UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF VIRGINIA
Lynchburg Division

In re OAKWOOD COUNTRY CLUB,) Case No. 10-60246-LYN
INCORPORATED,)
)
Debtor,)
)

ORDER

For the reasons stated in the accompanying memorandum, the motion of the Debtor to sell substantially all of the assets of the debtor shall be and hereby is denied.

So ORDERED.

Upon entry of this Order the Clerk shall forward a copy to the Richard C. Maxwell, Esq., Loc Pfeiffer, Esq., T. Henry Clarke, IV, Esq., Jennie T Allman, William F. Schneider, Esq., Roy Terry, Esq., and Margaret K. Garber, Esq., of the United States trustee's office.

Entered on this 6th day of April, 2010.

William E. Anderson
United States Bankruptcy Judge

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	)	
Debtor,	)	
	)	

MEMORANDUM

This matter comes before the court on a motion by Oakwood Country Club, Inc. ("the Debtor" or "the Debtor Club") to sell substantially all of its assets to EWP (Oakwood) Venture, L.L.C. ("EWP"), under Sections 105 and 363 of the Bankruptcy Code.

Jurisdiction

This court has jurisdiction over these matters. 28 U.S.C. §§ 1334(a) & 157(a). This is a core proceeding. 28 U.S.C. § 157(b)(2)(A)&(N). Accordingly, this court may render a final order. This memorandum shall constitute the court's findings of fact and conclusions of law as directed by Fed.R.Civ.P. 52 which is made applicable in this contested matter by Fed. R. Bankr. P. 9014(c) and 7052.

Facts

The Debtor is a social club that was founded in 1914. The Debtor owns real property consisting of approximately 85 acres[1] of land and improvements ("the Real Property"). The land may be divided into two parcels. The first parcel consists of approximately 77 acres on which is a nine-hole golf course ("the Golf Property"). The second parcel consists of approximately eight acres of land ("the Clubhouse Property") with improvements consisting, among other things, of a clubhouse, swimming pool and tennis courts. In its schedules, the Debtor valued the Real Property with improvements at $1,450,000.00.

The Debtor scheduled personal property at a value of $608,782.00. As noted in the schedules, however, this represents the book value (purchase price less depreciation taken) and the actual market value of this property is substantially less. At the hearing on this matter, none of the parties argued that the value of the personal property should affect the consideration of whether the motion now before this court should be granted.

The Debtor once consisted of 650 members. In the 1980s, the Debtor found it necessary to require each member to purchase preferred shares of stock for $3,000.00 to facilitate repairs. Some 240 members decided to resign from the Debtor rather than purchase the shares. Since then, the Debtor has experienced increasingly severe financial hardship caused primarily by a continued reduction in membership. The Debtor now has 229 members and employs 29 persons.

On or about December 12, 2007, the Debtor execute a note in favor of New Vision Golf for $1,212,000.00 with the proviso that the price would be reduced to $725,000.00 (less amounts paid up to an aggregate reduction of $125,000.00) if paid by January 1, 2011. New Vision Golf

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[1] Schedule A indicates that the Debtor Club owns 85.02 acres of land.

filed a proof of claim in the amount of $1,107,410.00. The Debtor scheduled the debt owed to New Vision Golf at $720,000.00.

In September of 2008, the Debtor began marketing the Real Property, sending out invitations to 750 developers. In December of 2008, the Debtor selected Celebration Associates of Charlottesville (“Celebration”). In May of 2009, Celebration concluded that the investment was not feasible for it. In June of 2009, the Debtor contacted EWP. In September of 2009, EWP and the Debtor entered into a joint venture to develop the Real Property. This agreement is no longer in effect, for reasons that are not entirely clear.

During the summer or fall of 2009, the Debtor discovered that its bookkeeper had embezzled approximately $30,000.00 and had failed to pay certain taxes on behalf of the Debtor. The Debtor is currently experiencing a $10,000.00 monthly negative cash flow from operations and has another $20,000.00 per month in debt service that it cannot pay. The filing of the petition was precipitated when the City of Lynchburg executed against approximately $30,000.00 in the Debtor’s bank account. The Debtor is further pressed by the urgent need to prepare the tennis and swimming facilities for spring use.

On January 29, 2010, the Debtor filed a voluntary chapter 11 petition with the clerk of this court. The Debtor’s debts are substantially as follows. Wachovia Bank, N.A. (“Wachovia”) holds a first deed of trust on the Real Property securing a debt in the approximate amount of $725,000.00. A group of twenty-four members of the Debtor, designated as “The Oakwood Indoor Tennis lenders” (“the OIT Lenders”) in the Debtor’s schedules, holds a second deed of

trust on the Real Property securing a debt ("the OIT Debt") in the approximate amount of $540,000.00.[2] There are approximately $104,000.00 in priority claims against the Debtor.[3]

The Debtor scheduled unsecured claims in the amount of $941,568.53. This includes attorney's fees in the amount of $41,000.00 and the debt owed to New Vision Golf in the amount of $720,000.00. The balance of the debt is mostly trade debt and unsecured loans from members of the Debtor.

