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Proposed Counsel for Debtors-in-Possession

**UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK**

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In re:	:	Chapter 11
	:	
ADVANCE SCIENCE TECHNOLOGIES, INC., and FS-IP LLC,	:	Case No. 17-13668 (SMB)
	:	
Debtors. ¹	:	Joint Administration Requested
	:	
-----	X	

**DEBTORS’ MOTION FOR INTERIM AND FINAL ORDERS
PURSUANT TO SECTIONS 105(a), 362(a)(3), AND 541 OF THE
BANKRUPTCY CODE AND BANKRUPTCY RULE 3001 ESTABLISHING
NOTICE AND HEARING PROCEDURES FOR TRADING OF THE
BENEFICIAL OWNERSHIP OF RELATED PARTY EQUITY SECURITIES**

TO THE HONORABLE UNITED STATES BANKRUPTCY JUDGE:

Advance Science Technologies, Inc. (“*AST*”) and FS-IP LLC (“*FS-IP*”), as debtors and debtors-in-possession (collectively, the “*Debtors*”), respectfully represent:

PRELIMINARY STATEMENT

1. These chapter 11 cases are “prepackaged Chapter 11 case[s]” within the scope and definition set forth in Part II of the Guidelines for Prepackaged Chapter 11 Cases in the United States Bankruptcy Court for the Southern District of New York (the “*Guidelines*”)² as the

¹ The Debtors in these cases, along with the last four digits of each Debtor’s federal tax identification number, are: Advance Science Technologies, Inc. (6977); and FS-IP LLC (5674). Contemporaneously herewith, the Debtors have filed a motion requesting joint administration of the Debtors’ bankruptcy cases.

² Part II of Guidelines provides that “a ‘prepackaged Chapter 11 case’ is one in which the Debtor, substantially contemporaneously with the filing of its Chapter 11 petition, files a Confirmation Hearing

Debtors, contemporaneously with the filing of their respective chapter 11 petitions, filed, among other documents, the *Debtors' Joint Prepackaged Plan of Reorganization* (the "**Plan**") and *Information and Disclosure Statement* (the "**Disclosure Statement**"). All classes of creditors and shareholders entitled to vote accepted the Plan prior to the Petition Date (as defined herein).³ All other claims and equity interests are not impaired under the Plan.

2. This Motion seeks interim and final orders establishing notice and hearing procedures that must be satisfied before certain transfers of the beneficial ownership of equity securities in the Debtors' non-debtor parent entity Fortior Solutions, Inc. (f/k/a SureID, Inc.) ("**Fortior**") and in AST are deemed effective. This Motion seeks immediate entry of an interim order and is brought on an emergency basis to avoid immediate and irreparable harm to the Debtors' estates.

BACKGROUND

3. On the date hereof (the "**Petition Date**"), the Debtors each commenced with this Court a voluntary case (collectively, the "**Chapter 11 Cases**") under chapter 11 of title 11 of the United States Code (the "**Bankruptcy Code**"). The Debtors are authorized to continue to operate their businesses and manage their assets as debtors in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code. No trustee, examiner, or statutory committee of creditors has been appointed in these chapter 11 cases.

4. Prior to the Petition Date, the Debtors commenced and completed the solicitation of votes on the Plan, through its Disclosure Statement.

5. Additional factual background regarding the Debtors, including their business operations, corporate and capital structure, and the events leading to these chapter 11 cases, is set

Scheduling Motion for Prepackaged Plan in substantially the form annexed [to the Guidelines] as Exhibit A and satisfying the criteria set forth in Part III.A. below, Prepackaged Plan, disclosure statement (or other solicitation document), and voting certification."

³ Capitalized terms used but not otherwise defined herein shall have the meanings given to such terms in the Plan.

forth in the *Declaration of Sean Sullivan Pursuant to Local Bankruptcy Rule 1007-2, in Support of First Day Pleadings* (the “*Sullivan Declaration*”).

JURISDICTION AND VENUE

6. This Court has jurisdiction over these chapter 11 cases under 28 U.S.C. §§ 157 and 1334 and the Amended Standing Order of Reference from the United States District Court for the Southern District of New York, dated December 1, 2016. This matter constitutes a core proceeding under 28 U.S.C. § 157(b)(2).

