In the United States Bankruptcy Court
for the
Southern District of Georgia
Brunswick Division

In the matter of:	)	
	)	Chapter 11 Cases
FIRST AMERICAN HEALTH	)	
CARE OF GEORGIA, INC.	)	Numbers <u>96-20188</u>
and its wholly owned subsidiaries	)	through <u>96-20218</u>
listed on Exhibit "A")		
	)	
Debtors	)	

MEMORANDUM AND ORDER
ON OBJECTION TO CLAIM OF GUNAR CHRISTENSEN

Respondent, Gunar Christensen, filed proof of interest and claim number 703 on June 26, 1996, stating that he holds 2,236 options to purchase stock of the Debtor and also has a corresponding claim for an undetermined amount arising from his Stock Option Plan interest. On November 13, 1996, the Debtor and the Official Committee of Equity Security Option Holders filed a joint objection to the same. After a hearing on January 30, 1996, I now make the following Findings of Fact and Conclusions of Law pursuant to Bankruptcy Rule 7052.

FINDINGS OF FACT

Debtor operates a home health care business with far flung operations across the United States. On or about June 30, 1994, the Debtor, acting through its chairman and chief executive officer, created a non-qualified stock option plan. The plan contained a number of provisions relevant to the matter in controversy at this time. Specifically, the plan created a committee to administer the plan and granted the committee complete authority to determine (1) the individuals who would be granted options, (2) the total number of options which would be granted to any optionee, and (3) the terms and conditions for exercising the same. The committee further was granted complete and exclusive authority to interpret the plan or to prescribe, amend, and rescind rules and regulations relating to it.

Specifically, the plan provided that when an option was granted by the committee, an option agreement stating the number of shares, the option price, the term of the option, and other relevant specifics was to be delivered to the optionee. All option agreements were to provide that the option "shall terminate with respect to the optionee as of the date the optionee ceases to perform services for the company . . . or to be an employee of the company . . . other than by reason of disability . . . or death." (Exhibit 2, paragraph 5f). An optionee who wished to exercise the option (1) was required to give written notice of the optionee's intent to purchase a specific number of shares, (2) was required to pay the purchase price of the option, (3) became subject to the call rights of the company, and (4) was entitled to the exercise put rights. Pursuant to its call rights and after giving written notice, the company had the right to repurchase the shares at a price to be set by the committee relying primarily on an appraisal by an independent third-party appraiser. Additionally, the optionee, upon exercise of an option, received "put rights," which, upon exercise through written notice, required the company to purchase shares acquired under the option at any time after the shares were issued. Again, the company was required to purchase such shares at the then current market value set by the committee based on an appraisal. (Exhibit 2, paragraph 9).

Upon exercise of the "put rights" by an optionee, "the company shall have the discretion to pay the optionee . . . either one lump sum cash payment or in substantial equal payments over a period no greater than 10 years." (Exhibit 2, paragraph 9). Furthermore, any time the company was required to issue shares pursuant to the exercise of an option, the company had the right to require the recipient to remit, in advance, "an amount sufficient to satisfy any federal, state and local withholding tax requirement prior to the delivery of any certificates for such shares." (Exhibit 2, paragraph 11)

The plan was introduced to the key employees of the Debtor company at a meeting held in Atlanta on September 14, 1994. Debtor's ERISA counsel, David H. Williams, presented the plan during a meeting at which key employees who were to be granted options under the plan were in attendance. Mr. William's presentation concerned the general mechanics of the plan, including an explanation of provisions relevant to this proceeding summarized as follows:

(i) <u>Purpose</u>: primarily to compensate key employees of the

Company and its subsidiaries and to secure and retain their services;

(ii) Method of Exercise: options granted under the Stock Option Plan had to be exercised by written notice, accompanied by payment of the $1.00 option exercise price;

(iii) Taxes: upon exercise, the Company had the right to require the Optionee to remit to the Company an amount in cash sufficient to satisfy any federal, state and local withholding tax requirements before the delivery of any certificate for any shares of common stock;

(iv) Payment/Put Rights: upon the exercise of a put to the Company of shares of common stock acquired upon exercise of an option, the Company had the discretion to pay the Optionee either one lump-sum cash payment or in substantially equal payments including interest made over a period no greater than ten years; and

(v) Termination of Options: prior to the Second Amendment to the Stock Option Plan dated February 19, 1996, the Option Agreement terminated upon an Optionee ceasing to perform services for the Company or a subsidiary, or ceasing to be an employee of the Company or a subsidiary, other than by reason of disability or death.

