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Proposed Counsel for the
Official Committee of Unsecured Creditors

UNITED STATES BANKRUPTCY COURT

EASTERN DISTRICT OF CALIFORNIA, FRESNO DIVISION

In re:

WEST COAST GROWERS, INC.,

Debtor-in-Possession.

Case No.: 15-11079-B-11

Chapter 11

DCN: KDG-5

**OPPOSITION OF THE OFFICIAL
COMMITTEE OF UNSECURED
CREDITORS TO MOTION FOR ORDER
AUTHORIZING DEBTOR-IN-
POSSESSION TO MAKE FIRST
INTERIM DISTRIBUTION TO 2014
GROWERS**

Hearing Date, Time and Place

Date: May 14, 2015

Time: 2:30 p.m.

Place: 2500 Tulare Street, Fifth Floor

Dept. B

Fresno, CA 93721

Honorable W. Richard Lee

1 Comes now, the Official Committee of Unsecured Creditors (the “Committee”) of West
2 Coast Growers, Inc. (the “Debtor”), by and through its undersigned proposed counsel, hereby files
3 its Opposition to Motion for Order Authorizing Debtor-in-Possession to Make First Interim
4 Distribution to 2014 Growers (the “Motion”), and in furtherance thereof, provides as follows:

5 The Committee was appointed by the Office of the United States Trustee on April 27, 2014,
6 pursuant to section 1102 of Title 11 of the United States Code (the “Bankruptcy Code”). *See* Docket
7 No. 132. The Committee convened its first meeting on May 7, 2015. The Committee has reviewed
8 the Motion and substantially all of the pleadings in this matter, and has serious questions regarding
9 the Debtor’s intentions with this case, including the Motion. The Motion makes it clear to the
10 Committee that this case is being operated solely for the benefit of the purported secured creditors of
11 the Debtor. If the Debtor has its way in this case, it will liquidate substantially all of its assets, pay
12 its secured creditors with the sale proceeds, and then hand over an administratively insolvent estate
13 to a Chapter 7 trustee. The Committee believes that this Motion will be followed by others, which is
14 why the distribution is termed the “first” interim distribution. As property and inventory is sold,
15 secured creditors will be demand to be repaid, even where there is no legal basis to do so, and the
16 Debtor will comply. The Debtor has stated that it may have avoidance actions against some or all of
17 its secured creditors, and even in the face of those potential actions the Debtor believes it is
18 appropriate to pay \$1 million in payments to these same creditors. The Debtor, which is supposed to
19 be a fiduciary for all creditors, appears to the Committee to be the marionette of its secured creditors
20 in this matter. The Motion should be denied.

21 **A. Without A Proper Means To Pay The Administrative Expenses Of The Debtor And A**
22 **Benefit To Unsecured Creditors, This Case Should Be Dismissed Or Converted**

23 As a starting point, the Committee finds it difficult to appreciate the reasons for the instant
24 case being one under Chapter 11 instead of one under Chapter 7. The Debtor has made it clear that
25 the Debtor’s sole purpose in the instant case is to liquidate its assets. The Debtor’s non-litigation
26 assets on the petition date totaled \$10 million. *See* Docket No. 1, p.8. Of those assets,
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1 approximately \$8.8 million is associated with raisin inventory/receivables, \$578,333 is related to an
2 insider receivable, \$476,865 in miscellaneous FF&E, and \$160,000 in baseball tickets.

3 According to the Debtor's schedules, there are two (2) buckets of secured creditors that hold
4 liens over substantially all of the Debtor's assets. The Debtor asserts that Central Valley Community
5 Bank holds blanket liens on the Debtor's assets in an amount exceeding \$37 million. *See* Docket
6 No. 1, pp. 19-20. The Debtor also asserts that the producers of raisins for the 2014 crop year that
7 sold their raisins/grapes to the Debtor have priming secured claims totaling as much as \$10.5
8 million. *See* Growers' Support of Motion for Order Authorizing Debtor In Possession to Make
9 First Interim Distribution to 2014 Growers (the "Growers' Support of Motion"), p. 2, lines 6-7; *see*
10 *also* Exhibits to Motion, Exhibit B, p. 5. There are scheduled unsecured claims totaling more than
11 \$8.2 million.

