UNPUBLISHED OPINION

#352

IN THE UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF UTAH

CENTRAL DIVISION

In re: AMBRA OIL AND GAS COMPANY, Debtor.	Bankruptcy Number 89B-07810 [Chapter 11]

MEMORANDUM DECISION AND ORDER

Ambra Oil and Gas Company (Ambra), is a public corporation and the chapter 11 debtor herein. Ambra operates its own oil and gas wells, as well as providing management services of a similar nature for other entities.

Ambra proposes a plan of reorganization that provides for the liquidation of all of its assets over a two year period. The assets consist of Ambra's interests in various oil and gas wells that it owns outright or participates in as a general partner of various limited partnerships, as well as personal property consisting of automobiles, office furnishings and field production equipment.

The plan proposes a sales schedule that specifies dates from 120 to 720 days from the effective date of the plan by which each asset will be liquidated. If an asset is not liquidated by the date set forth in the plan, it will be surrendered to secured creditors claiming an interest in the asset. Ambra's remaining secured creditors are primarily governmental taxing authorities.. During the liquidation period, Ambra will continue to

operate its business to maximize the value of its assets pending liquidation. At the end of the liquidation period, Ambra will have no tangible assets.

Creditors overwhelmingly approved the plan. Although the plan provides that little, if any, payment will be made to holders of $510,000 in unsecured claims, over 150 ballots were cast and each class of creditors accepted the plan.[1] Only one interest holder objected to the plan. The objection cited the plan's failure to comply with 11 U.S.C. section 1141(d)(3),[2] lack of feasibility and violation of the absolute priority rule. The objection also asserted that the plan had not been proposed in good faith.

The court has determined that the objections are not well taken,[3] but provides the following review of the issue regarding the objection based on section 1141(d)(3).[4] The plan provides that upon confirmation, Ambra will receive a discharge of all of its debt, including the $510,000 in listed unsecured debt. Under section 1141(d)(3), discharge is permissible only if the evidence indicates that Ambra will engage in business after

---

[1] The plan provides that the value at confirmation of Ambra's assets is $363,000. All of Ambra's assets are to be liquidated over time in an amount sufficient to generate $363,000. The proceeds of the liquidation will be paid to administrative and secured creditors, and the remaining balance, if any, will be paid to unsecured creditors. It appears that little, if any, proceeds of sale will be available for unsecured creditors.
The plan also provides that if proceeds from the sale of assets reach $363,000 at any time before the end of the liquidation period and Ambra still possesses assets available for sale, the benefit of the value of the remaining assets will inure to equity interest holders. Ambra predicts that this event will only occur if during the liquidation period the oil and gas market improves to such an extent that the value of Ambra's assets will have a greater value than the value at the confirmation date.

[2] Future references are to Title 11 of the United States Code unless otherwise specified.

[3] The plan liquidates all of Ambra's assets. Although the testimony presented at the confirmation hearing did not give much comfort that Ambra had specific plans as to the method of liquidation of its assets, the plan provision calling for surrender of the assets at specific dates if not sold and the testimony that Ambra had access to sufficient funds to operate during liquidation, constituted sufficient evidence for the court to find that the plan complies with section 1129(a)(11). The objection premised on the argument that the plan was not fair and equitable was neutralized by the acceptance of the plan by each class. The good faith argument is not well taken because the plan complies with section 1129(a)(7).

[4] There is no argument that Ambra, as a corporation, would be denied a discharge under section 727(a)(1).

consummation of the plan. If Ambra will not engage in business after consummation, the plan improperly provides for discharge, does not comply with section 1129(a)(1) and cannot be confirmed.

The evidence indicated that all of Ambra's assets will be liquidated at a rate sufficient to generate a sum equal to the value of those assets on the effective date of the plan in accord with section 1129(7)(A)(ii). An asset would remain with Ambra only if the value of all the assets to be sold increases over the next two years and exceeds $363,000. Accordingly, any assets which did not need to be sold to generate the $363,000 plan value would remain property of Ambra at the end of the liquidation period.

