UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NORTH CAROLINA
CHARLOTTE DIVISION

In Re:	)	**Case No. 92-31886**
	)	**Chapter 13**
HARVEY ERSKINE PLYLER and	)	
SUSAN ANNETTE PLYLER	)	
aka Pit Plyler,	)	
	)	
Debtor.	)	
	)	

ORDER

This matter comes before the Court upon the Chapter 13 Trustee's Motion to Determine Status of Claim of Royal Auto Sales ("Royal") and the verbal response made thereto. A hearing was conducted on May 29, 1996. Based upon the record before it and the evidence presented, the Court makes the following findings of fact and conclusions of law:

FINDINGS OF FACT

1. On April 21, 1991 and prior to filing Bankruptcy, the Debtors entered into an Agreement with Royal pertaining to a 1988 Chevrolet Celebrity automobile. This Agreement called for the Debtors (1) to make a $500 down payment, (2) trade-in to Royal a vehicle having a $1,000 value, and (3) make payments of $54.71 per week for two hundred and eight (208) weeks to Royal. In exchange, the Debtors would have the use of the vehicle. During the contract term, title to the vehicle would remain in the name of Royal. However, upon completion of the Agreement, the Debtors are to be given clear title to the car for no additional consideration. (Paragraph 11.D). During the term of the Agreement, the Debtors are responsible for insurance, maintenance, and taxes. No

warranties are provided by Royal to the Debtors in this Agreement. There is no right to terminate the Agreement prior to the end of the contract term.

2. On October 16, 1992, the Debtors filed a Chapter 13 case with this Court. The First Meeting of Creditors was conducted on November 19.

3. Royal filed no proof of claim in this bankruptcy case. However, in accordance with the Code, on December 9, 1992, the Debtors filed a claim for Royal. This claim treated Royal as secured with regard to the 1988 Chevy Celebrity.

4. On January 6, 1993, the Trustee objected to the claim for the lack of documentation. No response was made to this objection by either the Debtors or Royal. On February 17, 1993, an Order was entered sustaining the Trustee's Objection and treating Royal's claim as an unsecured obligation in this bankruptcy case.

5. In 1995, in accordance with the Plan, the Trustee commenced disbursements to Royal and to other unsecured creditors.

6. Thereafter the Debtors wrecked the vehicle. After notice and opportunity for hearing, an Order was entered authorizing the Debtors to use the insurance proceeds received due to their wreck to purchase a replacement vehicle, with a lien to attach thereto in favor of Royal. (Order dated July 26, 1995). The Debtors are holding some $2,300 of insurance proceeds for this purpose.

7. The Trustee upon realizing the confusion regarding the Royal claim then filed the current Motion seeking a determination of Royal's claim. Royal, previously silent in this case, appeared

at the hearing to make known its position. Royal now contends that it is a lessor of this equipment, is the owner of same, and claims entitlement to these monies. The Trustee's position and that of the Debtors, is that the agreement between the Debtor and Royal is a disguised security agreement under the Uniform Commercial Code, and not a true lease. The Debtors believe that if adequate protection is given to Royal, they are entitled to use this collateral under 11 U.S.C. § 363, including but not limited to substitution of the collateral as obtained in the Amended Order.

CONCLUSIONS OF LAW

Under 11 U.S.C. § 365, the Debtor must assume or reject a lease of property. Unlike a secured claim, a Debtors' Chapter 13 Plan cannot modify the terms of a true lease. Since both the Debtors' proposal to roll the insurance proceeds into another vehicle and the Trustee's prior treatment of the claim as an unsecured obligation in this bankruptcy case purport to modify the Agreement, the Court must determine the nature of the parties' contract.

The issue of whether an agreement constitutes a true lease or is instead a disguised security agreement is a question of state law. Butner v. U.S., 440 U.S.C. 48, 995 S.Ct. 914 (1979). Under the Uniform Commercial Code, this determination is made pursuant to the standards set out at U.C.C. Section 1-201(37). (NCGS 25-1-201(37)).

Subsection (a) of 1-201(37) cites four factors, the presence of any one of which in an agreement, deems the arrangement a security agreement. Subsection (a) provides:

> . . . a transaction creates a security interest if:
>
> (i) The original term of the lease is equal to or greater than the remaining economic life of the goods, or
>
> (ii) The lessee is bound to renew the lease for the remaining economic life of the goods or is bound to become the owner of the goods, or
>
> (iii) The lessee has an option to renew the lease for the remaining economic life of the goods for no additional consideration or nominal additional consideration upon compliance with the lease Agreement, or
>
> (iv) The lessee has an option to become the owner of the goods for no additional consideration or nominal additional consideration upon compliance with the lease Agreement.

N.C.G.S. § 25-1-201(37)(a)(i-iv).

The current dispute is readily resolved by reference to Section 1-201(37(a). Specifically, this matter falls within the parameters of 25-1-201(37)(a)(iv). It is clear under the parties' agreement that the lessee becomes the owner of the vehicle in question at the termination of this contract and for no additional consideration.

Paragraph 11.D of the Agreement states:

> "Subletor agrees upon completion of full performance of the Agreement (including payment schedule) the sales agreement, if any, automatically becomes enforceable and subletee/buyer shall receive clear title from subletor/owner to the vehicle within thirty (30) days of full and final payment and title shall be released to subletee/buyer."

Clearly, the contract between these parties contemplates that the Debtor will become the owner at the end of the lease for no additional consideration. This fact was acknowledged by Royal at hearing. However, Royal argues that the "option" itself would exist only if the Debtors had made all of the payments under the contract prior to filing bankruptcy. Its position is that as the Debtors defaulted before completion of the contract, they did not have such an option and subsection (a)(iv) is not met.

This view is misplaced. The statute determines the nature of a contract by its written terms. If the contract provides that upon completion the Debtor automatically becomes the owner of the goods, the contract is a security agreement, not a lease. Successful completion of the contract is simply a requirement to be met before exercising the option, it is not a condition precedent to the existence of that option.

That said, the question is raised as to the appropriate treatment of this claim in the present bankruptcy case. This issue was not addressed at the prior hearing. This Court previously characterized this obligation as an unsecured debt and the claim has been treated as such in the Chapter 13 plan to date. Later, at Debtors request the Amended Order dated April 10, 1996 was entered which provided for the imposition of a lien in favor of this creditor. This is of course proper if Royal had a perfected secured claim in the first vehicle, but is not proper if it is unsecured in that vehicle.

Inasmuch as the record does not reflect whether Royal had taken steps sufficient to perfect a lien on the original vehicle, the Court will conduct a further hearing in this matter on the 23rd day of July, 1996 at 2:00 p.m. in the Charles R. Jonas Federal Building, Courtroom 126, 401 West Trade Street, Charlotte, NC to consider, in view of this ruling, the appropriate treatment of this claim and whether either of its earlier Orders should be amended.

This the 9th day of July, 1996.

United States Bankruptcy Judge