

IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE SOUTHERN DISTRICT OF TEXAS  
HOUSTON DIVISION

IN RE: § Chapter 11  
§  
LUCA INTERNATIONAL GROUP LLC<sup>1</sup> § CASE NO. 15-34221-H2-11  
§  
Debtors. § Joint Administration Pending  
§ Judge David R. Jones  
§

**EMERGENCY MOTION SEEKING AN ORDER AUTHORIZING DEBTORS’  
PAYMENT OF PRE-PETITION CRITICAL VENDORS IN AN AMOUNT LESS THAN  
\$213,941.97**

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**THIS MOTION SEEKS AN ORDER THAT MAY ADVERSELY AFFECT YOU. IF YOU OPPOSE THE MOTION, YOU SHOULD IMMEDIATELY CONTACT THE MOVING PARTY TO RESOLVE THE DISPUTE. IF YOU AND THE MOVING PARTY CANNOT AGREE, YOU MUST FILE A RESPONSE AND SEND A COPY TO THE MOVING PARTY. YOU MUST FILE AND SERVE YOUR RESPONSE WITHIN 23 DAYS OF THE DATE THIS WAS SERVED ON YOU. YOUR RESPONSE MUST STATE WHY THE MOTION SHOULD NOT BE GRANTED. IF YOU DO NOT FILE A TIMELY RESPONSE, THE RELIEF MAY BE GRANTED WITHOUT FURTHER NOTICE TO YOU. IF YOU OPPOSE THE MOTION AND HAVE NOT REACHED AN AGREEMENT, YOU MUST ATTEND THE HEARING. UNLESS THE PARTIES AGREE OTHERWISE, THE COURT MAY CONSIDER EVIDENCE AT THE HEARING AND MAY DECIDE THE MOTION AT THE HEARING.**

**REPRESENTED PARTIES SHOULD ACT THROUGH THEIR ATTORNEYS.**

**EMERGENCY CONSIDERATION OF THIS MOTION HAS BEEN GRANTED. BECAUSE THE COURT WILL CONSIDER THE MOTION ON AN EMERGENCY BASIS, YOU WILL HAVE LESS THAN 23 DAYS TO ANSWER. IF YOU OBJECT TO THE REQUESTED RELIEF OR IF YOU BELIEVE THAT THE EMERGENCY CONSIDERATION IS NOT WARRANTED; YOU SHOULD FILE AN IMMEDIATE RESPONSE.**

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**TO THE HONORABLE UNITED STATES BANKRUPTCY COURT:**

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<sup>1</sup> The Debtors in these cases, along with the last four digits of their respective taxpayer ID numbers, are Luca International Group LLC (1086), Luca Operation, LLC (0343), Luca International Group (Texas) LLC (5577), Luca Barnett Shale Joint Venture, LLC (5340), Luca Energy Fund LLC (0677), Luca Energy Resources, LLC (0000), Luca Resources Group, LLC (1699), Luca I, LP (4104), Luca II, LP, (9778), Luca Oil, LLC (8161), Luca To-Kalon Energy LLC (3922), Luca Oil II Joint Venture (6604).

Luca International Group LLC (“LIG”), Luca International Group (Texas) LLC (“LIGTX”), Luca Operation, LLC (“LOL”), Luca Barnett Shale Joint Venture, LLC (“LBSJV”), Luca Energy Fund LLC (“LEF”), Luca Energy Resources, LLC (“LER”), Luca Resources Group, LLC (“LRG”), Luca I, LP (“Luca I”), Luca II, LP (“Luca II”), Luca Oil, LLC (“Luca Oil”), Luca To-Kalon Energy, LLC (“LTKE”), and Luca Oil II Joint Venture (collectively “Debtors”), (collectively “Debtors”), file this Emergency Motion Seeking an Order Authorizing Debtors’ Payment of Pre-Petition Critical Vendors in an Amount Less Than \$213,941.97 and show the following:

**I. Jurisdiction**

1. This Court has jurisdiction by virtue of 28 U.S.C. §§ 157 and 1334. This matter is a core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A).