The court concludes that at the point of plan consummation as defined by section 1101(2), substantially all of Ambra's assets will be liquidated[5] and there will be no tangible property available with which Ambra may operate its service business. The only assets available to Ambra upon consummation with which it may operate its business consist of the skill of its principal and employee, Ambra's name and a corporate shell. The testimony indicated that one of Ambra's employees and one principal had extensive skill in operating oil and gas wells, that their skills and expertise were marketable, and that they would be available to conduct Ambra's business after liquidation. Evidence also indicated that Ambra's name as one of a few surviving oil and gas companies in Utah has some intrinsic value. No objective value was placed upon the corporate name in the liquidation analysis and the court discounts this testimony. However, there may be value inherent in

---

[5] The uncontradicted evidence indicated a general decline in the natural gas market. More specifically, large volume purchasers of natural gas have ceased buying from most or all of Ambra's fields. Only a major up-turn in the natural gas market, such as that created by beneficial legislation, war, or changes in OPEC pricing, could possibly increase the value of Ambra's assets.

the existence of the shell of a publicly held corporation. *In re Rath Packing Co.*, 55 B.R. 528, 533 (Bankr. N.D. Iowa 1985)(the court received testimony that it may take as long as seven years and several hundred thousand dollars to achieve publicly held status). No evidence exists in this case regarding the value of Ambra's corporate shell.

The only evidence presented was that Ambra intended to conduct business after the liquidation of its assets. No credible evidence was produced that indicated a specific market for the skills of Ambra's principal and employee, and no specific contracts, ventures or projects were identified. Thus, the issue is whether the mere intent to engage in business after consummation of the plan is sufficient to enable a discharge to be issued as provided in the plan.

In a chapter 7, all assets are liquidated, the debtor does not continue in business and no discharge is issued. The debts that remain unsatisfied through liquidation of the assets of the corporate chapter 7 debtor remain attached to the corporate entity. Should equity holders attempt to revive the corporate debtor and try to operate its business, the corporate entity would still be encumbered by the nondischarged debt that attached to it pre-petition.

Similarly, in a corporate chapter 11 where the assets of the debtor are liquidated, it appears to be the intent of Congress that no discharge issue if the debtor does not engage in business after consummation of the chapter 11 plan. The intent of Congress was to prevent trafficking in corporate shells and in bankrupt partnerships. *Liberty Trust Co. Employees Profit Sharing Trust v. Holt (Matter of Liberty Trust Co.)*, 130 B.R. 467, 471 (Bankr. W.D. Tex. 1991); *In re Maxim Indus., Inc.*, 22 B.R. 611 (Bankr. D. Mass. 1982), *citing*, House

Report No. 95-595, 95th Cong., 1st Sess. 384-85 (1977);[6] Senate Report No. 95-989, 95th Cong., 2d Sess. 98-99 (1978), U.S. Code Cong. & Admin. News 1978, p. 5787. In fact, the Congressional sub-committee reports equate such a practice to bankruptcy fraud. Because of the seriousness of the issue, it is incumbent upon the court to carefully consider what activity Congress sought to proscribe and whether that proscription applies to this case. The court has a duty to deny confirmation when the requirements of section 1129 are not met. *In re Economy Cast Stone Co.,* 16 B.R. 647 (Bankr. E.D. Va. 1981).

The legislative history does not offer great clarity regarding the perceived injury to the public that Congress sought to prohibit by limiting the potential for trafficking in corporate shells, but case law and commentators have clarified some of the potentially harmful events that could occur. In *N.L.R.B. v. Better Building Supply Corp.*, 837 F.2d 377, 378-379 (9th Cir. 1988), the court prohibited a chapter 7 corporation from operating post-filing because it succeeded another corporation that was liable for damages under the NLRA for unfair labor practices and had been assessed back pay damages. The court found that the new corporation had been created for the purpose of avoiding the NLRB ruling. The court stated that:

---

[6] With respect to Section 727(a)(1), the House Report stated that:

> This section is the heart of the fresh start provisions of the bankruptcy law. Subsection (a) requires the court to grant a debtor a discharge unless one of eight conditions is met. The first condition is that the debtor is not an individual. This is a change from present law, under which corporations and partnerships may be discharged in liquidation cases, though they rarely are. The change in policy will avoid trafficking in corporate shells and in bankrupt partnerships.

> The primary concern underlying this section was to prevent businesses from evading liability by liquidating debtor corporations and resuming business free of debt. . . .
>
> In adopting section 727(a)(1), Congress intended that corporate debt would survive chapter 7 proceedings and be charged against the corporation when it resumed operations.