[After the enactment of the Second Amendment to the Stock Option Plan dated February 19, 1996, the Option Agreement terminated only upon an Optionee voluntarily ceasing to perform services for the Company or the expiration date of the option.]

(Exhibit 2, paragraph 5). Mr. Christensen attended the September 1994 meeting in Atlanta when the Stock Option Plan's provisions were explained to all fifty-one optionees. He asked certain questions of Mr. Williams, who made the presentation, and was briefed on the terms of the option plan by virtue of the presentation made at that time, and by virtue of the fact that he was provided with all relevant documents.

Gunar Christensen was offered a non-qualified stock option granting him the right to purchase from the company up to 1,500 shares of its common stock by grant number forty-three executed as of July 25, 1994. A confidential offer and memorandum dated December 15, 1994, was provided each of the key employees who were covered by the plan. (Exhibit 5). On March 6, 1995, Mr. Christensen partially exercised his option by notifying the company that he wished to purchase 750 shares of common stock of First American Health Care of Georgia, Inc. (Exhibit 7). On the same date he exercised his put rights requiring the company to repurchase the 750 shares. (Exhibit 8). He tendered the sum of $750.00, or $1.00 per share. (Exhibit 9). The committee, by action dated March 15, 1995, resolved to repurchase the optionee's 750 shares at a price of $47.628 per share and agreed to pay the optionee in one lump-sum payment after deducting applicable income taxes. (Exhibit 10). Mr. Christensen clearly was aware of the specific exercise requirements as demonstrated by his exercise of 750 options on March 6, 1995. On November 2, 1995, Mr. Christensen received an additional option grant of 1,391 shares. (Exhibit 13).

The purpose of the plan was to provide additional compensation to certain key employees who were considered essential to the successful operation of the company and to ensure their continued services to the company. It was also designed, based on the current cash flow of the business, so that the company could elect a long term payout if it so desired. At the time Mr. Christensen exercised his rights to 750 shares, the committee apparently determined that the company could afford to pay him in cash and did not require him to remit, in advance, the amount of his applicable tax liability, although it had the right to do so under the terms of the agreement.

On or about November 9, 1995, Mr. Christensen forwarded a check in the amount of $100.00 in an apparent effort to exercise his option to acquire 100 additional shares. He received a letter back from Robert J. Mills the company chairman and CEO reminding him that in addition to including a check for the amount of options exercises, he had to complete the Notice of Exercise of Stock Options and include a check to pay any federal, state, or other withholding obligations that he would owe on the exercise of his option. Mr. Mills referred him to Frank Wickline for a calculation of how much that liability would be. The letter also stated that Mr. Christensen might wish to wait to exercise his option because Mills was attempting, as part of his negotiations to sell the company, to reach an agreement for employees to "exercise your option without having to first pay your federal, state or other withholding tax obligations in cash at the time of exercise." (Exhibit 14b). Apparently after receiving this letter, Mr. Christensen decided not to pursue the matter further.

On February 19, 1996, immediately before Debtor's Chapter 11 case was filed, a second amendment to the stock option plan was enacted by the company to provide that, if an employee involuntarily ceased to perform services for the company, such employee would be permitted to exercise option rights until the expiration date of the option. This constituted a change from the original plan, because of the anticipated sale or merger of the company, to protect optionees who might be terminated anytime preceding a merger or change in control. The amendment further provided that after a change in control of the company the option could be exercised whether or not an employee continued to perform services or remained an employee. (Exhibit 16a). In other words, before February 19, 1996, employees who left the Debtor whether voluntarily or involuntarily would cease to hold any stock options. After February 19, 1996 and prior to a change in control of the Debtor, employees who left the Debtor voluntarily ceased to possess any stock options, although employees who were involuntarily terminated would have their interests protected. Finally, any change in control of the Debtor would automatically preserve an employee's stock interest whether they subsequently left the Debtor voluntarily or involuntarily.

On April 5, 1996, Mr. Christensen tendered his written resignation from the company effective May 3, 1996. Debtor’s Plan was confirmed on October 4, 1996, and Debtor merged into Integrated Health Services (“IHS”) post-confirmation. Mr. Christensen gave no notice of intent to exercise any further option rights prior to his last day of work and understood, as of that date, his option rights were lost. He subsequently went to work with a competitor, received an increase in pay and later decided that he might still retain some right to exercise his options. He conceded that the fair market value of his unexercised options which are in issue was approximately $120,000.00, assuming that the company's obligation to repurchase would have been exercised at approximately $53.00 per share. In the event of exercise of his put rights under the option plan at that price, his federal and state tax liabilities, plus the $1.00 per share option price, would have required him to advance approximately $40,000.00 to exercise rights in stock that would have netted him $120,000.00 either in cash or over a ten-year payout.

