



SO ORDERED.

SIGNED this 02 day of February, 2007.

ROBERT E. NUGENT  
UNITED STATES CHIEF BANKRUPTCY JUDGE

NOT DESIGNATED FOR PUBLICATION

IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF KANSAS

IN RE:	)	
	)	
NORMAN SABBAGH	)	
MARY LOU SABBAGH,	)	Case No. 05-14212
	)	Chapter 7
Debtors.	)	
_____	)	
IN RE:	)	
	)	
DALE R. WEAVER,	)	Case No. 05-14837
	)	Chapter 7
Debtor.	)	
_____	)	
IN RE:	)	
	)	
MICHAEL E. LOWE	)	Case No. 05-14936
JACQUELINE E. FLOWERS-LOWE,	)	Chapter 7
	)	
Debtors.	)	
_____	)	

<b>IN RE:</b>	)	
	)	
<b>CEDRIC W. HOLLINS,</b>	)	<b>Case No. 05-15967</b>
	)	<b>Chapter 7</b>
<b>Debtor.</b>	)	
_____	)	
<b>IN RE:</b>	)	
	)	
<b>ALVIN JOHNSON,</b>	)	<b>Case No. 05-17141</b>
<b>BETTY JOHNSON,</b>	)	<b>Chapter 7</b>
	)	
<b>Debtors.</b>	)	
_____	)	
<b>IN RE:</b>	)	
	)	
<b>KENNETH P. COX,</b>	)	<b>Case No. 05-19743</b>
	)	<b>Chapter 7</b>
<b>Debtor.</b>	)	
_____	)	

**INTERIM ORDER ON CHAPTER 7 TRUSTEES' MOTIONS FOR  
TURNOVER OF SPIRIT AEROSYSTEMS' DISTRIBUTIONS TO DEBTORS  
MADE UNDER EQUITY PARTICIPATION PROGRAM**

These cases came on for evidentiary hearing on January 30, 2007 upon the chapter 7 trustees' motions requiring debtors to turnover certain cash and stock distributions made to them by Spirit AeroSystems, Inc. ("Spirit") under a Union Equity Participation Plan ("EPP") established pursuant to the collective bargaining agreements ("CBA") between Spirit and the International Association of Machinists and Aerospace Workers ("IAM") and the International Brotherhood of Electrical Workers ("IBEW") (collectively referred to as the "Unions"). Debtors are former employees of The Boeing Company represented by the Unions who became employees of Spirit on June 17, 2005 upon Spirit's completion of the

acquisition of Boeing's commercial aircraft operations in Wichita and Tulsa. The question before the Court is whether the distributions under the EPP are property of the estate and subject to turnover.

Trustee Carl Davis appeared in the Sabbagh, Weaver, Lowe, and Cox cases. Trustee Edward J. Nazar appeared in the Hollins and Johnson cases. Debtors Sabbagh appeared in person and by their counsel David Lund. Debtor Weaver appeared by his counsel Thomas Gilman. Debtors Lowe appeared by their counsel Elaine F. Winter. Debtors Johnson appeared in person and by their counsel Steven Wagle. Debtor Cox appeared by his attorney David Nelson. Debtor Hollins proceeds pro se in his bankruptcy and he did not appear.

The Court took evidence in the Sabbagh and Johnson cases. The trustees and counsel for the debtors declined the Court's invitation to present further evidence in the remaining four cases and submitted them to the Court on the record made in Sabbagh and Johnson. The Court admitted into evidence the EPP, the CBAs, a spreadsheet of the cash distributions to certain of the debtors, and a distribution statement letter from Spirit to debtor Mary Sabbagh (Sabbagh Ex. A). The Court advised the parties that it would issue an interim order on the turnover motions, subject to a later, full evidentiary hearing on the merits and final determination of whether the EPP benefits constitute property of the estate.