7. Venue is proper in this district under 28 U.S.C. §§ 1408 and 1409.

8. The statutory predicates for the relief sought herein are sections 105(a), 362(a)(3), 363(c), and 541 of the Bankruptcy Code, and Bankruptcy Rules 3001.

RELIEF REQUESTED

9. As set forth in more detail in the Disclosure Statement, the Debtors have filed a prepackaged Plan that, if confirmed, will result in a change in ownership percentages for the Debtors’ non-debtor parent entity Fortior. A significant portion of the value of the Debtors on a reorganized basis is attributable to the potential future use of Fortior’s NOLs and Tax Attributes (both defined below). The Debtors are seeking to establish the notice and hearing procedures at this stage of the bankruptcy case in order to preserve the value of those NOLs under the Plan.

10. Further, as part of these prepackaged bankruptcies, the Debtors and Fortior entered into a *Restructuring Support Agreement* (the “**RSA**”).⁴ As described in the Disclosure Statement and exhibits thereto, as part of the RSA, SureID, Inc. changed its name to Fortior Solutions, Inc. (as previously defined, Fortior), and amended its articles of incorporation and bylaws to impose specified restrictions on the transfer of Fortior’s capital stock. Specifically, under the amended articles of incorporation, no shares of capital stock of Fortior may be sold, assigned, transferred or conveyed without the consent of Fortior’s Board of Directors.

⁴ The Debtors filed a separate motion seeking authority to assume the RSA.

11. The transfer restrictions contemplated under this Motion are consistent with the transfer restrictions that were expressly voted on, and approved by, Fortior's shareholders in conjunction with approval of the RSA. Here, the Debtors seek entry of an order, pursuant to sections 105(a), 362(a)(3) and 541 of the Bankruptcy Code, establishing notification and hearing procedures for certain transfers of the beneficial ownership of equity securities in Fortior or AST, including Options (defined below) to acquire such equity securities that must be complied with before such transfers of equity securities are deemed effective. The procedures for trading the beneficial ownership of Fortior's or AST's equity securities are necessary to protect and preserve the value of U.S. federal and state tax attributes, including but not limited to, net operating loss carryforwards ("*NOLs*" and, collectively with any capital losses, unrealized built-in losses and certain other tax and business credits and other tax attributes, the "*Tax Attributes*").

12. As of the Petition Date, Fortior had approximately (i) 26,084,660 voting common shares, (ii) 10,593,520 preferred series A shares, (iii) 9,004,480 preferred series B shares, and (iv) 1,111,110 nonvoting common shares outstanding. Under the Debtors' prepackaged Plan, there will be a change in ownership percentages for Fortior. Under the Plan, equity of Fortior will effectively be held by (a) the current shareholders of Fortior, (b) the Lenders and (c) Fortior's management team, with the Lenders effectively owning 25% of the equity interests in Fortior and Fortior's shareholders effectively owning the remaining balance. Up to 10% of the remaining balance of shares will be available for issuance to Fortior's senior management team and certain other key employees as non-voting incentive units pursuant to a long-term equity incentive plan.

13. The restrictions on trading proposed under terms of this Motion will bolster the trading restrictions under the RSA. Without trading restrictions on Fortior's and AST's equity securities, the ability to use Fortior's Tax Attributes could be reduced or eliminated, which could lead to significant negative consequences for the Debtors, their estates, creditors, stakeholders, and other parties in interest. To preserve, to the fullest extent possible, the flexibility to maximize the use of the Tax Attributes, the Debtors seek limited relief that will enable the Debtors to closely monitor certain transfers of the beneficial ownership of Fortior's and AST's equity

securities, so as to be in a position to act expeditiously if necessary to preserve their Tax Attributes. Thus, the Debtors request that this Court enter the proposed order submitted herewith, thereby preserving the status quo in this regard.

14. In addition, the Debtors request that this Court schedule a final hearing on the Motion to consider approval of the Motion on a final basis.

