

1 Cara J. Hagan, Bar No. 146665
2 Andrea M. Dumond, Bar No. 258948
3 HAGAN & ASSOCIATES
4 110 E. Wilshire Avenue, Suite 405
5 Fullerton, California 92832
6 Telephone: (714) 526-3377
7 Facsimile: (714) 526-3317
8
9 Attorneys for Creditor,
10 PNL POMONA, L.P.

11
12 **UNITED STATES BANKRUPTCY COURT**
13 **CENTRAL DISTRICT OF CALIFORNIA**

14 *In Re*) CASE NO. 1:09-bk-13356-KT
15)
16)
17 MERUELO MADDUX PROPERTIES, INC.)
18) Chapter 11
19 Debtor.) **OBJECTION OF PNL POMONA, L.P.**
20) **TO ADEQUACY OF DEBTOR'S**
21) **DISCLOSURE STATEMENT FOR ITS**
22) **JOINT AND CONSOLIDATED PLAN OF**
23) **REORGANIZATION**
24 PNL POMONA, L.P., a Delaware limited)
25 partnership,)
26)
27 Plaintiff,)
28 vs.) Date: June 14, 2010
Time: 9:30 a.m
MERUELO MADDUX PROPERTIES, INC., a)
California corporation,)
Defendants.)

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

TABLE OF CONTENTS

I. INTRODUCTION -1-

II. FACTS RELEVANT TO PNL -2-

 A. The Loan -2-

 B. Status of the Property. -3-

III. LEGAL ARGUMENT -3-

 A. The Debtor’s Disclosure Statement Fails to Provide “Adequate Information,” as Required by Section 1125 of the Bankruptcy Code. -3-

 1. The Value of the Properties is Lacking. -4-

 2. There Is No Discussion Of Marketing or Ability to Sell. -5-

 3. Debtors Intend to Use Insurance Proceeds as Interest Payments. -6-

 4. \$10 Million Is Simply Not Enough Money to Satisfy All These Debts. -6-

 5. Balloon Payments. -7-

 6. Debtors Suggests Payment From Unlikely Sources Without Explanation. -8-

 7. The Eminent Domain Proceeding is Not Addressed. -8-

 8. The Issues of Consolidation. -9-

 B. The Plan and Disclosure Statement Violates Ninth Circuit Law By Providing For An Injunction and Discharge of Non-Debtor Parties.. -9-

 C. The Plan Is Unconfirmable and Hence The Disclosure Statement Should Not Be Approved. -10-

 1. The Plan Unfairly Discriminates Against PNL. -11-

 2. The Plan Violates the Absolute Priority Rule. -11-

 The settlement with the Tax Assessor. -12-

 The settlements with other Creditors. -12-

The New Value Argument. -12-

 3. The New Value Contribution is Inadequate as a Matter of Law. -14-

 4. The Plan Does Not Provide Secured Creditors with the Indubitable

1		Equivalent of Their Secured Claims.	<u>-15-</u>
2	5.	The Plan Classifies Claims in An Improper Attempt to Gerrymander Voting for Purposes of Cramdown.	<u>-16-</u>
3			
4	D.	The Loan Modification Documents are Inappropriate.	<u>-16-</u>
5	IV.	CONCLUSION.	<u>-17-</u>
6			
7			
8			
9			
10			
11			
12			
13			
14			
15			
16			
17			
18			
19			
20			
21			
22			
23			
24			
25			
26			
27			
28			

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

TABLE OF AUTHORITIES

STATUTES

11 U.S.C. §1125 1, 3, 8
 11 U.S.C. §1129 11, 15

CASES

Bank of America National Trust & Savings Ass’n v. 203 North LaSalle Street Partnership
 526 U.S. 434, 119 S.Ct. 1411, 143 L.Ed2d 607 (1999) -12, 13, 14-

Bonner Mall Partnership v. U.S. Bancorp Mortgage Co., (In re Bonner Mall Partnership)
 2 F.3d 899 (9th Cir. 1993) -12-

Byrsan Properties XVIII, 961 F.2d 496 (4th Cir. 1992) -16-

In re American Hardwoods, 885 F.2d 621, 626 (9th Cir. 1989) -9-

In re Applegate Property, Ltd., 133 B.R. 827, 829 (Bankr. W.D. Tex. 1991) -4-

In re Armstrong World Indus., Inc., 432 F.3d. 507 (3d Cir. 2005) -11-

In re Bjolmes Realty Trust, 134 B.R. 1000, 1002 (Bankr. D. Mass. 1991) -10-

In re Brandon Mills Farms, Ltd., 37 B.R. 190, 192 (Bankr. N.D. Ga. 1984) -1-

In re California Fidelity, Inc., 198 B.R. 567, 571 (9th Cir. BAP 1996) -4-

In re Cardinal Congregate I, 121 B.R. 760, 766-67 (Bankr. S.D. Ohio 1990) -1-

In re Crowthers McCall Pattern, Inc., 120 B.R. 279, 300 (Bankr. S.D.N.Y. 1990) -4-