### Jurisdiction

These cases are core, contested matters over which the Court has subject matter

jurisdiction.<sup>1</sup>

### Factual Background

In each of these cases the trustees have filed motions for turnover, requiring debtors to turnover the distributions or benefits received, or to be received, under Spirit's EPP.<sup>2</sup> Debtors have objected to turnover, contending the EPP distributions are not property of the estate.

Under both the IAM and IBEW versions of the CBA, Spirit agreed to establish an equity participation program that would provide for represented employees to participate in profit earned by Spirit on ten percent of its initial common stock upon one of three events: (1) a substantial sale by its investors; (2) a change of control merger; or (3) an initial public offering ("IPO") of the stock.<sup>3</sup> This was the only reference to the EPP in the CBAs. Each CBA became effective on the date of closing of Spirit's acquisition of Boeing, June 16, 2005.<sup>4</sup> When and if one of these events occurred, represented eligible employees would participate in any increased value of the stock offered through distributions of cash and stock.

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<sup>1</sup> See 28 U.S.C. § 157(b)(1) and (b)(2)(E); 28 U.S.C. § 1334(b); 11 U.S.C. § 542(a) and Fed. R. Bankr. P. 9014.

<sup>2</sup> No. 05-14212, Dkt. 17; No. 05-14837, Dkt. 25; No. 05-14936, Dkt. 19; No. 05-15967, Dkt. 20; No. 05-17141, Dkt. 14; No. 05-19743, Dkt. 21.

<sup>3</sup> IAM CBA, Art. 17, p. 86; IBEW CBA, Art. 16, p. 50.

<sup>4</sup> Throughout this Order the Court references Spirit as the entity that acquired Boeing's commercial operations in Wichita and Tulsa. The Court takes note that initially, Onex Corporation purchased Boeing's commercial division and operated for a short time under the name Mid-Western Aircraft Systems. Upon closing of the asset purchase agreement, Mid-Western changed its name to Spirit AeroSystems, Inc. For ease of reference, the Court will refer to Spirit as the acquiring entity, and the successor to Boeing.

On October 27, 2006, Spirit established the Union Equity Participation Plan (Initial Public Offering) (“EPP”). Under the EPP, upon the closing date of the IPO, “Eligible Employees” would receive cash and stock. Indeed, on December 6, 2006, the Eligible Employees each received approximately \$34,556 in cash, before withholding for taxes. They will receive the other portion in Spirit securities or cash (depending upon their employment status) on March 15, 2007.

The EPP defines an “Eligible Employee” as one that must have been (1) an hourly employee; (2) represented by the IAM or IBEW; (3) employed at Spirit on “Day One”<sup>5</sup> or on approved leave from Boeing on “Day One”; and (4) employed for 90 consecutive days during the period from June 17, 2005 through December 31, 2005.<sup>6</sup> Section 3.01 of the EPP makes clear that eligible employees have no interest in or rights with respect to the contemplated benefits even as of the October 27, 2006 effective date of the EPP:

Notwithstanding anything herein, no individual Eligible Employee shall have any rights with respect to or interest in the Appreciation Rights, or any right to be allocated any portion of any Net Proceeds and no Eligible Employee is assured that he or she will receive an allocation of any Net Proceeds.<sup>7</sup>

As of the Effective Date of the EPP, Spirit was to issue “Appreciation Rights” covering approximately 4.8 million shares of its stock for the benefit of eligible employees. The Effective Date is defined in the EPP as the date of its execution, October 27, 2006. As

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<sup>5</sup> Closing of the sale to Spirit occurred on June 16, 2005 and Spirit took over operations on June 17, 2005, known as Day One.

<sup>6</sup> See EPP, § 3.01.

