THIS OPINION IS NOT INTENDED FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

IN RE	)	CASE NO. 98-51628
	)	
THE WARNER GROUP, INC.	)	CHAPTER 11
	)	
DEBTOR(S)	)	JUDGE MARILYN SHEA-STONUM
	)	
	)	**ORDER DENYING**
	)	**CONFIRMATION OF DEBTOR'S**
	)	**PLAN OF REORGANIZATION**

On April 27, 1999, the Court held a hearing on confirmation of the debtor's Third Amended Plan of Reorganization. Appearing at that hearing were Michael Moran, counsel for debtor; Joel Dayton, counsel for Key Bank; Tim Coerdt, counsel for Adesco Industrial Co., Ltd. and China Machinery Import & Export Corporation Harbin Branch ("CMC-Harbin"); and Andrew Vara, Attorney Advisor for the Office of the United States Trustee for Region 9. During the hearing, the Court received evidence in the form of exhibits and in the form of testimony from the following: (1) Stan Smith, appraiser with Industrial Assets of Studio City, California; (2) Ralph Thomas, accountant for the debtor; (3) John Graebing, salesman for Browning Bearing & Chain, Inc. ("BB&C"); and (4) Barry Gentzler, the sole shareholder, officer and director of the debtor. At the conclusion of the hearing the matter was taken under advisement.

This proceeding arises in a case referred to this Court by the Standing Order of Reference entered in this District on July 16, 1984. This matter is a core proceeding

pursuant to 28 U.S.C. §157(b)(2)(L) over which this Court has jurisdiction pursuant to 28 U.S.C. §1334(b). Based upon testimony and evidence presented at the April 27, 1999 hearing, the arguments of counsel and the documents of record in this case, the Court makes the following findings of fact and conclusions of law.

I. FACTS

On May 27, 1998, the debtor filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code. Since its filing, the debtor has remained in possession of its property and has operated its business in accordance with 11 U.S.C. §1107 and §1108. On March 5, 1999, the Court held a hearing on the debtor's request for approval of its Second Amended Disclosure Statement which was filed on February 16, 1999. At the conclusion of the hearing the Court granted the debtor's request to approve its disclosure statement, subject to the revisions needed to resolve outstanding objections to approval of that document. On March 9, 1999, the debtor filed its Third Amended Disclosure Statement (the "Disclosure Statement") and Third Amended Plan of Reorganization (the "Plan") and an order approving the Disclosure Statement was entered later on that same date. That order also set April 15, 1999 as the last day for voting on the Plan and April 21, 1999 as the last day to file objections to plan confirmation.

In the Plan the debtor designates the following classes of claims or interests: (1) Class One - Administrative Claims; (2) Class Two - Secured Claim of Key Bank; (3) Class Three - Priority Unsecured Claims of Governmental Units; (4) Class Four - General Unsecured Claims; and (5) Class Five - Claim of Barry Gentzler as the Sole Shareholder of the Debtor. During the confirmation hearing, the debtor argued that the Plan was affirmatively accepted by Classes One, Two, Four and Five. With respect to Class Four - General Unsecured Claims, the debtor asserted that eight creditors voted in favor of the Plan

while just two voted timely to reject the Plan. The debtor reported that $15,613.49 of the claims represented by Class Four voted to reject the Plan while $870,090.15 of the claims represented by Class Four voted to accept the Plan. In computing both the number and amount of claims voting on the Plan, the debtor included a ballot cast by The Warner Group Ltd.. Barry Gentzler submitted the ballot accepting the Plan on behalf of The Warner Group Ltd. in the amount of $841,704.00. That claim amount reflected on The Warner Group Ltd.'s ballot is identical to the amount identified by the debtor on its Schedule F.

The Warner Group Ltd. is a Delaware corporation of which Barry Gentzler is the sole shareholder, officer and director. The debtor owes this insider entity funds resulting from prepetition inventory purchases. In the Plan, the debtor subordinates the claim of The Warner Group Ltd. to the claims of all other creditors and provides that no dividend is to be paid on this claim. Pursuant to an order entered in the United States District Court for the Northern District of Ohio, Eastern Division on September 14, 1998, the claim of The Warner Group Ltd. was assigned to CMC-Harbin, a judgment creditor of the Debtor. On November 5, 1998, CMC-Harbin filed a "Notice of Involuntary Transfer of Claim" in this bankruptcy case.

