member Security Agreement”) (see Exhibit 7) and a continuing guaranty of the principals of the Debtor. The nature and extent of the security interest granted under the 1997 Member Security Agreement was determined in In re Clarkeies Market, L.L.C., 2003 BNH 002 (“Clarkeies I”).

In late 1998 the Debtor entered into two additional transactions with AGNE in which it acquired stores in Woodsville, New Hampshire and Berlin, New Hampshire from Kelley’s Food Town, Inc. In the first transaction the Debtor borrowed \$160,718.97 from AGNE under the terms of a promissory note dated November 30, 1998 (the “Woodsville Note”). See Exhibit 2. In connection with the Woodsville Note the Debtor also executed an agreement whereby it pledged any and all stock in AGNE owned by the Debtor and granted a security interest in any patronage refunds or other distributions due to the Debtor from AGNE as security for its obligations under the agreement and the other Loan Documents (the “Woodsville Member Agreement”). See Exhibit 5. Under the Woodsville Member Agreement the term “Loan Documents” was defined to include the Woodsville Note, the security agreement executed in connection with the Woodsville Note (the “Woodsville Member Security Agreement”) (see Exhibit 8) and a continuing guaranty of the principals of the Debtor. The nature and extent of the security interest granted under the Woodsville Member Security Agreement was determined in Clarkeies I.

In the second transaction the Debtor borrowed \$138,080.74 from AGNE under the terms of a promissory note dated November 30, 1998 (the “Berlin Note”). See Exhibit 3. In connection with the Berlin Note the Debtor also executed an agreement whereby it pledged any and all stock

in AGNE owned by the Debtor and granted a security interest in any patronage refunds or other distributions due to the Debtor from AGNE as security for its obligations under the agreement and the other Loan Documents (the “Berlin Member Agreement”). See Exhibit 6. Under the Berlin Member Agreement the term “Loan Documents” was defined to include the Berlin Note, the security agreement executed in connection with the Berlin Note (the “Berlin Member Security Agreement”) (see Exhibit 9) and a continuing guaranty of the principals of the Debtor. The nature and extent of the security interest granted under the Berlin Member Security Agreement was determined in *Clarkeies I*.

III. DISCUSSION

This phase of the dispute between the Debtor and AGNE involves the determination of the value of the stock in AGNE owned by the Debtor and the obligations against which that value may be applied by AGNE or the Debtor under the provisions of the 1997 Member Agreement, the Woodsville Member Agreement and the Berlin Member Agreement (collectively the “Member Agreements”). The parties have agreed upon the value of the stock subject to the Court resolving the dispute between them over the valuation date to be utilized. The application of the value of such stock depends upon a determination of the meaning of the word “member” under the Debtor’s various agreements with AGNE and the terms of the Member Agreements.

The Debtor contends that each of the four stores operated by the Debtor prepetition is a separate “member” under the terms of the Member Agreements. The Debtor bases its argument on (1) the contention that AGNE always accounted for patronage dividends and any resulting cash payments or Class B stock distributions on a store by store basis, (2) the receipt of a separate IRS form 1099 each year reflecting the patronage dividends earned by each store, (3) the provisions in

each of the Member Agreements that require each store to purchase at least 50% of its inventory from AGNE and (4) the provisions in AGNE's Bylaws that required the Debtor to purchase one share of Class A stock and such amounts of Class B stock as AGNE's Board of Directors determined from time to time for each store that it operated. The Debtor argues that the AGNE stock pledged by each of the four "member" stores secures only the obligations to AGNE related to that store.

AGNE contends that the plain, unambiguous language in the Member Agreements and the Bylaws and Articles of Agreement of AGNE compel a conclusion that the Debtor is the sole "member" under each and every one of the Member Agreements and that all AGNE stock owned by the Debtor is pledged to secure all of the Debtor's obligations. AGNE also argues that the language of the Member Agreements permits it to apply the value of such stock to any one or more of the obligations of the Debtor, as the sole Member, in AGNE's sole discretion.

