

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
WINSTON-SALEM DIVISION

ENTERED
JAN 21 2004
U.S. BANKRUPTCY COURT
MDNC - AHH

In re)
)
Clementine Carter,) 03-80823
)
Debtor.)
_____)

**ORDER ALLOWING CLAIM OF
WILLIAM AND SONYA KEARNEY**

This matter came on before the Court on November 20, 2003, upon the Motion by the Trustee to Allow the Claim of William and Sonya Kearney. Appearing before the court was Benjamin Lovell, attorney for the Chapter 13 Trustee, Rhonda Bagshawe, attorney for the Debtor, and William and Sonya Kearney, appearing pro se. The Court, after receiving the testimony and the exhibits and reviewing the file, makes the following findings of fact and conclusions of law pursuant to Rule 7052 of the Federal Rules of Bankruptcy Procedure.

FACTS

On January 1, 2002, the Debtor, Clementine Carter, and William and Sonya Kearney (the "Kearneys") entered into a lease agreement (the "Lease") which included an option to purchase real property (the "Property"). The Lease provided for a lease term of two years, with rent payable on the first of each month in the amount of \$600. In addition, the Kearneys' had paid \$2,500 for the option to purchase real property upon the expiration of the Lease on January 1, 2004. In the event that the Kearneys' exercised their option to purchase, the \$2,500 was to be applied towards the purchase price of the Property.

The Debtor filed a voluntary petition under Chapter 13 of the Bankruptcy Code on March 6, 2003. At the time of the bankruptcy filing, the Property was the subject of pending

foreclosure proceedings and a foreclosure sale was scheduled for March 7, 2003. Upon learning of the pending foreclosure, the Kearneys ceased paying rent. On April 22, 2003 the Debtor filed a Chapter 13 Plan which provided that the Debtor would reject the Lease with the Kearneys pursuant to section 365 of the Bankruptcy Code. An order confirming the Debtor's Chapter 13 Plan was entered on May 21, 2003. The bar date for filing claims in this case was July 19, 2003.

Upon the rejection of the Lease, the Kearneys made plans to relocate. The Kearneys vacated the premises by mid-June. On June 11, 2003, the Trustee received a claim (the "Claim") in favor of the Kearneys in the amount of \$2,500 for the damages due to the rejection of the Lease with option to purchase. In addition, at the hearing on this matter, the Kearneys amended their claim by providing additional testimony regarding moving expenses incurred as a result of the rejection of the Lease.

The Trustee erroneously filed a motion recommending that the Court enter an order disallowing the Claim as untimely filed. The Court entered an order on September 3, 2003, disallowing the Claim. The Trustee subsequently filed the present motion, recommending that an order be entered allowing the Claim of William and Sonya Kearney.

The Debtor filed an objection to the Claim. The Debtor concedes that she owes the Kearneys \$2,500 for damages from the cancellation of an option to purchase; however, she contends that the Kearneys owe her unpaid rent in the amount of \$3,000. The Kearneys contend that they only owe unpaid rent for three and one half months, or \$2,100. The Debtor requests that the damages from the cancellation of the contract be offset with the unpaid rent.

DISCUSSION

Subject to the provisions of § 365 of the Code, a Chapter 13 debtor's plan may provide for the assumption, rejection, or assignment of any executory contract not previously rejected.

11 U.S.C. § 1322(b)(7). Under § 365(g)(1), rejection of an unexpired executory contract or lease by a debtor constitutes a breach of that lease prepetition. Section 502(g) provides that a claim arising under § 365 from a rejection of an executory contract of the debtor that has not been assumed shall be determined, and shall be allowed as if such claim had arisen before the date of the filing of the petition and the nondebtor party to the lease becomes the holder of an unsecured claim. 11 U.S.C. § 502(g); see also In re Milstead, 197 B.R. 33 (Bankr. E.D. Va. 1996); In re Legg, 51 B.R. 444 (Bankr. Va. 1985).

In this case, the Debtor rejected the Lease on May 21, 2003, pursuant to the terms of her confirmed Chapter 13 plan. Therefore, the Kearneys are entitled to a prepetition unsecured claim for damages that resulted from the rejection of the Lease. In this case, the parties agree that the Debtor owes the Kearneys \$2,500 for damages from the cancellation of the option to purchase contained within the Lease. In addition, the Kearneys have claimed numerous damages for the breach of the lease including moving expenses of \$1,245, lost wages for time spent in bankruptcy court and at foreclosure proceedings, and pain and suffering. The court finds that the Kearneys are entitled to an unsecured claim for moving expenses in the amount of \$1,245, in addition to \$2,500 for damages from the cancellation of the option to purchase, resulting in a total claim of \$3,745.

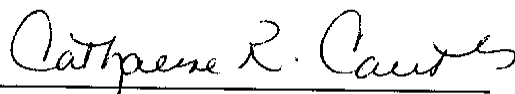
The Trustee has suggested that a portion of the Claim should be accorded priority pursuant to section 507(a)(6), which provides for a sixth priority claim for a prepetition deposit in connection with the purchase, lease, or rental of property. In this case, the \$2,500 payment made by the Kearneys for the option to purchase is not a deposit according to the terms of the Lease. Rather, this sum was paid for and in consideration of the option to purchase. While the sum was to be applied to the purchase price if the Kearneys exercised their option to purchase, if

the Kearneys did not exercise the option to purchase, the \$2,500 was to be retained by the Debtor. Therefore, the court finds that section 507(a)(6) is not applicable in this instance.

The Debtor contends that the Kearneys' Claim should be offset by the amount of unpaid rent. The estate has an action against the Kearneys for any unpaid rent during the period of occupancy; however, there is no authority by which the unpaid rent can be offset against the Kearneys' claim. Section 365(h) provides that a nondebtor lessee who chooses to remain in possession of the leasehold despite rejection of the lease may offset against the rent the value of any damage caused by the nonperformance after the date of rejection. In this case, however, the Kearneys have chosen to treat the lease as terminated and vacate the premises. Furthermore, there is no provision in the lease to offset damages by unpaid rent.

Based on the foregoing, it is therefore ORDERED that the Claim of William and Sonya Kearney is allowed as a general unsecured claim in the amount of \$3,745.00.

This the 21 day of January 2004.



Catharine R. Carruthers
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
FOR THE MIDDLE DISTRICT OF NORTH CAROLINA

IN RE:)
)
Clementine Carter) Case Number: 03-80823C-13D
)
Debtor)

CERTIFICATE OF SERVICE

THIS IS TO CERTIFY that on the below date, the undersigned Deputy Clerk served a copy of the Order Allowing Claim of William and Sonya Kearney by depositing the same, enclosed in a postpaid wrapper, properly addressed to the following parties in interest, at their last known addresses as shown below, in a post office or official depository under the exclusive care and custody of the United States Postal Service:

William & Sonya Kearney
Rt. 2, Box 399
Warrenton, NC 27589

Rhonda W. Bagshawe
P. O. Box 472
Warrenton, NC 27589

Clementine Carter
Rt. Box 165AC
Warrenton, NC 27589

Richard H. Hutson (Via Trustee's Box)
P. O. Box 3613
Durham, NC 27702

THIS the 21 day of January, 2004.

OFFICE OF THE CLERK

BY: Ann Helms
Case Administrator