UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re:	)	Chapter 11
PRONERVE HOLDINGS, LLC, *et al.*,[1]	)	Case No. 15-10373 (KJC)
Debtors.	)	(Jointly Administered)
	)	**Related Docket No. 16**

DEBTORS' OMNIBUS REPLY IN SUPPORT OF THE DEBTORS' SALE MOTION

The above-captioned debtors and debtors in possession (collectively, the "Debtors") hereby file this omnibus reply (this "Reply") to the objections filed in connection with the *Debtors' Sale Motion* [Docket No. 16] (the "Sale Motion," and the transaction contemplated thereunder, the "Sale"). In support of this Reply, the Debtors respectfully state as follows:[2]

Response to the Committee's Objection

1. The Committee's objection is replete with inaccurate facts and arguments unsupported by the record. The Committee asserts that the Sale leaves the Debtors' estates with no money to administer these Chapter 11 Cases. Yet, the Debtors' exit strategy, which has been discussed at length with the Committee, contemplates a chapter 11 liquidating plan (the "Liquidating Plan"), which will be funded by excess funds remaining out of the $1.69 million in cash that the Stalking Horse Bidder has agreed to leave behind, in addition to chapter 5 avoidance actions (which the Debtors believe may be substantial). These terms are in the

[1] The Debtors, together with the last four digits of each Debtor's federal tax identification number, are: ProNerve Holdings, LLC (1653); ProNerve, LLC (2155); Boulder Intraoperative Monitoring, LLC (9147); Colorado Intraoperative Monitoring, LLC (5837); Denver South Intraoperative Monitoring, LLC (3164); Eugene Intraoperative Monitoring, LLC (0718); ProNerve Technologies, LLC (1814); Riverside Intraoperative Monitoring, LLC (6963); and Topeka Intraoperative Monitoring, LLC (6151). The location of the Debtors' corporate headquarters and the service address for all Debtors is 7600 E. Orchard Road, Suite 200 N, Greenwood Village, Colorado 80111.

[2] Capitalized terms used but not otherwise defined herein shall have the meanings set forth in the Sale Motion.

Stalking Horse Agreement, and the Committee has known this from day one. Additionally, the Debtors' estimate that the general unsecured claims pool will be approximately $1 million (not $5.3 million, as the Committee alleges), after taking into account intercreditor claims, waived claims, and claims associated with contracts that have been or will be assumed and cured. Again, this figure has been discussed at length with the Committee.

2. Under the Debtors' proposal, unsecured creditors *may* receive a distribution. The Committee is demanding a more definitive distribution for unsecured creditors, but the facts simply do not support such an outcome in these Chapter 11 Cases. The fact that unsecured creditors may receive a small distribution in these Chapter 11 cases does not mean that there is no case solution as the Committee suggests. Also contrary to the Committee's belief, the Bankruptcy Code does not mandate that unsecured creditors receive a meaningful recovery in every chapter 11 case.

3. The Committee takes a "kitchen sink" approach in an attempt to fashion an argument that unsecured creditors should receive a distribution greater than what is contemplated by the Liquidating Plan. The Committee casually mentions substantive consolidation and lien avoidance actions, all of which are unsupported by the record. With respect to lien avoidance, notwithstanding a fairly simple capital structure and four weeks to investigate the Liens (a time period that was extended by the Court), the Committee has no facts to support avoidance of the Liens.

4. With respect to substantive consolidation, while the Committee hints at facts that may support substantive consolidation (many of which the Debtors disagree with), such an endeavor would be months away from a determination by the Court, during which time the Debtors will run out of cash and be forced to liquidate, thereby forcing 200 employees out of

work. All of this in an effort to obtain a distribution for approximately $1 million in general unsecured claims, despite the Debtors' current proposal that provides an opportunity for a recovery by general unsecured creditors without violating the absolute priority rule.

5. The Committee argues that the Debtors have manifested an illusory need for exigency in these Chapter 11 Cases, and that the Debtors have failed to provide the Committee with any evidence supporting such need. To the contrary, the Debtors repeatedly have stressed the importance of their relationships with their customers and employees. In particular, the Debtors' technicians are the lifeblood of their business. In the Debtors' business—providing monitoring services during certain critical surgeries—trust in the quality of the services provided by technicians is important. Physicians often elect to work with technicians with whom they have worked before. Therefore, loss of technicians corresponds directly with loss of revenues.

6. Prior to execution of the Stalking Horse Agreement, the Debtors employed 130 technicians. The Stalking Horse Bidder made employment offers to all of these technicians, subject to the approval of the Sale by this Court. Of these technicians, 101 technicians signed letters stating that they intended to continue their employment with the Stalking Horse Bidder if it acquired the Debtors' businesses. The other 29 resigned and likely have joined competitors. As more and more time goes by, and as more and more technicians become impatient, more and more revenues are lost by the Debtors. The Debtors have not hired a single new technician since January 2015 and have lost over 20% of their workforce. Continued delay only risks continued loss of technicians.

7. Moreover, the Debtors have continued to lose customers, and the Debtors have not entered into any new customer contracts since January 2015. Of the approximately 220 customers with which the Debtors had contractual relationships as of January 2015, over 60

contracts have expired and have not been renewed. Moreover, another 35 contracts are up for renewal in the next six months, the period that should be used to negotiate a renewal of those contracts. Since January 2015, the Debtors have not entered into any new customer contracts and have only lost customers.