In the Plan the debtor provides that all of the assets of BB&C will be conveyed to Key Bank, the debtor's sole secured creditor, and that Key Bank will in turn transfer control of those assets to the reorganized debtor. Despite the transfer of all of its assets, the Plan provides that BB&C will retain all of its liabilities. BB&C is an Ohio corporation of which Barry Gentzler is the sole shareholder, officer and director. Like the debtor, BB&C is engaged in the distribution of mechanical power transmission products such as bearings and chains. The debtor and BB&C share machinery, equipment and office furniture at locations in Macedonia and Twinsburg, Ohio. At the time the debtor filed its petition, BB&C owed

the debtor approximately $287,000.00.

In the Plan the debtor also provides that Barry Gentzler will receive 100% of the new stock in the reorganized debtor. In exchange for receiving such stock, Mr. Gentzler proposes to contribute $20,000.00 to the reorganized debtor and to waive his Class Five claim.

On April 21, 1999, the United States Trustee filed an objection to the Plan. In that objection, the United States Trustee contends that the affirmative vote of The Warner Group Ltd. should not be counted because pursuant to the involuntary transfer to CMC-Harbin, The Warner Group Ltd. is not a holder of a claim against the debtor. Even if The Warner Group Ltd. was considered to still hold a claim against the debtor, the United States Trustee argues that, pursuant to the standards set forth in 11 U.S.C. §1126(e), that claim was not submitted in good faith. The United States Trustee also contends that Mr. Gentzler's proposed $20,000.00 contribution to the reorganized debtor is not sufficient enough to meet the new value exception to the absolute priority rule. Apart from the United States Trustee, no other creditor or party in interest filed an objection to the Plan.

II. DISCUSSION

A plan of reorganization may be confirmed if each of the requirements set forth in 11 U.S.C. §1129(a) is satisfied. Having heard the Court's initial views of this matter at the April 27, 1999 confirmation hearing, the debtor proceeded on the assumption that it was unable to meet the requirements of §1129(a)(8). Based upon the evidence concerning the assignment of the claim for the purpose of satisfying the judgment held by CMC-Harbin and the scheduled treatment of the specific claim, the Court finds that the ballot of The Warner Group Ltd. should not be counted.

Because the requirements of subsection (a)(8) were not satisfied, the debtor

requested that the Plan be confirmed pursuant to the provisions of 11 U.S.C. §1129(b). Section 1129(b) provides that even if the requirements of §1129(a)(8) are not met, a court may still confirm a plan if all the other applicable requirements of subsection (a) are met and if the plan does not discriminate unfairly, and is fair and equitable with respect to each class of claims or interests that is impaired under, and has not accepted, the plan. Before considering whether a plan discriminates unfairly and is fair and equitable, the court must determine if all the other requirements of §1129(a) have been satisfied. The plan proponent bears the burden of proof on each such element. *See In re Keaton*, 88 B.R. 154, 156 (Bankr. S.D. Ohio 1988).

With the exception of the United States Trustee's objection regarding satisfaction of §1129(a)(8), there were no objections regarding the debtor's satisfaction of the other subsections of §1129(a). Notwithstanding the absence of objections, the Court has an independent duty to determine whether all §1129(a) requirements are met before considering confirmation of a plan. *In re Montgomery Court Apartments of Ingham County Ltd.,* 141 B.R. 324, 329 (Bankr. S.D. Ohio 1992). In this case, the Court concluded that the debtor has failed to meet the requirements of §1129(a)(1) and §1129(a)(11).

Section 1129(a)(1): Section 1129(a)(1) requires that a proposed plan "compl[y] with the applicable provisions of this title." 11 U.S.C. §1129(a)(1). As drafted, the Plan contemplates that all of the assets of BB&C will be transferred to the reorganized debtor through Key Bank. The Plan also contemplates that BB&C will retain all of its liabilities. Because BB&C would be stripped of all assets but retain all liabilities, BB&C's creditors would have a sufficient stake in the outcome of the confirmation proceedings. Given their sufficient stake, BB&C's creditors are "parties in interest" in this case. *In re Amatex Corp.,* 755 F.2d 1034, 1042 (3rd Cir. 1985); *Kaiser Aerospace and Electronics Corp. v. Teledyne*

Industries, Inc., 229 B.R. 860, 872 (Dist. S.D. Fla. 1999).