In re Dakota Rail, Inc., 104 B.R. 138, 143 (Bankr. D. Minn. 1989) -4-

In re Felicity Assocs., Inc. 197 B.R. 12, 14 (Bankr. D.R.I. 1996) -10-

In re Genesse Cement, Inc., 31 B.R. 442, 443-44 (Bankr. E.D. Mich. 1983) -10-

In re Global Ocean Carriers, Ltd., 251 B.R. 31 (Bankr. D. Del. 2000) -14-

In re Greystone III Joint Venture, 102 B.R. 560, 575 (Bankr. W.D. Tex. 1989) -14, 16-

In re Hirt, 97 B.R. 981, 983 (Bankr. E.D. Wis. 1989) -1-

In re Kehn Ranch, Inc., 41 B.R. 832-832-33 (Bankr. D.S.D. 1984) -10-

In re Kemp, 134 B.R. 413 (Bankr. E.D. Cal. 1991) -10-

In re Lowenschuss, 67 F.3d 1394, 1401 (9th Circuit 1995) -9-

1 *In re Lumber Exchange Ltd. Partnership*, 126 B.R. 1000 (Bankr. D. Minn. 1991) -16-
2 *In re Main St. AC, Inc.*, 234 B.R. 771, 775 (Bankr. N.D. Cal. 1999) -10-
3 *In re McCall*, 44 B.R. 242, 243 (Bankr. E.D. Pa. 1984) -10-
4 *In re Murel Holding Corp.*, 75 F.2d 941 (2nd Cir. 1935) -15-
5 *In re Pect*, 53 B.R. 768 (Bankr. E.D. Va. 1985) -10-
6 *In re Revco D.S., Inc.*, 131 B.R. 615, 620 (Bankr. N.D. Ohio 1990) -10-
7 *In re Rusty Jones, Inc.*, 110 B.R. 362, 373 (Bankr. N.D. Ill. 1990) -10-
8 *In re Sandy Ridae Development Corporation*, 881 F.2d 1346, 1350 (5th Cir. 1989) -15-
9 *In re Sea Garden Motel and Apartment*, 195 B.R. 294, 301 (D.N.J. 1996) -14-
10 *In re Unichem Corp.*, 72 B.R. 95, aff'd, 80 B.R. 448 (Bankr. N.D. Ill. 1987) -10-
11 *In re Weiss-Wolf, Inc.*, 59 B.R. 653, 656 (Bankr. S.D.N.Y. 1986) -10-
12 *Pecht*, 53 B.R. at 769-70 -10-

13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

MEMORANDUM OF POINTS AND AUTHORITIES

I. INTRODUCTION

PNL Pomona, LP (hereinafter “PNL”) submits this objection to Meruelo Maddux Properties, Inc. (“MMPI”) Second Amended Disclosure Statement. Many of these issues have been raised as a part of the previous objections and remain issues at this point. Further, many of these issues were raised as a part of the “Dear Judge” process which was already submitted to the court. However, for clarity, PNL has presented all of these issues again herein.

MMPI and its related debtor entities (collectively “Debtors”) request that this Court approve this amended disclosure statement even though this Disclosure Statement continues to fail to provide insufficient information as required under 11 U.S.C. §1125 and sets forth a Chapter 11 Plan of Reorganization (“the “Plan”) which is patently unconfirmable. While this statement has addressed several of the issues raised during the last hearing, it still fails to address many of the concerns raised. All relevant statutory authority and prevailing case law mandates that this Court deny approval of this Amended Disclosure Statement. PNL therefore seeks an Order of the Court denying the approval of the Disclosure Statement.

It must be asserted that the purpose of the Disclosure Statement is a tool to provide Creditors with information to decide on how to vote on the Plan. Fundamental to the Chapter 11 process is full and complete disclosure. *In re Brandon Mills Farms, Ltd.*, 37 B.R. 190, 192 (Bankr. N.D. Ga. 1984). This Debtor has failed to provide the requisite information to support the approval of the Disclosure Statement and presentation of a confirmable Plan. “Where inaccuracies are so numerous or significant that creditors or interest holders can no longer make an informed judgment about whether to accept or reject the proposed plan of reorganization, approval of the Disclosure Statement must be denied.” *In re Cardinal Congregate I*, 121 B.R. 760, 766-67 (Bankr. S.D. Ohio 1990); *see also In re Hirt*, 97 B.R. 981, 983 (Bankr. E.D. Wis. 1989).

1 **II. FACTS RELEVANT TO PNL**

2 **A. The Loan**

3 Debtor by and through Belinda Meruelo, the Estate of Homero Meruelo and the Meruelo
4 Living Trust U.D.T., dated November 11, 1988, holds title to certain real property located at 1875
5 W. Mission Blvd., Pomona, California 91766 (the "Property"). The property consists of a vacant
6 warehouse on a corner lot. The property has been vacant for the better part of the last decade. The
7 Debtor has owned the property for most of this time and has sought to either redevelop the property
8 and/or sell the property. The property has no tenants and generates no income. The state of the
9 property has been unchanged since PNL's involvement in the property.