On February 24, 2010, the Debtor entered into an Asset Purchase Agreement ("APA I") with EWP, pursuant to which the Debtor proposes to sell to EWP substantially all of the Real Property and the Debtor's personal property, except any avoidance actions that might be owned by the Debtor. In return, EWP would pay or assume the following secured, administrative, and priority claims arising from debts owed to creditors of the Debtor:

Creditor	Approximate Amt.	Status	Method of "Payment"
Wachovia Bank	$ 725,000.00	Secured	Cash to creditor
Marc Schewel	$ 10,000.00	Secured	Cash to creditor
Priority Claims	$ 104,000.00	Priority	Cash to creditors
Administrative Exp.	$ 40,000.00	Priority	Cash to creditors
Subtotal	**$ 879,000.00**		
OIT Lenders	$ 540,000.00	Secured	Assumption of the Debt
Total	**$1,419.000.00**[4]		

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[2] The Debtor estimates that the amount of this debt will be $541,112.28 as of May 1, 2010.

[3] The priority claims include $8,450.00 in deposits, $16,176.88 in employees wages, and $76,307.22 in taxes due.

[4] The Debtor proffered at the hearing on this matter that this total is approximately $1,464,000.00 as of the date of the hearing. The differential does not affect the analysis of whether the motion to sell should be granted.

On March 8, 2010, the Debtor filed a motion to approve APA I. The motion also requests that the court approve a bidding procedure to allow competing bids. The motion proposes that interested parties notify it by March 25, 2010, and then bid at the hearing on this matter, which was held on April 1, 2010. The motion also requests that the court approve a break up fee in an amount equal to EWP's actual third-party out-of-pocket costs incurred in determining whether to enter into APA I, subject to a limit of $150,000.00.[5]

At the hearing on this matter, it was brought to the court's attention, by parties objecting to the motion to sell, that EWP had previously entered into another Asset Purchase Agreement ("APA II") to sell the Clubhouse Property and personal property to a recently created entity, Oakwood Swim & Tennis Club, L.L.C. ("the New Club"). The president and board of the New Club are the same as the president and the board of the Debtor Club. It is anticipated that the New Club will have the same membership as the Debtor Club. APA II is conditioned upon the approval of APA I by this court.

Under the terms of APA II, the New Club would assume the OIT debt from EWP. In addition, EWP would lease office space from the New Club for three years at the rate of $50,000.00 per year. EWP would also pay the New Club 26% of its "cash available for distribution"[6] (if any) from the development of the Golf Property ("the Development Payments"). APA II provides that the first $700,000.00 of the Development Payments will be used to renovate the clubhouse on the Clubhouse Property. Any amount beyond $700,000.00 will be used to retire the OIT Debt.

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[5] As of the date of the hearing on this matter, EWP had incurred $112,638.39 in out-of-pocket expenses.

[6] "Cash available for distribution" is a defined term in APA II.

The United States trustee, certain creditors, and the unsecured creditors committee oppose the motion to sell.

Discussion

The motion is brought under 11 U.S.C. § 363(b) which provides in relevant part that a trustee may sell property of the estate other than in the ordinary course of business, after notice and a hearing. The Debtor is currently a debtor-in-possession and continues to manage and operate its business pursuant to 11 U.S.C. §§ 1107 and 1108. A debtor-in-possession has the same rights with respect to Section 363 as a trustee in chapter 11. 11 U.S.C. § 1107(a).

The sale of all assets of a chapter 11 debtor is disfavored in the absence of a full disclosure, a plan and a vote by all creditors entitled to vote. See In re North Atlantic Millwork Corp., 155 B.R. 271, 283 (Bankr. D. Mass. 1992) (Citing In re Braniff Airways, Inc., 700 F.2d 935 (5th Cir.1983). It is now generally accepted that Section 363 allows the sale of substantially all of the assets of a debtor if the proponent of the sale demonstrates a good sound business justification for conducting the sale before confirmation, that the price is fair and reasonable, that the sale has been proposed in good faith, and that there has been adequate notice of the sale . See 4 Collier on Bankruptcy, "Use, Sale or Lease of Property", ¶ 362.02[3], (15th ed. rev.)

I.