**II. Venue**

2. Venue is proper in this district pursuant to 28 U.S.C. § 1408(1) because the Debtor’s principal places of business have been located in this district for more than 180 days preceding the filing of these bankruptcy cases.

**III. Background Information**

3. The above captioned bankruptcy cases were each filed on August 6, 2015 (collectively “Petition Date”), under Chapter 11 of Title 11 of the Bankruptcy Code, 11 U.S.C. §§101 *et seq.* (the “Bankruptcy Code”). The Debtors continue to manage their property as debtors-in-possession pursuant to §§ 1107 and 1108 of the Bankruptcy Code. A Motion seeking joint administration of these cases was filed on August 6, 2015 (Docket #2) and remains pending before the Court.

4. No trustee or examiner has been appointed in the Debtors’ bankruptcy cases and

no official committee of unsecured creditors has been established.

5. A detailed factual background of the Debtors' business and operations, as well as the commencement of these Chapter 11 cases, is more fully set forth in the *Affidavit of Loretta R. Cross in Support of the Debtors' Chapter 11 Petitions and Requests for First-Day Relief* filed contemporaneously herewith and incorporated herein by reference. A brief summary of the factual background is listed below.

6. The Debtors are engaged in the exploration and production of natural gas, petroleum and related hydrocarbons. Bingqing Yang ("Yang") is the sole member for Debtors. Debtors obtained money from investors that was placed into various entities and were utilized in the operations of other entities.

7. LOL and LIG have a draft reserve report that was prepared in March by Gustavson Associates. The reserve report indicates that LOL has proved developed non-producing and proved behind pipe net reserves of approximately 3.2 billion cubic feet of gas and 450 million barrels of oil. The reserve report did not address proved undeveloped, probable or possible reserves.

8. On July 6, 2015, under Case No. 15-cv-03101, the Securities and Exchange Commission ("SEC") filed a lawsuit against several LUCA entities, including the Debtors, other Debtor affiliates, Yang and certain other individuals in the United States District Court of the Northern District of California, San Francisco Division ("SEC lawsuit"). The SEC lawsuit alleged securities fraud against the defendants for a scheme targeting the Chinese American community as well as investors in Asia to invest in the various unregistered offerings. There are SEC allegations of funds being used for Bingqing Yang's personal expense. The SEC has sought the appointment of a receiver, and this matter remains pending.

9. In order to restore credibility to the operation, the Debtors, pursuant to various consents executed by Yang, retained Loretta R. Cross of Stout Risius Ross, Inc. as Chief Restructuring Officer (the “CRO”) of the Debtors with full authority to operate the Debtors. Ms. Cross has served in that capacity since July 16, 2015.

### **III. Property & Operations**

10. Debtors are engaged in the exploration and production of natural gas, petroleum and related hydrocarbons. The primary assets are located in Iberville and Ascension Parishes in Louisiana. These assets include 3 operating oil and gas wells – Belle Grove 1, Dugas & Leblanc 1 and Jumonville 2. In addition, the assets include a water disposal well, Acosta 1, and a shut-in oil and gas well, Jumonville 1. The Luca entities also own oil and gas leases in Texas and working interests in various locations.

11. LOL and LIG have a draft reserve report that was prepared in March by Gustavson Associates. The reserve report indicates that the Debtors have proved developed non-producing and proved behind pipe net reserves of approximately 3.2 billion cubic feet of gas and 450 million barrels of oil. The reserve report did not provide an estimated value for proved undeveloped, probable or possible reserves.

### **IV. Debt**

12. Liens. Over \$500,000 of liens have been placed against the Belle Grove #1 well.

13. Unsecured debt. Collectively, the Debtors’ records show more than \$10,000,000 of unsecured debt. LOL has accounts payable of approximately \$2.1 million. The Critical Vendors, as discussed further below, are owed approximately \$316,755.91.