<sup>7</sup> *Id.*

noted in § 4.01 of the EPP, the appreciation rights do not in themselves confer upon eligible employees any “legal or beneficial ownership” of any actual stock in the company. Only when the right became vested would it be converted into the right to receive a distribution of the net proceeds of the IPO on the “measurement date.” The Measurement Date is defined as the closing date of the IPO. According to the distribution statement letter issued to Mrs. Sabbagh, the IPO closed on November 27, 2006.<sup>8</sup> This is the defined Measurement Date. Section 4.02 of the EPP specifically states that the Appreciation Rights vest on the Measurement Date. Accordingly, these employees’ appreciation rights in the distribution did not vest until at least November 27, 2006.<sup>9</sup> The net proceeds to be distributed pro rata among the eligible employees was to be determined by the difference between the proceeds of the IPO and aggregate threshold price of the stock at offering. Distribution of the cash portion of the proceeds was to be made as soon as practicable after the measurement date (November 27, 2006) with the stock portion to be paid later.<sup>10</sup> As the EPP plainly states, the appreciation rights are non-transferable and non-assignable.<sup>11</sup>

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<sup>8</sup> Sabbagh Ex. A.

<sup>9</sup> This vesting date is consistent with other terms of the EPP which provide for the automatic termination or expiration of the Appreciation Rights upon the occurrence or nonoccurrence of certain events. For example, if the IPO was not consummated by June 30, 2007, the Appreciation Rights would terminate on that date. *See* EPP, § 7.02. In short, eligible employees were not assured of receiving any distribution, even after the EPP was established and the Appreciation Rights were issued.

<sup>10</sup> *See* EPP, § 4.04(b)(I) and (ii).

<sup>11</sup> *See* EPP, § 4.07.

In each of these cases before the Court today, at least one of the debtors was employed by Boeing when it conveyed its operations to Spirit.<sup>12</sup> Each of these debtors filed their petitions after Day One (June 17, 2005) and after the effective date of the CBAs, but before the EPP was established by Spirit and before its October 27, 2006 effective date.<sup>13</sup> Some, but not all, of the debtors had satisfied the criteria for an eligible employee to participate in the EPP before they filed their petition.

The debtors in these six cases received a post-petition cash distribution under the EPP on or about December 6, 2006. In the cases of Sabbagh, Johnson, and Cox, debtors have spent the cash distribution to pay various bills and obligations. Weaver and Lowe are holding their cash distribution in separate, interest bearing accounts. Debtor Hollins did not appear at the hearing and it is unclear if any of his cash distribution remains. These debtors anticipate receiving a second distribution of stock or cash on March 15, 2007 pursuant to the EPP.<sup>14</sup>

The trustees' motions for turnover were filed in these cases on December 7, 8, 12, and 14, 2006.

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<sup>12</sup> In the case of Mrs. Sabbagh, she was on medical leave and returned to work sometime in June 2005. It was not clear from her testimony whether she came off medical leave before or after the sale to Spirit closed.

<sup>13</sup> Debtors in these six cases filed their petitions in the summer and fall of 2005, prior to the effective date (October 17, 2005) of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. The Sabbaghs filed on July 11, 2005. Weaver filed on August 5, 2005. The Lowes filed on August 9, 2005. Hollins filed on September 16, 2005. The Johnsons filed on October 7, 2005. Cox filed on October 15, 2005.

<sup>14</sup> See Sabbagh Ex. A.

## Analysis

11 U.S.C. § 541 defines the scope of the property of the estate. As a general rule, the estate consists of all legal and equitable interests of the debtor on the date the case was commenced.<sup>15</sup> Section 541(a)(6) adds the proceeds and products of that property to the estate while excluding post-petition earnings of the debtor.

The trustees seek this Court's order that the Spirit distributions be turned over pending this Court's final determination of the underlying turnover proceedings. The Court sees this interim request for relief as akin to that for an injunction and deems the same principles to apply.<sup>16</sup> To enter a preliminary injunction, a Court must determine that (1) the movant will suffer an irreparable injury without the relief; (2) the movant's risk of harm outweighs any harm the non-movant may suffer; (3) the relief is not adverse to the public interest; and (4) the movant has a substantial likelihood of success on the merits.<sup>17</sup> The movant's right to a preliminary injunction must be clear and unequivocal.<sup>18</sup> The Court now analyzes the evidence and findings of fact in light of these four factors and the requisite proof.

