

**UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF WISCONSIN**

Cite as: [Unpublished]

**William J. Rameker, Trustee, Plaintiff v.
Farmers & Merchants Union Bank, Defendant Cross-Complainant v.
United States of America – Farm Service Agency – CCC, Defendant**

(In re Beth Anne and Jeffrey M. Hahn, Debtors)

Bankruptcy Case No. 98-36236-7

Adversary Case No. 00-3054-7

United States Bankruptcy Court
W.D. Wisconsin, Madison Division

July 27, 2001

William J. Rameker, Murphy Desmond, S.C., Madison, WI for Plaintiff
Michael B. Van Sicklen, Foley & Lardner, Madison, WI for Defendant Cross-Complainant
Richard D. Humphrey, Madison, WI for Defendant

Robert D. Martin, United States Bankruptcy Judge

MEMORANDUM DECISION

This adversary proceeding was originally commenced by the chapter 7 trustee against Farmers & Merchants Union Bank (“Farmers Bank”) to determine the validity of Farmers Bank’s security interest in proceeds from crop support contracts between the debtors and the United States Department of Agriculture (“USDA”). The parties reached a stipulated resolution. In exchange for Farmers Bank releasing its claim on proceeds that had been paid to the estate, the trustee agreed to assist Farmers Bank in securing unpaid proceeds that the USDA had refused to pay. The USDA was then joined. All parties agreed to have the matter resolved by this bankruptcy court on briefs and upon the following stipulated facts.

1. In 1996, the debtors Jeffrey and Beth Hahn entered into production flexibility contracts (“PFC”) with the Commodity Credit Corporation (“CCC”).¹ The Hahns executed an

¹ The CCC is a government corporation within the Department of Agriculture, subject to the direct supervision of the Secretary of Agriculture and created to finance federal farm programs. 15 U.S.C.A. §714. In 1996, Congress enacted the Federal Agriculture Improvement and Reform Act,

assignment of PFC contract proceeds in favor of Farmers Bank which properly perfected the assignment by a U.C.C. filing. In addition to that collateral, Farmer Bank obtained a lien on all real and personal property owned by the Hahns.

2. On August 3, 1998, Farmers Bank commenced proceedings in state court to foreclose on all collateral securing its debt. The Hahns stipulated to judgment in favor of Farmers Bank and that judgment was entered on August 28, 1998. A court-appointed receiver took control of the collateral pending a sale.
3. On December 12, 1998, and prior to any sale being held, Beth Hahn filed a chapter 11 petition. Her husband filed a chapter 11 petition on April 9, 1999. On June 4, 1999, the Court entered an order substantively consolidating the two cases.
4. On April 9, 1999, the debtors obtained approval of a loan to finance the planting of crops during the 1999 growing season. Shortly thereafter, the debtors planted field corn, soybeans, peas, sweet corn and snap peas.
5. On June 18, 1999, Farmers Bank filed a motion for relief from the automatic stay and abandonment of all of its collateral stating that the debtors had previously stipulated to granting the requested relief if no plan of reorganization was filed by May 31, 1999.
6. On July 7, 1999, the Court entered an order lifting the stay and abandoning all collateral described in Farmers Bank's motion, including all "crops and proceeds thereof" and all "general intangibles, accounts, contract rights, chattel paper and instruments."
7. On July 16, 1999, the chapter 11 case was converted to one under chapter 7 and a trustee was duly appointed. The trustee was authorized to conduct the business of the debtors, for a limited period.
8. On October 4, 1999, the trustee obtained an order approving a secured loan to finance crop harvesting expenses.
9. The trustee then hired the debtors to harvest the crops. A sale of the crops generated \$313,338.94 in total proceeds. After the crop financing loan and the operating expenses were paid, a net surplus of \$51,075.13 remained for the estate.

Pub.L. No. 104-127, 110 Stat. 888, which replaced most prior farm subsidy programs with a new production flexibility contract payment program. The program requires the Secretary of Agriculture to enter into 7-year contracts with all eligible farmers on eligible cropland. §§7 U.S.C. 7211, 7212. The CCC executes the contracts on behalf of the Secretary. 7 C.F.R. §§1412.102, 1412.103. Farmers who participate in the program agree to abide by certain wetland, conservation, and land use requirements in exchange for receiving fixed decreasing payments. §§7 U.S.C. 7211, 7213. The payments are guaranteed if statutory prerequisites are satisfied. §7212(b)(2).

10. Prior to the harvest, the debtors filed an application with the USDA for Loan Deficiency Payments (“LDP”) for the corn, wheat and soybean crops in the respective amounts of \$28,884.74, \$2,441.42 and \$21,538.00.
11. The debtors also applied to the USDA for a Market Loss Assistance payment (“MLA”) of \$25,889.00, an Oil Seed payment of \$2,721.00 and a Production Flexibility Contract (“PFC”) payment of \$25,889.00.
12. The USDA concedes that the debtors are properly entitled to the Oil Seed payment and the LDP payment for the soybeans, but refuses to make the MLA payment, the PFC payment and the LDP payments for the corn and wheat.

