

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

JOHN S. ADASEK, JR.

CASE NO. 06-63904

Debtor

Chapter 13

APPEARANCES:

KEVIN D. BURGESS, ESQ.
313 East Willow Street #105
Syracuse, NY 13203

SAUNDERS, KAHLER, AMOROSO
& LOCKE, L.L.P.
Attorneys for 700 Varick Corporation
185 Genesee Street, Suite 1400
Utica, NY 13501

MERRITT S. LOCKE, ESQ.
Of Counsel

GETNICK LIVINGSTON ATKINSON
GIGLIOTTI & PRIORE, LLP
Attorneys for Oneida Construction Company
258 Genesee Street
Utica, NY 13502

NICHOLAS S. PRIORE, ESQ.
Of Counsel

JOSEPH HOBAICA, ESQ.
Attorney for City of Utica
1 Kennedy Plaza
Utica, NY 13502

MAXSEN D. CHAMPION, ESQ.
Staff Attorney for Chapter 13 Trustee
Mark W. Swimelar, Esq.
250 South Clinton Street, Suite 203
Syracuse, New York 13202

Hon. Stephen D. Gerling, Chief U.S. Bankruptcy Judge

MEMORANDUM-DECISION, FINDINGS OF FACT,

CONCLUSIONS OF LAW AND ORDER

Before the Court is a motion filed on June 8, 2007 by John S. Adasek, Jr., *dba* Backstreets Brewing Co., *aka* an officer and director of Adacorp of Utica (“Debtor” and “Debtor’s Motion”) which seeks an Order, pursuant to § 363 of the United States Bankruptcy Code, 11 U.S.C. §§ 101-1532 (the “Code”)¹ approving the sale of Debtor’s real property located at 700 Varick St., Utica, New York, to Debtor’s third party tenant 700 Varick Corp. (“Varick”).²

On June 21, 2007, Creditor Oneida Construction Corporation (“Oneida”) filed an objection to Debtor’s Motion, to which Varick replied in two responding Affidavits filed June 21 and 22, 2007. Oneida filed a Supplemental Objection to Debtor’s Motion on June 25, 2007.³

The Motion was heard on June 26, 2007 at the Court’s regular motion term in Utica, New York. Following oral argument, the Court adjourned the Debtor’s Motion to July 31, 2007, and gave the parties until July 24, 2007 to submit additional memoranda of law.

On July 16, 2007 the Chapter 13 Trustee filed a letter with the Court stating, in effect, his support for Oneida’s objection to the Debtor’s Motion.

Oneida filed a second Supplemental Objection to Debtor’s Motion on July 24, to which Varick filed a response on July 24. Varick then filed another Supplemental Reply on July 27,

¹ The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (“BAPCPA”) was signed into law on April 20, 2005, and made applicable to cases filed after October 16, 2005. For purposes of this decision “Code” refers to the law in effect at the time the Debtor’s case was filed (June 4, 2003), unless otherwise indicated.

² Debtor’s Motion to sell the Real Property also seeks the disbursement of the proceeds of sale pursuant to his Chapter 13 Plan and the granting of a discharge to Debtor.

³ Oneida is listed as a creditor in Debtor’s Schedule ‘F’ in the amount of \$14,069.76, as “Tax Certificates purchased by non-governmental entity.”

2007.

Following oral argument on July 31, 2007, the Court indicated that it would take the matter under submission as of that date without the need for further briefing (unless the Court later reached the conclusion that it could not issue a decision without further testimony or affidavits, in which case the parties would be notified).

JURISDICTIONAL STATEMENT

The Court has core jurisdiction over the parties and subject matter of this contested matter pursuant to 28 U.S.C. §§ 1334, 157 (a),(b)(1) and (b)(2)(N) and (O).

FACTS

The Debtor filed a voluntary petition pursuant to Chapter 13 of the Code on June 4, 2003, along with his plan. Among Debtor's assets is an income property located at 700 Varick Street in Utica, New York (the "Real Property"). The Real Property is a three-story brick building consisting of 3,150 square feet (finished, first floor only), currently occupied by Varick, which operates a bar at the site known as the "Electric Company." Debtor originally leased the Real Property to Anthony Donaldson and Brian Dewey d/b/a Dewzees on January 12, 2002.⁴ This lease (the "Lease") was assigned, with Debtor's permission, on May 21, 2002, to Varick (Anthony Donaldson, President). "Amendment #1" to the Lease, acknowledging this assignment,

⁴ It is alleged that the lease was not prepared by an attorney.

was executed on May 23, 2002 and is now appended to the Lease.