10 Creditor PNL is the successor in interest to the original lender on a Promissory Note secured
11 by a Deed of Trust on the Property in the principal sum of Nine Million Eight Hundred Thousand
12 Dollars (\$9,800,000.00) bearing a variable interest rate with a floor at 10.75% and a maximum of
13 15.75%. The total of principal, interest, loan fees and expenses were to be paid on or about April 1,
14 2009.

15 In early 2008, PNL Pomona learned that the parties had violated the terms of the loan. As
16 a result of these defaults and an agreement as to how to handle the situation, the parties entered into
17 a Reinstatement Agreement. The Agreement reaffirmed and provided incorporation of all of the
18 previous documents, including but not limited to the Continuing Guaranty of Payment and
19 Performance, dated November 11, 1998, waived all defenses to the enforcement of the documents
20 and confirmed all the appropriate parties.

21 However, not long after, on or about February 1, 2009, the Meruelos again defaulted on their
22 payments. At that time the principal balance on the Note was Eight Million Four Hundred Sixty Two
23 Thousand Nine Hundred Thirty Nine Dollars and Seventy Cents (\$8,462,939.70) with interest
24 accrued amounting to approximately One Hundred Two Thousand One Hundred Ninety Two and
25 Eighty Nine Cents (\$102,192.89) as of February 11, 2009. Both judicial and non-judicial foreclosure
26 proceedings commenced. The Note then matured on April 1, 2009 and the instant bankruptcy
27 followed.

28

1 To date, no payments whatsoever have been received from the Debtor for the last year, since
2 approximately February 2009. At the point, the Debtors have been able to avoid over \$1,500,000
3 in payments to PNL.¹ Moreover, it goes without saying that while this Secured Creditor has gone
4 without payment, the Debtor's have continued in their normal status quo with their officers receiving
5 salaries in excess of \$400,000 per year and car allowances of approximately \$2,500 per year. Their
6 lives have been unaffected and yet this Secured Creditor has had to cover the costs associated with
7 this property. While, everyone understands that this is part of the parameter of Bankruptcy, it is
8 important for this court to see the actual damage that these Secured Creditors are suffering due to this
9 extended and protracted process.

10 **B. Status of the Property.**

11 The property is a vacant warehouse facility. In approximately April 2009, the property
12 suffered fire damage due to the vagrants at the site. The insurance finally paid off on that damage
13 in the approximate sum of \$1,800,000.00 which was held in a DIP account. A significant portion
14 of this money has now been used to demolish the building on the property. The property has had
15 recent offers; however, the Debtors have failed to engage in any transaction.

16
17 **III. LEGAL ARGUMENT**

18 **A. The Debtor's Disclosure Statement Fails to Provide "Adequate Information,"**
19 **as Required by Section 1125 of the Bankruptcy Code.**

20 The confirmation process is premised, in large part, upon the mandate of Section 1125 that
21 all creditors and equity holders of a debtor be provided with information regarding the debtor and
22 any proposed plan of reorganization. Specifically, Section 1125(b) of the Bankruptcy Code provides
23 that approval of the proposed plan may not be solicited unless, at or prior to such solicitation, a
24 written disclosure statement, approved by the Bankruptcy Court as containing "adequate
25 information," has been provided to such claimant or interest holder. The very purpose of a
26 disclosure statement is to give all creditors a source of information which allows them to make an

27
28

¹ That being without the maturity of the note. The previous payments on the obligation were approximately \$102,000 per month. The Note fully matured on April 1, 2009. PNL has been without payments since February, 2009 for a total of \$1,632,000 (\$102,000 x 16 months)

1 informed choice regarding the approval or rejection of a plan.” *In re California Fidelity, Inc.*, 198
2 B.R. 567, 571 (9th Cir. BAP 1996). Therefore, the courts have found that the disclosure of
3 information occupies a “paramount position” in the confirmation process. *In re Crowthers McCall*
4 *Pattern, Inc.*, 120 B.R. 279, 300 (Bankr. S.D.N.Y. 1990). Whether a disclosure statement contains
5 the requisite information must be decided on a case-by-case basis, upon an examination of all
6 relevant facts. *In re Applegate Property, Ltd.*, 133 B.R. 827, 829 (Bankr. W.D. Tex. 1991); *In re*
7 *Dakota Rail, Inc.*, 104 B.R. 138, 143 (Bankr. D. Minn. 1989).

8 Here, the Debtor’s Disclosure Statement fails to provide fundamental, accurate information
9 necessary to make an informed decision regarding whether to accept or reject the Plan and hence
10 must not be approved.

11 **1. The Valuation of the Properties is Lacking.**

12 The Disclosure Statement entirely relies upon the representations of the principal of the
13 Debtor for the values of the properties. As the court is aware, these values have been repeatedly
14 challenged by nearly every Creditor in this case. The appraisals completed by independent MIA
15 appraisers have, for the most part, been far less than the value assigned by the Debtor. It is
16 inappropriate for the parties reviewing the disclosure statement to have the impression that the values
17 placed in the plan are somehow independent valuations, when in fact, they are not. Either the
18 competing valuations should be included or proper appraisals should be done to demonstrate the
19 actual value of the assets. As stated, this is not sufficient evidence for creditors to accurately
20 determine the value of the Debtor’s overall assets and make a determination as to whether the Plan
21 is feasible. This failure also raises a question as to whether there is sufficient equity in the Property
22 to fully collateralize its secured claims.