THE TAX ATTRIBUTES

15. Fortior generated, and is currently generating, a significant amount of Tax Attributes for U.S. federal income tax purposes. The Debtors estimate that Fortior has federal NOLs of approximately \$86 million that are available to offset future taxable income. By the Motion, the Debtors seek authorization to protect and preserve the value of Fortior's Tax Attributes, including, without limitation, Fortior's NOLs. While the value of Fortior's Tax Attributes is dependent upon the amount of Fortior's future taxable income that may be offset by the Tax Attributes before they expire, Fortior's NOLs and other Tax Attributes could translate into significant future tax savings for the reorganized Debtors.

16. Fortior's Tax Attributes are valuable to the Debtors' estates because after confirmation they may be beneficial to Reorganized AST, to be owned by the Senior Secured Lenders and their affiliates. This is one of the results of the negotiations leading to the prepackaged Plan; in exchange, among other things most of the ultimate equity ownership of Fortior will remain in the hands of Fortior's current equity holders. From there, the Debtors and these estates will benefit if Fortior can carry forward its Tax Attributes to reduce or eliminate future income tax liability. Accordingly, the Debtors benefit if Fortior can carry forward the NOLs and credits to reduce Fortior's future tax liability, thereby potentially increasing net after tax income and increasing the value of the reorganized Debtors. *See* 26 U.S.C. §§ 39, 172.

POTENTIAL LIMITATIONS ON THE USE OF FORTIOR'S TAX ATTRIBUTES

17. As a general matter, if a corporation undergoes an "ownership change," Section 382 ("**Section 382**") of title 26 of the United States Code, the Internal Revenue Code of

1986, as amended (the “**IRC**”), could severely limit or eliminate the corporation’s ability to use its NOLs and certain other tax attributes to offset future taxable income. *See* IRC § 382. Under Section 382, an ownership change occurs when the percentage, by value, of a company’s equity held by one or more persons each holding five percent or more of the stock (taking into account ownership attribution rules and, in certain cases, taking into account Options to acquire such stock) has increased by more than fifty percentage points over the lowest percentage of equity owned by such shareholders at any time during the preceding three-year period or since the last ownership change, as applicable (the “**Testing Period**”). *Id.* at § 382(g), (i), and (k). If there has been a prior ownership change, the Testing Period for determining whether another ownership change has occurred begins on the first day following the date of the prior ownership change. *Id.* § 382(i)(2). Section 383 of the IRC (“**Section 383**”) imposes a similar limitation on certain tax credits of a corporation. *Id.* § 383. For clarity, this discussion refers only to Section 382 but the rules, principles, and policies regarding Section 382 are also generally applicable to Section 383’s limit on a corporation’s use of credits after an ownership change and are incorporated by reference into Section 383 by the IRC and the Treasury Regulations promulgated thereunder. *See id.* § 383(e); 26 C.F.R. § 1.383-1(g) (2014).

18. The general purpose of Section 382 is to prevent a company with taxable income from reducing its tax obligations by acquiring control of another corporation with NOLs, net unrealized built-in losses (“**Built-in Losses**”) or certain other tax attributes. To achieve this objective, Section 382 limits the amount of taxable income that can be offset by a pre-change loss to an amount equal to the product of the long-term tax-exempt rate (as published monthly by the U.S. Department of the Treasury) as of the ownership change date and the value of the equity of the loss corporation immediately before the ownership change (a “**Section 382 Limitation**”).⁵

⁵ The Section 382 Limitation may be increased if the loss corporation has a net unrealized built-in gain at the time of the ownership change. *See* IRC § 382(h)(1)(A).

Built-in Losses recognized during the five-year period after the ownership change may be subject to similar limitations.