Section 1109(b) provides that a party in interest "may raise and may appear and be heard on any issue in a case under this chapter." In this case, the debtor did not serve either the Disclosure Statement or the Plan on any BB&C creditor. Because those creditors are parties in interest and because the were not afforded the opportunity to be heard on confirmation, as provided for in §1109(b), the Court finds that the requirements of §1129(a)(1) were not met.

Section 1129(a)(11): Section 1129(a)(11) requires a debtor to prove that a proposed plan is feasible by demonstrating that confirmation is not likely to be followed by the liquidation or the need for further financial reorganization of the debtor or any successor to the debtor under the plan. 11 U.S.C. §1129(a)(11). In determining whether a proposed plan is sufficiently feasible for confirmation, a court may consider any factors which would materially reflect on a debtor's ability to operate successfully and implement the proposed plan, including the economic and market conditions of the debtor's industry, the ability of debtor's management and the debtor's ability to meet its requirements for capital expenditures. *In re Kemp*, 134 B.R. 413 (Bankr. E.D. Ca. 1991). Based upon the evidence presented at the confirmation hearing, the Court finds that the debtor has not met its burden in proving that the Plan is feasible.

Although the debtor has historically acquired most of its inventory from Asian sources, no testimony was provided regarding the effect of the recent Asian financial crisis on the availability or cost of future inventory purchases. Such information is clearly important in considering feasibility given Mr. Graebing's testimony that at least 50% of the reorganized debtor's inventory would have to be purchased to meet projected sales revenues of $70,000.00 per month. The only reference to the effect of economic conditions came

during Mr. Gentzler's testimony when he briefly remarked that, because the potential market for the debtor's product is so large and because potential clients are so many, the market could face a downturn without much effect on the debtor. Such conclusory statements do not, however, constitute credible evidence in support of feasibility of the Plan. Further, the absence of support from the majority of the trade creditors whose ballots were reported to the Court begs the question of how the debtor would fill in gaps in its existing inventory.

During the confirmation hearing, Mr. Graebing also testified that in order to meet projected sales revenues of $70,000.00 per month, the reorganized debtor would have to sell its existing inventory. It is unclear, however, whether that inventory is even in saleable condition. Although the appraiser testified that a review of the inventory showed it to be in good condition and stored in an orderly fashion, that testimony is not persuasive given that his inspection occurred only one night prior to the confirmation hearing and was limited to only one of the debtor's inventory locations.

Although it appears that $70,000.00 per month in projected sales revenues could be an attainable goal for the reorganized debtor, the debtor failed to produce sufficient evidence on how it will consistently meet that goal. For instance, no evidence was presented as to whether Mr. Graebing is under a contractual duty to remain employed by the reorganized debtor or what ability the reorganized debtor would have to replace Mr. Graebing should he leave its employ. Because ongoing sales are crucial to the reorganized debtor's success, testimony regarding a contingency plan for the loss of an experienced salesperson would have been useful in evaluating feasibility. Also, no evidence was presented as to typical lag time between when a sale is made and when payment for that sale is collected. Without receipt of sale proceeds, it is unclear as to how the reorganized debtor plans to replenish its inventory supply.

Issues as to feasibility also exist given Mr. Gentzler's past practice of creating various closely related corporate entities that operate in the same or similar business as the debtor. In at least one of these situations, the sole secured creditor of the debtor is also the primary secured creditor of the related entity. Given these past practices and given that the Plan proposes to pay unsecured creditors only after the debtor's secured creditor is paid in full, it is possible that future assets could be filtered through a related entity to the detriment of the reorganized debtor.

Section 1129(b): Because the debtor has failed to satisfy more that just subsection (8) of §1129(a), the debtor cannot proceed under §1129(b). Moreover in light of the recent opinion in *Bank of America National Trust and Savings Association v. 203 North Lasalle Street Partnership*, ___ S.Ct. ___, 1999 WL 257631 (U.S. May 3, 1999) (No. 97-1418), the

Plan could not be confirmed under §1129(b) because no one other than the existing shareholder was provided any opportunity to infuse new value. It is now clear that whatever Mr. Gentzler's opportunity to purchase the equity of the reorganized entity, it was not a right exclusive to him. *Id.*

III. CONCLUSION

For all the reasons set forth above, the Court determines that all parties in interest were not afforded an opportunity to be heard in this case and that the Plan is not feasible. Accordingly, confirmation of the Plan is denied.

IT IS SO ORDERED.

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MARILYN SHEA-STONUM
Bankruptcy Judge

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DATED: 5/7/99