23 In addition, Debtor goes to great lengths to explain Mr. Meruelo’s experience in real estate.
24 In one section they actually tout that Mr. Meruelo has reviewed “hundreds of MIA appraisals”.
25 Frankly speaking, probably most attorneys on this matter, and the court for that matter, have reviewed
26 hundreds of MIA appraisals. This does not make any one of us qualified to complete the analysis
27 of the market and provide a valuation of commercial property. Likewise, Mr. Meruelo is not an
28

1 appraiser and that should be clear to all those who review this Disclosure Statement. Based upon
2 what has been provided, it does not appear that this is the case.

3 **2. There Is No Discussion Of Marketing or Ability To Sell**

4 The Debtor goes to great lengths to explain the company's history and specialties. In fact,
5 the Amended Disclosure Statement goes on ad nauseam about the history of the company and the
6 experience they have, yet they do not provide any information as to how the reorganized Debtor is
7 going to be any different than the original Debtor. Obviously, the Business Plan this Debtor had
8 previously employed was unsuccessful - hence this bankruptcy. There is nothing in this Amended
9 Disclosure Statement which sets forth to how this reorganized Debtor will be any different. The
10 limited marketing plan suggested appears to be exactly the same. The management team is the same.
11 The goal is the same. The only difference is PNL does not get paid under the agreed terms of the
12 Contract. This is not sufficient for a disclosure statement. Information on how they are going to
13 effectively accomplish these sales in this economy should be set forth.

14 Most troubling to PNL is that there is no analysis or discussion of the likelihood that PNL's
15 property, let alone the other properties, can be sold within the time frame contemplated under the
16 Plan. As to the Pomona property, the property has sat vacant for nearly a decade. There has been
17 no serious interest in the property even during the height of the market. At our last hearing related
18 to this property, it was learned that the City is going to make it next to impossible to put anything on
19 the property that they do not specifically approve of. Hence, there is an utter lack of discussion as
20 to how this "plan" is suppose to work. There is absolutely nothing in this Amended Disclosure
21 Statement which suggests that this property has any reasonable chance of sale in this down market
22 or any time in the future. There is no discussion of the marketing efforts which are to be used or
23 what efforts **differing** from the unsuccessful efforts of the last decade will, in fact, work. This goes
24 for all the properties. This company's base business was the sale and development of real estate
25 during the height of the real estate market. Yet, they have found themselves in bankruptcy with a
26 flawed business model. Now, they are suggesting that they continue on with business at status quo.
27 What is there to allow anyone to believe that this same model, which didn't work during the height
28 of the real estate boom, is now going to be successful in the worst market in history? There is

1 nothing in this Statement which gives any discussion of the fact that these Debtors' business model
2 has been, and currently is, unsuccessful and that they can now turn this around. This failure to
3 disclose makes it impossible for a reasonable Creditor to evaluate their intentions, the situation and
4 the likelihood of success.

5 **3. Debtors Intend to Use Insurance Proceeds as Interest Payments.**

6 In the last couple of months nearly \$2,000,000.00 has been obtained as insurance proceeds
7 for the damage to the PNL collateral. In the last couple of plans, the Debtor has failed to include any
8 information regarding the insurance proceeds and their intended use. This round, Debtor actually
9 mentions these funds in a single sentence. That sentence says that Debtor intends to use PNL's
10 collateral funds (the insurance proceeds) to pay to PNL its interest only payments and the payment
11 of taxes. That is unconscionable. Debtor wants to deplete the collateral and technically the
12 "adequate protection " in this property by way of payment to PNL. This leaves this Debtor with
13 absolutely **no risk** whatsoever and this Secured Creditor holding **all of the risk** that this Debtor will
14 be able to find a "sale" which is acceptable to them. While one understands that the Debtor has the
15 right to pick and chose what sale terms they are willing to accept on a property they own, one must
16 question how far this goes. Under this scenario, **PNL takes all the risk** and is to sit by and accept
17 interest only payments paid to them from their own collateral- with this Debtor not having to go out
18 of pocket with their own money at all- while Debtor plays a craps game with this property. That is
19 not in the spirit of the Bankruptcy code and should not be condoned by this Court. The fact that
20 Debtor intends to act in this capacity must be disclosed in this statement so that all creditors can
21 make a decision as to whether they intend to accept these terms.

22 A Debtor should not be able to take the Creditors collateral and deplete it, essentially
23 contributing to the reduction in whatever equity there may be. The proceeds, where they came from,
24 and why they are still here, should be disclosed.

