

In the United States Bankruptcy Court

for the Northern District of Iowa

ADRON M. REESE and
ROBERTA L. REESE
Debtor(s).

Bankruptcy No. 99-02176F

Chapter 7

ORDER RE : TRUSTEE'S MOTION TO PAY ADMINISTRATIVE CLAIM

The matter before the court is the Chapter 7 trustee's motion to pay a secured claim and an administrative expense claim from the proceeds of the harvest of debtors' 1999 crops. Hearing on the matter was held June 21 in Fort Dodge. Appearing were Habbo G. Fokkena, Chapter 7 trustee, *pro se*, and Rush M. Shortley for the debtors Adron and Roberta Reese. This is a core proceeding under 28 U.S.C. § 157(b)(2)(A) and (B).

Findings of Fact

Reeses filed a Chapter 7 petition on August 17, 1999. On that date, they owned growing corn and soybean crops. The trustee agreed that Adron Reese would harvest and sell the crops and turn the proceeds over to the trustee. The trustee agreed to pay Reese his reasonable expenses for the harvesting work.

Reeses submitted an itemized statement to the trustee. See Docket 27, Exhibit A. The statement, dated February 2, 2000, requested \$27,851.35. On April 17, 2000, the trustee filed the motion at issue. Docket 24. The motion recites that Iowa Trust & Savings Bank has a perfected security interest in the grain proceeds. The trustee requests the court to authorize payment of the bank's secured claim. The trustee further requests approval of payment of \$441.34 as the balance owing on the Reeses' administrative claim for harvesting the crops.

Attached as exhibits to the trustee's motion are an accounting of the harvesting income and the proposed payment to Reeses for harvesting expenses. In calculating the administrative claim, the trustee deducted payments Reeses received post-petition from federal farm programs. In December 1999, they received loan deficiency payments (LDP) of \$10,627.62 and \$6,204.45. On or about November 1, 1999, they received a market loss assistance payment (MLA) in the amount of \$8,467.80. The trustee further reduced Reeses' claim by eliminating \$1,242.00 requested for discing endrows in the fields and \$810.26 for temporary storage of corn.

In May 1996, Reeses enrolled in the federal production flexibility contract program. Exhibit 1. On December 7, 1998, Reeses certified the acreage and crop covered by the contract for crop year 1999. Exhibit 2.

Discussion

The court first notes the issues that are not in dispute. No one has objected to the payment of Iowa Trust & Savings Bank's secured claim. Reeses concede that the LDP payments were property of the bankruptcy estate and that the trustee may deduct the amount of those payments from their administrative claim. At the hearing on the trustee's motion, Adron Reese testified about his practice of discing endrows and the circumstances of incurring temporary storage costs. As was stated at the hearing, the court is satisfied that the expenses for discing endrows and temporary storage were reasonable and necessary expenses incurred while harvesting the crops for the benefit of the estate.

The only remaining issue is whether the MLA payment was property of the debtors or property of the estate. If the latter, the trustee correctly reduced Reeses' administrative claim by the amount of the MLA payment. Reeses argue that they had no rights in the MLA payment as of the date of their filing, and that it was a new form of property which came into existence post-petition. The trustee contends that the MLA was estate property because it was a right under the existing production flexibility contract.

In 1996, Congress enacted the Agricultural Market Transition Act, codified at 7 U.S.C. §§ 7201-7334. Pub. L. No. 104-127, Title I, 110 Stat. 896 (April 4, 1996). The purposes of the Act, among others, were--

(1) to authorize the use of binding production flexibility contracts between the United States and agricultural producers to support farming certainty and flexibility while ensuring continued compliance with farm conservation and wetland protection requirements; [and]

(2) to make nonrecourse marketing assistance loans and loan deficiency payments available for certain crops.

7 U.S.C. § 7201(b). The production flexibility contract (PFC) program is codified at 7 U.S.C. §§ 7211-7218. Non-recourse marketing assistance loans and the LDP program are governed by 7 U.S.C. §§ 7231-7237.

