

IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF: )  
)  
ADESTA COMMUNICATIONS, INC., ) CASE NO. BK01-83236-TJM  
)  
Debtor(s). ) CHAPTER 11

MEMORANDUM

Hearing was held in Omaha, Nebraska, on June 28, 2010, on motion for contempt filed by Frankel, Zacharia, Arnold, Nissen, Stamp & Reinsch, L.L.C., Trustee of the Adesta Secured Creditors' Trust (Fil. #1451) and responses by the Illinois Secretary of State (Fils. #1456 and 1457). David J. Skalka appeared for the Frankel Zacharia firm, Val C. Simhauser appeared for the Illinois Secretary of State, Karen L. Gilman appeared for Lumbermen's Mutual Casualty Company, and Walter H. Curchak appeared for Travelers Guarantee Insurance Company. This memorandum contains findings of fact and conclusions of law required by Federal Rule of Bankruptcy Procedure 7052 and Federal Rule of Civil Procedure 52. This is a core proceeding as defined by 28 U.S.C. § 157(b)(2)(O).

The court has jurisdiction over this dispute by virtue of paragraph 12.1(g) of the plan<sup>1</sup> and

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<sup>1</sup>Article XII of the plan addresses retention of jurisdiction:

12.1 Continued Jurisdiction Of The Bankruptcy Court. Under §§ 105(a) and 1142 of the Bankruptcy Code, and notwithstanding entry of the Confirmation Order and occurrence of the Effective Date, the Bankruptcy Court shall retain jurisdiction over all matters arising out of, and related to, the Chapter 11 Case and the Plan to the fullest extent permitted by law, including, among other things, jurisdiction to:

...

(e) Hear and determine any and all adversary proceedings, motions, applications, and contested or litigated matters arising out of, under, or related to, the Chapter 11 Case;

(f) Enter such orders as may be necessary or appropriate to execute, implement, or consummate the provisions of the Plan and all contracts, instruments, releases, and other agreements or documents created in connection with the Plan, the Disclosure Statement or the Confirmation Order;

(g) Hear and determine disputes arising in connection with the interpretation, implementation, consummation, or enforcement of the Plan, including disputes arising under agreements, documents or instruments executed in

(continued...)

paragraph L of the confirmation order<sup>2</sup>.

Pre-petition, Adesta Communications, Inc., was in the business of constructing telecommunication facilities throughout the United States, laying and maintaining fiber optic lines in a number of states. The company filed a Chapter 11 bankruptcy petition on November 2, 2001. The debtor's plan of reorganization was confirmed on July 19, 2002. The plan provisions most relevant to the matter at bar transferred substantially all of the debtor's assets to the Adesta Secured Creditors' Trust and Adesta, L.L.C. The plan also called for the cancellation of the debtor's old common stock and the issuance of new common stock to the Adesta Secured Creditors' Trust, for no monetary consideration. According to the trustee's evidence, 100 shares of new common stock in Adesta Communications, Inc., with a par value of one cent, was issued to the Trust on July 31, 2002. The Trust was the sole shareholder of the new stock. Thereafter, the debtor company had no ongoing business operations. It existed primarily to enforce pre-petition contract obligations as necessary. On September 30, 2008, the Trust sold substantially all of its assets to Zayo Bandwidth

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<sup>1</sup>(...continued)

connection with the Plan;

...

(i) Issue injunctions, enter and implement other orders, or take such other actions as may be necessary or appropriate to restrain interference by any entity with implementation, consummation, or enforcement of the Plan or the Confirmation Order;

...

(l) Enforce all orders, judgments, injunctions, releases, exculpation, indemnifications [in] connection with the Chapter 11 Case; wherever located;

...

(p) Hear and determine matters and disputes related to the Adesta Secured Creditors Trust or the Adesta Unsecured Creditors Trust, the assets held therein or distributed therefrom . . . .

Modified First Amended Plan of Reorganization of Adesta Communications, Inc., at 31-32 (Fil. #788).

<sup>2</sup>That paragraph address retention of jurisdiction:

Notwithstanding the entry of this Confirmation Order and the occurrence of the Effective Date, the Bankruptcy Court shall retain such jurisdiction over the Chapter 11 Cases after the Effective Date as is legally permissible, including jurisdiction over the matters set forth in Article XII of the Plan, which provisions are incorporated herein by reference.

Order Confirming Modified First Amended Plan of Reorganization of Adesta Communications, Inc. Under Chapter 11 of the Bankruptcy Code, at 24-25 (Fil. #790).

Tri-State II, LLC. The purchase agreement between the parties contemplated that Adesta Communications, Inc., was qualified to do business in the state of Illinois. The trustee discovered that Adesta Communications, Inc., had not filed annual reports with the Illinois Secretary of State since plan confirmation and therefore was not qualified to do business in Illinois. The trustee took steps to file the reports and pay approximately \$1,000.00 in reinstatement fees, interest and penalties, and the corporate franchise tax based on Adesta Communications, Inc.'s post-bankruptcy capitalization of \$1.00. The Illinois Secretary of State rejected the forms, asserting that approximately \$1.9 million was due for post-confirmation franchise taxes, based on the debtor's pre-bankruptcy capitalization.

Under Illinois law, the corporate franchise tax and annual report fee for 2002-03 were due by July 1, 2002, shortly before plan confirmation. As a debt incurred during the pendency of the bankruptcy case, it was an administrative claim. However, the State of Illinois did not file a request for payment of this claim, and it now concedes that its claim for those taxes and fees has been discharged. The fees and taxes due for 2003-04 and subsequent years remain in dispute.