25 **4. \$10 Million Is Simply Not Enough Money to Satisfy All These Debts.**

26 The Amended Disclosure Statement is still providing for execution of the Plan through
27 \$10,000,000.00 of new equity. It is impossible to understand how this will be enough money to pay
28 the interest on all the debt of the secured creditors and pay off the unsecured creditors let alone

1 maintain sufficient operational expense. These funds are going to run out almost instantaneously;
2 and then, the Debtors will be in their exact same position - unable to pay any of their secured
3 creditors.

4 While the court has continued to extend exclusivity to this Debtor, the court must at some
5 point acknowledge that there are other parties who can and would immediately step up to the plate
6 and submit a plan which is more beneficial to every creditor in this matter. This Debtor is simply
7 playing a game to provide the least amount of money as “equity”. This is patently unfair and against
8 the spirit of the bankruptcy process. If this Debtor’s numbers are to be believed, there is more than
9 \$200,000,000.00 in equity in these properties. Debtor is suggesting that it’s insiders are able to
10 purchase up this equity--without making it available to anyone outside of the shareholders, for that
11 matter, not even making it available to all of the shareholders— for a mere \$10,000,000.00. What
12 a deal. This Debtor has been able to suggest a plan which would allow them to retain
13 \$200,000,000.00 for just \$10,000,000.00. Doesn’t this seem patently unfair? This is certainly unfair
14 when there are competing parties who would be pleased to provide a better deal and can make that
15 transaction happen immediately and with a better return to all of the creditors.

16 Further, based upon the Budgets provided to date, the Debtor has been running at a significant
17 short-fall². Therefore, there is no reasonable way to execute a Plan and satisfy all the Creditors with
18 only \$10,000,000.00. The court should either (1) allow for the bidding as appropriate and/or (2)
19 allow for competing plans to be filed to see if there is a better deal amongst the Creditors.

20 **5. Balloon Payments.**

21 One only surmises that the balloon payments due are going to be paid from the sale of the
22 properties. However, the Amended Disclosure Statement still fails to identify exactly how the Debtor
23 will be able to sell the properties and make any of the “balloon payments” to its Creditors as it is
24 suggesting and within the five/seven year time frame. The Disclosure Statement provides no details
25 on this issue and suggests that the creditors should simply trust the actions of this Debtor who has
26 essentially defaulted on every Note obligation it has entered into.

27
28

²At one point this was nearly \$3,000,000.00.

1 **C. The Plan Is Unconfirmable and Hence The Disclosure Statement Should Not Be**
2 **Approved.**

3 The Court may consider substantive plan issues at the disclosure statement hearing and deny
4 approval to disclosure statements predicated upon facially unconfirmable plans. A court is authorized
5 at a disclosure statement hearing to address legal issues that determine whether a plan can be
6 confirmed. *See also In re Felicity Assocs., Inc.*, 197 B.R. 12, 14 (Bankr. D.R.I. 1996). Although
7 objections to a plan of reorganization ordinarily are reserved for the plan confirmation hearing, where
8 the plan is patently unconfirmable because it violates the requirements for conformation set forth in
9 Section 1129, the Disclosure Statement accompanying the Plan cannot be approved. *See In re Main*
10 *St. AC, Inc.*, 234 B.R. 771, 775 (Bankr. N.D. Cal. 1999); *In re Bjolmes Realty Trust*, 134 B.R. 1000,
11 1002 (Bankr. D. Mass. 1991); *In re Pecht*, 57 B.R. 137, 139 (Bankr. E.D. Va. 1986). Thus, when
12 a plan to which a disclosure statement relates is defective, the defects in the plan may be raised as
13 objections to the disclosure statement. *In re Pect*, 53 B.R. 768 (Bankr. E.D. Va. 1985). When these
14 defects render a plan unconfirmable, the disclosure statement should be dismissed as the proceeding
15 relating thereto would be a waste of judicial resources and impose an unnecessary expense on the
16 estate and its creditors. *In re Unichem Corp.*, 72 B.R. 95, aff'd, 80 B.R. 448 (Bankr. N.D. Ill. 1987);
17 *In re Weiss-Wolf, Inc.*, 59 B.R. 653, 656 (Bankr. S.D.N.Y. 1986); *Pecht*, 53 B.R. At 769-70; *In re*
18 *McCall*, 44 B.R. 242, 243 (Bankr. E.D. Pa. 1984); *In re Kehn Ranch, Inc.*, 41 B.R. 832, 832-33
19 (Bankr. D.S.D. 1984); and *In re Genesse Cement, Inc.*, 31 B.R. 442, 443-44 (Bankr. E.D. Mich.
20 1983). The Plan violates the most basic elements necessary to confirmation provisions contained in
21 the Code, thereby rendering the Plan unconfirmable.

22 The standards governing confirmation of a plan of reorganization are set forth in Section 1129
23 of the Bankruptcy Code. The proponent of a Chapter 11 plan bears the burden of proving that the
24 plan satisfies each of the statutory requirements set forth in Section 1129. *See In re Kemp*, 134 B.R.
25 413 (Bankr. E.D. Cal. 1991); *In re Revco D.S., Inc.*, 131 B.R. 615, 620 (Bankr. N.D. Ohio 1990); and
26 *In re Rusty Jones, Inc.*, 110 B.R. 362, 373 (Bankr. N.D. Ill. 1990).