### **Irreparable Harm**

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<sup>15</sup> § 541(a)(1).

<sup>16</sup> *See* Fed. R. Civ. P. 65.

<sup>17</sup> *Dominion Video Satellite, Inc. v. Echostar Satellite Corp.*, 356 F.3d 1256, 1260 (10<sup>th</sup> Cir. 2004).

<sup>18</sup> *Id.* at 1261. *Greater Yellowstone Coalition v. Flowers*, 321 F.3d 1250, (10<sup>th</sup> Cir. 2003) (Preliminary injunction is an extraordinary remedy; right to relief must be clear and unequivocal.).



The irreparable harm requirement is the single most important requirement for the issuance of a preliminary injunction and for that reason, the movant must first demonstrate that injury is likely before considering the other requirements.<sup>19</sup> The injury must be both certain and great, not merely serious or substantial.<sup>20</sup>

Both of the debtors (Sabbagh and Johnson) who testified stated they had already spent the cash portion of the distributions received in December of 2006, rendering futile the trustees' attempts to avoid irreparable harm. Based upon representations of counsel for debtor Cox, he likewise has spent the December cash distribution. Debtors Lowe and Weaver have segregated the December cash distribution and are holding the same in an interest bearing account. Counsel for these debtors represented the debtors' intent to hold the cash distribution pending a final resolution of the turnover motions. The Court has been given no reason to doubt debtors' sincerity and intent to secure these funds. The status of the cash distribution to debtor Hollins is unknown but this debtor's pro se response to the trustee's turnover motion suggests that it has probably been spent as well.

With respect to the stock to be distributed in March of 2007, the parties acknowledged that it is likely to be "locked up" – incapable of transfer by the debtors for some period of time.<sup>21</sup> Delivery of the stock to be distributed under the EPP is subject to the eligible

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<sup>19</sup> *Dominion Video*, 356 F.3d at 1260.

<sup>20</sup> *Id.* at 1263, quoting *Prairie Band of Potawatomi Indians v. Pierce*, 253 F.3d 1234 (10<sup>th</sup> Cir. 2001).

<sup>21</sup> *See* EPP, § 5.01.

employees opening a brokerage account and providing certain information to facilitate the deposit of the stock in the brokerage account.<sup>22</sup> The Court heard no evidence that any of the debtors had satisfied the conditions to receiving the stock. Nor was any evidence presented that registration of the stock to be issued has occurred or become effective or a timeline when that will occur.<sup>23</sup>

Under these circumstances, the Court cannot conclude that the estates will suffer certain and great irreparable harm if the turnover motions are not granted on an interim basis.

### **Balancing of Harm to Estates and Debtors**

Nor does the balance of harm to the estates outweigh the harm to debtors. These debtors' fresh start will be significantly impaired if their access to these distributions is restricted. The Court cannot conclude that the potential dissipation of what are questionable estate assets at best, outweighs the harm to debtors by depriving them of the EPP benefits.

### **Public Interest**

The public interest certainly supports the protection of estate property, and granting the turnover motions would not be adverse to that public interest. At the same time, this public interest is countered somewhat by the competing fresh start policy of our bankruptcy laws.

### **Success on the Merits**

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<sup>22</sup> See EPP, § 4.04(b)(ii), § 4.05 and §4.06.

<sup>23</sup> See Sabbagh Ex. A. None of the stock may be sold until the registration statement becomes effective.

Even if the Court believed that the trustees had clearly and unequivocally demonstrated the first three requirements, the trustees have not met their burden of showing they have a substantial likelihood of prevailing on the merits of their turnover motions. While Courts may “relax” this requirement in some cases, the modified standard occurs only when the first three requirements weigh heavily in movant’s favor.<sup>24</sup> That is not the case here and the Court will not apply a relaxed standard for the “success on the merits” requirement. The Court now turns to the heart of this matter – whether the EPP distributions are property of the estates.