19. Certain provisions of Section 382 modify this general limitation as applied to the Debtors. For example, the limitations imposed by Section 382 in the context of a change of ownership that occurs pursuant to a confirmed chapter 11 plan are significantly more relaxed than the general limitation. See 26 U.S.C. § 382(1)(5) and (6).⁶ Additionally, the occurrence of such an ownership change would reset to zero the testing period and consequently reset the cumulative ownership change in Fortior's equity securities. Because of these provisions, an ownership change resulting from a transfer to Fortior's prepetition lenders pursuant to the Plan can be expected to maximize Fortior's ability to utilize its NOLs by (a) allowing the Debtors and Fortior to avail of the special bankruptcy-related rules under section 382 that would reduce the severity of the general limitation; (b) reducing the likelihood of an ownership change post-confirmation that would not qualify for such special bankruptcy-related rules, and thus would subject Fortior to the more severe general limitation; and (c) reducing the likelihood that Fortior would need to enforce transfer restrictions which will apply to its equity securities post-confirmation and which are intended to prevent a section 382 ownership change from occurring after the effective date of the Plan.

⁶ Under a safe harbor in section 382(1)(5) of the IRC that would apply if stockholders and "qualified creditors" (as determined in accordance with applicable rules under section 382 and the Treasury regulations promulgated thereunder) of the corporation undergoing an ownership change beneficially own stock, pursuant to such a plan of reorganization approved by the court, constituting at least 50% of the total combined value and voting power of equity interests in the corporation immediately after the ownership change, such corporation is not subject to the limitations imposed by section 382 with respect to that ownership change. Although section 382(1)(5) imposes no limitation, the entirety of the NOL carryforward can be lost if there is an ownership change in the two years following emergence from bankruptcy. Under section 382(1)(6), if a corporation experiences an ownership change pursuant to a confirmed plan and section 382(1)(5) does not apply (either because the corporation elects out of that provision or because its requirements are not satisfied), the appropriate value of the reorganized corporation's equity for the purposes of calculating the limitation under section 382 would reflect the increase in value of the reorganized company's equity resulting from the restructuring of creditor claims in the plan.

**PROPOSED PROCEDURES FOR TRADING OF THE BENEFICIAL
OWNERSHIP OF THE SECURITIES**

20. By establishing procedures for continuously monitoring the trading of the beneficial ownership of Fortior's and AST's equity securities, the Debtors and Fortior can preserve their ability to seek substantive relief at the appropriate time, particularly if it appears that additional trading of the beneficial ownership of Fortior's or AST's equity securities prior to the effective date of the Plan may result in an ownership change that would jeopardize the use of Fortior's Tax Attributes. Accordingly, the Debtors request that this Court enter the proposed order establishing the below procedures for trading of the beneficial ownership of Fortior's or AST's equity securities:⁷

- a) Any purchase, sale, or other transfer of the beneficial ownership of Fortior's or AST's equity securities in violation of the procedures set forth herein (including without limitation, the notice requirements below) shall be null and void *ab initio* as an act in violation of the automatic stay under sections 362 and 105(a) of the Bankruptcy Code;
- b) Any person or entity (as defined in Treasury Regulations Section 1.382-3(a)(1) (2014)) who currently is or becomes a Substantial Shareholder (as defined in paragraph (f) below) shall file with this Court and serve on the "Notice Parties" a notice of such status, in the form of **Exhibit 1** attached to the proposed order submitted herewith, on or before the later of (i) fourteen (14) calendar days after the date of entry of the Notice of Order (as defined below) and (ii) five (5) calendar days after becoming a Substantial Shareholder. "Notice Parties" means counsel for (i) the Debtors; (ii) the U.S. Trustee; (iii) any statutory committee(s); and (iv) Goldman Sachs Specialty Lending Group, L.P., as Administrative Agent for the Lenders under the Debtors' senior secured credit facility;
- c) At least thirty (30) calendar days prior to effectuating any transfer of the beneficial ownership of equity securities (including transfers or grants of Options to acquire or sell such securities, as defined below and transfer of such securities pursuant to the exercise of Options) that would result in an increase in the amount of Stock (as defined below) beneficially owned by a Substantial Shareholder or

⁷ With respect to the procedures set forth herein, the Debtors request that the Court permit the Debtors to waive, in writing and in their sole and absolute discretion, but in any event subject to the terms of the RSA, any and all restrictions, stays and notification procedures contained in the Motion or in any order entered with respect hereto should the Debtors conclude in their sole discretion that any such restriction, stay or notification procedure is not necessary to protect its Tax Attributes; *provided, however*, the Debtors shall provide notice of any such waiver to the Administrative Agent, the U.S. Trustee and any statutory committee in writing within three business days thereafter.