The objecting parties contend that the terms of the non-qualified stock option plan are unambiguous and that no option rights exist in favor of Mr. Christensen following his voluntary termination in April 1996. They contend that while he was protected pursuant to the February amendment against involuntary termination, his voluntary resignation automatically resulted in a loss of his option rights, and that no change in control of the company had occurred until at least the date of the confirmation of the plan. The objecting parties also asked for imposition of sanctions contending that this litigation was not brought in good faith.

Mr. Christensen asserts that because any act in violation of the automatic stay is void any attempt to exercise stock options post-petition and prior to leaving the company was futile. Thus, Mr. Christensen contends that his claim or interest was established on the date that Debtor filed for bankruptcy and is unaffected by any post-petition acts regardless of whether they are contrary to the requirements of the stock option plan. Mr. Christensen also contends that the "change in control" provisions of the second amendment should protect him because a merger agreement had been entered into between the Debtor and IHS prior to the time that he voluntarily left employment of the Debtor.[1]

At the time Mr. Christensen resigned, he had no present intention to exercise any option rights. Subsequently, there were some conversations between him and representatives of IHS about returning to work with the Debtor which was to be merged into IHS. He initially indicated he might consider doing so if his option rights were reinstated, but the offer subsequently extended to him did not include a restoration of his option rights and he declined to rejoin the company.

Based on the evidence before me I conclude that the objection to Mr. Christensen's claim is sustained and the request for sanctions is denied.

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[1] A dispute continued through the date of the hearing as to whether Mr. Christensen was entitled to exercise options to 2,236 shares as he contends or whether the company's recapitulation of his shares of 2,170 shares is correct. I informed the parties that rather than labor over the recapitulation of the number of outstanding options I would rule on Mr. Christensen's entitlement to exercise his option rights, based on the figures calculated by the company, and would convene a hearing at a later date should the issue not be resolved as to whether he is entitled to the full 2,236 shares.

CONCLUSIONS OF LAW

In pertinent part, Section 362(a)(6) of the Bankruptcy Code provides,

> (a) . . . a petition filed under [this] section . . . operates as a stay, applicable to all entities of, ---
>
> (6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title;

11 U.S.C. § 362(a)(6). This provision automatically stays any attempt to enforce a pre-petition claim against a debtor outside of the bankruptcy forum. As mentioned previously, Mr. Christensen contends that 11 U.S.C. Section 362 should be viewed as suspending an optionee's rights and preserving them notwithstanding a voluntary termination of employment. This contention is incorrect.

A stock option agreement is merely a contract to permit the purchase of shares in a corporation upon the fulfillment of certain conditions. *See* Wells v. L.W.A., Inc. et al., 221 Ga.App. 116, 118 (1996). Pursuant to the Bankruptcy Code, Section 362(a) does not toll the running of a specific time under a contract. *See* Moody v. Amoco Oil Co., 734 F.2d 1200, 1213 (7th Cir. 1984), *cert. denied* 469 U.S. 982 (1984). In addition, Section 362(a) will not prevent the post-petition termination of a contract by its own terms. *See* Hazen First State Bank v. Speight, 888 F.2d 574, 576 (8th Cir. 1989). Moreover, Section 362(a) does not enlarge the rights of an individual under a contract or give an individual any greater rights in a contract. *See* Id. at 576.

In the present case, Debtor contracted with each optionee to issue shares in the corporation upon exercise of their option. At the time of the grant and before the option's termination, the optionees possessed no ownership right or interest in the Debtor corporation, but rather a right to purchase shares at a subsequent date. The decision to exercise an option did not affect property of the estate because it only required the Debtor to issue an equity interest in the corporation in exchange for the purchase price. Exercise of the option was not stayed by Section 362(a)(6) because it was not an act to recover a claim as defined by Section 101(5)(A)&(B).[2] On the other hand, if the option were exercised and shares issued, an employee's enforcement of his or her "put right" post-petition arguably would be stayed by Section 362 because at that point the shareholder would be making a monetary claim against the Debtor's estate.