The following provisions of the Lease are relevant to this decision:

TERM. The lease will begin on January 12, 2002 and will terminate on January 12, 2005[;] see attached sheet for renewal and purchase options.

OPTION TO PURCHASE. Tenant shall have the option to purchase the Premises from Landlord at the end of the lease effective March 16, 2005. Tenant shall receive a credit on the closing statement equal to twenty-five percent (25%) of the lease payments paid as of the date of closing as a down payment. If Tenant exercises such options, Tenant shall have no further obligations under this lease.

RIGHT OF FIRST REFUSAL. If during the term of this lease, or any extended term, Landlord receives an offer from a third party to purchase the Premises, Landlord shall promptly provide Tenant with a copy of the offer and Tenant shall have the right to purchase the Premises, upon the same terms and conditions thereof.

RENEWAL OF LEASE: At the end of the lease term, tenant shall have the options [*sic*] to enter into an additional lease term of three (3) years upon the same terms and conditions of this lease.

In January of 2005 Varick decided not to renew the Lease with the Debtor, and became a month to month tenant. *See* Affidavit of Laura S. Ruberto, July 24, 2007, Dkt. #113, ¶ 5.

Oneida filed a Proof of Claim in Debtor's case on October 28, 2003 in the amount of \$20,097.40 plus interest. This claim was the result of Oneida's purchase of six real property tax certificates from the City of Utica.⁵

Debtor's Third Amended Plan ("Plan") was confirmed by Order of this Court ("Confirmation Order") on August 12, 2004.

⁵ Oneida asserts that as of June 19, 2007 the principal amount due on this claim was \$8,021.37 (*See* Oneida's Affidavit in Opposition to Debtor's Motion Approving Sale of Real Property, June 21, 2007, Dkt. #103, ¶ 4).

ARGUMENTS

Varick

Varick first argues that Oneida lacks standing to object to the Debtor's Motion because the proposed sale envisions Oneida's claims being paid in full from the sale proceeds. Varick also asserts that Code §§ 363 (f)(3) and (f)(5) allow the Debtor to sell to real property free and clear of Oneida's lien.

Varick contends that the Lease between Debtor and Varick was validly assumed because there is affirmative language in the Plan specifically referencing the Lease, and that the Court was aware of the Lease. Varick asserts that because the Lease was assumed, the entire agreement, including the purchase option provision, was assumed. Varick also contends that even if the Lease had been rejected, Varick maintained all of its rights under the Lease, including the purchase option provision, pursuant to Code § 365 (h)(1)(A)(ii).

More importantly, Varick argues that the purchase option remains in full force and effect, despite the Lease's 2005 termination date, because the purchase option is a separate and distinct portion of the Lease, not dependent on the term of the Lease. Varick contends that the purchase option was exercisable "*at any time after the end of the Lease.*" See Varick's Affidavit in Response to Opposition to Debtor's Motion, June 22, 2007, Dkt.# 106, ¶ 17. ⁶

In response to Oneida's contention that the purchase option is illusory or unenforceable because of its lack of a price term, Varick cites to the New York Court of Appeals's decision in

⁶ However, this contention is at odds with Varick's statements in at least two other places, when it maintains that the option was not effective or exercisable until the March 16, 2005 date, two months after the termination of the Lease. See Varick Affidavit, July 27, 2007, Dkt.# 116, ¶ 6. See also Varick Second Supplemental Response, July 24, 2007, Dkt.# 114, ¶ 4.

In re 166 Mamaroneck Ave. Corp., 78 N.Y.2d 88 (1991) for the proposition that the lack of a definite term is not always justification for striking down a contract.

Varick asserts that in March of 2005 Laura Ruberto of Varick advised the Debtor of its “intent to exercise the option.” *See* Affidavit of Laura S. Ruberto, July 24, 2007, Dkt. #113, ¶ 5. Thus, Varick argues that it has a valid cause of action under New York State law against the Debtor for specific performance of the purchase option, and that this cause of action matured only after the Debtor was in bankruptcy. Varick contends that, as a result, pursuant to Code § 108(c), it has six years (the New York Statute of Limitations), or 30 days after the automatic stay is lifted, to commence the action.⁷

Oneida

Oneida first contends that standing is not an issue because in a July 16, 2007 letter to the Court, the Chapter 13 Trustee indicated his full support for Oneida’s position that the sale should be open to competitive bidding.