would result in a person or entity becoming a Substantial Shareholder, such Substantial Shareholder (or person or entity that may become a Substantial Shareholder) shall file with this Court and serve on the Notice Parties advance written notice, in the form of **Exhibit 2** attached to the proposed order submitted herewith, of the intended transfer of the beneficial ownership of equity securities;

- d) At least thirty (30) calendar days prior to effectuating any transfer of the beneficial ownership of equity securities (including transfers or grants of Options to acquire or sell such securities, as defined below and transfer of such securities pursuant to the exercise of Options) that would result in a decrease in the amount of Stock beneficially owned by a Substantial Shareholder or would result in a person or entity ceasing to be a Substantial Shareholder, such Substantial Shareholder shall file with this Court and serve on the Notice Parties advance written notice, in the form of **Exhibit 3** attached to the proposed order submitted herewith, of the intended transfer of the beneficial ownership of equity securities (the notices required to be filed and served under paragraph (c) and this paragraph (d), each a “*Notice of Proposed Transfer*”);
- e) The Debtors shall have thirty (30) calendar days after receipt of a Notice of Proposed Transfer to file with this Court and serve on such Substantial Shareholder (or person or entity that may become a Substantial Shareholder) an objection to any proposed transfer of the beneficial ownership of equity securities described in the Notice of Proposed Transfer on the grounds that such transfer may adversely affect the Debtors’ ability to utilize the Tax Attributes. If the Debtors file an objection, such transaction will not be effective unless approved by a final and non-appealable order of this Court. If the Debtors do not object within such 30-day period, such transaction may proceed solely as set forth in the Notice of Proposed Transfer. Further transactions within the scope of this paragraph (e) must be the subject of additional notices as set forth herein, with an additional 30-day waiting period; and
- f) For purposes of these procedures, (A) a “*Substantial Shareholder*” is any person or entity (as defined in Treasury Regulations Section 1.382-3(a)) which beneficially owns at least 4.5% of any issued and outstanding common or preferred shares of Fortior Solutions, Inc. (f/k/a SureID, Inc.) or of Advance Science Technologies, Inc. (the “*Stock*”), and (B) “beneficial ownership” (or any variation thereof of the Stock and Options to acquire the Stock) shall be determined in accordance with applicable rules under Section 382, Treasury Regulations promulgated thereunder and rulings issued by the Internal Revenue Service, and thus, to the extent provided therein, from time to time shall include, without limitation, (i) direct and indirect ownership (e.g., a holding company would be considered to beneficially own all shares owned or acquired by their subsidiaries); (ii) ownership by the holder’s family members and persons acting in concert with the holder to make a coordinated acquisition of stock; and (iii) ownership of an Option to acquire the Stock, but only to the extent such Option is treated as exercised under Treasury Regulation section 1.382-4(d). An “*Option*” to acquire stock includes any contingent purchase, warrant, convertible debt, put,

stock subject to risk of forfeiture, contract to acquire stock, or similar interest, regardless of whether it is contingent or otherwise not currently exercisable.

21. To ensure parties in interest receive appropriate notice of the procedures for trading of the beneficial ownership of the equity securities, the Debtors request that this Court approve the following provisions.

22. Following entry of the Interim Order, the Debtors propose to send a notice in substantially the form attached to the proposed order submitted herewith as **Exhibit 4** (the “*Notice of Order*”) to: (i) U.S. Trustee; (ii) all creditors of the Debtors; (iii) all parties entitled to notice pursuant to Local Rule 2002; (iv) any directly registered holders of the Stock; (v) any record holders (i.e., banks, brokers, intermediaries, other nominees or their mailing agents (collectively, the “*Nominees*”) of the Stock; and (vi) the transfer agent(s) for the Stock.

23. Upon receipt of the Notice of Order, the Nominees shall serve the Notice of Order to any beneficial holders by no later than five (5) business days after being served with the Notice of Order. Additionally, any person or entity or broker or agent acting on such person or entity’s behalf who sells an aggregate amount equal to 4.5% of any class of issued and outstanding shares of the Stock (or an Option with respect thereto) to another person or entity will be required to provide a copy of the Notice of Order to such purchaser of such Stock or to any broker or agent acting on such purchaser’s behalf.

