UNPUBLISHED OPINION

#393

IN THE UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF UTAH

CENTRAL DIVISION

In re	)	
	)	
CDX CORPORATION,	)	Bankruptcy Case No. 92C-22665
	)	
Debtor.	)	Chapter 11
	)	
	)	
ROBERT E. WILCOX, LIQUIDATOR OF SOUTHERN AMERICAN INSURANCE COMPANY,	)	Adversary Proceeding No. 94PC-2112 (Consolidated)
	)	
Plaintiff,	)	
	)	
vs.	)	MEMORANDUM OPINION AND ORDER REGARDING THE UNITED STATES DISTRICT COURT'S ORDER OF REMAND
CDX CORPORATION, VALLEY TITLE COMPANY, a limited partnership and Trustee under a Trust Deed, THOMAS W. SEILER, ESQ., Trustee under Trust Deed with Assignment of Rents, ASPEN INVESTMENT LTD., a limited partnership, COREY COMBE d/b/a COMBE'S TREE FARMS, CRESTLINERS, INC., and VALLEY ASPHALT, INC.,	)	
	)	
Defendants.	)	
	)	

CDX CORPORATION,	)
	)
Plaintiff,	)
	)
vs.	)
	)
C&A CONSTRUCTION; COREY COMBE dba COMBE'S TREE FARMS; WASATCH ORNAMENTAL IRON & WELDING; GENEVA ROCK PRODUCTS; CONCRETE PRODUCTS CO.; PROBST MASONRY, INC.; VALLEY ASPHALT, INC.; AND CRESTLINERS, INC.,	)
	)
Defendants.	)

This matter came before the court on August 13, 1996, on remand from an ORDER of the United States District Court dated June 12, 1996. John D. Morris appeared in behalf of the debtor CDX Corporation ("CDX"); Brent D. Wride and Robert J. Dale appeared in behalf of Robert E. Wilcox, Liquidator of Southern American Insurance Company (the "Liquidator"); and Harold L. Reiser and Adam S. Affleck appeared in behalf of Valley Asphalt, Inc. ("Valley Asphalt").

JURISDICTION

This court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334. This is a "core" proceeding within the meaning of 28 U.S.C. § 157(b)(2)(A)(B)(K) and (O).

PROCEDURAL SETTING

On April 12, 1995, the Liquidator moved the court for summary judgment on the fifth claim for relief of the amended complaint in the adversary proceeding. In response, Valley Asphalt filed a cross motion for summary judgment. This court granted summary judgment in favor of Valley Asphalt determining its mechanic's lien to be valid and enforceable. The Liquidator appealed the decision to the United States District Court, which on June 12, 1996, issued its ORDER remanding the matter to this court. The ORDER on remand instructs the court to first decide

> what this Court finds to be a threshold inquiry and issue, and that is to determine who is the owner or real party in interest of the properties liened. After this inquiry is satisfied pursuant to statute and the law as above noted, then the Court can proceed to address whether other technicalities and arbitrary rules can be dispensed with as having no demonstrative value to the facts at hand.

The District Court goes on to state: "The legal and factual issue of alter ego or piercing of the corporate veil, while not properly before this court, may very well determine whether in fact there is more than one owner of the properties involved."

Because Valley Asphalt raised the issue of alter ego and equitable subordination in its motion for summary judgment, those issues properly remain before the court and will be considered in this ruling.

STATEMENT OF ISSUES

1. Who is the owner or the real party in interest of the liened properties according to statute and the law?

2. Should CDX, Southern American Insurance Company ("SAIC"), BCD Corporation ("BCD") and Seven Peaks Funicular, Inc., ("Funicular") be treated as alter egos of one another for the purpose of determining the validity of Valley Asphalt's lien?

(a) Does confirmation of the CDX and BCD plans serve as res judicata to defeat any argument that CDX and BCD are alter egos of one another?

(b) Does the jurisdictional limitation found in 11 U.S.C § 109(d) preclude this court from finding that SAIC, a stock insurance company, is an alter ego of CDX and BCD?

3. Does Victor Borcherds' conduct and dealings with CDX and SAIC support equitable subordination of the SAIC secured claim, and does the conduct of the Liquidator support subordination of the SAIC secured claim?

(a) Does confirmation of the CDX plan serve as res judicata to defeat any argument regarding equitable subordination of the SAIC secured claim?

FINDINGS OF FACT

The Liquidator and Valley Asphalt have submitted Statements of Material Facts with their memorandum pursuant to Federal Rule of Bankruptcy Procedure 7056 and Bankr. D. Ut. 522(b)(4). Having reviewed the Statements of Material Facts in support of and in opposition to the Summary Judgment Motions the court finds the following uncontroverted facts.

CDX Corporation

1. CDX is a Utah corporation which is the reorganized debtor in the above-captioned Chapter 11 case.

2. CDX, at all material times, was the owner of Seven Peaks Golf Course, Inc. (the "Golf Course") located in Provo, Utah.