As for Varick’s claim that the Lease contains a valid purchase option, Oneida contends that because there is no specific mention of assumption of the Lease in Debtor’s Plan, the Lease was not assumed, and was deemed rejected upon the Plan’s confirmation.

Oneida contends that even if the Lease were to have been assumed, it terminated by its

⁷ Code § 108 (c) reads, in relevant part: “...if applicable nonbankruptcy law, an order entered in a nonbankruptcy proceeding, or an agreement fixes a period for commencing or continuing civil action in a court other than a bankruptcy court on a claim against the debtor...and such period does not expire until the later of - (1) the end of such period, including any suspension of such period occurring on or after the commencement of the case; or (2) thirty days after notice of the termination or expiration of the stay under section 362, 922, 1201 or 1301 of this title...with respect to such claim.”

own terms on January 12, 2005, and that the purchase option explicitly states that the tenant will have the option to purchase the real property “at the end of the Lease effective March 16, 2005.” Oneida argues that any attempt to exercise the option more than two years after the term of the Lease expired in no way falls within this language. Oneida cites case law for the proposition that the period in which to exercise a purchase option will not be extended beyond the original lease term by a holdover tenancy. Hence, the purchase option expired when the Lease terminated. As a result, Code § 363 open bidding must be allowed.

Oneida argues that Varick’s reading of the Lease term would result in a “perpetual purchase option,” violating New York law prohibiting such an unreasonable restriction on alienability of the fee.

To highlight what it contends is the unsupportable nature of Varick’s reading of the purchase option, Oneida points out that if Varick’s interpretation is correct, the tenant would eventually be able to purchase the Real Property for nothing. This is because the tenant is, by the purchase option’s own terms, entitled to a credit against the purchase price of the real property of 25% of “lease payments paid”: assuming Varick continued to pay rent to the Debtor, with 25% of each rental payment set aside for a credit on the purchase price, the Debtor (and hence, the estate) could expect to be forced to sell the Real Property to Varick for \$0.⁸

Oneida cites to the New York Court of Appeals’s decision in *Jarecki v. Louie*, 95 N.Y.2d 665, 669 (2001): “an option found in a lease generally runs with the land and, absent unequivocal

⁸ This raises the ancillary, but interesting, issue of the enforceability of the 25% rental payment credit portion of the already muddled purchase option. The extent to which the estate and creditors would be penalized by this *de facto* preference to Varick raises enforceability issues which, given this Decision’s findings on other grounds, the Court need not address.

language to the contrary, may not be exercised beyond the lease term if such creates an unreasonable result.”

Oneida contends that the purchase option is illusory and unenforceable because it lacks a method for determining the price (a material term of the purchase option) at which the tenant could exercise the purchase option.⁹

Oneida denies Varick’s contention that pursuant to Code § 108(c) it has six years (the New York Statute of Limitations), or 30 days after the automatic stay is lifted, to commence an action for specific performance of the purchase option. Oneida asserts that Code § 108(c) “provides for the tolling of a statute of limitations and does *not* toll or extend contractual rights or duties of a non-debtor.” *See* Oneida’s Reply Affidavit in Response to Varick’s Second Supplemental Response, July 27, 2007, Dkt. # 117, ¶ 4 (emphasis in original). Oneida also contends that Varick, given the lack of specificity regarding a material term (i.e. the purchase price) of the purchase option, has no basis upon which to bring an action for specific performance.

Oneida does not address Varick’s argument that it maintains all rights under its Lease with the Debtor, including the purchase option provision, pursuant to Code § 365(h)(1)(A)(ii).

DISCUSSION

⁹ This argument was made by both Oneida in its July 27, 2007 Reply Affidavit, and by the Chapter 13 Trustee at Oral Argument on July 31, 2007.

Standing

Neither party provides relevant case law or secondary authority to support its arguments on the question of Oneida's standing. The Court first resorts to a leading bankruptcy treatise:

An unsecured creditor as well as a secured creditor may object to a sale, especially where the sale is to be free and clear of the secured creditor's lien; the secured creditor is not limited to a challenge based only on grounds related to the sale free and clear of the lien.