### **V. Relief Sought**

14. The Debtors request that the Court enter an order approving Debtors' payment of \$213,941.97 or 68% of the total estimated amount owed to these Critical Vendors. Many of the vendors provide critical safety and environmental services, the loss of which could expose the Debtors to significant remediation liability and compliance costs. Also, the vendors have liens or the right to file liens, which are not barred by the automatic stay. The following table summarizes the estimated total amount due to each Critical Vendor, the requested amount and the ratio of requested amount to estimated total amount due.

Critical Vendors			
Vendor	Est. Amount Due	Proposed Payment	% of Est.
Coastal Chemical Co. LLC	\$ 2,181.01	\$ 2,181.01	100%
Core Laboratories, LP	4,167.00	4,167.00	100%
DNOW L.P.	9,108.17	9,108.17	100%
F.A.S. Environmental Services, LLC	56,014.00	41,912.00	75%
Global Logistics, LLC	14,175.95	10,000.00	71%
Gustavson Associates, LLC	20,035.75	20,035.75	100%
Ingo Energy, LLC	5,031.00	5,031.00	100%
Ingo Gauging Services, LLC	30,855.62	30,855.62	100%
K-J Company, Inc.	2,000.00	2,000.00	100%
Ranger Specialty & Supply	651.42	651.42	100%
Ric Bajon & Associates, LLC	<u>172,535.99</u>	<u>88,000.00</u>	<u>51%</u>
	\$ 316,755.91	\$ 213,941.97	68%

15. **Coastal Chemical Co. LLC** provides oilfield chemicals analysis and supplies to the Debtors. Coastal Chemical provides analysis of the bacteria and other contaminants in water produced by each well. Using this analysis, Coastal Chemical develops a treatment program for the water that complies with environmental regulations and minimizes the growth of bacteria. Bacteria can clog disposal wells and limit the Debtors' ability to dispose of water as it is produced. The Debtors have a limited amount of storage for produced water and could be forced to shut in the producing wells without an efficiently operating disposal well.

16. **Core Laboratories, LP** provides storage of valuable gas and condensate

samples from the Debtors' wells. Core Laboratories is the sole provider of secure, high pressure storage for flammable fluids and gases. In addition, these sample are used for production tests, reservoir analysis and will be used in the Debtor's planned asset marketing efforts. The Debtors are at risk of Core Laboratories disposing of the samples unless a payment is released.

17. **DNOW LP** provides oil field parts and services critical to the maintenance of the wells. Lost production time leads directly to lost production and lost revenue. Furthermore, it is the closest large, diverse source of needed parts. Switching to an alternative vendor would increase delivery times and transportation costs.

18. **FAS Environmental** is a critical supplier of emergency response services as well as water hauling and disposal services. The long-standing relationship with FAS Environmental, coupled with their willingness to work with Luca despite a poor credit rating, makes replacing them extremely difficult. The Debtors believe it would be very difficult to contract with another company that provides "first responder" services given the Debtors' reputation in the marketplace. In addition, FAS Environmental owns a nearby water disposal well that the Debtors have used when the Acosta well is out of service. Other third party water disposal sites are farther away and have higher transportation costs.

19. **Global Logistics, L.L.C.** provides environmental and regulatory consultants who advise, and offer guidance about complying with local, state, and national environmental regulations. Global Logistics also handles necessary reporting to local, state, and national environmental entities. This vendor has an extensive background with knowledge of the company that make them expensive to replace.

20. **Gustavson Associates** prepares the annual, independent, reserves report. Replacing this vendor with another reserve engineering firm would lead to unnecessary

duplication of well analyses and modeling. The Debtors will save money by paying the pre-petition invoice for services related to drafting the March reserve report and engaging Gustavson to update the report with current information. An alternative firm would require several weeks to develop an understanding of the wells and reserves before beginning to prepare an estimate of the value. The Debtors intend to begin marketing the properties as soon as a revised report is complete. Any delays will lead to higher, burdensome, administrative expenses.

21. **Ingo Energy, LLC** and **Ingo Gauging Services** provide water hauling services critical to production and pumping and gauging services necessary for production at wells. Ingo has years of familiarity with the properties and a deep understanding of the mechanical systems in place. Replacing this vendor would require the new vendor to spend a considerable amount of time developing a familiarity with the systems and lead to higher costs for the Debtors. Gary Ingo is one of the Debtors' emergency contacts and is available to respond to and alleviate emergency situations in the field.