3. CDX was formerly known as Seven Peaks Golf Course, Inc., having its name changed on April 8, 1992, from Seven Peaks Golf Course, Inc. to CDX.

4. CDX commenced its Chapter 11 case by filing a petition seeking relief under the Bankruptcy Code on April 16, 1992, in this court.

5. CDX is presently a reorganized debtor under a March 31, 1994, order of this court having confirmed its Amended Plan of Reorganization dated January 7, 1994.

6. Between May 15, 1990, and July 21, 1992, Victor Borcherds ("Borcherds") was president of CDX.

7. The CDX Property is located at approximately 300 North 1450 East, Provo, Utah, and includes a golf course, golf cart paths, a 500-space parking lot built to service both the golf course and the proposed funicular at the Seven Peaks Resort, and other miscellaneous improvements.

8. The CDX Property was sold free and clear of liens with liens to attach to proceeds of sale pursuant to a March 31, 1994, order of this court.

9. CDX received approximately $2,125,000 from the sale of the CDX Property.

10. At all times relevant, the CDX Property was part of the resort and recreation center known as the Seven Peaks Resort.

BCD Corporation

11. BCD was formerly known as the Provo Aquatic Water Park, Inc. Its name was changed from Provo Aquatic Water Park, Inc. to BCD on April 8, 1992.

12. BCD commenced its Chapter 11 proceeding by filing a petition seeking relief under the Bankruptcy Code on April 16, 1992, in this court.

13. BCD is presently a reorganized debtor under a March 31, 1994, order of this court confirming BCD's Fourth Amended Plan of Reorganization.

14. Between March 28, 1990, and July 21, 1992, Borcherds was president of BCD.

15. BCD formerly owned property located at approximately 300 North 1450 East, Provo, Utah. The property consisted of a water park, an ice rink, a parking lot, and other miscellaneous improvements (the "BCD Property").

16. During the administration of BCD's estate, the BCD Property was sold free and clear of liens with liens to attach to proceeds of sale pursuant to an order of this court.

17. At all times pertinent, the BCD Property was part of the resort and recreation center known as the Seven Peaks Resort.

Seven Peaks Funicular, Inc.

18. Funicular is a former Utah corporation.

19. Between May 15, 1990, and July 21, 1992, Borcherds was president of Funicular.

20. Funicular formerly owned property located at approximately 300 North 1450 East, Provo, Utah (the "Funicular Property"). The property was improved with a golf cart path and excavation for a proposed funicular service.

21. At all times relevant, the Funicular Property was part of the resort and recreation center known as Seven Peaks Resort.

Southern American Insurance Company

22. SAIC was a stock insurance company domiciled in the state of Utah. Pursuant to the order of the Third District Court, Salt Lake County, State of Utah, SAIC is being liquidated by the Utah Insurance Commissioner.

23. The liquidation is being supervised by the Third District Court in the case of In re Southern American Insurance Company, Civil No. 920901617.

24. Between January 1991 and March 26, 1992, Borcherds was president of SAIC.

25. SAIC formerly owned property located at approximately 300 North 1450 East, Provo, Utah (the "SAIC Property"). The SAIC Property contained improvements including a large barn/chalet-type office building ("Office Building"), a 200-space parking lot built to service the proposed funicular at the Seven Peaks Resort, and other miscellaneous improvements.

26. The SAIC Property, including the Office Building, was operated as a part of, and used to service, the resort and recreation center known as the Seven Peaks Resort.

The Valley Asphalt Claim

27. Valley Asphalt provided materials and services for certain improvements to the CDX Property, the BCD Property, the Funicular Property and to the SAIC Property (collectively the "Seven Peaks Resort Properties") including (a) a 700-space, 300,000 square-foot parking lot and incidental access roads on the CDX Property, the SAIC Property and the BCD Property which were built to service the proposed funicular (the "Parking Lot"); (b) a 580-foot long, 12-foot wide golf cart path located north of the Parking Lot; (c) repair work on golf cart paths; and (d) grading work on the water park ice rink.

28. The above-referenced materials and services were supplied, and improvements made by Valley Asphalt, between July 31, 1991, and November 11, 1991, as part of on-going improvements being made by Valley Asphalt and others to the Seven Peaks Resort Properties.

29. Prior to the commencement of the CDX and BCD bankruptcy cases, Valley Asphalt billed the above-referenced materials and services to "Seven Peaks Resort c/o Dale Berg." At the request of Dale Berg, Valley Asphalt sent additional invoices dividing

amounts due between "Seven Peaks Resort" (two thirds) and "Southern American Insurance" (one third).

30. The four separate pieces of property worked on by Valley Asphalt were owned separately by CDX, BCD, Funicular and SAIC (the "Seven Peaks Resort Entities").

31. Between 1990 and 1992, Valley Asphalt negotiated, performed, and was paid under several express and implied contracts for improvements to the Seven Peaks Resort Properties. These contracts included contracts between Valley Asphalt and the entities listed in Valley Asphalt's Notice of Lien. Pursuant to the separate contracts, Valley Asphalt sent separate invoices to the various entities.