A. How Many Members?

The starting point for determining the rights and obligations of the Debtor and AGNE are the terms of the Member Agreements. The parties agreed on the record that the Member Agreements are substantively identical in form. The 1997 Member Agreement was executed in connection with the initial financing from AGNE for the two stores in Colebrook, New Hampshire and Groveton, New Hampshire. The Woodsville Member Agreement and the Berlin Member Agreement were executed in connection with the Debtor's purchase, and AGNE's financing, of the Woodsville, New Hampshire and Berlin, New Hampshire stores. The Member Agreements define AGNE as the "Cooperative," the Debtor as the "Member" and the Debtor's principals, Alan and Susan Clarke as the "Guarantors." The purpose of the Member Agreements was to provide additional security to AGNE beyond that provided under the promissory notes, security agreements

and guaranties delivered to AGNE in the three loan transactions with the Debtor. Paragraph 1 of each of the Member Agreements provides:

1. Security. In addition to any security given under the Loan Documents, and in accordance with Article IV(c) of the Cooperative's Articles of Agreement and Articles V and VIII of the Cooperative's Bylaws, Member hereby pledges any and all stock of the Cooperative which Member owns directly or indirectly, legally or beneficially, and grants a security interest in and right to any patronage refunds, or other distributions, or member savings account funds due or outstanding to Member from the Cooperative as security for the payment in full of their obligations under this Agreement and under the Loan Documents.

See Exhibits 4, 5 and 6. Articles IV(c)(ii) and (iii) of AGNE's Articles of Agreement provide:

(ii) For each store which makes purchases from the Corporation owned directly or indirectly by a member of the corporation, such member shall be required to own one (1) share of Class A stock and such number of shares of Class B stock as is necessary to meet the requirements as established from time to time by the Board of Directors.

(iii) Each stockholder who is a member shall have the right to one (1) vote only with respect to any matter submitted to a vote of the member stockholders irrespective of the number of shares of capital stock of the corporation owned directly or indirectly by such member

See Exhibit 12. Article V of the AGNE Bylaws provides in part:

Any payments payable to a member stockholder on account of any patronage dividend, certificate of indebtedness or stock may be applied against any indebtedness payable to the Corporation or any subsidiary thereof by such member stockholder, and only the balance, if any, shall be paid to the member.

See Exhibit 11. Article VIII of the AGNE Bylaws provide in part:

5. For each Purchasing Store owned directly or indirectly by a member, such member shall be required to purchase from the Corporation shares of Class B stock in such amounts as the Board of Directors of the Corporation may establish from time to time.

6. Members shall purchase one share of Class A stock upon becoming a member of the Corporation for each Purchasing Store owned directly or indirectly by such member. Members shall purchase shares of Class B stock to meet the requirements as established by the Board of Directors from time to time pursuant to the above as follows:

(a) A percentage as shall be established from time to time by the Board of Directors of the value of each member's Purchasing Store(s) weekly purchases from the Corporation shall be added to the weekly bill for such purchases for each Purchasing Store. . . . Such amounts will be accumulated during each fiscal year of the Corporation, with no interest paid thereon. Class B stock will be purchased as of the fiscal year-end with the amounts so accumulated for the per share value of Class B stock as determined by the Board of Directors at the beginning of the immediate succeeding fiscal year

Id.

The Member Agreements specifically incorporate by reference the provisions of AGNE's Articles of Agreement and Bylaws set forth above. Each of the Member Agreements expressly provides that the Debtor, not any particular store, is the "member." The Member Agreements, Articles of Agreement and Bylaws all clearly and unambiguously contemplate that a single member shareholder of AGNE may own more than one store and that the Class A and Class B stock purchase requirements shall be determined on a per store basis for each individual member. Consequently, the fact that AGNE annually accounted for patronage dividends, stock ownership obligations and issued separate IRS form 1099's on a store by store basis is not remarkable and is consistent with the terms of the Member Agreements. It is also clear that a single member could own one or more stores that did not purchase from AGNE.¹ Under the terms of each of the Member Agreements both the Debtor and AGNE contemplated that after the initial purchase of one share of Class A stock for each store purchasing from AGNE, the Debtor would have an ongoing obligation to purchase additional Class B shares, based upon the purchases from AGNE by each store, as determined by the Board of Directors.

¹ In Article VIII.2 of the Bylaws a "Purchasing Store" is defined as a retail store owned by a member which makes or is to make purchases from AGNE.

Based upon the clear and unambiguous provisions of the Member Agreements, and the provisions of AGNE's Articles of Agreement and Bylaws incorporated therein by reference, the Debtor, not each individual store, is the sole member and stockholder under each of the Member Agreements.

B. Pledged Stock As Collateral

Article V of the Articles of Agreement of AGNE provides that any payments due to a member stockholder on account of any stock or patronage dividends may be applied against any indebtedness of such member stockholder to AGNE. Paragraph 1 of each of the Member Agreements also specifically provides:

In the event of a default by the Member or the Guarantors . . . under the Loan Documents, Cooperative may, in its sole discretion, apply any and all stock which Member owns in the Cooperative and the amount of any and all patronage refunds or other distributions due . . . Member from the Cooperative to principal and interest outstanding under the Loan and to offset any loss, damage, expense, or other detriment incurred, made or suffered by Cooperative as a result of such default. Member hereby consents to such application.