The USDA argues that the PFC contracts were rejected, either by the debtors’ failure to assume them in the chapter 11 case or, after conversion of the case, by the trustee’s failure to assume them in the 60 days following conversion. It contends that rejection was a deemed breach of the PFC contracts, which breach entitled the USDA to treat the contracts as void. Because the MLA, PFC and LDP payments (for corn and wheat) are only available to applicants covered by valid PFC contracts, the USDA argues that the debtors were ineligible to receive those payments as well.

The trustee and Farmers Bank argue that the PFC contracts were abandoned in the chapter 11 case, leaving nothing to be rejected either before or after the case was converted. They contend that the abandonment removed the contracts from the estate and from the requirements 11 U.S.C. §365 places on assumption of executory contracts. They argue further that because the USDA has not asserted any other defense to the MLA, PFC and LDP contracts, payment has been improperly withheld.

The effect of abandonment is to remove property from the estate and divest the court of jurisdiction over matters concerning the abandoned property. In In re Chicago, Rock Island & Pacific R.R. Co., 794 F.2d 1182 (7th Cir.1986) (Sanborn II), the Seventh Circuit held that bankruptcy jurisdiction lapses when a dispute no longer affects the estate or relations among creditors of the estate. In that case, it was determined that bankruptcy jurisdiction was lacking over a dispute between a lessee and purchaser regarding property formerly owned by the debtor. The Seventh Circuit stated:

That some land was once owned by a bankrupt does not supply federal jurisdiction of disputes concerning that land. New disputes--arising after the closure of the bankruptcy, or after the land has been sold by the Trustee to a third party--must be resolved through the processes available for such independent disputes.... The court's jurisdiction lapses with its control of the property.

Id. at 1186. The holding of Sanborn II was extended in In re Xonics, Inc., 813 F.2d 127, 131 (7th Cir.1987) to cases involving abandoned property of the estate. In Xonics, the chapter 11 debtor Xonics Medical Services, Inc. established an escrow fund for receivables in which two creditors, Elscint, Inc. and First Wisconsin Financial Corp., held security interests. Subsequently, the fund was abandoned in the debtor's confirmed plan. The creditors failed to agree on how to divide the fund and moved the bankruptcy court to resolve the dispute. The bankruptcy court dismissed for want of jurisdiction, and the district court affirmed. The Seventh Circuit vacated and remanded the case for a determination of whether resolution of the dispute could impact creditors other than the two warring creditors. It determined that the party seeking relief in the bankruptcy court must point to a sufficient nexus between disposition of claims to abandoned property and treatment of claims of creditors of the estate. The Seventh Circuit stated:

Elscint's principal argument is that once a bankruptcy court acquires jurisdiction of a dispute, the power to decide lasts forever. The accounts receivable of Xonics and related firms were property of the estate under 11 U.S.C. § 541(a). Adjusting competing claims of creditors to the property of a bankrupt is the central function of bankruptcy law. Elscint and First Wisconsin disagree about which has a security interest in which payments. The bankruptcy court had jurisdiction of disputes of this kind under 28 U.S.C. § 157(b)(2)(K) and (O) at the outset of the case.... But Sanborn II establishes that jurisdiction does not follow the property. It lapses when property leaves the estate. Sanborn II dealt with a dispute between the former tenant of the bankrupt and the person who purchased the property from the bankrupt. While the property belonged to the estate, the court was empowered to adjudicate rental disputes. Sanborn II concluded that once the property has been sold the court needs a new source of jurisdiction (such as diversity), if the dispute is to remain in federal court, and this is so even if the parties' anticipation about the outcome of future disputes with tenants affects the price the estate can charge for the property.... Otherwise anyone who could trace his title to a bankrupt could invoke federal jurisdiction to settle disputes affecting that property.

Id. at 131 (citations omitted). See also In re Green, 241 B.R. 187, 197 (Bankr. N.D. Ill. 1999) (“[w]hen property leaves the bankruptcy estate, whether by sale or otherwise, the bankruptcy court’s jurisdiction over the property lapses”).

In our case, the PFC contracts were abandoned by a proper order in the chapter 11 case. That abandonment removed the contracts from the chapter 11 estate and ended the bankruptcy court's jurisdiction over them.² *Ipsa facto*, the requirement that the contracts be

²A limited exception to the termination of a bankruptcy court's jurisdiction over abandoned property may arise in a "consumer case" if the debtor makes a timely motion to redeem abandoned property (see Robert E. Ginsberg and Robert D. Martin, *Ginsberg & Martin on Bankruptcy* sec.

assumed under §365 to be effective ended as well.