32. Valley Asphalt's contract negotiations for improvements to the Seven Peaks Resort Properties took place in the same offices with the same persons including Borcherds and other agents.

33. When requesting proposals or ordering materials and services, Borcherds and other agents of the Seven Peaks Resort Entities did not distinguish whether the materials and services were to be provided by Valley Asphalt on behalf of or on property owned by CDX, BCD, Funicular, or SAIC. Rather, the projects and properties were referred to collectively by Borcherds and other Seven Peaks Resorts Entities agents as the "Seven Peaks Resort."

34. At no time did Borcherds or any other person supply Valley Asphalt with site plans, property maps, or other materials showing separate property ownership by each of the Seven Peaks Resort Entities. Rather site plans that were supplied to Valley Asphalt referencing "Seven Peaks Resort" as the project name or property owner of the entire Seven Peaks Resort Properties.

35. Express contracts entered into with respect to construction of the Parking Lot included a written proposal to Seven Peaks Resort for 300,000 square-feet of 3" asphalt at $.48 per square foot which was accepted by Borcherds (the "Asphalt Contract").

36. Borcherds subsequently provided Valley Asphalt with two written contracts dated September 26, 1991, which divided and re-documented the Asphalt Contract between Funicular and SAIC (the "September 26 Contracts"). The September 26 Contracts identified Funicular as the contracting party and owner of the "North East Parking Lot" and SAIC as the contracting party and owner of the "South East Parking Lot." The September 26 Contracts were signed by Borcherds.

37. Although Funicular was purported to be the owner of the "North East Parking Lot" in the September 26 Contracts, Funicular made no payments for materials or services for the Parking Lot. Instead, payments were made exclusively by CDX and SAIC.

38. Purchase orders for materials for the Parking Lot were received from "Seven Peaks Resort" and SAIC, but not from Funicular.

39. Each of the Seven Peaks Resort Properties is physically connected with asphalt (on parking lots, roads and paths) that Valley Asphalt supplied.

40. On January 22, 1992, in connection with a records search for preparation of a mechanic's lien, Valley Asphalt became aware that the Seven Peaks Resort Properties were separately owned of record by the Seven Peaks Resort Entities.

41. On January 28, 1992, prior to the commencement of CDX's and BCD's bankruptcy cases, Valley Asphalt filed a single notice of lien (the "Notice of Lien") at the Utah County Recorder's Office for all amounts owed by the Seven Peaks Resort Entities for the materials and services described above. The Notice of Lien identifies CDX, BCD, Funicular and SAIC as the property owners.

42. On January 28, 1992, Valley Asphalt sent copies of the Notice of Lien by certified mail to "Seven Peaks" and "Provo Aquatic Water Park" using the addresses appearing on the last completed real property assessment roll of Utah County for the parcels described in the Notice of Lien.

43. Valley Asphalt knew when it filed its Notice of Lien that the property on which it had done work was owned by more than one entity.

44. Valley Asphalt could not readily survey and apportion the location of its improvements prior to filing its Notice of Lien and, therefore, filed the single Notice of Lien against all of the Seven Peaks Resort Properties.

45. Before filing its Notice of Lien, Valley Asphalt contacted Borcherds to determine whether he could clarify the location of improvements with respect to property ownership.

46. Borcherds did not and could not clarify property ownership nor identify the location of improvements on the Seven Peaks Resort Properties. When informed of Valley Asphalt's intent to file a single Notice of Lien filed against the Seven Peaks Resort Properties, Borcherds responded that it did not matter if a single Notice of Lien was filed and stated that "I own them all."

47. Valley Asphalt filed a proof of claim against CDX asserting a secured claim in the total amount of $104,237.09 for labor and supplies provided in connection with the Seven Peaks Resort Properties (the "Valley Asphalt Claim").

Operations of the Seven Peaks Resort Entities

48. CDX, BCD and SAIC each used the Office Building as its registered address, as its office, and as its mailing address.

49. CDX, BCD and SAIC had common officers and directors.

50. CDX, BCD and SAIC each used the Office Building as the location for its accounting department and as a location for transacting business.

51. From September 1988 through April or May 1991, Terry Atkinson, a full-time employee of SAIC, supervised all of the accounting for BCD and CDX. This accounting was done by Terry Atkinson and other SAIC employees during their normal working hours without compensation from BCD or CDX.

52. CDX used the Office Building as a work location for outside professionals, including the engineering firm of Sowby & Berg Consultants, who provided engineering services to CDX.

53. CDX and BCD used office space, equipment, and personnel of SAIC, including the Office Building, telephones, receptionists, copiers, desks, office support, fax machines, supplies, equipment and SAIC staff, without compensating SAIC for the same.

54. CDX and BCD had a common incoming telephone line located at the Office Building (in fact, the line was hooked up to the telephone switchboard located at the SAIC's receptionist desk) and the incoming calls to the BCD and CDX were answered by SAIC's receptionist without any compensation from BCD or CDX.