3 Lawrence P. King *et al.*, *Collier on Bankruptcy*, P 363.02[1][c] at 363-14 (15th ed. 2007).

It is true that "a prospective purchaser has no standing to object to a [§ 363] sale." *See In re Condere Corp.*, 228 B.R. 615, 624 (Bankr. S.D. Miss. 1998). However, it is clear that Oneida is more than a mere prospective purchaser, having filed a valid proof of claim in this case. *See also In re Nepsco, Inc.*, 36 B.R. 25, 26 (Bankr. D. Me. 1983) (finding that a prospective purchaser objecting to a trustee's "not widely advertised" § 363 sale did not have standing to object because it "[was] not a creditor of the estate.")¹⁰

At least one court has found that even if a party lacked standing to object to a proposed Code § 363 sale, the bankruptcy court would not be precluded from considering that party's offer in ascertaining whether the proposed sale "is in the best interest of the estate." *See In re Planned Systems, Inc.*, 82 B.R. 919, 923 (Bankr. S.D. Oh. 1988). The Court believes this same reasoning applies to the instant case. Even if Oneida were to be found to lack standing, this would not preclude the Court from considering its (as well as the Chapter 13 Trustee's) argument that a

¹⁰ Similarly, a party that has merely filed a *lis pendens* on the property to be sold does not have standing to object to a Code § 363 sale. *See In re Adamson*, 312 B.R. 16, 20 (Bankr. D. Mass. 2004).

public auction would be in the best interest of the estate.

This is especially true given the Chapter 13 Trustee's July 16, 2007 letter to the Court, indicating his full support for Oneida's position that the sale should be open to competitive bidding. At the very least, Varick has failed to provide the Court with any basis for ignoring the Chapter 13 Trustee's request.

Was the Lease Assumed or Rejected?

Varick contends that the Lease was assumed because when the Debtor's plan was confirmed on August 12, 2004,

[t]he Chapter 13 Trustee, the Court, the Debtor and presumably all creditors who had appeared in the action (including Oneida Construction Corp.) were on notice of the terms and conditions of the Lease and option to purchase which were being assumed...No one objected to the assumption by Debtor of the Lease at the time of the third amended plan.

Varick Affidavit, July 27, 2007, Dkt #115, ¶ 8.

Although the Debtor's Plan does reference the Lease in its "Other Provisions" section, this refers only to repairs the Debtor is to make to the leased premises, and the rental arrears Varick will bring current in return. No specific mention of assumption is made. Nor does the Court's Confirmation Order mention the assumption of a lease. Case law requires that any assumption, or rejection, of an unexpired lease must be approved by the bankruptcy court. "[A]ny assumption or rejection of an unexpired lease is devoid of validity without the court's approval." See *In re Kelly Lyn Franchise Co., Inc.*, 26 B.R. 441, 445 (Bankr. M.D. Tenn. 1983)(quoting *Frank C. Videon, Inc. v. Marple Publishing Co.*, 20 B.R. 933, 934 (Bankr. E.D. Pa. 1982). See also *In re Gamma Fishing Co., Inc.*, 70 B.R. 949, 953 (Bankr. S.D. Ca. 1987)

(stating that “cases which have considered the application of §365 to an executory contract or lease have consistently decided that § 365(a) means what it says, i.e., that an express order of the judge approving an assumption or rejection is required.”).

More specifically, in the Chapter 13 context, at least one court has opined that Code § 365 “applies in Chapter 13 cases, but that its requirements may be satisfied through the plan process.” *See In re Ford*, 159 B.R. 930, 931 (Bankr. W.D. Wa. 1993) (denying debtor’s late motion to assume the lease because, *inter alia* “[n]one of the [debtor’s] plans expresses a clear, unequivocal, affirmative intention to assume the ... lease, or sets out the minimal cure, compensation, and adequate assurance requirements of a motion to assume under § 365(b)(1)”). *See also In re Damianopoulos*, 93 B.R. 3, 9 (Bankr. N.D.N.Y. 1988) (holding that “[e]ven if something less than a motion was required [to assume the lease of nonresidential real property] under Code § 365(d)(4), *the debtor’s general statement in his original plan -- the only action he took regarding the lease-- did not constitute the clear, unequivocal, affirmative and specific act of assumption required.*”) (emphasis added).