Mr. Christensen failed to exercise his options before leaving the company voluntarily. Pursuant to the plain language and unambiguous terms of the agreement, Section 362(a) does not extend his time to exercise that option or prevent the post-petition termination of his option and does not nullify the effect of Mr. Christensen's

[2] Section 101(5)(A) & (B) provides as follows:
(5) "claim" means--
(A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or
(B) right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured;

post-petition actions.[3]

Mr. Christensen also contends that because the Debtor agreed to merge with Integrated Health Services, Inc., on February 21, 1996, his options are preserved. In support of this position, Mr. Christensen cites the provisions of the Second Amendment to the 1994 Stock Option Plan which states in pertinent part as follows:

> . . . after a change in control of the Company, the Optionee may exercise his Option regardless of whether he is performing services for the Company . . .

(Exhibit A). Mr. Christensen asserts that Debtor's entering into of an agreement to merge constitutes a "change in control" sufficient to preserve his stock options notwithstanding his voluntary termination of employment. This contention is also incorrect. Paragraph Seven of the Second Amendment to the 1994 Stock Option Plan defines "change in control" as (1) a sale of substantially all of the assets, (2) a merger or consolidation in which the Debtor is no longer the surviving corporation, or (3) a merger or reorganization in which the shareholders of the Debtor are required to

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[3] Nothing in the agreement prevented Mr. Christensen from exercising his options prior to leaving the corporation. Clearly, the exercise of an option in a debtor corporation is a risk. At the time, either because of that uncertainty or perhaps the lack of financial resources, Mr. Christensen chose not to act - either through the exercise of his options in the normal course or petitioning the Court for relief from stay - when he left the Debtor for the employ of another health care provider at a higher salary. Certainly, Mr. Christensen was aware of the terms of the agreement because subsequent to his departure he considered returning to the Debtor and requested their reinstatement as part of his compensation package. Mr. Christensen now requests the Court to honor his interest when he chose not to remain with the company or exercise his options prior to leaving Debtor's employ. In other words, he was unwilling to offer either his services or financial commitment at a time when the options may have been worthless and now he requests compensation from a solvent corporation when he did not fulfill his own contractual obligations.

exchange their stock for cash and/or stock in another corporation. (Exhibit 16b). It is undisputed that while Debtor was attempting to merge with IHS it did not consummate a merger or incur a "change of control" pursuant to the above definition until after confirmation on October 4, 1996 and subsequent to Mr. Christensen's voluntary termination of employment.

Mr. Christensen made an intentional decision to leave a corporation that recently had filed for bankruptcy and pursue employment at a higher salary with a competitor. As a result, pursuant to the express terms of the 1994 Stock Option Plan, upon his voluntary decision to seek other employ without first exercising his stock options, Mr. Christensen forfeited all contractual rights to purchase stock options and, therefore, his proof of claim or interest must be disallowed.

The Official Committee for Equity Option Holders also moves this Court under Bankruptcy Rule 7011 to assess sanctions in the amount of attorneys' fees and expenses incurred while objecting to Mr. Christensen's claim pursuant their fiduciary duty. That rule in pertinent part states that,

> Every petition, pleading, motion and other paper served or filed . . . shall be signed by at least one attorney of record . . . . The signature . . . constitutes a certificate that the attorney or party has read the document; that to the best of the attorney's or party's knowledge, information, and belief formed after reasonable inquiry it is well grounded in fact and is warranted by existing law; and that it is not interposed for any

> improper purpose, such as to harass, or to cause unnecessary delay, or needless increase in the cost of litigation or administration of the case.

Fed.R.Bankr.P. 7011. The rule also permits a court to impose on the attorney, the represented party, or both sanctions which may include expenses and reasonable attorney fees. During this hearing, this Court was required to decide a question of first impression in this district of whether an exercise of an option is stayed by Section 362. Although I have ruled adversely to Mr. Christensen's position, I cannot conclude that his position was, after a reasonable inquiry, either not well grounded in fact or unwarranted by existing law and, therefore, decline to award sanctions.

O R D E R

For the foregoing reasons, IT IS THE ORDER OF THIS COURT that the objection of the Official Committee for the Equity Option Holders is sustained and the proof of claim or interest of Mr. Gunar Christensen, No. 703, be disallowed in its entirety.

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Lamar W. Davis, Jr.
United States Bankruptcy Judge

Dated at Savannah, Georgia

This ____ day of April, 1997.