BASIS FOR RELIEF REQUESTED

24. Courts have uniformly held that a debtor’s NOLs constitute property of the estate under section 541 of the Bankruptcy Code and, as such, courts have the authority to implement certain protective measures to preserve the NOLs. The seminal case articulating this rule is *Prudential Lines*, in which this court held that a “debtor’s potential ability to utilize NOLs is property of an estate.” *Official Comm. of Unsecured Creditors v. PSS Steamship Co. (In re Prudential Lines, Inc.)*, 107 B.R. 832, 838 (Bankr. S.D.N.Y. 1989); *see also Nisselson v. Drew Indus., Inc. (In re White Metal Rolling & Stamping Corp.)*, 222 B.R. 417, 424 (Bankr. S.D.N.Y. 1998) (“It is beyond peradventure that NOL carrybacks and carryovers are property of the estate

of the loss corporation that generated them.”). Because Fortior’s NOLs will inure to the benefit of the Debtors under terms of the prepackaged Plan and Fortior is a co-proponent of the Plan, this Court has the authority under section 362 of the Bankruptcy Code to enforce the automatic stay by restricting the transfer of the Debtors’ equity securities that could jeopardize the existence or value of this asset. *See In re Phar-Mor, Inc.*, 152 B.R. 924, 927 (Bankr. N.D. Ohio 1993) (holding that section 362 of the Bankruptcy Code prohibited the sale of stock in the debtors as an exercise of control of the debtors’ NOLs, which were property of the debtors’ estates).

25. The requested relief does not bar all trading of the beneficial ownership of Fortior’s or AST’s equity securities. The Debtors seek to establish procedures enabling them only to monitor those types of trading of the beneficial ownership of Fortior’s or AST’s equity securities that pose a serious risk under the Section 382 ownership change test, so as to preserve the Debtors’ ability to seek substantive relief if it appears that a proposed trade of equity securities will jeopardize the use of the Tax Attributes. The procedures requested by the Debtors in this Motion would permit most trading of the beneficial ownership of Fortior’s or AST’s equity securities to continue subject only to applicable securities, corporate, and other laws (including the restrictions approved under terms of the RSA).

26. Accordingly, the Debtors respectfully request that the Court enter the proposed interim final orders approving the procedures to protect the Debtors against the possible loss of Fortior’s Tax Attributes, including the NOLs.

NECESSITY FOR IMMEDIATE RELIEF

27. Bankruptcy Rule 6003 provides that “Except to the extent that relief is necessary to avoid immediate and irreparable harm, the court shall not, within 21 days after the filing of the petition, grant ... (b) a motion to use, sell, lease or otherwise incur an obligation regarding property of the estate, including a motion to pay all or part of a claim that arose before the filing of the petition ...” As stated above and in the Sullivan Declaration, transfer of Fortior’s or AST’s equity securities prior to the Effective Date of the Plan may result in an ownership change that

would seriously jeopardize the use of the Tax Attributes. Therefore, the Debtors submit that any delay in either granting the relief requested in this Motion could result in severe, immediate, and irreparable harm to the Debtors and their estates. Accordingly, an order granting this Motion should be entered immediately under Bankruptcy Rule 6003(b), with a waiver of the fourteen-day stay imposed by Bankruptcy Rule 6004(h).

NOTICE

28. Notice of this Motion will be provided to: (i) the attorneys for Goldman Sachs Specialty Lending Group, L.P., as administrative agent for the Debtors' principal secured lenders, (ii) all creditors of the Debtors, (iii) the U.S. Trustee, and (iv) all parties who have requested notice in these chapter 11 cases pursuant to Bankruptcy Rule 2002. In light of the nature of the relief requested herein, no other or further notice is necessary.

NO PRIOR REQUEST

29. No previous request for the relief sought herein has been made to this Court or any other court.

CONCLUSION

30. For the foregoing reasons, the Debtors respectfully request that the Court enter interim and final orders, substantially in the form attached to this Motion.

Dated: December 29, 2017
New York, New York

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