Generally, producers were required to enter into a PFC in 1996. 7 U.S.C. § 7212(a)(2). Under the PFC program, an eligible producer receives declining annual contract payments for crop years 1996 through 2002. 7 U.S.C. § 7213(a); Sierra Club v. Glickman, 156 F.3d 606, 611 (5th Cir. 1998); In re Sauer, 223 B.R. 715, 719 n.3 (Bankr. D. N.D. 1998). In return, the producer must comply with statutory and regulatory requirements. 7 U.S.C. § 7211(a) (conservation, wetland protection, and planting flexibility requirements, use of land for "agricultural or related activity"); see also 7 C.F.R. § 1412.101 et seq.; Appendix to Form CCC-478, Production Flexibility Contract, OMB Form No. 0560-0092 (incorporating other regulations by reference). "The term of a contract shall extend through the 2002 crop, unless earlier terminated by the owner or producer." 7 U.S.C. § 7212(b)(2).

On October 22, 1999, MLA payments were authorized under an appropriations act which provided in pertinent part:

Sec. 802. Market Loss Assistance.

(a) Assistance Authorized - The Secretary [of Agriculture] shall use not more than \$5,544,453,000 of funds of the Commodity Credit Corporation to provide assistance to owners and producers on a farm that are eligible for final payments for fiscal year 1999

under a production flexibility contract for the farm under the Agricultural Market Transition Act (7 U.S.C. § 7201 et seq.).

(b) Amount - The amount of assistance made available to owners and producers on a farm under this section shall be proportionate to the amount of the contract payment received by the owners and producers for fiscal year 1999 under a production flexibility contract for the farm under the Agricultural Market Transition Act.

Pub. L. No. 106-78, § 802, 113 Stat. 1176, (Oct. 22, 1999). See also Pub. L. No. 105-277, § 1111, 112 Stat. 2681-44 (Oct. 21, 1998) (authorizing MLA payments of \$3 billion to "owners and producers on a farm who are eligible for final payments for fiscal year 1998 under a production flexibility contract").

For fiscal years 1996 through 1998, an owner or producer was entitled to 50% of the annual contract payment early in the fiscal year and the balance by September 30. 7 U.S.C. § 7212(d)(1), (2). For fiscal year 1999, the owner or producer was entitled to full payment of the annual contract payment at any time during the fiscal year. 7 U.S.C. § 7212(d)(3). Therefore, anyone still participating in the PFC program in fiscal year 1999 was immediately eligible for a final payment at the beginning of the fiscal year. One requirement for receipt of an annual contract payment may have been the certification of acreage under the contract for the year. If so, Reeses were "eligible for final payments for fiscal year 1999 under a production flexibility contract" within the meaning of § 802(a), quoted above, no later than December 7, 1998. Exhibit 2.

Property of a bankruptcy estate is defined by 11 U.S.C. § 541(a), the scope of which is very broad. United States v. Whiting Pools, Inc., 103 S.Ct. 2309, 2313 & nn. 8, 9 (1983). The estate includes "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1). Property of the estate includes contingent interests. Potter v. Drewes (In re Potter), 228 B.R. 422, 423-24 (B.A.P. 8th Cir. 1999); In re Bell, No. 98-01587S, slip op. at 4-5 (Bankr. N.D. Iowa June 23, 2000) (discussing cases). Certain types of property interests arising after the commencement of the case also come into the estate. An inheritance, property settlement or life insurance benefit acquired within 180 days after the petition date becomes property of the estate under 11 U.S.C. § 541(a)(5). Proceeds of property of the estate and any interest that the estate acquires post-petition enter the estate pursuant to §§ 541(a)(6) and 541(a)(7).

As of the date of their filing, Reeses had rights under a production flexibility contract. Any proceeds of the contract, except for earnings from post-petition services performed by the Reeses, became property of the estate. 11 U.S.C. § 541(a)(6). The term "proceeds" is not defined in the Bankruptcy Code. The term is not restricted to the Uniform Commercial Code definition, "but is intended to be a broad term to encompass all proceeds of property of the estate." White v. United States (In re White), 1989 WL 146417 *3 (Bankr. N.D. Iowa 1989) (quoting H.R. Rep. No. 95-595 at 367-68 (1977); S. Rep. No. 95-989 at 82-83 (1978)); cf. Iowa Code 554.9306(1) ("proceeds' include whatever is received upon the sale, exchange, collection or other disposition of collateral or proceeds"). A general definition of the term is "that which results, proceeds, or accrues from some possession or transaction." State Highway Commission v. Spainhower, 504 S.W.2d 121, 125 (Mo. 1973) (cited in Black's Law Dictionary (6th ed.)).