The trustees rely on the extremely broad definition of the scope of property of the estate contained in § 541(a)(1) (“all legal and equitable interests. . .”) as it has frequently been interpreted in the courts. In one of the leading decisions construing “property of the estate,” *United States v. Whiting Pools, Inc.*, the Supreme Court noted the broad reach of § 541 in defining what constitutes the estate as all interests of the debtor whether tangible, intangible, future, non-possessory, or contingent.<sup>25</sup>

Section 541(a)(1) makes clear that the property comprising the estate is determined

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<sup>24</sup> See *Greater Yellowstone Coalition v. Flowers*, 321 F.3d 1250, 1255-56 (10<sup>th</sup> Cir. 2003) (If the first three requirements tip strongly in favor of movant, the test is modified, and the movant may satisfy the success on the merits requirement by showing that questions going to the merits are so serious, substantial, and doubtful as to make the issue deserving of more deliberate investigation.).

<sup>25</sup> 462 U.S.198, 204-06 (1983). *Whiting Pools* itself dealt with a secured creditor’s (IRS) pre-petition seizure of a chapter 11 debtor’s property. The Supreme Court held that such seized property was property of the estate and subject to turnover, even though debtor did not possess the property on the date of filing. *Whiting Pools* bears little factual resemblance to the case at bar.

as of the date of the bankruptcy petition: “. . . all legal or equitable interests of the debtor in property *as of the commencement of the case.*”<sup>26</sup> This section also states: “Such estate is comprised of all the property, *wherever located and by whomever held.*”<sup>27</sup> Thus, the Court here focuses on what interest debtors had in the EPP benefits in 2005 when they commenced their cases.

The trustees argue that the debtors’ rights under the CBAs and the EPP are “stock options” in which the debtors had contingent or future interests on the dates their cases were filed. Several bankruptcy courts have dealt with stock options and concluded that whether or not the options could be exercised pre-petition, they constitute property that is swept into the estate at the date of filing.

The trustees rely on one particular case, *In re Dibiase*,<sup>28</sup> in support of their claims. In *Dibiase*, the debtor executed a stock option agreement in 2000 that granted the debtor the right to purchase shares of the employer at a given price and in a limited quantity in each year of his employment. Six months later, Dibiase filed his bankruptcy case and attempted to exempt some of the option on the basis that, because he could not exercise it for a year, he had no “vested” interest in it. The bankruptcy court instead concluded that the stock option itself was property of the estate because it represented a contingent or future interest even though the debtor could not exercise the option until after the case was filed.

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<sup>26</sup> § 541(a)(1) [Emphasis added].

<sup>27</sup> § 541(a) [Emphasis added].

<sup>28</sup> 270 B.R. 673 (Bankr. W.D. Tex. 2001).

This Court finds that *Dibiase* and the other stock option cases<sup>29</sup> are eminently distinguishable from the EPP benefits and distributions in the cases at bar. First, these cases do not appear to involve stock options. Indeed, eligible employees did not receive an option to be exercised by them; rather, upon the effective date of the EPP, appreciation rights were issued. The appreciation rights did not confer upon the eligible employees any ownership of any stock or the right to purchase stock. If and when the IPO yielded a stock price in excess of the threshold price, the appreciation rights would be converted into the right to receive a distribution payable to eligible employees in cash and stock.<sup>30</sup> They had no “option” per se and did not have to take any steps to “exercise” the “option.”<sup>31</sup>

Second, and far more important for today’s purposes, the record shows that neither the IPO nor the EPP existed at the time these debtors filed their cases. All the debtors had before the EPP was executed on October 27, 2006 was the hope, anticipation, or expectation that in the event of an IPO, they would receive a share of the profits. That is the only “future” or contingent” interest the Court can glean from the CBA terms.