Better Bldg. Supply, 837 F.2d at 379; *see also, N.L.R.B. v. Goodman, (In re Goodman)* 873 F.2d 598, 602 (2d Cir. 1989); *Liberty Trust*, 130 B.R. at 472 (the court prohibited a defunct chapter 7 corporate debtor from continuing to operate in order to manage causes of action abandoned by the Trustee); *In re Maxim Indus., Inc.* 22 B.R. 611 (Bankr. D. Mass. 1982)(confirmation of chapter 11 plan denied where the primary purpose was to permit the use of shell corporation for the personal benefit of the officers of the corporation).

Impermissible tax consequences are also an articulated reason for limitation of trafficking in corporate shells. *In re Rath Packing Co.*, 55 B.R. 528, 537 (Bankr. N.D. Iowa 1985)(tax avoidance would be impermissible objective of plan modification); *see also, Developments In Confirmation Standards for Chapter 11 Plans,* 573 PLI/Comm 389 (April 1991)(discussion of section 1129(d) prohibition against confirmation if the principal purpose of the plan is tax avoidance). Improper use of a shell corporation with tax losses is also prohibited under the Bankruptcy Code. Section 382 of the Internal Revenue Code, as amended in the Tax Reform Act of 1986, limits a bankrupt corporation's use of net operating loss carryovers to reduce future corporate income of the reorganized corporation and makes trafficking in loss corporations (corporations with NOL's) more difficult, if not impossible. *New Limitations on NOL Carryovers Following the TRA*, 66 J. Taxation 258 (May 1987)(indicating that section 1141(d)(3) is limited to situations where the plan calls for liquidation and where no business credit is extended in good faith to the debtor after

confirmation). Enactment of more specific forms of legislation, working in tandem with the Bankruptcy Code, reduces trafficking in corporate shells for improper purposes.[7]

It is also conceivable that trafficking in corporate shells could harm equity interest holders, especially in light of the exemption from securities law provided in section 1145. A debtor should not be able to confirm a plan utilizing section 1145 that provides for the issuance or sale of securities of a debtor and also liquidates all assets of the debtor without continued operation. The debtor could then attempt to market the securities without any new value ascribed to the continued business enterprise.

As these concerns are applied to this case, there is no evidence that the scheme as proposed in the plan has been created for the purpose of avoiding legitimate debts of Ambra. Ambra's plan provides for some payment on all debt even though recovery by unsecured creditors may be slight. No evidence has been introduced that the primary motivation for the plan was creation of a shell corporation for the personal benefit of the principals of the corporation. Although the sole remaining shareholder benefits from a discharge being granted to Ambra because he can then use the shell for his own purposes, this argument is more appropriately brought as an objection to the shareholder's acquisition through the plan of all Ambra's equity. Had the court been required to rule on whether the plan was fair and equitable, this issue would have been in contention. However, shareholders and creditors approved the plan and it is not appropriate for the court to venture into the thicket of the new value exception to the absolute priority rule without

---

[7] The IRS continues to refine a bankrupt corporation's ability to use NOL's by proposing new regulations affecting a bankrupt corporation's use of NOL's to reduce income which will appear at 26 C.F.R. Part 1.

cause. *Travelers Ins. Co. v. Bryson Properties XVIII, (In re Bryson Properties XVIII)*, 1992 WL 77524 (4th Cir. N.C., April 20, 1992).

There is no evidence that tax avoidance is the primary motivation for the plan. There is no indication in the schedules or disclosure statement that Ambra has a net operating loss that will be improperly used in the future. Furthermore, any concern regarding issuance or sale of securities is inapplicable in this case where only one shareholder remains.

This case has been before the court since its filing on December 22, 1989. No evidence has been discovered during that time and presented to the court that would imply that any of the perceived abuses of trafficking in corporate shells is present in this case. Mere intent to operate in the future, without more tangible proof of ability to operate, is a slim basis for finding compliance with section 1141(d)(3)(B). However, in the absence of any evidence showing the presence of abuse and in light of the overwhelming support of creditors for the plan, the court will find that the plan meets the provisions of this section, as well as section 1129. Therefore, it is hereby

ORDERED, that the objection to confirmation is denied, and it is further,

ORDERED, that all requirements of section 1129 are met, and it is further

ORDERED, that Ambra prepare an order of confirmation consistent herewith.

DATED this 29 day of May, 1992.

JUDITH A. BOULDEN
United States Bankruptcy Judge