55. When employees were hired by CDX or BCD, they were given an I.D. card from Seven Peaks Resort/Southern American Insurance Company.

56. All SAIC employees received a free season pass to the water park located on the BCD Property. SAIC employee family members could purchase season passes at a discount rate.

57. Company picnics were held for SAIC, BCD and CDX employees in common and free T-shirts were issued to all employees. The T-shirts had "Seven Peaks Employee" printed on them.

58. An annual combined Christmas party was held for all employees of SAIC, BCD and CDX. As well, a children's Christmas party and Halloween party were held in common for the employees of SAIC, BCD and CDX.

59. Management of BCD and CDX were enrolled in the long-term disability policy for SAIC employees, and payment of the premiums on the policy was made by SAIC without reimbursement from BCD or CDX.

60. A single personnel director served as the personnel director for CDX, BCD and SAIC.

61. SAIC provided significant financial benefits to or for the benefit of CDX and BCD, frequently without any consideration whatsoever to SAIC.

62. During 1990 and 1991, a series of transfers between CDX, BCD and SAIC occurred. These transfers were incident to shareholder advances made by Borcherds and Suzanne Borcherds totalling over three and one-half million dollars.

SAIC Lien Claim & Objection

63. On August 12, 1992, the Liquidator filed a proof of secured claim on behalf of SAIC in CDX's bankruptcy case in the amount of $1,309,107.07 (the "SAIC Lien Claim") for amounts owed on a trust deed note dated December 20, 1991, which was secured by a trust deed recorded on January 10, 1992.

64. On August 18, 1992, CDX commenced an adversary proceeding in its bankruptcy case to determine the nature, extent, and validity of lien as set forth in the SAIC Lien Claim. CDX v. Yancey, 92PC-2372 (the "SAIC Claim Objection"). In the SAIC Claim Objection, CDX specifically disputed the amount set forth in the SAIC Lien Claim and requested an accounting on the same.

65. CDX obtained responses to discovery from the Liquidator in February 1993 in connection with prosecution of the SAIC Claim Objection in which the Liquidator itemized the SAIC Lien Claim as follows: legal fees paid by SAIC of $400; payment to the FDIC for the deposit of the Golf Course land by SAIC of $51,300; a wire transfer to the FDIC from SAIC for the balance due at closing on the Golf Course land of $975,258.07; payment to Ray's Golf Carts by SAIC of $150; and earthmoving equipment received in kind - $110,971.77; for a total of $1,138,079.84.

Alter Ego Claims

66. The Liquidator commenced and prosecuted adversary proceedings in this court alleging that SAIC, CDX and BCD were alter egos. Yancy v. CDX Corporation, Adv. Pro. No. 92PC-2432 and Yancey v. BCD Corporation, 92PC-2431 (the "Bankruptcy Alter Ego Claims"). The Liquidator also commenced an action in SAIC's state-court liquidation proceedings prosecuting similar alter ego claims and breach of fiduciary duty claims against the controlling persons of SAIC, CDX and BCD. Southern American Ins. Co. v. Borcherds, Civil No. 920400257CN (Utah 4th Dist. Ct.) (the "State Alter Ego Claims") (referred to collectively with the Bankruptcy Alter Ego Claims as the "Alter Ego Claims").

67. In early 1993, CDX filed a motion for summary judgment in proceedings on the Bankruptcy Alter Ego Claims seeking a determination that CDX, BCD and SAIC were separate and distinct entities. The Liquidator vigorously opposed the motion arguing that CDX, BCD and SAIC were alter egos of one another. The court denied CDX's motion.

Liquidator's Control Over CDX and SAIC

68. In September 1993, the Liquidator gained complete control of CDX. The Liquidator had controlled 2% of CDX's stock since April 17, 1992, and on September 10, 1993, purchased the remaining 98% of CDX's stock.

69. After the Liquidator obtained control of CDX, CDX ceased prosecution of the SAIC Claim Objection.

70. On February 25, 1994, in answer to a February 14, 1994, order to show cause regarding lack of prosecution, CDX, under the Liquidator's control, filed a response that CDX's proposed plan provided for dismissal of the SAIC Claim Objection. After confirmation, CDX and the Liquidator filed a Joint Stipulation and Notice of Dismissal dated May 9, 1994, dismissing the SAIC Claim Objection without prejudice.

71. On September 29, 1993, the Liquidator stipulated to voluntary dismissal of the two Bankruptcy Alter Ego Claims. The Liquidator, however, did not dismiss proceedings on the State Alter Ego Claims which remain pending.

72. The disclosure statement filed with CDX's plan (the "Disclosure Statement") included mention that the SAIC Lien Complaint was pending but was intended to be dismissed in light of the Liquidator's purchase of CDX's stock. No disclosure was provided regarding the merits of the SAIC Claim Objection or the discovery obtained that the SAIC Lien Claim was based on a trust deed filed in January 1992 to secure debts incurred between July 1989 and August 1991.