Moreover, pursuant to Code § 365(d)(2)¹¹, the Lease could have been assumed or rejected only at any time prior to confirmation.¹² As mentioned *supra*, the Debtor’s Plan was confirmed

¹¹ Section 365(d)(2) reads, in relevant part: “In a case under chapter 9, 11, 12, or 13 of this title, the trustee may assume or reject an executory contract or unexpired lease of residential real property or of personal property of the debtor at any time before the confirmation of a plan...” 11 U.S.C. § 365(d)(2).

¹² It is Code § 365(d)(4) which deals with the assumption or rejection of leases of nonresidential real property, but only where the debtor is lessee. “Apparently Congress was not thinking about those situations in which the debtor is *lessor* [of nonresidential property], since neither paragraph (2) nor (4) of section 365(d) provides a time period for the assumption or rejection of a nonresidential lease by a debtor lessor.” *See* 3 Lawrence P. King *et al.*, *Collier on Bankruptcy*, P 365.04[5] at 365-48 (15th ed. 2007) (emphasis added). As a result, Bankruptcy

by Order of this Court on August 12, 2004.

Thus, the Lease was neither assumed nor rejected by the deadline specified in Code § 365(d)(2). In such an instance, “[c]ase law has developed a ‘ride through’ or ‘pass through’ doctrine applicable to those situations in which the debtor fails to assume an executory contract [or unexpired lease] and both parties continue to perform as if there had been no bankruptcy filing.” See *In re Ward*, No. 03-66503, slip op. at 7 (Bankr. N.D.N.Y. Feb. 28, 2005). See also *In re Shoppers Paradise, Inc.*, 8 B.R. 271, 278 (Bankr. S.D.N.Y. 1980) (holding that “[u]ntil assumed or rejected, an executory contract or unexpired lease remains in force and if neither assumed nor rejected, passes with other property of the debtor to the reorganized corporation.”). Accord *Boland v. Parmelee*, 1997 U.S. Dist Lexis 16157 *14 (N.D.N.Y. 1997) (applying the *Shoppers Paradise* holding in the Chapter 13 context).

Because the Lease was not assumed or rejected by Order of this Court, either prior to confirmation or as part Debtor’s confirmed Plan, the Court finds that the Lease “passed through” , and remained in effect until it expired on its own terms.

Varick’s Code § 365 (h)(1)(A)(ii) Argument

Varick argues that if the Lease is deemed to be rejected, Code § 365 (h)(1)(A)(ii) applies

Judge Jack B. Schmetterer of the Northern District of Illinois has stated that “[b]ecause the special limits of section 365(d)(4) are inapplicable when the debtor is a lessor, the better approach would be to apply the rule of section 365(d)(2) to leases of nonresidential real property under which the debtor is lessor, in recognition of the apparent oversight.” See *In re Sae Young Westmont-Chicago, L.L.C.*, 276 B.R. 888, 893 (Bankr. N.D. Ill. 2002).

and that Varick “maintains all rights under the Lease, including the option to purchase.”¹³ See Varick’s Affidavit in Response, June 22, 2007, Dkt. #106, ¶ 15.

Because the Court finds that the Lease was not rejected, Code § 365(h)(1) does not apply to this situation.

Even if Code § 365(h) were applicable to the instant case, however, Code § 365(h)(1)(A)(ii) only provides the lessee with its rights under the lease “for the balance of the term of such lease and for any renewal or extension of such rights to the extent such rights are enforceable under applicable nonbankruptcy law.” The Lease expired under its own terms on January 12, 2005. Section 365(h)(1)(A)(ii) cannot extend that term any further. The relatively narrow scope of Code § 365(h) was addressed by former Bankruptcy Judge David A. Scholl of the Eastern District of Pennsylvania:

[W]e believe that the rights of a lessee whose lease has been rejected by a lessor-debtor are narrowly circumscribed by the precise language of § 365 (h). That Code section... allows only a *lessee* the choice to remain in possession under the terms of the lease. It does *not* provide that the lease continues, but merely accords a *lessee* the choice to remain in a rented premises *under the terms* of the lease.

In re Carlton Restaurant, Inc., 151 B.R. 353, 356 (Bankr. E.D. Pa. 1993) (emphasis in original).