Payments received pursuant to contracts in connection with government farm programs have been held to be proceeds of the contract. Sandage Real Estate, Inc. v. Liebe (In re Liebe), 41 B.R. 965, 968 (Bankr. N.D. Iowa 1984) (PIK entitlements were proceeds of PIK contract, applying § 552) (citing Matter of Sunberg, 35 B.R. 777, 783-84 (Bankr. S.D. Iowa 1983), aff'd, 729 F.2d 561 (8th Cir.

1984)); Thorp Credit, Inc. v. Fowler (In re Fowler), 41 B.R. 962, 964 (Bankr. N.D. Iowa 1984) (same).

The court concludes that the MLA payment was property of the estate. The sole basis on which the payment was made was the existence of the production flexibility contract. The amount of the payment was calculated as a proportion of the PFC payment made for 1999. Reeses argue that the existence of the contract was a condition for receipt of a new benefit, and that the MLA payment was not a benefit of the existing contract. The court disagrees with this characterization. The payment was a supplemental entitlement of the contract. The MLA payment was proceeds of property of the estate within the meaning of 11 U.S.C. § 541(a)(6).

The post-petition enactment date does not prevent the MLA payment from becoming property of the estate. Reeses' argument that the enactment date is dispositive is relevant under § 541(a)(1), relating to property existing on the date of filing. Proceeds, by their nature, come into the estate post-petition pursuant to § 541(a)(6). Reed v. Philadelphia Housing Authority (In re Reed), 94 B.R. 48, 52-53 (E.D. Pa. 1988). The concept is not in conflict with § 541(a)(1).

The exception under § 541(a)(6) for earnings from services performed post-petition is not applicable here. Reeses needed to do nothing more after their filing date to establish rights in the MLA payment. They had become eligible for their final PFC payment for 1999 several months prior to filing. The LDP program is an optional program distinct from the basic PFC. It was not necessary for Reeses to harvest their crops or prove eligibility for final LDP payments before becoming eligible for the MLA payment.

Reeses next argue that the trustee is not entitled to receive proceeds of the production flexibility contract, because it was an executory contract that is deemed rejected for the trustee's failure to assume. An executory contract, in general terms, is one on which performance remains due by both parties to the contract. Cameron v. Pfaff Plumbing & Heating, Inc., 966 F.2d 414, 416 (8th Cir. 1992) (discussing Countryman definition); 3 Collier on Bankruptcy, ¶ 365.02[1] (15th ed. rev. 2000) (same). Reeses' production flexibility contract was an executory contract on the date of their petition. Reeses had continuing obligations relating to the use of the land; the government had an obligation to make annual payments through 2002.

The contract became property of the estate on Reeses' bankruptcy filing date. This court has previously recognized the split of authority on whether an executory contract or unexpired lease becomes property of the estate immediately at the time of filing. Sergeant v. Trunnelle (In re Trunnelle), Adv. No. 92-3270XF, slip op. at 13-15 (Bankr. N.D. Iowa Aug. 18, 1994). A number of cases have followed Cheadle v. Appleatchee Riders Assn. (In re Lovitt), 757 F.2d 1035, 1041 (9th Cir. 1985), which stated that such contracts or leases come into the estate only if the trustee affirmatively assumes the property. Although Lovitt was a case under the Bankruptcy Act, the principle of that case continues to be applied in some jurisdictions in cases under the Code. See Plitt Amusement Co. of Washington, Inc., 233 B.R. 837, 840 (Bankr. C.D. Cal. 1999). The better view is that an executory contract comes into the estate under the broad reach of § 541(a)(1). Trunnelle, slip op. at 14; In re El Paso Refinery, L.P., 220 B.R. 37, 41-42 (Bankr. W.D. Tex. 1998).