73. The liquidation analysis in the Disclosure Statement assumed the validity of all classified secured claims, including the SAIC Lien Claim, and projected no distribution

to unsecured creditors. Total assets were estimated at $2,405,000. Total claims against the estate were disclosed as follows:

Total Secured Claims	$3,139,565.00
Total Administrative Claims	$61,267.34
Total Unsecured Claims	$283,085.17

74. CDX's plan makes no reference to issues of alter ego among the Seven Peaks Resort Entities. Although the Liquidator's dismissal of the Bankruptcy Alter Ego Claims was noted in the Disclosure Statement, no alter ego or substantive consolidation issues were litigated or considered at the confirmation hearing.

75. CDX's plan reserves the right to object to claims post-confirmation and preserves all avoiding powers of CDX as a debtor-in-possession to the extent not barred by 11 U.S.C. § 546(a).

76. CDX's plan allows the SAIC Lien Claim in the amount of $1,309,107.07, to the extent secured by a lien against estate property and to the extent determined to be an allowed secured claim by the court.

77. CDX's plan provides that Classes 2A through 2H are impaired. The Class 2F claim of John Deere Credit and the Class 2G claim of E.C.C., if determined to have a valid first lien on their collateral, will be paid by an abandonment of their collateral after the sale of the Golf Course, with any deficiency to be treated as general unsecured claims.

All other claims in Classes 2A through 2H, in such amounts as may be allowed by the court, shall be paid from the proceeds of the sale of their collateral, with any deficiency to be treated as a general unsecured claim.

78. CDX's plan provides that Class 2E - Valley Asphalt, Inc. will be allowed in the amount of $109,305.19, to the extent secured by a mechanic's lien against the Golf Course, and to the extent determined to be an allowed secured claim by the court.

79. CDX's plan expressly preserves for the benefit of the estate all powers, claims and interests possessed by the debtor pursuant to § 510 of the Bankruptcy Code.

80. On May 23, 1994, approximately two months after plan confirmation, CDX commenced this adversary proceeding to determine the validity and extent of liens on the CDX Property (the "CDX Complaint"). Liens of all secured claimants as set forth in the Disclosure Statement were challenged except the SAIC Lien Claim.

CONCLUSIONS OF LAW

Summary judgment is appropriate only when there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. This means that after the opportunity for discovery, if the moving party demonstrates that there is no genuine issue of material fact as to the existence of any element essential to the non-moving party's case, then summary judgment is appropriate. Once this initial burden is met, it becomes

the burden of the non-moving party to come forward with specific facts, supported by the evidence in the record, upon which a reasonable trier of fact could rule for the non-moving party. Tiberi v. Cigna Corporation, 89 F.3rd 1423 (10th Cir. 1996). This court must examine the factual record and all reasonable inferences that can be drawn therefrom in the light most favorable to the non-moving party. Wolf v. Prudential Ins. Co. of America, 50 F.3rd 793 (10th Cir. 1995). Summary judgment is appropriate if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. Sellers v. Allstate Insurance Company, 82 F.3rd 350 (10th Cir. 1996).

ALTER EGO

In the ORDER OF REMAND, the court was instructed to find who was the owner of the property encumbered by Valley Asphalt's Lien. The court has found that the owners of record of the property were four entities, CDX, BCD, Funicular and SAIC, the "Seven Peaks Resort Entities". Valley Asphalt argues that for purposes of determining the validity of its lien, the court should find that the Seven Peaks Resort Entities are alter egos of one another and should be considered as a single owner of the Property. To support a finding of alter ego as alleged by Valley Asphalt, the court must satisfy a two-part test:

(1) there must be such unity of interest and ownership that the separate personalities of the corporation and the individual no longer exist, viz., the corporation is, in fact, the alter ego of one or a few individuals; and (2) the observance of the corporate form would sanction a fraud, promote injustice, or an inequitable result would follow. Norman v. Murray First Thrift & Loan Co., 596 P.3d 1028, 1030 (Utah 1979). The Court of Appeals for the Tenth Circuit has adopted a very similar two-part test:

> (i) was there such unity of interest and lack of respect given to the separate identity of the corporation by its shareholders that the personalities and assets of the corporation and the individual are indistinct, and (ii) would adherence to the corporate fiction sanction a fraud, promote injustice, or lead to an evasion of legal obligations.

National Labor Relations Board v. Greater Kansas City Roofing, 2 F.3rd 1047, (10th Cir. 1993) at 1052.

Valley Asphalt asserts that prepetition conduct by Borcherds supports the court's treating the Seven Peaks Resort Entities as alter egos of one another for purposes of Valley Asphalt's lien, and that the postpetition conduct of the Liquidator estops the Liquidator from claiming that Valley Asphalt's alter ego argument is invalid.

Regarding the prepetition conduct of Borcherds, the Liquidator argues that "[i]t would be inequitable for the court to impute the alleged inequitable conduct of Mr. Borcherds and SAIC, the predecessors in interest to the disputed claim, to the Liquidator who cannot adequately or properly defend himself against such accusations."