See Exhibits 4, 5 and 6. Accordingly, under the clear and unambiguous terms of the Member Agreements, in the event of a default under any of the three sets of loan documents, AGNE had the right, but not the obligation, to apply any or all of the value of the stock owned by the Debtor against the principal and interest outstanding under any one or more of the 1997 Note, the Woodsville Note and the Berlin Note. Under the terms of the Woodsville Member Agreement and the Berlin Member Agreement, AGNE's liability under the Kelley guaranty would constitute "loss, damage, expense, or other detriment incurred, made or suffered" by AGNE as a result of the Debtor's default under the Woodsville Note and the Berlin Note against which AGNE could offset the value of the pledged stock.

Finally, the Member Agreements are ambiguous on whether the value of the pledged stock and the patronage dividends may be applied to other obligations of the Debtor to AGNE. Each of the Member Agreements incorporate by reference Article V of AGNE's Bylaws, which provide that payments of any stock or patronage dividends may be applied to any indebtedness of the member/stockholder to AGNE. However, the express terms of the Member Agreements provide that the pledge of stock and the granting of the security interest in the patronage dividends is security for payment of obligations under the Member Agreement and the loan documents executed in connection therewith. It may be that the language is broad enough to cover all obligations or it may be that the express terms of the Member Agreement limit the obligations against which the stock and patronage dividends may be applied. However, the Court need not resolve this issue since it appears that the amounts due under the promissory notes and the Kelley guaranty significantly exceed the value of the security under the Member Agreements.

C. The Valuation Date

Under AGNE's Bylaws, Class A stock is purchased back from a member at a fixed value of \$5,000.00. See Exhibit 11 at Article IX.2(a). Accordingly, there is no dispute regarding the valuation of the Class A stock and it should be applied to AGNE's claim on that basis. With regard to the Class B stock and the patronage dividends, the parties have stipulated that the valuation date is either the petition date, the hearing date or the date of confirmation of a plan of reorganization. However, based upon AGNE's Bylaws and the incorporation of portions thereof in the Member Agreements, the valuation date for the pledged stock should be based upon the date a default was declared by AGNE as Class B stock is purchased for the value determined by the Board of Directors at the beginning of the fiscal year in which the event giving rise to the purchase

option occurs.² See Exhibit 11 at Article IX.2(b). Therefore, if the Debtor's default occurred during the fiscal year ending on or about March 31, 2001, then the value of the Class B stock as of the beginning of that fiscal year, or April 1, 2000, would control and the patronage dividends payable on account of the fiscal year ending March 31, 2001 would be applied to the Debtor's obligations under the promissory notes, all in accordance with the Bylaws, which require the AGNE Board of Directors to determine and establish the value of the Class B stock at the beginning of each fiscal year at between 90% and 100% of the book value of AGNE (see Exhibit 11 at Article VIII.7) and to pay patronage dividends annually after the close of the fiscal year in which they were earned (see Exhibit 11 at Article V).

Accordingly, the value of the pledged Class A stock applied by AGNE to any of the Debtor's obligations under one or more of the promissory notes shall be \$5,000.00 per share, the value of the Class B stock applied by AGNE to any of the Debtor's obligations under one or more of the promissory notes shall be the value of the stock established by AGNE's Board of Directors at the beginning of the fiscal year during which the event, AGNE's exercise of its discretion to apply such value to one or more of the Debtor's obligations, occurs, and the value of the patronage dividends shall be the value established by AGNE's Board of Directors at the end of the fiscal year during which they were earned. The final allowed amount of the AGNE claim shall include a credit for the amounts computed under the above rulings.

² While AGNE is not actually purchasing the pledged stock but rather applying it to a member stockholder's obligations to it, neither the Member Agreements, AGNE's Articles of Agreement nor AGNE's Bylaws establish how the value of pledged stock shall be determined upon AGNE's exercise of its discretion to apply the value of such stock to the Debtor's obligations. However, there is nothing in the record and no argument by either party that the value should be determined in any manner other than that described in Article VIII.7 of the Bylaws.

IV. CONCLUSION

This opinion constitutes the Court's partial findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052, but shall not constitute a final order on the allowance of the claims of AGNE or ALC until the Court enters a order on allowance of such claims.

ENTERED at Manchester, New Hampshire.

July 31, 2003

/s/ J. Michael Deasy
J. Michael Deasy
Bankruptcy Judge