27 Since the Plan cannot be confirmed as stated, it would be a waste of judicial resources and cause
28 these Creditors to expend significant funds to proceed with extended hearings on the adequacy of
the Disclosure Statement.

1 **1. The Plan Unfairly Discriminates Against PNL.**

2 The Plan, as stated, violates section 1129(b) by proposing to modify the rate of interest accruing
3 on PNL’s claim post-petition, and extend the term of the Debtor’s obligation to PNL, and modify
4 other terms of the Loan Documents. The PNL loan has fully matured. PNL’s appraisal on the
5 property shows the collateral is not worth that suggested by the Debtor and arguably continues to lose
6 value daily. The Debtor proposes to modify the secured obligation by extending the maturity and
7 reducing the interest rates. Moreover, this Plan suggests to provide similar modifications to all the
8 secured creditors regardless of whether they are under secured or over secured. Such is simply
9 inappropriate. This treatment fails to recognize, among other things, the difference in each of these
10 secured creditors’ positions with this Debtor and specifically fails to address the rights of PNL with
11 this Debtor. The loan documentation, as provided, fails to protect the Creditor in what would be the
12 same terms and conditions as set forth in the original loan documentation. Hence, it is unacceptable.

13 **2. The Plan Violates the Absolute Priority Rule.**

14 A non-consensual plan of reorganization can be confirmed over the dissent of impaired classes
15 of creditors or interest holders if the treatment of the impaired class is “fair and equitable.” 11 U.S.C.
16 § 1129(b). With respect to a class of unsecured claims, Subsection 1129(b)(2)(B) provides that a plan
17 is not fair and equitable and may not be confirmed over the objection of a non-accepting unsecured
18 creditor class that will receive less than full payment if the holder of any claim or interest that is
19 junior to the claims of the unsecured creditor class, including an equity holder, receives or retains any
20 property under the Plan. 11 U.S.C. § 1129(b)(2)(B); *see In re Armstrong World Indus., Inc.*, 432
21 F.3d. 507 (3d Cir. 2005). Subsection 1129(b)(2)(B)(ii) sets forth what is commonly referred to as the
22 “absolute priority rule.”

23 Assuming the Debtor can actually overcome the Plan’s defects, the Debtor nevertheless cannot
24 confirm the Plan under the “cram down” provisions contained in Section 1129(b) of the Bankruptcy
25 Code. Pursuant to the Plan, the New Value investors which it appears will ultimately end up being
26 the prior management team, still are retaining the full value of their Interests, while PNL is impaired
27 and receiving less than a full distribution on account of its secured claim. Therefore, the Plan clearly
28 violates Section 1129(b)(2)(C) on its face. If the holders of general unsecured claims vote to reject

1 the Plan, the Plan cannot be confirmed unless the equity holders provide “new value” in exchange
2 for the retention of their interests. *Bonner Mall Partnership v. U.S. Bancorp Mortgage Co., (In re*
3 *Bonner Mall Partnership)*, 2 F.3d 899 (9th Cir. 1993). This is the “new value” exception to the
4 absolute priority rule.

5 It appears that the Interest Holders are attempting to avail themselves of this “new value”
6 exception to the absolute priority rule. However, such a stand fails. In order to prevail, the Debtor
7 must demonstrate to this Court the validity of a new value exception to the absolute priority rule.
8 Debtor has failed to do so. Further, even assuming that the Debtor can overcome this burden, the
9 Debtor must then prove that the Plan, which provides for vesting equity in the reorganized Debtor
10 as the Interest Holders, properly extended an opportunity to other parties to either compete for the
11 new equity or to propose a competing reorganization plan. *Bank of America National Trust &*
12 *Savings Ass’n v. 203 North LaSalle Street Partnership*, 526 U.S. 434, 119 S.Ct. 1411, 143 L. Ed.2d
13 607 (1999). This is not occurring.

14 **The settlement with the Tax Assessor.**

15 Debtor clearly intends the settlement with the tax assessor as nothing more than a
16 gerrymandering of the voting on the plan. They intend to set up their own controlled class- the
17 assessor- as an impaired class which has voted to accept the plan and hence force the approval of the
18 plan. Again this is nothing more than gerrymandering and is in violation of the spirit of the
19 bankruptcy code. The assessor is not an impaired class and should not be treated as such.

20 **The settlements with other Creditors.**

21 While the Debtor continues to attest that they have settled many of their issues, this is far from
22 the case. Over the last 16 months, the Debtor has settled very little. If one were to take the total
23 value of the settlement claims versus those which are still outstanding, it is but a small fraction. This
24 Debtor should not be able to use these minor issues to convince the court that it is acting in good faith
25 to resolve cases. This is simply not true.