The Lease contained the following Renewal Option:

¹³ Code § 365 (h)(1)(A) reads, in relevant part:

*If the trustee rejects an unexpired lease of real property under which the debtor is the lessor and -*** (ii) if the term of such lease has commenced, the lessee may retain its rights under such lease (including rights such as those relating to the amount and timing of payment of rent and other amounts payable by the lessee and any right of use, possession, quiet enjoyment, subletting, assignment, or hypothecation) that are in or appurtenant to the real property for the balance of the term of such lease and for any renewal or extension of such rights to the extent that such rights are enforceable under applicable nonbankruptcy law.* 11 U.S.C. § 365(h)(1)(A)(ii) (emphasis added).

RENEWAL OF LEASE: At the end of the lease term, tenant shall have the options [*sic*] to enter into an additional lease term of three (3) years upon the same terms and conditions of this lease.

Section 365 (h)(1)(A)(ii) would arguably provide Varick with renewal rights “to the extent such rights are enforceable under applicable nonbankruptcy law.” The renewal option contained in the Lease was exercisable “at the end of the lease term” on January 12, 2005. It is uncontested that Varick did not choose to renew the Lease. That renewal option, under applicable nonbankruptcy law, is not exercisable at any time after January 12, 2005. *See Warren Street Associates v. City Hall Tower Corp.*, 202 A.D.2d 200, 200 (1st Dept. 1994) (holding that renewal options exercisable after the initial lease term are null and void); *Ritz Entertainment Org., Inc. v. Unity Gallega of the United States, Inc.*, 166 A.D.2d 186, 187 (1st Dept. 1990) (holding that where tenant’s decision not to exercise its renewal option when required by the lease did not result from mistake or excusable fault, tenant was not entitled to exercise its renewal option *nunc pro tunc*).¹⁴

Lack of a Definite Pricing Term in the Option

In response to the allegation of Oneida and the Chapter 13 Trustee that the purchase option fails because it lacks a mechanism for determining the price at which Varick was entitled to exercise the purchase option, Varick quotes former Chief Judge Wachtler’s language in *166 Mamaroneck Ave. Corp.* to the effect that a definite term (price) may be lacking and the contract

¹⁴ *But see J.N.A. Realty Corp. v. Cross Bay Chelsea, Inc.*, 42 N.Y.2d 392, 397-98 (1997) (holding that a tenant may be entitled to equitable relief if it did not prejudice the landlord, where failure to exercise a renewal option was due to a “mere venial inattention” and would result in a forfeiture).

provision may still stand if “there exists an objective method for supplying a missing term.” *Id.* at 91. Varick does contend that “upon information and belief, although not explicitly set forth in the Lease, it was contemplated between the parties [that] the purchase price would be the fair market value of the real property at the time the option was [to be] exercised.” *See* Affidavit of Laura S. Ruberto, July 24, 2007, Dkt.# 113, ¶ 4.

A significant problem with Varick’s argument is its selective quotation of the New York Court of Appeals’ *166 Mamaroneck Ave. Corp.* decision. In the paragraph immediately following the language quoted by Varick, Judge Wachtler went on to state that the New York Court of Appeals had

identified two ways in which the requirement of definiteness could be satisfied in the absence of an explicit contract term: (1) an agreement could contain ‘a methodology for determining the missing term *within the four corners of the lease*, for a term so arrived at would have been the end product of agreement between the parties themselves; or (2) an *agreement could invite recourse to an objective extrinsic event*, condition or standard on which the amount was made to depend.

In re 166 Mamaroneck Ave. Corp., 78 N.Y.2d at 91-92 (emphasis added).

In the instant case, in order to overcome the lack of a definite price term, Varick is completely unable to point to “a methodology for determining the missing term *within the four corners of the lease...*” Nor can Varick show where the Lease “*invite[s] recourse to an objective extrinsic event*, condition or standard on which this amount was made to depend.” Varick’s/Ruberto’s *post hoc* assertion that “upon information and belief, although not explicitly set forth in the Lease, it was contemplated between the parties [that] the purchase price would be the fair market value of the real property at the time the option was [to be] exercised” is both too remote in time, and too vague (“upon information and belief”, “contemplated”) to be

convincing. *See* Affidavit of Laura S. Ruberto, July 24, 2007, Dkt.# 113, ¶ 5. Most importantly, however, the statement, as demonstrated *supra*, does not even approach meeting either of the two requirements the New York Court of Appeals set out in *166 Mamaroneck Ave. Corp.* for overcoming the lack of a definite term in a lease or contract.