(Liquidator Reply Memorandum at p. 27). However, it is well established that the successor in interest stands in the shoes of the debtor and can take no greater rights than the debtor himself had. The successor takes subject to all valid claims, liens, and equities which might have been asserted against the debtor and is subject to the same defenses as could have been asserted by the defendant had the action been instituted by the debtor. Sender v. Simon, 84 F.3rd 1299 (10th Cir. 1996).

Prepetition

The uncontroverted facts show that there was a strong unity of interest and ownership between the Seven Peaks Resort Entities to the point that the separate personalities of the corporations ceased to exist (intercorporate transfers without consideration, all entities controlled by one individual, common directors, common mailing and registered addresses, use of common employees, use of common equipment and facilities, representations by Borcherds that work was for "Seven Peaks Resort"). In this situation, observance of the separate corporate forms of the Seven Peaks Resort Entities would serve to sanction the fraud perpetuated by Borcherds and would promote an inequitable and unjust result under the circumstances.

Valley Asphalt was led to believe that Seven Peaks Resort was a single entity. When Valley Asphalt discovered otherwise, Borcherds could not give the information to Valley Asphalt necessary to correctly file the Notice of Lien such as clarify ownership or

identify the location of the improvements of the properties, and Borcherds responded that it did not matter if a single Notice of Lien were filed stating that "I own them all." "[I]f a principal shareholder or owner conducts his private and corporate business on an interchangeable or joint basis as if they were one, he is without standing to complain when an injured party does the same." Coleman v. Coleman, 743 P.2d 782, 786 (Utah Ct.App. 1987).

Postpetition

Upon obtaining complete control of CDX, the Liquidator began treating CDX and SAIC as a single entity. The Liquidator's decision to challenge the validity of every secured creditor's lien discussed in the Disclosure Statement except the lien in favor of SAIC is significant to this court. The Liquidator, in his capacity as the person in control of CDX agreed to the dismissal of the Bankruptcy Alter Ego Claims after having initiated the adversary proceedings himself as the Liquidator of SAIC[1]. Perhaps the best illustration of the degree to which the Liquidator suffers from an identity crisis concerning his duty

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[1]The court notes with some interest that prior to gaining complete control of CDX, the Liquidator himself brought an adversary proceeding against CDX alleging alter ego claims. Yancy v. CDX Corporation, Adv. Pro. No. 92PC-2432. Shortly after gaining complete control of CDX, the Liquidator stipulated to the voluntary dismissal of the alter ego complaint. Now, despite having asserted that CDX is an alter ego, the Liquidator aggressively defends against the same alter ego argument formerly asserted by the Liquidator. "A litigator is required to be consistent in his conduct. He may not maintain a position regarding a transaction wholly inconsistent with his previous acts in connection with the same transaction." Paul v. Monts, 906 F.2d 1468, 1473 (10th Cir. 1990).

to treat each corporate entity as a separate and distinct unit is found in the Liquidator's own statement made in response to Valley Asphalt's allegations regarding the Liquidator's inequitable conduct. The Liquidator states: "The Liquidator holds approximately 95% of all unsecured debt against the estate and therefore a preference action against 'himself' would have made virtually no difference to unsecured creditors . . . ." (Liquidator Reply Memorandum at p. 27-28). The Liquidator's statement not only evidences the state of mind suffered by the Liquidator that corporations under his control are nothing more than extensions of himself, but it also reveals the Liquidator's willingness to sacrifice the economic interests of other creditors (the remaining 5%) in favor of the economic interests of a corporation controlled by the Liquidator. This type of inequitable conduct justifies the court's estopping the Liquidator from denying that the Seven Peaks Resort Entities are alter egos of one another.

Had the Liquidator persisted in the Bankruptcy Alter Ego Claims rather than causing the matters to be dismissed, the court might have found the corporations to be alter egos of one another. Had the Liquidator successfully challenged the validity of the SAIC Lien Claim, Valley Asphalt might possibly be paid in full as an unsecured creditor and have no need to advance an alter ego theory. In sum, it appears that the Liquidator's postpetition conduct displays a unity of interest and sufficient inequitable conduct to estop

the Liquidator from denying that the Seven Peaks Resort Entities are alter egos of one another for the limited purpose of considering the validity of the Valley Asphalt Lien.

RES JUDICATA - ALTER EGO

The Liquidator argues that any alter ego theory concerning the Seven Peaks Resort Entities cannot stand because confirmation of CDX and BCD's separate plans are res judicata as to the separate identity of the corporations. The doctrine of res judicata precludes the parties or their privies from relitigating issues that were or could have been raised in that action. It is intended to relieve parties of burdensome multiple lawsuits, prevent inconsistent decisions, and encourage reliance on adjudication. Allen v. McCurry, 449 U.S. 90, 101 S. Ct. 411 (1980). To prevail on a defense of res judicata the defendant must establish: (1) a final judgment on the merits in the prior action, (2) the claims raised in the subsequent action were identical to those decided in the prior action, and (3) the prior action involved the same parties or their privies. Hoxworth v. Blinder, 74 F.3d 205 (10th Cir. 1996). The Liquidator's res judicata argument fails because the orders confirming CDX and BCD's plans were not judgments on the merits concerning claims identical to the alter ego claims asserted by Valley Asphalt. Without the issue being raised in the pleadings or at the confirmation hearings on the respective plans, the order confirming the CDX or the BCD plans of reorganization cannot be characterized as a final