12 In short, there are no assets of the Debtor that are not subject to purported liens.
13 Approximately 88% of the value of the Debtor's assets are subject to purported producer's liens.
14 There are no assets left for unsecured creditors, including administrative expense and priority
15 creditors, other than litigation claims. The *Stipulation Authorizing Further Use of Cash Collateral*
16 *Through May 16, 2015 in Accordance with Court's Prior Order Authorizing Cash Collateral Use*
17 does not provide for a carve-out from the purported secured creditors' collateral to pay the
18 administrative expenses of the case, including claims entitled to administrative expense priority
19 pursuant to section 503(b)(9). There is a line item in the budget to pay some administrative
20 expenses, but not a carve-out from collateral to do so.

21 The administrative expenses of this case will be large. The Debtor's counsel claims that it
22 will incur "at least \$100,000" in fees and expenses through June 30, 2015. *See* Debtor's Application
23 for Order Authorizing Employment of General Insolvency Counsel Pursuant to 11 U.S.C. § 327(a),
24 p. 5, lines 5-6. The Committee is unaware of the totality of 503(b)(9) claims because no such bar
25 date has been set, but there is at least one creditor, Landsberg, that has filed a motion for allowance
26 and payment of a 503(b)(9) claim in the amount of \$16,240. *See* Docket No. 51. This case was
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1 administratively insolvent when filed, and continues to be administratively insolvent without carve-
2 outs from secured creditors to ensure administrative solvency.

3 This case is being operated for the benefit of secured creditors at the expense of
4 administrative expense creditors. For that reason alone the Motion should be denied as the
5 Committee intends on filing a motion for shortened notice of a request to dismiss or convert this
6 matter to Chapter 7. Approval of the Motion will only increase the administrative expenses of the
7 Debtor, and the Debtor does not have the ability to pay those expenses.

8 **B. The Growers Are Adequately Protected**

9 At bottom, the Motion seeks to provide its “2014 Growers” with adequate protection for the
10 use of their purported cash collateral. The only legal basis for the proposed interim distribution in
11 the Motion is section 361 of the Bankruptcy Code. As provided for in the Motion, “[t]o provide the
12 2014 Growers with adequate protection, Debtor-in-possession agreed to provide the 2014 Growers
13 periodic cash payments.” Motion, p. 2, lines 27-28. The 2014 Growers are already adequately
14 protected. The cash payments are not adequate protection, but rather post-petition payments on pre-
15 petition claims. The Motion provides that pursuant to section 361 of the Bankruptcy Code “the
16 debtor-in-possession is authorized to give the creditor a cash payment or periodic cash payments; an
17 additional or replacement lien; or other relief that will result in the creditor receiving the ‘indubitable
18 equivalent’ of the creditor’s interest in the property subject to its lien.” *Id.* at lines 24-27. This is a
19 deliberate incomplete cite of section 361 of the Bankruptcy Code.

20 *Cash Payments Under Section 361(1)*

21 As to periodic cash payments, the Debtor conveniently leaves out the second requirement
22 under section 361(1) of the Bankruptcy Code, which is that those periodic payments may be required
23 to be made when use of cash collateral “results in a decrease in the value of such entity’s interest in
24 such property.” *See* 11 U.S.C. § 361. Regarding the payment of adequate protection payments,
25 simply stating that payments are being made is not enough. The Debtor must show that the
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1 payments are being made because of the diminution in value of the underlying collateral because of
2 the Debtor's use of the cash collateral. *See In re Cook*, 205 B.R. 437, 440 (Bankr. N.D. FL 1997).