26 **The New Value Argument**

27 The Amended Disclosure Statement provides that there will be a private placement to “certain
28 accredited” parties who shall have the right to subscribe and purchase shares of the Offered New

1 Equity Interest. Yet, once again, we are held in suspense to find out who these parties are and how
2 this will occur. Once again we are left to ask, "Who are these 'certain selected' individuals? Are
3 they the same as the "Top 200"? Or are they the same as those previously suggested as the New
4 Value Investors? To date, although repeated questions have been raised, we still do not know.
5 Further, what this clearly demonstrates is that this Debtor has its idea for how it is going to get
6 around the New Equity/La Salle problems and it just keeps trying. This is not fair and should not be
7 condoned.

8 This new rights offering is no different than the original contention of the First Disclosure
9 Statement which left all the rights in the original management team or in the rights to the "top 200"
10 as previously suggested. This does nothing more than keep the rights in the hands of the
11 management team and leaves the Creditors with no interests. This is hardly an open "bidding"
12 process.

13 The Supreme Court in *LaSalle* limited any new value exception and established certain
14 requirements equity interest holders must meet in order to retain their interests. The Court was
15 particularly concerned by the debtor's retention of the exclusive right to propose a plan, thereby
16 precluding others (including the objecting creditor) from proposing a plan "selling" the equity to
17 another. 526 U.S. at 456. The Court specifically stated:

18 Hence it is that the exclusiveness of the opportunity, with its protection against
19 the market's scrutiny of the purchase price by means of competing plan
20 proposals, renders the partners' right a property interest extended 'on account
21 of' the old equity position and therefore subject to an unpaid senior creditor's
22 class's objection.
23 *Id.*

24 *LaSalle* continues to be entirely on point. As proposed, it appears that the new offering will
25 allow these same individuals to continue to hold their control of the Debtor by way of the "NE"
26 Interest and will have retained their exclusive right to determine who will be the owner of the
27 reorganized Debtor. This control of the Debtor is a right which they hold solely due to their current
28 position as controlling shareholders of the Debtor. Therefore, it violates the absolute priority rule.
While this New Equity concept attempts to solicit outside parties, it really is just a smoke-screen of
these parties maintaining control of this business. There is simply no public auction or competing
plans or the ability of anyone else to intervene. This is entirely unacceptable when there are a

1 number of parties who have made it abundantly clear that they would provide a competing plan
2 which would provide better terms and more equity. This Debtor is trying to set this up with just
3 enough so that it can continue to control its assets for as little an exchange as possible. This is not
4 proper. The matter should be set for open bid and/or for competing plans. These creditors are
5 entitled to the “best deal” that is available. The Debtor is simply stopping that process which is
6 patently unfair to these creditors.

7 To avoid this unfair result, the Debtor must subject the “exclusive opportunity” to determine
8 ownership of the reorganized Debtor to the marketplace test. *LaSalle*, 526 U.S. at 457. This can be
9 achieved by either terminating exclusivity and allowing others to file a competing plan, or allowing
10 others to **bid** for the equity (or the right to designate who will own the equity) within the confines
11 of the Debtor’s Proposed Plan. *Id* at 458. *See also In re Global Ocean Carriers Ltd.*, 251 B.R. 31
12 (Bankr. D. Del. 2000). This is no “bid” procedure. This actually is the Debtors giving it to its
13 preselected insiders. This is not the “bidding” procedure intended.

14 This continues to be exactly what the Supreme Court prohibited in *LaSalle*. The Plan was filed
15 within the Debtors’ exclusivity period, and does not allow for the “benefit of market valuations.”
16 Unless the Debtor can satisfy the Supreme Court’s requirements in *LaSalle*, the Plan cannot be
17 confirmed. Hence, the Disclosure Statement cannot be approved in its current form.

18 **3. The New Value Contribution is Inadequate as a Matter of Law.**

19 The Debtors contemplate an infusion of New Value by the offering is just for \$10,000,000.00.
20 Simply stated, such is inadequate.

21 As suggested by the Court, “[c]ontributions that are merely nominal, or gratuitous, token cash
22 infusions proposed primarily to ‘buy’ cheap financing, will not suffice.” *In re Sea Garden Motel and*
23 *Apartment*, 195 B.R. 294, 301 (D.N.J. 1996). *See also In re Greystone III Joint Venture*, 102 B.R.
24 560, 575 (Bankr. W.D. Tex. 1989), *affd*, 127 B.R. 138 (W.D. Tex. 1990), *rev’d* on other grounds,
25 995 F.2d 1274 (5th Cir. 1991), *cert. den’d*, 506 U.S. 821 (1992) (“[The new value exception] is not
26 intended as a device by which pre-filing owners can buy their way back into the venture, much less
27 preserve their ownership interest.”). The gravamen of the problem is that the system, as understood,
28 to obtain new equity, is nothing more than letting the principals do as they want. This is not a

1 bidding process nor does it give anyone equal ability to obtain interest. Once again, the equity,
2 according to Debtor,s in certain property is significant. These New Value investors are getting
3 ownership by paying a small fraction of the equity value in these properties. This is nothing more
4 than a token cash infusion that is to be prohibited. Hence, the Plan is unconfirmable in its current
5 form and the Court should deny approval of the Debtor’s Disclosure Statement.