22. **K-J Company, Inc.** serves as regulatory/compliance consultants, as well as file necessary reporting with the appropriate government bodies in order to continue production. This vendor's deep familiarity with the Debtors and properties makes replacing K-J Company a long, expensive process.

23. **Ranger Specialty** provides a satellite-linked alarm system essential to the safe and proper operations of the Debtors' wells. The Debtors do not have an employee in the field and require remote monitoring of the production systems. Ranger Specialty's system monitors well pressures, oil levels in the storage tanks, and provides fire detection. In the event of an incident, the system immediately alerts Dale Weatherbee, the Debtors' Chief Operating Officer, and Gary Ingo of Ingo Energy and Ingo Gauging, among others, so that the Debtors can prepare

a response. Prompt responses to leaks or pressure changes in the wells will minimize the likelihood of accidents and reduce or limit remediation costs. Ranger Specialty's sensors are an integral part of the production equipment and replacing this system would be an unnecessary burden on the estate.

24. **Ric Bajon & Associates, LLC** provides leasing and land services. The company possesses extensive on-the-ground, local experience, and their familiarity with properties, assets, and leases is critical to completing the water disposal well operating agreements. This firm is a familiar middleman between the landowners and the Debtors. Replacing them would require a new landman to develop relationships with each of the 28 different parties involved in the disposal well agreements, delaying completion of this important contract and requiring the Debtors' to continue using trucks to haul salt water to third party disposal sites. In addition, Ric Bajon and Associates are in the process of recording several signed leases. Unless the leases are recorded in the appropriate parish clerk's records, the Debtors will be unable to transfer the leases as part of the intended asset sale.

#### **VI. Circumstances Justifying Request to Pay Vendors**

25. The Debtors believe that the goods and services supplied by the vendors are critical to their operations in that their businesses could not continue to operate without access to such goods and services. As of the Petition Date, many of the vendors deemed critical by the Debtors have outstanding claims against the Debtors arising from pre-petition deliveries of goods and pre-petition performance of services. The Debtors anticipate they will be able to continue to transact with a majority of the vendors on which their day-to-day business operations depend despite non-payment by the Debtors of such vendors' pre-petition claims. Non-payment of the pre-petition claims of certain of the Debtors' vendors, however, creates a significant risk of

disruption to the Debtors' operations. Thus, the Debtors anticipate there will be instances in which payment of the pre-petition claims of certain vendors will benefit all creditors because such payment will allow the Debtors' businesses to avoid a likely loss, or to gain a likely economic advantage, disproportionate to the amount of such vendors' pre-petition claims.

26. In preparation for filing their Chapter 11 cases, the Debtors evaluated goods and services vendors likely to have outstanding claims against the Debtors as of the Petition Date. The Debtors analyzed whether there were any providers of goods and services that are critical to their ability to operate their businesses. The Debtors distinguished the vendors as "**Critical Vendors**" according to the following criteria:

(a) Whether (i) the goods and services supplied by a particular vendor are essential to the continued operation of the Debtors' businesses and cannot be obtained from any other vendor, or, could be obtained from another vendor only at such extra cost or at such delay as to outweigh the cost of paying the pre-petition claim, or (ii) whether the vendor was in possession of valuable property of the Debtors that is necessary to their ability to generate revenue;

(b) Whether the cost of paying the pre-petition claim of such vendor, to the extent that such claim is fixed, non-contingent, liquidated, and undisputed (the "**Critical Vendor Claim**"), is outweighed by the benefit such payment is likely to secure on behalf of the Debtors' estates and other creditors; and

(c) Whether such vendor would likely continue doing business with the Debtors notwithstanding non-payment of pre-petition claims, such as those vendors subject to long-term, non-terminable contractual commitments.