judgment on the merits of any alter ego claim. Moreover, as discussed below, alter ego is a narrow concept that is very different from substantive consolidation[2]. This court's orders finding the CDX and BCD plans confirmable speak for themselves. Nowhere in the orders is there language dealing with the issues raised in Valley Asphalt's alter ego claim. Because the claims raised in this action were not raised or decided by the court in the confirmation process, Valley Asphalt's alter ego claim is not barred by res judicata.

11 U.S.C. § 109

The Liquidator argues that the court is precluded from finding the Seven Peaks Resort Entities as alter egos of one another because to do so will strip the court of jurisdiction pursuant to 11 U.S.C. § 109(d) and render any order void. The Liquidator's argument is based upon the assumption that the only alter ego ruling the court can make will consolidate the corporations into a single entity, and that an alter ego theory cannot be used for the limited purpose of complying with statutory lien requirements. However, the Tenth Circuit has used the alter ego theory to find that a tax lien filed against a

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[2]Perhaps the issue of substantive consolidation is rendered res judicata by the confirmation of two separate plans, but not the issue of alter ego for the limited purpose of lien determination. Certainly the issue of substantive consolidation would be rendered moot by the confirmation of two separate plans.

corporation determined to be the alter ego of the taxpayer was valid and enforceable. United States v. Gosnell, 961 F.2d 1518 (10th Cir. 1992).

The Liquidator in essence argues that a finding that the corporations are alter egos substantively consolidates the corporations into one entity. A finding of substantive consolidation requires much more. Substantive consolidation combines the assets of two or more entities, eliminates intercompany claims, and treats the claims of creditors as if they were incurred by a single entity. FDIC v. Colonial Realty Co., 966 F.2d 57, 58-59 (2nd Cir. 1992). In Fish v. East, 114 F.2d 177 (1940) the United States Court of Appeals for the Tenth Circuit described eight factors to be considered in substantive consolidation. The impact of substantive consolidation on creditors demands a rigorous examination of all factors and requires specific findings determining what creditors will benefit and what creditors will be harmed by the consolidation. Matter of Gulfco Inv. Corp., 593 F.2d 921 (10th Cir. 1979).

Alter ego and substantive consolidation are different concepts. F.D.I.C. v. Colonial Realty Co., 966 F.2d 57 (2nd Cir. 1992). The finding that corporations are alter egos does not consolidate the Seven Peaks Resort Entities into one insurance company.

EQUITABLE SUBORDINATION

Valley Asphalt argues that the Liquidator's lien rights derived from the SAIC Lien Claim should be subordinated pursuant to 11 U.S.C. § 510 to the claims of all creditors based upon SAIC's prepetition and postpetition inequitable conduct.

> 11 U.S.C. § 510(c) provides that the court may
>
> > (1) under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim or all or part of an allowed interest to all or part of another allowed interest; or
> >
> > (2) order that any lien securing such a subordinated claim be transferred to the estate.

The party seeking equitable subordination under § 510 must demonstrate that (1) the claimant has engaged in inequitable conduct; (2) The conduct has injured creditors or given unfair advantage to the claimant; and (3) subordination of the claim is not inconsistent with the Bankruptcy Code. In re Castletons, Inc., 990 F.2d 551, 559 (10th Cir. 1993).

Prepetition

Prepetition, CDX and SAIC were controlled by Borcherds. They shared common officers, directors and controlling shareholders. Loans, advances and transfers were made between CDX and SAIC that were less than arms length transactions and not commercially reasonable. SAIC and CDX shared office space and office resources including personnel,

telephone lines and office equipment. SAIC and CDX shared the "Seven Peaks Resort" logo, used identical mailing addresses, and a single personnel director for the employees of both corporations. As a result of the common sharing of office space, equipment, personnel and resources, SAIC was in an advantageous position to gain preferential treatment from CDX that other creditors did not enjoy. Enjoying such an advantage is grounds for subordination. Matter of Fabricators, Inc., 926 F.2d 1458 (5th Cir. 1991).

The SAIC Lien Claim is based on a trust deed note and trust deed recorded on January 10, 1992, just 96 days before CDX's petition date. The trust deed note and trust deed were taken in satisfaction of unsecured obligations originating in 1990 and 1991. Borcherds used his control over the debtor and the affiliated corporations to his benefit and to the detriment of creditors. Such a use of control is grounds for subordination. Pepper v. Litton, 308 U.S. 295 (1939), 60 S.Ct. 238. Borcherds exerted his control over the debtor to transform an unsecured debt owed by CDX to SAIC to a secured debt owed by CDX to SAIC. Use of corporate control to transform a unsecured debt into a secured debt is grounds for subordination. In re Otis & Edwards, P.C., 115 B.R. 900 (Bankr. E.D. Mich. 1990).