This is a markedly different situation than that before the *Dibiase* court. In that case, the stock option agreement and the debtor’s interest in it existed before the debtor filed his

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<sup>29</sup> See also *In re Michener*, 342 B.R. 428 (Bankr. D. Del. 2006) (Employee stock option agreement entered into prepetition but stock options not exercisable by employee until post-petition were property of estate.).

<sup>30</sup> See EPP, Section 4.01.

<sup>31</sup> See Sabbagh Ex. A. The distribution statement letter issued to eligible employees characterized the distributions as an “award” and “payout” considered to be supplemental income.

case. Here, these debtors' expectations, if any, were based on the possibility or hope that a sale, merger, or IPO might occur during the term of the CBA. The employees had no control whatever over when or if that might occur because the decision to sell, merge, or publicly offer stock remained entirely within Spirit's discretion. Where the debtor's interest is entirely dependent upon the economic decisions of another party, this Court simply cannot conclude on this record that such an expectancy arises to a legal or equitable interest in property.

The Court believes this fact pattern more closely resembles the situation in *In re Bracewell*.<sup>32</sup> In that case, the chapter 7 trustee sought turnover of post-petition crop disaster payments to debtor. The post-petition payment to debtor was based upon debtor's pre-petition crop loss. But the government program authorizing the crop disaster payment was not enacted until after debtor commenced his case. Under these circumstances, the debtor did not have a legal or equitable interest in the disaster payment as of the commencement of the case.

We join the other circuits and conclude that until legislation was enacted authorizing the disaster payments and specifying the criteria for those payments, [debtor] had no legal or equitable interest in a payment. This is true even though before he filed his case he satisfied the criteria for payment that, as it turns out, Congress would eventually require. . . . Not until the enactment of the legislation elevated [debtor's] hope to an entitlement did it become an interest cognizable under § 541(a)(1).<sup>33</sup>

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<sup>32</sup> 454 F.3d 1234 (11<sup>th</sup> Cir. 2006).

<sup>33</sup> *Id.* at 1239. *See also, In re Burgess*, 438 F.3d 493 (5<sup>th</sup> Cir. 2006); *In re Vote*, 276 F.3d 1024 (8<sup>th</sup> Cir. 2002); *In re Schmitz*, 270 F.3d 1254 (9<sup>th</sup> Cir. 2001).

The post-petition enactment of the government program by Congress in *Bracewell* is similar to Spirit's post-petition creation of the EPP and the IPO in the case at bar.

Until Spirit established the EPP on October 27, 2006 and consummated the IPO, debtors had no legal or equitable interest in the distributions. Until then, the debtors stood in the same position as the debtor-farmer in *Bracewell*. They had nothing more than a hope and expectation that an EPP would be established and an IPO occur. Under the EPP, an eligible employee had no right to receive anything until, at the earliest, the effective date of the EPP, October 27, 2006, and, more likely, until November 26, 2006, the Measurement Date. Each of the cases before the Court today was filed well before the effective date of the EPP and the Measurement Date. It is therefore difficult, if not impossible, to determine that these distributions are “sufficiently rooted in the pre-bankruptcy past and so little entangled with the bankrupts’ ability to make an unencumbered fresh start” that they could conceivably be property of the estate.<sup>34</sup>

Therefore, the Court concludes that the trustees’ likelihood of success on the merits is slight. In the absence of being presented any persuasive authority to the contrary, the Court concludes that these debtors acquired their interest in the EPP benefits well after their cases were filed and that none of them had a legal or equitable interest in any of the distributions on the date their cases were filed.

### Conclusion

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<sup>34</sup> See *Segal v. Rochelle*, 328 U.S. 375, 379-80 (1966).

Accordingly, the trustees' interim motions for turnover must be DENIED and these matters advanced for evidentiary hearing at the Court's convenience.

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