27. According to the above criteria, the Debtors were able to distinguish, from the

numerous vendors with whom the Debtors deal, a small group of vendors that the Debtors deem to be Critical Vendors. These vendors provide goods and services to the Debtors necessary to maintain and otherwise perform critical functions related to operation of the oil and gas wells. Certain of the Critical Vendors are relatively small companies and any one payment by the Debtors could represent a significant portion of their income.

28. The Debtors perceive a risk that, for certain of their Critical Vendors, a default by the Debtors would extinguish the Debtors' access to necessary goods and services, (a) because the vendor will refuse to continue doing business with the Debtors if its pre-petition claim remains unpaid, or (b) because the vendor may choose to continue doing business with the Debtors only upon the condition that the Debtors provide trade term accommodations such as advance deposits or payment by wire transfer prior to delivery. Alternatively, the Debtors believe that vendors in possession of the Debtors' property may assert liens on such property and/or will not return such property to the Debtors in the ordinary course of business as long as their pre-petition claims remain unpaid.

29. The Debtors anticipate that there may be instances in which the Debtors will require authority to pay the pre-petition claim of a Critical Vendor that has refused to continue to deal with the Debtors, that is at risk of going out of business, or that has demanded trade term accommodations the Debtors cannot meet, because the Debtors will be unable to operate their businesses or an arm thereof without the goods and supplies provided by such Critical Vendor. The Debtors feel they will not be able to fulfill their duty to their estates and creditors to preserve the value of their businesses without the authority to pay the pre-petition claims of those vendors the Debtors have identified as Critical Vendors as and when such payments prove necessary.

## VII. Authority

30. A bankruptcy court may authorize the payment of prepetition obligations when necessary to facilitate a debtor's reorganization. *See, e.g., In re Equalnet Communications Corp.*, 258 B.R. 368 (Bankr. S.D. Tex. 2000). This authority stems from the common-law "necessity of payment" doctrine, which courts have applied when the failure to pay prepetition obligations poses a real and significant threat to a debtor's reorganization. *See Dudley v. Mealey*, 147 F.2d 268 (2d Cir. 1945), *cert. denied* 325 U.S. 873 (1945). In a well-established line of cases, this doctrine was first applied in conjunction with railroad reorganizations. *See, e.g., Gregg v. Metropolitan Trust Co.*, 197 U.S. 183 (1905) ("the payment of the employees of the [rail]road is more certain to be necessary in order to keep it running than payment of any other class of previously incurred debt"); *Miltenberger v. Logansport, Crawfordsville & Southwestern Railway Co.*, 106 U.S. 286 (1882) (permitting the payment of pre-receivership claim prior to reorganization in order to prevent the cessation of "indispensable business relations").

31. The "necessity of payment" doctrine was eventually expanded beyond railroad reorganizations, beginning with *Dudley v. Mealey*. 147 F.2d 268. In *Dudley*, the court held that the creditors' interest in continuing the debtor's hotel business justified paying the prepetition claims of creditors who furnished supplies essential to keeping the hotel open. *Id.* at 271. Numerous courts have applied *Dudley's* doctrine in situations similar to this case, recognizing that the payment of certain prepetition wage, salary, medical-benefit, and business-expense claims was justified since no business debtor can hope to reorganize without the cooperation of its employees. *In re Ionosphere Clubs, Inc.*, 98 B.R. 174, 175-76 (Bankr. S.D.N.Y. 1989).

32. The modern analogue to the "necessity of payment" doctrine appears in Section 105(a) of the Bankruptcy Code, which provides, in pertinent part: "[t]he court may issue any

order, process, or judgment that is necessary or appropriate to carry out the provisions of this title.” 11 U.S.C. § 105(a). Debtors respectfully submit, this includes the power to authorize the payment described above.

**Prayer**

The Debtors pray that the Court enter an order approving Debtors payment of \$213,941.97 or 68% to the above-listed Critical Vendors and for further and such relief as the Court deems appropriate.

DATED: August 6, 2015

Respectfully submitted,

HOOVER SLOVACEK LLP

*/s/ Brendetta A. Scott*

By: \_\_\_\_\_

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