As a result, even before considering whether the purchase option remained in effect during the time Varick claims it did, the Court finds that the lack of a material term in the purchase option itself is fatal to the effective exercise of that option by Varick.

Enforceability of the Purchase Option Itself

Oneida makes much of the assertion that a plain reading of the purchase option provision yields the understanding that the purchase option could be exercised in perpetuity. In this regard Oneida quotes the New York Court of Appeals's decision in *Jarecki*:

To permit plaintiff to wield a 'phantom' or 'shadow' bilateral contract at his whim for an indeterminate time even after the end of the sublease would unreasonably undermine the alienability of defendants' property and would significantly impede their ability to sublet the apartment to a third party.

Jarecki, 95 N.Y.2d at 669.

In this same decision the New York Court of Appeals states that

an option found in a lease generally runs with the land and, *absent unequivocal language to the contrary*, may not be exercised beyond the lease term if such exercise creates an unreasonable result.

Id. (emphasis added).

One thing clearly lacking in the Lease regarding the exact term (commencement and expiration) of the purchase option is unequivocal language. Because of this fact, and because such an exercise would, in the court's opinion, violate New York state law as set out in *Jarecki*,

the Court finds that the purchase option cannot be exercised beyond the term of the Lease.

Varick does cite *Hutt v. Johnson*, 135 A.D.2d 501 for the proposition that a purchase option not exercisable until three months after the lease term ends is not necessarily terminated by the end of the lease term. This holding does not support Varick's argument for two reasons. First, the language of the instant purchase option does not meet the New York Court of Appeals's requirement for "unequivocal language" indicating that the option does *not* run with the land (i.e. terminate with the lease). Second, the *Hutt* court was presented with facts in which 1) the lease and option agreement were intended to be separate and distinct, and 2) the landlord was attempting to use a condemnation proceeding to terminate the lease and void the purchase option based on a *de minimus* taking in the condemnation. These facts are enough to remove the court's holding from the realm of law, into equity. In fact, the last sentence of the decision states that the result the landlord was seeking in *Hutt* was one "which equity will not countenance." *Hutt*, 135 A.D.2d at 502. It may have been in an attempt to bolster its analogy to the facts in *Hutt* when Varick stated that "the Option to Purchase was a separate and distinct portion of the Lease Agreement not tied into the Lease term and extended the term of the Agreement." See Varick's Affidavit in Response to Opposition, June 22, 2007, Dkt.# 106, ¶ 16 (emphasis in original). However, the Court believes the subject purchase option is *not* a separate and distinct portion of the Lease, and that it *is* tied into the lease term. The Court's findings in this respect are supported by a review of the pre-eminent treatise on this topic, *Warren's Weed New York Real Property*:

It is possible to draft the [purchase option] provision to give the lessee an option to purchase as an independent contractual right, separable from the lease, but such a provision would be an unusual one.... it is therefore to be inferred, *in the absence of an expression of an intention of the parties to the contrary*, that an option is intended to be inseparable from the leasehold estate...

10-101 *Warren's Weed New York Real Property* § 101.14 Differentiating Option and Lease; Separability (emphasis added).

The Court is unable to find in the purchase option, or in the entire Lease itself, for that matter, a coherent “*expression of an intention of the parties to the contrary*” which would be required in order to find that the purchase option was separable from the leasehold estate.

Additional case law argues for Oneida 's and against Varick's position. “[I]t is well settled that in order to validly exercise an option to purchase real property, one must strictly adhere to the terms and conditions of the option agreement.” *See Galapo v. Feinberg*, 266 A.D.2d 150, 151. Given the indeterminacy of the price term, as well as the termination of the purchase option in the instant case, strict compliance here would be an impossibility.

Varick's Code § 108 Argument

Varick argues that it has a valid cause of action under New York State law against the Debtor for specific performance of the purchase option, and that because this cause of action matured only after the Debtor was in bankruptcy, pursuant to Code § 108(c), Varick has six years (the New York Statute of Limitations), or 30 days after the automatic stay is lifted, to commence the action.