Postpetition

In August 1992, the Liquidator filed the SAIC Lien Claim. In response, CDX (then not controlled by the Liquidator) filed the SAIC Claim Objection challenging the validity

of SAIC's lien. Discovery obtained in the SAIC Claim Objection adversary proceeding indicated that SAIC's trust deed filed in January 1992 secured debts incurred between July 1989 and August 1991 and as such may be avoidable as an insider preference. After taking complete control of CDX, the Liquidator, rather than continuing to litigate the SAIC Claim Objection, chose a course more favorable to SAIC. CDX's Disclosure Statement failed to discuss the merits of the SAIC Claim Objection or the discovery obtained revealing that SAIC's secured claim may be supported by a trust deed subject to avoidance as a preference. Upon confirming CDX's plan of reorganization, the Liquidator proceeded to challenge the validity of every secured claim described in the Disclosure Statement with the exception of the SAIC Lien Claim. The only explanation for the Liquidator's failure to follow through with the challenge to the validity of SAIC's Lien Claim is found in the Liquidator's Reply Memorandum at pages 27-28 where he states: "The Liquidator holds approximately 95% of all unsecured debt against the estate and therefore a preference action against 'himself' would have made virtually no difference to unsecured creditors and would have not been in the best interest of the estate." Thus, it is clear that the Liquidator considers transactions and dealings between SAIC and CDX as transactions between "himself," and when making decisions for CDX, he places the interests of SAIC before the interests of the remaining CDX creditors.

In essence, the Liquidator has allowed his decision making capacity to be controlled by his own interests in SAIC.

> The purpose of equitable subordination is to distinguish between the unilateral remedies that a creditor may properly enforce pursuant to its agreements with the debtor and other inequitable conduct such as fraud, misrepresentation, or the exercise of such total control over the debtor as to have essentially replaced its decision-making capacity with that of the lender.

In re Castletons, Inc., 990 F.2d 551, 559 (10th Cir. 1993) (citing In re Clark Pipe & Supply Co., 893 F.2d 693 (5th Cir. 1990)). The Liquidator's conduct has been inequitable, it has injured creditors and given an unfair advantage to SAIC. Under these circumstances subordination of the SAIC claim in not inconsistent with the Bankruptcy Code. Castletons, 990 F.2d at 559.

RES JUDICATA - EQUITABLE SUBORDINATION

The Liquidator argues that because CDX's confirmed plan resolved the issue of status and priority of claims of the estate, Valley Asphalt's argument that SAIC's Lien Claim should be equitably subordinated is barred by the principle of res judicata. However, CDX's plan specifically reserves, for determination by the court, the extent of the secured claims of SAIC, Valley Asphalt and others. Because the extent of a secured claim can be affected by the priority of the claimant's lien, subordination issues fall within the scope of determinations to be made by the court under the plan. The plan's

reservation, for the benefit of the estate, of all powers, claims and interests possessed by the debtor pursuant to § 510 of the Bankruptcy Code puts all creditors and parties in interest, including the Liquidator, on notice that the issue of equitable subordination has not been precluded by the confirmation of the plan. The plan contains no language to exclude or prevent Valley Asphalt or any other party from raising the issue of equitable subordination. Accordingly, the court finds that the issue of equitable subordination regarding the SAIC Lien Claim is not barred by res judicata.

CONCLUSION

Because the Seven Peaks Resort Entities have been treated as a single entity by both Borcherds and the Liquidator, they will be viewed as a single entity for purposes of determining the validity of Valley Asphalt's Lien Claim, and the Liquidator will be estopped from denying the same. Nothing in the CDX confirmed plan is res judicata to this determination. The treatment of the Seven Peaks Resort Entities as alter egos for purposes of determining the validity of Valley Asphalt's Lien Claim does not offend the jurisdictional limitations found at 11 U.S.C. § 109(d).

Borcherds' conduct and the Liquidator's conduct both support the finding of this court that the SAIC Lien Claim should be equitably subordinated. Confirmation of the

CDX plan did not defeat the equitable subordination argument because the issue of equitable subordination was not raised in the confirmation process.

WHEREFORE, based upon the following, it is hereby

ORDERED that Valley Asphalt's motion for summary judgment is granted, and it is further

ORDERED that the Liquidator's motion for summary judgment is denied, and it is further

ORDERED that for purposes of determining the validity of the Valley Asphalt Lien Claim, the Seven Peaks Resort Entities will be treated as alter egos of one another, and it is further

ORDERED that the lien claim of Valley Asphalt is allowed as a valid and enforceable mechanic's lien under Utah law against the CDX Property, and it is further

ORDERED that the SAIC Lien Claim will be equitably subordinated and shall be treated under the terms of the CDX plan as a general unsecured claim.

DATED this 30 day of September, 1996.

BY THE COURT:

Glen E. Clark

GLEN E. CLARK, CHIEF JUDGE
UNITED STATES BANKRUPTCY COURT