We begin by examining whether the Debtor has demonstrated a sound business justification for conducting the sale before confirmation of a chapter 11 plan. Factors that are proper for consideration under the business judgment rule are whether the sale is for cash, whether the debtor's prospects for a confirmable plan are good, whether the sale has the support of the creditor's committee and the nature of the debtor's financial history. See, e.g., In re Condere Corp., 228 B.R.

615 (Bankr. S.D. Miss. 1998) (Court found a sound business justification for the sale given the debtor's troubled history, the fact that the sale was for cash, the unlikelihood of a confirmable plan, and the support of the creditor's committee).

In this case, it appears, at least in part, that the Debtor has a good business reason for selling the property. The Debtor is in dire straits financially. Its cash flow is negative and it has no cash to fund the difference. It is losing approximately $30,000.00 per month if debt service is included in the consideration. It is unlikely that the Debtor would be able to weather the storm long enough to obtain approval of a disclosure statement and confirmation of a chapter 11 plan. This, no doubt, is the reason that the Debtor chose to sell its assets rather than reorganize its affairs.

While the motion to sell is opposed by the creditor's committee and the sale is not for cash only, the timing of the motion to sell the Debtor's Real Property reflects good business judgment on the part of the Debtor. The problem, however, lies not in the decision to sell the property, but rather in the structure of the sale in light of the Debtor's fiduciary duty to the unsecured creditors.

II.

In the case of a sale of substantially all of the assets of the debtor, courts often require that the sales price to be "fair and reasonable". See In re Delaware & Hudson Railway Co., 124 B.R. 169 (D.Del. 1991). In order to determine whether the sales price is fair and reasonable, one must know the market value of what is being sold and the price that is being paid.

The property that is being sold is the Real Property which is composed of the Golf Property and the Clubhouse Property. The Debtor offered the Real Property to more that 750 prospective buyers, all of whom are developers. The court is convinced that the process employed by the Debtor

in marketing the Real Property is such that one would expect an offer that is fair and reasonable, especially in light of the urgency created by the Debtor's financial state and the condition of the Lynchburg real estate market.

It is, however, not so easy to ascertain what the present value of that price is. At first blush, it would appear that the price that is being paid for the Golf Property and the Clubhouse Property is approximately $1,445,000.00, an amount sufficient pay off all of the Debtor's secured debt and priority debt. But this is deceiving.

In order to determine the effect of granting the motion to sell, it is necessary to determine the combined effect of APA I and APA II by tracking the asset transfers, payments made, and debt assumed under those agreements. Under APA I, the Debtor will transfer the Golf Property and the Clubhouse Property to EWP. EWP will pay cash to the Debtor an amount sufficient to pay off the Wachovia debt, the Schewel debt, priority claims and some administrative expenses. These debts total approximately $879,000.00. EWP will also assume the OIT debt of $540,000.00.

Under APA II, EWP will transfer the Clubhouse Property to the New Club. EWP will also pay the New Club 26% of its "cash available for distribution" (if any) from the development of the Golf Property. In return, the New Club will assume the OIT debt.

The Debtor , EWP, and the New Club will experience the following changes if all parties perform their obligations under APA I and APA II. The Debtor will be divested of the Golf Property and the Clubhouse Property. The Debtor will also be relieved of obligations totaling $1,419,000.00. EWP will receive the Golf Property for which it will pay $879,000.00 to the Debtor and will pay the Development Payments to the New Club. The New Club will receive the Clubhouse Property and the Development Payments. In return, it will assume the OIT debt.

EWP is paying $879,000.00 plus the value of the Development Payments for the Golf Property. While no evidence was proffered that would allow an accurate estimate of the present value of the Development Payments, APA II provides that the first $700,000.00 from such payments will be used to renovate the clubhouse on the Clubhouse Property. APA II also provides that any additional amounts are to be used to help retire the OIT debt. It is contemplated by the parties to APA II, then, that the amount of the Development Payments to the New Club could exceed $700,000.00.[7] If the value of the Development Payments were $521,000.00 for purposes of this analysis, then it may be concluded that EWP is paying $1,400,000.00 for the Golf Property only.

In September of 2009, Wachovia appraised the Clubhouse Property at $870,000.00 for its best use which it determined to be residential development. Wachovia speculated that it would take approximately twelve months to sell the Clubhouse Property at that price. If the Clubhouse property is valued at $500,000.00 for a quick sale, then the actual sales price for the Real Property is $1,900,000.00. The sales price cannot be ascertained with any level of confidence, however, because the Debtor has not provided information regarding the present value of the Development Payments. Consequently, it cannot be concluded that the price is fair and reasonable. This is not to say that it is not fair and reasonable, it is only to say that the evidence before the court is not sufficient to make such a determination.

III.