3 The Debtor has not claimed that the inventory that the 2014 Growers claim to have a lien
4 over is diminishing in value. In fact, all signs point to the fact that the inventory is simply being
5 transformed from raisins to cash. There is a cost in turning that inventory to cash, but that cost
6 would be present even if the inventory were able to be returned to the 2014 Growers for resale. The
7 value of the inventory is not diminishing. What is more, as far as the Committee can tell, the Debtor
8 is not paying rent on the warehouse the inventory is being stored in, which would be an added cost
9 that the 2014 Growers themselves would have to pay if the inventory could be returned to them.

10 The Debtor is using inventory sale proceeds to fund some of the administrative expenses of
11 the estate (approximately \$51,950 per month), but (1) those expenses are being partially offset by the
12 profit margin being realized from the sale of the raisins that are being bought by the Debtor from
13 CalDak for blending purposes, and (2) the amount of those administrative expenses associated with
14 the chapter 11 case is a fraction of the amount proposed to be paid through the Motion.

15 The Motion provides that "[a]nother component of [] adequate protection was a provision
16 that ... [the Debtor] would pay 2014 Growers a portion of the proceeds." Motion, p. 3, lines 1-3.
17 The Committee has reviewed all of the cash collateral stipulations and orders on the Court's docket,
18 and none of those pleadings speaks to any agreement to make payments to the 2014 Growers. To
19 the Committee's knowledge, this Court has never considered the payments requested through the
20 Motion as a part of any of its prior entered cash collateral orders.

21 The Debtor has not shown that \$1 million in cash payments are appropriate under section
22 361(1) of the Bankruptcy Code. There is no relation between the \$1 million payment and any
23 diminution in value of the 2014 Growers' purported collateral.

24 *Replacement Liens Under 361(2)*

25 As for replacement liens, it appears that the Debtor believes that by operation of law the 2014
26 Growers receive replacement liens in the proceeds of the sale of the 2014 related inventory.

Indubitable Equivalent Under 361(3)

Adequate protection may also be provided by giving the lienholder any other relief that will allow the lienholder to realize the “indubitable equivalent” of its interest. *See In re Bear River Orchards*, 56 B.R. 976, 978 (Bankr. E.D. CA 1986). Creation of a reserve fund may provide the “indubitable equivalent” of a creditor’s interest. *See* Legislative Statement following Section 361. Regarding the providing of the indubitable equivalent of the 2014 Growers’ interest, the Debtor has already created a segregated account where sale proceeds of its current inventory are being deposited. The indubitable equivalent of the 2014 Growers’ interest, cash, is being set aside.

It is clear that the payments requested through the Motion are not adequate protection payments, but rather payments to certain growers because “[g]rowers are approaching the time when they need their crop proceeds to finish their 2015 crop and commence harvest.” Growers’ Support of Motion, ¶ 9. The Committee’s constituency is comprised partially of growers, and so it is empathetic to the cash needs of growers. However, the Debtor’s estate has many competing interests, including questions concerning the Debtors’ pre-petition operations and payments to creditors. Further, as provided for herein *infra*, too many questions exist as to whether any payments should be made even if a proper vehicle to request these payments was brought by the Debtor or a grower. As a motion for adequate protection, the Motion fails, and should be denied.

C. The Debtor Has Not Shown That A Post-Petition Payment On Pre-Petition Claims Is Appropriate

Courts have held that “[t]he general rule is that a distribution on pre-petition debt in a Chapter 11 case should not take place except pursuant to a confirmed plan of reorganization, absent extraordinary circumstances.” *In re Air Beds, Inc.*, 92 B.R. 419, 422 (9th Cir. BAP 1988). Courts have further held that the failure of a creditor to show why the retention of sale proceeds by a debtor-in-possession, with a lien attaching to the funds, would not protect said creditor pending confirmation of a plan as contemplated under the Bankruptcy Code, leans towards a denial of a request for payment outside of a plan of reorganization. *Id.* at 423.