6 **4. The Plan Does Not Provide Secured Creditors with the Indubitable**
7 **Equivalent of Their Secured Claims.**

8 The seminal case on the concept of “indubitable equivalent” is *In re Murel Holding Corp.*, 75
9 F.2d 941 (2nd Cir. 1935). In *Murel*, the reorganization plan proposed to pay the secured creditor
10 interest on the collateral for ten years, with full payment of the principal due at the end of that time.
11 75 F.2d at 942. According to the court, the proposed payments to the secured creditor did not meet
12 the indubitable equivalence test because:

13 “the amount to be advanced is a mere trifle compared with the debts; its effect
14 is wholly speculative based upon the expectations of those who have
15 everything to gain and nothing to lose. The mortgagee is to be compelled to
16 forego all amortization payments for ten years and take its chances as to the
fact of its lien at the end of that period, though it is now secured by a margin
of only ten per cent...it should appear that the plan proposed has better hope
of success; full details may not be necessary, but there must be some
reasonable assurance that a suitable substitute will be offered.”

17 The First Circuit in its analysis of *Murel*, stated that the plan in *Murel* failed to meet the
18 “indubitable equivalent” requirement because the plan made no provision for amortization of
19 principal or for maintenance of the collateral (an apartment building) over the ten-year-term and the
20 plan was “wholly speculative.” *In re Sandy Ridae Development Corporation*, 881 F.2d 1346, 1350
21 (5th Cir. 1989).

22 In the instant case, PNL’s claim is nearly \$10,000,000.00. According to the Plan, PNL will be
23 paid under the Plan as follows:

- 24 1. Interest only for seven (7) years.
- 25 2. The payment terms shall be 4.25% on the balance owed on the Effective Date,
26 payable monthly after the Effective Date of the Plan.

27 These terms do not meet the “indubitable equivalent” requirement of 11 U.S.C. §
28 1129(B)(2)(A)(iii) because PNL’s Loan is extended by seven (7) years and the interest rate is reduced

1 from 10.75% to 4.25%, which reduces PNL's interest and claim by millions of dollars. Moreover,
2 the Debtor suggests that the payments are to be made from PNL's own collateral which minimize
3 its protection and allows the Debtors to maintain the property, keep looking for its "pot of gold" from
4 the asset, and all while not having to pay a cent out of pocket. This places all the risk on PNL and
5 none of the risk on Debtors. This is not fair or the equivalent of what it previously held. As such,
6 the Plan is unconfirmable.

7 **5. The Plan Classifies Claims in An Improper Attempt to Gerrymander**
8 **Voting for Purposes of Cramdown.**

9 The Plan is also not confirmable because the Debtor has improperly classified claims in an
10 attempt to gerrymander voting for purposes of cramdown under the Plan. *See In re Greystone III*
11 *Joint Venture*, 948 F.2d 134 (5th Cir. 1991); *Byrsan Properties XVIII*, 961 F.2d 496 (4th Cir. 1992);
12 and *In re Lumber Exchange Ltd. Partnership*, 126 B.R. 1000 (Bankr. D. Minn. 1991), which prohibit
13 gerrymandering for purposes of cramdown. The Plan fails to include any of the Secured Creditor's
14 deficiency claims based upon the Debtor's failure to pay the amount of unpaid interest due under the
15 Note. The amount of these deficiency claims in the aggregate would be substantial and could
16 dominate the voting of the unsecured creditor's claims. Further, Debtor's new plan has included a
17 settlement with the tax assessors, setting forth that their claims are impaired when they are in fact
18 being paid in full. If that is the case, they are not impaired and are simply set forth in an attempt to
19 gerrymander the voting process.

20 Moreover, PNL has always had its asset in a single purpose entity. The Debtor has now moved
21 its assets around so as to place within PNL's class another parcel of property which appears to be
22 solely controlled by the Debtor in order to control a class which could vote in favor of the plan. This
23 again is inappropriate and unacceptable. PNL's asset is to be maintained in a single asset entity and
24 should not be forced into a class which precludes it from having any viable vote on this plan.

25 **D. The Loan Modification Documents are Inappropriate.**

26 As repeatedly discussed, the Loan Modification documentation provided entirely usurps the
27 Creditor of all the protections provided under the loan documents which are currently in place. The
28 form of this "modification" is inappropriate and the Creditor should not be forced to take

1 significantly less protections than it negotiated for in the first place. The point is to provide the
2 Indubitable Equivalent. That is certainly not the case with the Loan Documents as suggested.

3

4 **IV. CONCLUSION.**

5 For the foregoing reasons, PNL respectfully requests that the Court deny approval of the
6 Amended Disclosure Statement, and grant PNL such other relief as the Court deems just and
7 appropriate.

8

9 DATED: May 17, 2010

HAGAN & ASSOCIATES

10

11

12

By: /s/ Cara J. Hagan
CARA J. HAGAN
ANDREA M. DUMOND
Attorneys for Plaintiff, PNL POMONA LP

13

14

15

16

17

18

19

20

21

22

23

24

25

26

27

28