We turn now to the issue of good faith. The problem here is that the New Club is an insider of the Debtor. "Insider" for purposes of the bankruptcy code is defined at 11 U.S.C. § 101(31). The

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[7] EWP will also rent office space from the New Club for three years at $50,000.00 per year. These payments, however, do not constitute part of the sales price because they represent an income stream generated to the purchaser after it has purchased the property. These rental payments differ from the Development Payments in that the latter accrue to the seller after the execution of the sales agreement.

definition, however, is suggestive and not exclusive. An entity need not fall under the list of inclusions provided in Section 101(31) to be an insider. See In Loftis v. Minar (In re Montanino), 362 B.R. 307 (Bankr. D.N.J. 1981) (Holding generally that insiders are *those who have great influence over the debtor* and specifically that an insider may be defined as a relative of the debtor even when such person is not a blood relation of the debtor if there is sufficient closeness to the debtor to preclude the notion of an arms' length transaction between them.) (Emphasis added.) An"insider" generally is an entity whose close relationship with the debtor subjects any transactions made between the debtor and such entity to heavy scrutiny. 2 Collier on Bankruptcy, "Definitions", ¶ 101.31, (16th ed.).

The president and board of directors of the New Club are the same persons as the president and the board of directors of the Debtor Club. It is anticipated that the New Club will have the same membership as the Debtor Club. It would be an understatement to say that the New Club has an influence over the Debtor. The New Club is an insider of the Debtor. Further, it is clear that the New Club exercised influence over the Debtor in the drafting of APA I.

Under the two agreements, the New Club will obtain title to the Clubhouse Property free and clear of liens save that of the OIT Lenders, who are themselves insiders of both the Debtor and the New Club. In addition, the New Club will be the beneficiary of the Development Payments, which may have a present value in excess of $500,000.00. The bottom line is that this amount, which constitutes direct proceeds from the sale of the Golf Property, will return to insiders of the Debtor, while the unsecured creditors will receive nothing and will be forever enjoined from taking action to collect their debts.

The motion to approve APA I that is now before the Court is a *sub rosa* plan without the disclosure and procedural trappings that are required for confirmation. When APA I's effects are considered in conjunction with those of APA II, the Debtor's significant breach of its fiduciary duty to unsecured creditors is made manifest. The insider New Club will receive Development Payments that could exceed $500,000.00 and the unsecured creditors will get nothing. For this reason, the motion cannot be granted.

IV.

The last consideration is whether interested parties have received adequate notice of the sale. Notice was given in sufficient time for creditors and potential bidders to analyze the motion. The problem, and it is a significant one, lies in the fact that the Debtor did not disclose the existence of, much less the terms and conditions of, APA II. Without notice of APA II, parties had no knowledge of the fact that EWP is only purchasing the Golf Property nor did they have knowledge that EWP was willing to pay an undetermined additional amount equal to the Development Payments. Without notice of these things, potential buyers could not make an informed bidding decision. The motion to sell must also be denied because notice is inadequate.

Conclusion.

The motion cannot be granted at this time for three reasons: (1) the offered price, while probably fair and reasonable, is not subject to calculation; (2) an insider of the Debtor with no claim against the estate is to receive payments that could exceed $500,000.00 while unsecured creditors are to receive nothing; and (3) notice was deficient in that it did not include disclosure of APA II.

The court believes that the price being paid was negotiated after an arms' length negotiation. While that price is not subject to precise calculation, it is more than likely fair and

reasonable under the circumstances given the negotiation process and the relationship between EWP and the Debtor. The Court would be willing to accept the price, subject to evidence as to the expected present value of the Development Payments.

The Debtor's failure to disclose APA II is also fatal to its motion. The provision for payments to the New Club before unsecured creditors constitutes a sub rosa plan that breaches the Debtor's fiduciary duty to unsecured creditors.

This court is painfully aware that the Debtor is on the brink of financial ruin and that only imminent action will afford it a chance to continue as a viable entity. It is, however, one thing to seek to sell all of the Debtor's assets under this financial pressure and yet another to seek to direct the proceeds of that sale away from unsecured creditors and toward an insider that is nothing more than a legal reincarnation of the Debtor. The motion to sell substantially all of the Debtor's assets will be denied.

An appropriate order shall issue.

Upon entry of this Memorandum the Clerk shall forward a copy to the Richard C. Maxwell, Esq., Loc Pfeiffer, Esq., T. Henry Clarke, IV, Esq., Jennie T Allman, William F. Schneider, Esq., Roy Terry, Esq., and Margaret K. Garber, Esq., of the United States trustee's office.

Entered on this 6th day of April, 2010.

William E. Anderson
United States Bankruptcy Judge