1 As illustrated *supra*, the proposed payments in the Motion are not adequate protection
2 payments, but rather post-petition pay downs on pre-petition debt. The Debtor has shown no
3 extraordinary circumstances for the payments other than to ensure that some creditors receive
4 payments post-petition as similarly situated creditors received pre-petition. This is sidestepping the
5 chapter 11 process. Claim determination and treatment of claims is to be done through a plan, and
6 not through ad hoc motion practice. It is certainly not to be done before the Debtor even has a
7 handle on the avoidance actions that are to be brought against certain creditors. The Debtor claims
8 that the case is to be converted by the end of June 2015, but this is no guarantee. The inventory may
9 take more time to sell than first projected, an unexpected inflow of cash, or going concern sale may
10 all warrant a liquidating plan instead of conversion. The Committee's point is that no one can know
11 the absolute direction of the case at this point, but paying \$1 million to creditors at this stage would
12 be guessing the end game.

13 **D. The Bar Date Has Yet To Pass**

14 The Court has set the bar date for filing proofs of claim in this matter for July 22, 2015. The
15 bar date is more than two (2) months away. No pre-petition claims should be paid in this matter
16 until the bar date has passed. The worst case universe of claims cannot be known until creditors
17 have filed their proofs of claim. The Motion is seeking to essentially establish certain claims in this
18 matter before all creditors have spoken up as to what their claims are. The Debtor has attached a list
19 to the Motion of those 2014 Growers it intends on paying, but at least one member of the Committee
20 is on that list, and believes that list may be wrong, at least as to their claim. The Committee submits
21 that often times the true universe of claims in a Chapter 11 case is much different than the picture
22 painted by the debtor in its schedules. Without the claims process being worked through, the
23 Debtor's goal of ensuring equal treatment of the 2014 Growers may not be able to be met.

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E. The 2014 Growers May Be Subject To Surcharge

Section 506(c) of the Bankruptcy Code provides that:

The trustee may recover from property securing an allowed secured claim the reasonable, necessary costs and expenses of preserving, or disposing of, such property to the extent of any benefit to the holder of such claim, including the payment of all ad valorem property taxes with respect to the property.

In the instant case, there has been no carve-out for administrative expenses in preserving and/or selling the inventory of the Debtor. There is rent that is not being paid on the premises where the inventory is located, and there are countless line item expenses included in the cash collateral budgets that are associated solely with preservation and liquidation of the Debtor's inventory. The Debtor retains the right to surcharge any secured creditor for the costs incurred in preserving and liquidating the inventory. What these costs will be is unknown, but the Debtor must retain any and all proceeds to ensure that the estate is properly compensated for the costs it incurs in preserving or liquidating its inventory to the extent the Court finds that the costs benefited secured creditors.

F. Payments Are Barred By Section 502(d) Of The Bankruptcy Code

Section 502(d) provides, in relevant part:

...the court shall disallow a claim of an entity from which property is recoverable under section 542, 543, 550, or 553 of this title or that is a transferee of a transfer avoidable under section 522(f), 522(h), 544, 545, 547, 548, 549, or 724(a) of this title, unless such entity or transferee has paid the amount, or turned over any such property, for which such entity or transferee is liable under section 522(i), 542, 543, 550, or 553 of this title.

The Debtor hints to the fact that there may be causes of action for fraudulent/preferential transfers to certain growers by the Debtor pre-petition. If this is the case, the Debtor should not be requesting to pay any of those growers until all of the fraudulent/preferential transfer issues are worked through by the Debtor. Section 502(d) of the Bankruptcy Code clearly allows the Debtor to use 502(d) as a defense mechanism to a request by a creditor for payment on a claim.

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CONCLUSION

Based on the foregoing, the Committee respectfully requests that the Court deny the Motion, and for any and all other relief that the Court deems just and appropriate.

Dated: May 13, 2015

BLAKELEY LLP

By: /s/ Ronald A. Clifford
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Ronald A. Clifford
Proposed Counsel for the Official
Committee of Unsecured Creditors of West
Coast Growers, Inc.