Although the agreement of the parties to have this court determine all issues presented may arguably be insufficient by itself to confer any jurisdiction over the contracts after their abandonment, the dispute between the trustee and Farmers Bank over the contract proceeds properly placed this dispute before this court. To retain jurisdiction to completely resolve that dispute and give effect to the stipulations reached is not improper. But that limited retention of jurisdiction does not reimpose any requirement of assumption under §365.

The abandoned status of the contracts was not altered by the conversion of the case to chapter 7. Conversion does not nullify or reverse actions taken in the pre-converted case. The court in In re Maralak, Ltd., 104 B.R. 446 (Bankr. M.D. Fla. 1989) explained:

The conversion of a case from Chapter 11 to Chapter 7 does not erase the prior proceedings. Court orders lifting the stay, court approved stipulations, rejections of executory contracts and other such matters pertinent to the progress of a Chapter 11 case are not wiped out with an order of conversion.

Id. at 449.

The abandonment of the PFC contracts in the chapter 11 case meant that the contracts never entered into the chapter 7 estate upon conversion. Section 541(a) provides that an estate is created upon commencement of a bankruptcy case, consisting of almost all property in which the debtor has an interest:

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

11 U.S.C. §541(a)(1). Section 348(a) states (subject to exceptions not relevant here) that conversion does not change the date of the filing of the petition, the commencement of the case, or the order for relief:

Conversion of a case from a case under one chapter of this title to a case under another chapter of this title constitutes an order for relief under the chapter to which the case is converted, but, except as provided in subsections (b) and (c)

506[B] (4th ed. 2000), but that exception is of no moment in this case.

of this section, does not effect a change in the date of the filing of the petition, the commencement of the case, or the order for relief.

11 U.S.C. §348(a). Thus, in a converted case, the estate of the pre-converted case passes into the estate of the converted case. As the court explained in In re K & M Printing, Inc., 210 B.R. 583 (Bankr. D. Ariz. 1997):

[t]he Code does provide that conversion constitutes an "order for relief" under the chapter to which the case is converted. 11 U.S.C. § 348(a). However, this "order for relief" does not create a new bankruptcy estate. An estate is created at the commencement of a case. The date of commencement is not changed by conversion.... When converted from Chapter 11 to Chapter 7, property of the estate is determined by the Chapter 11 petition filing date, not by the conversion date.

Id. at 584-585. See also In re Haendiges, 158 B.R. 871, 873-74, (Bankr. M.D. Fla. 1993) ("[section] 348 makes clear that the commencement of the case is unaffected by conversion to another chapter. All that transpired in the previous chapter is not undone by converting to a new chapter... The case is continued under the new chapter; it is not a new case") (citation omitted); In re Lybrook, 951 F.2d 136, 138 (7th Cir.1991) ("the Chapter 13 estate passes unaltered into Chapter 7 upon conversion"). In our case, because the PFC contracts were abandoned and removed from the chapter 11 estate, they were not transferred with other property of the chapter 11 estate to the chapter 7 estate upon conversion.³ See In re Winom Tool and Die, Inc., 173 B.R. 613 (Bankr. E.D. Mich. 1994) (property removed from the estate upon plan confirmation did not pass into the chapter 7 estate upon conversion of the case). Accordingly, the PFC contracts were not subject to assumption or rejection in the chapter 7 case either.

The effect of abandonment was to return all parties to the PFC contracts to their legal positions prior to the bankruptcy filing. Abandonment did not nullify or void the PFC contracts. Rather the PFC contracts and the parties' relationships thereto stood as if the bankruptcy case had never been filed. The debtors and their assignees regained whatever pre-bankruptcy rights they had in the contracts and could once again assert those rights, subject to obligations imposed on them by the contracts. See In re Cruseturner, 8 B.R. 581, 591-592 (Bankr. D. Utah 1981) ("when the trustee abandons property, the property stands as if no bankruptcy had been filed and the debtor enjoys the same claim to it and interest in it as he held previous to the filing of bankruptcy").

³The USDA's contention that "only the contract rights" and not the "whole" contracts were abandoned is under the circumstances of this case mere sophistry. The characterization of the interest conveyed to creditors is driven by the categories of property identified in Article 9 of the UCC and not by the actual legal interest held by either the debtor or the secured creditor.

Because the PFC contracts were abandoned in the chapter 11 case and thus not subject to assumption or rejection either in the chapter 11 case or in the converted chapter 7 case and because the USDA has not offered any defense other than the purported rejection, the USDA is liable to make the MLA payment, the PFC payment and the LDP payments for the corn and wheat, in addition to the payments which the USDA concedes are properly sought, i.e. the LDP payment for the soybeans and the Oil Seed payment. It may be so ordered.