In reviewing the background of this matter, an issue came to light that may be dispositive without the necessity of addressing the confirmation order's effects on the State's actions. In December 2002, the Illinois Secretary of State revoked the debtor's authority to do business in Illinois, citing its failure to pay the 2002-03 franchise tax. Because Illinois did not pursue its administrative claim for that tax, the debt was discharged, so the State's attempt to force the debtor to pay that debt was in violation of the discharge injunction. 11 U.S.C. § 524(a)(2).<sup>3</sup>

The discharge injunction serves to ensure that after a debt is discharged, the debtor will not be pressured in any way to repay it. Everly v. 4745 Second Ave., Ltd. (In re Everly), 346 B.R. 791, 795 (B.A.P. 8th Cir. 2006) (citing legislative history). Debtors may utilize motion practice to seek to hold creditors in contempt for allegedly violating the discharge injunction. Englund v. SBS Fin'l Serv., Inc. (In re Englund), 401 B.R. 377, 378 (B.A.P. 8th Cir. 2009). A willful violation of the § 524(a)(2) discharge injunction will warrant a finding of civil contempt and imposition of sanctions. In re Lang, 398 B.R. 1, 3 (Bankr. N.D. Iowa 2008) (citations omitted). The movant has the burden to show by clear and convincing evidence that the creditor had knowledge of the discharge and willfully violated it by pursuing collection activities. Id. Here, the Secretary of State filed a claim in the case in December 2001. By voluntarily submitting to the bankruptcy court's jurisdiction through the filing of the claim, the State became a party to the case and received timely notice of, *inter alia*, the plan, the confirmation order, and the discharge order.

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<sup>3</sup>(a) A discharge in a case under this title —

...  
(2) operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover or offset any such debt as a personal liability of the debtor, whether or not discharge of such debt is waived[.]

The State of Illinois concedes that it cannot collect the 2002-03 taxes and fees, but it stands by its revocation of the debtor's authority to do business. The only basis given for the revocation is the failure to pay the taxes and fees which were discharged in bankruptcy. By way of comparison, an Oklahoma bankruptcy court enjoined the state insurance commissioner who attempted to revoke a debtor's insurance license for failure to pay a debt which had been discharged in bankruptcy. Jacobs v. Oklahoma ex rel. Weatherford, 149 B.R. 983 (Bankr. N.D. Okla. 1993). The court stated:

The proceeding to revoke Jacobs' license is an attempt to use color of State law to extort payment, or to punish nonpayment, of a debt which Federal bankruptcy law says need not be repaid. As such, the Commissioner's action violates the bankruptcy discharge under 11 U.S.C. § 524(a)(2), the nondiscrimination provisions of 11 U.S.C. § 525(a), and the Supremacy Clause of the U.S. Constitution[.]

Id. at 992.

The Secretary of State's action here falls into the same category. Moreover, as noted by the Jacobs court, § 525(a) protects debtors against discriminatory treatment based on their status as bankruptcy debtors. It specifically provides that governmental units – which includes states and state agencies per 11 U.S.C. § 101(27) –

may not deny, revoke, suspend, or refuse to renew a license, permit, charter, franchise, or other similar grant to . . . a person that is or has been a debtor under this title . . . solely because such . . . debtor is or has been a debtor under this title . . . , or has not paid a debt that is dischargeable in the case under this title . . . .

11 U.S.C. § 525(a). See also F.C.C. v. NextWave Pers. Communications, Inc., 537 U.S. 293, 301-02 (2003) (“Section 525 means nothing more or less than that the failure to pay a dischargeable debt must alone be the proximate cause of the cancellation – the act or event that triggers the agency's decision to cancel, whatever the agency's ultimate motive in pulling the trigger may be.”)

The motion for a finding of civil contempt is granted. The act of revoking the right to do business in Illinois solely because of failure to pay a discharged debt is a sanctionable violation of the discharge injunction and §525(a). In this case, the appropriate sanction is to declare the unlawful revocation void from the date it occurred. As the revocation was not effective, the debtor still has the right to do business in Illinois, subject to paying late charges and franchise taxes for the years 2003-2010 on the capitalization it has by virtue of confirmation of the plan. The doctrine of Ex Parte Young, 209 U.S. 123 (1908), gives federal courts the power to enforce the Supremacy Clause by enjoining state officials in order to conform their conduct to the requirements of federal law. Schmitt v. Missouri W. State Coll. (In re Schmitt), 220 B.R. 68, 72 (Bankr. W.D. Mo. 1998). See also In re Moore, 407 B.R. 855, 861-62 (Bankr. E.D. Va. 2009) (where school willfully violated discharge injunction by requiring payment of discharged student loan debt before releasing transcript, the court ruled that coercive sanctions in the form of a hefty fine until the transcript was released were appropriate).

A separate order will be entered.

DATED: August 5, 2010

BY THE COURT:

/s/ Timothy J. Mahoney  
United States Bankruptcy Judge

Notice given by the Court to:

\*David J. Skalka  
Val C. Simhauser  
Walter H. Curchak  
Karen L. Gilman  
United States Trustee

Movant (\*) is responsible for giving notice to other parties if required by rule or statute.

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IT IS ORDERED: For the reasons stated in the Memorandum of today's date, the motion for a finding of civil contempt (Fil. #1451) is granted. The act of revoking the right to do business in Illinois solely because of failure to pay a discharged debt is a sanctionable violation of the discharge injunction and §525(a). In this case, the appropriate sanction is to declare the unlawful revocation void from the date it occurred. As the revocation was not effective, the debtor still has the right to do business in Illinois, subject to paying late charges and franchise taxes for the years 2003-2010 on the capitalization it has by virtue of confirmation of the plan.

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