The trustee did not assume the Reeses' contract within 60 days of their filing date. The contract is deemed rejected. 11 U.S.C. § 365(d)(1). Rejection is the trustee's decision not to perform the debtor's executory obligations under the contract. Matter of Executive Technology Data Systems, 79 B.R. 276, 282 (Bankr. E.D. Mich. 1987). It constitutes a breach of the contract. 11 U.S.C. § 365(g). The other party to the contract has a pre-petition claim for any damages arising from the breach. 11 U.S.C. §

365(g)(1). Rejection does not terminate an executory contract. Eastover Bank for Savings v. Sowashee Venture (Matter of Austin Development Co.), 19 F.3d 1077, 1081-82 (5th Cir. 1994), cert. denied, 115 S.Ct. 201 (1994); Trunnelle, slip op. at 9-10; see generally 3 Collier ¶ 365.09[3]. Rejection does not alter the substantive rights of the parties under the contract. Megafoods Stores, Inc. v. Flagstaff Realty Associates (In re Flagstaff Realty Associates), 60 F.3d 1031, 1034 (3d Cir. 1995); Executive Technology Data Systems, 79 B.R. at 282 (rejection is not the equivalent of rescission) (quoting Murphy v. C & W Limited Corp. (In re Murphy), 694 F.2d 172 (8th Cir. 1982)).

The court is aware that some courts and commentators consider rejection effectively an abandonment of the contract. See In re Reed, 94 B.R. at 52 (rejection of residential leasehold amounted to abandonment to Chapter 7 debtor); Michael T. Andrew, Executory Contracts in Bankruptcy: Understanding "Rejection", 59 U. Colo. L.Rev. 845, 863, 897 (1988)(rejection is estate's decision to decline the asset). This court disagrees. The Bankruptcy Code does not require such a result. Trunnelle, slip op. at 15. If, under applicable nonbankruptcy law, the debtor's contract rights remain intact despite breach, such rights remain in the bankruptcy estate. Executive Technology Data Systems, 79 B.R. at 282; (Ben-Dak Investment Co. v. Vertich (In re Vertich)), 5 B.R. 684, 686 (Bankr. D. S.D. 1980); Mitchell R. Julis, Classifying Rights & Interests under the Bankruptcy Code, 55 Am. Bankr. L.J. 223, 253 (1981).

Proceeds of an executory contract existing on the date of filing become property of the estate, even if the contract is a personal services contract that cannot be assumed by the trustee. Banner v. Bagen (In re Bagen), 186 B.R. 824, 829 n.5 (Bankr. S.D.N.Y. 1995), aff'd, 201 B.R. 642 (S.D. N.Y. 1996). The proceeds become available for distribution by the trustee, subject to the exclusion for earnings for the debtor's post-petition services. 11 U.S.C. § 541(a)(6); In re Bagen, 186 B.R. at 829-30; Brown v. Molstad (In re Brown), Adv. No. X90-0119S, slip op. at 6-8 (Bankr. N.D. Iowa July 31, 1990).

Treating the MLA payment as property of the estate does not violate the prohibition against partial assumption of an executory contract. See United States v. Gerth, 991 F.2d 1428, 1432 (8th Cir. 1993) (election to assume requires assumption of "all the benefits and burdens;" "trustee cannot accept the benefits of an executory contract without assuming its burdens as well"). The MLA payment did not come into the Reeses' bankruptcy estate on account of their post-petition services or performance of the production flexibility contract. It was proceeds of the Reeses' rights in the contract as they existed on the date of their filing.

IT IS ORDERED that the trustee's motion is granted in part and denied in part. The trustee shall pay the secured claim of Iowa Trust & Savings Bank with interest as prayed for in the motion.

IT IS FURTHER ORDERED that the trustee shall pay an administrative expense claim for Adron Reese's harvesting expenses. The claim should exclude the amounts already received by Reeses in the form of LDP and MLA payments, which were property of the estate. The claim should include Reese's expenses for discing endrows and temporary storage, for a total remaining administrative claim in the amount of \$2,493.60.

SO ORDERED THIS 6th DAY OF SEPTEMBER 2000.

William L. Edmonds
U.S. Bankruptcy Judge