This would seem to make for both a convincing and a perplexing argument. Convincing, because at first glance it seems uncontrovertable that Varick did in fact have a cause of action for specific performance under the purchase option provision of the Lease. Perplexing, because if this were the case, and the Court were to grant Varick's request to enforce the purchase option

provision over the objections of Oneida and the Chapter 13 Trustee¹⁵ on the basis of the § 108 argument, the Court would be precluded from addressing the merits of a dispute concerning a matter over which it has core jurisdiction (*See* 28 U.S.C. § 157 (b)(2)(N),(O)), because the matter would then be adjudicated in state court.

This conundrum is disposed of when it is recalled that the purchase option on which Varick purports to base its cause of action under New York State law is part of what was, at the time of the petition, an unexpired lease. Unexpired leases are governed by Code § 365, not § 108.

Other courts have addressed this seeming conflict:

Section 365 contains comprehensive instructions for the treatment of executory contracts...Additionally, neither the legislative history of § 108 nor any of the comments thereto contain any indication that § 108 applies to executory contracts...Section 108(b) is a general provision as to the extension of time. Section 365 is entitled ‘Executory Contracts and *Unexpired Leases*.’ This appears to be the more specific provision. Where two statutory provisions apply, the more specific will govern. Further, where one section of the Bankruptcy Code governs an issue, another section will not be interpreted to cause an irreconcilable conflict.

In re McLouth Steel Corporation, 20 B.R. 688, 690 (Bankr. E.D. Mich. 1982) (emphasis added).¹⁶

See also In re Circle K Corp., 190 B.R. 370, 378 n.9 (9th Cir. B.A.P. 1995) (indicating that there is a direct conflict between § 108(b) and § 365 as applied to executory contracts and unexpired leases.)

Hence, Varick’s avenues for relief (enforcement of the purchase option as part of the

¹⁵ *See* Varick’s Second Supplemental Response, July 24, 2007, Dkt.# 113, pgs. 3-5.

¹⁶ Although the *McLouth Steel* court uses the term “executory contracts” in this passage, it is clear from the context that the same reasoning applies to “unexpired leases”, especially since the *McLouth Steel* court explicitly relies upon the exact title of § 365, which includes the words “unexpired leases.”

unexpired lease) were either to seek an order of this Court compelling the Debtor to assume the Lease and enforce the purchase option, or to pursue the remedies available to a tenant in a § 363 sale pursuant to § 363(e). Because it has done neither, Varick cannot now invoke Code §108 (c) in order to escape this Court's jurisdiction over matters concerning the sale or liquidation of property of the estate. Varick does not have recourse, by way of Code § 108(c), to a specific performance cause of action under New York State law.

As set out above, the Court finds that 1) Oneida does have standing to object to the Debtor's proposed sale of the Real Property to Varick, 2) Varick's Lease with the Debtor was not assumed or rejected, but passed through with other property of the Debtor, and remained in full force and effect until it expired by its own terms, 3) Code § 365(h) does not apply, and would not provide Varick with any rights which would survive a Code § 363(a) sale of the Real Property even if it did apply, and 4) Varick cannot invoke Code § 108(c) in order to bring an action for specific performance against the Debtor in state court.

The Court also finds, primarily on specific, contract-based principles, that the subject purchase option provision of the Lease is not enforceable.¹⁷

Based on the foregoing, it is hereby

¹⁷ By way of analogy, however, the Code provides a similar example of a Trustee's power to sell property of the estate over the objections of a party-in-interest with ostensibly even more rights than the holder of a purported purchase option. Under Code § 363(h) a trustee may sell both the estate's interest in property *as well as that of a non-filing co-owner* (joint tenant, tenant in common or tenant by the entirety), assuming certain conditions are met: (1) partition of the property is impracticable, (2) sale of the estate's interest only would realize significantly less for the estate, (3) the benefit to the estate of the sale of both its and co-owners' interests outweighs the detriment to the co-owners and (4) the property is not used in the electric energy or gas industry.

ORDERED that Debtor's Motion is denied; and it is further

ORDERED that creditor Oneida's and the Chapter 13 Trustee's Objections to Debtor's Motion¹⁸ are sustained, and their request that the sale of the Real Property be subject to higher and better offers in open competitive bidding is granted; and it is finally

ORDERED that Debtor shall file and notice a new motion to sell the Real Property pursuant to Code § 363(f) to the highest responsible bidder.

Dated at Utica, New York

this 6th day of September 2007

STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge

¹⁸ Seeking an Order approving the sale of Real Property to Varick.