8. As described in the Pillari Declaration, the Debtors have conducted a fulsome sale process and believe that the Sale to the Stalking Horse Bidder is in the best interests of the Debtors estates and creditors. Even if all of the Committee's allegations are true, the Debtors would be left with a $9 million bid (the "Prasari Bid") that contains a due diligence contingency for an unknown duration, for which there is no evidence that the bidder ("Prasari") has the ability to consummate the transaction. Even more striking is that the individual supporting the Prasari Bid is the Debtors' founder and former board member (until January 2015), Jeffrey Thramann, who at times has held close to half of the Debtors' equity. This individual was also part of the prepetition sale process and submitted a letter of intent (contrary to the Committee's statement that its efforts led to this bid). Prasari and Mr. Thramann have had more than sufficient time to conduct due diligence—indeed, more time than the Stalking Horse Bidder, which was able to conduct due diligence, negotiate and draft the Purchase Agreement, and negotiate and document the DIP financing in approximately one month.

9. Perhaps most importantly, substantially all $9 million received by the Debtors from a sale to Prasari—assuming such sale ever closed—would be distributed to the Stalking Horse Bidder, as the Debtors' secured lender. To escape such an outcome, the Committee would need to demonstrate that some portion of the Stalking Horse Bidder's lien should be avoided. Historically, government receivables for the Debtors and Affiliated Practices have collectively represented approximately 20% of all receivables for those entities. As set forth in the Pillari

Declaration, assuming that (i) the Committee is successful in substantively consolidating the Debtors' estates with the Affiliated Practices (for which there is scant, if any, evidence), (ii) Prasari consummates the sale with a purchase price of $9 million, and (iii) the Committee is successful in avoiding 20% of the Stalking Horse Bidder's liens, the Committee would obtain a distribution for unsecured creditors in the amount of approximately $33,000 because the Stalking Horse Bidder would have an unsecured deficiency claim that would dwarf the other unsecured claims. Thus, it is a near mathematical impossibility for unsecured creditors to receive anything more than a *de minimis* distribution under the Committee's proposal, which will be equal to or less than a distribution that results from consummating the Sale with the Stalking Horse Bidder.

10. The Committee also asserts potential preference payments made on account of the Loan Commitments. Yet, no payments whatsoever have been made by the Debtors or the Affiliated Practices on account of the Loan Commitments since October 1, 2014.

11. The Committee has had ample time—approximately four weeks, a period of time already extended by this Court—to conduct an investigation, and not only has the Committee spent money that could have gone directly to their constituency, they have come up empty with a $9 million bid that is highly unlikely to close and coupled with half-baked arguments, which, even if taken to their logical conclusion would result in the same (or worse) outcome for unsecured creditors. Of course, this wholly ignores the Stalking Horse Bidders' credit bidding rights, which the Committee has not found any new basis to challenge (aside from simply wanting more money for unsecured creditors). The Committee and its professional should not be permitted to torpedo these Chapter 11 Cases by delaying the inevitable, fueling more unnecessary professional fees, and driving the Debtors into liquidation.

a. The Sale Should Be Approved.

i. The Sale Represents a Sound Exercise of the Debtors' Business Judgment.

12. The proposed Sale represents a sound exercise of the Debtors' business judgment and the Court should not permit the Committee to substitute the business judgment of its advisors for that of the Debtors' management. As a rule, a debtor's decision to sell property out of the ordinary course of business enjoys a strong presumption "that in making a business decision the directors . . . acted on an informed basis, in good faith and in an honest belief that the action taken was in the best interests of the company." In re Integrated Res., Inc., 147 B.R. 650, 656 (Bankr. S.D.N.Y. 1992) (quoting Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985)); see also In re Bridgeport Hldgs., Inc., 388 B.R. 548, 567 (Bankr. D. Del. 2008) (stating that directors enjoy a presumption of honesty and good faith with respect to negotiating and approving a transaction involving a sale of assets). In objecting to the proposed Sale, the Committee must actually establish "bad faith, self-interest, or gross negligence." Integrated Res., 147 B.R. at 656; see also In re Johns-Manville Corp., 60 B.R. 612, 616 (Bankr. S.D.N.Y. 1986). In other words, if the proposed Sale satisfies the business judgment rule, then it should be approved under section 363(b)(1) of the Bankruptcy Code. As the Committee knows, it cannot satisfy this burden. The Debtors' transactions with the Stalking Horse Bidder result from an independent, arm's length process. Specifically, the discussions between the Debtors and the Stalking Horse Bidder were led by the Debtors' independent Chief Executive Officer, the Debtors' restructuring professionals, and supervised by the Debtors' independent directors. The proposed Sale, therefore, is entitled to deference under the business judgment standard and should be approved.

13. In any event, the Debtors respectfully submit that sound business reasons support their decision to enter into the Stalking Horse Agreement. Inexplicably, the Committee would prefer that the Debtors give up the proposed Sale for a highly speculative path that seeks essentially the same result or worse.

- First, the proposed Sale provides benefits to the Debtors' estates, including the Stalking Horse Bidder's commitment to fund a wind-down and the costs of preparing the Liquidating Plan by leaving behind $1.69 million. This is in addition to the Stalking Horse Bidder's agreement to pay for certain additional accrued and unpaid postpetition expenses of employees and trade vendors (estimated to be approximately $1.37 million), continue paying the salaries of administrative employees pursuant to a transition services agreement, and even provide retention bonuses and severance payments for administrative employees.

- Second, the Debtors have extensively marketed their assets during successive marketing processes for more than a year.

- Third, the Debtors respectfully submit that it is reasonably likely that no bidder will submit a bid approaching, let alone exceeding, the amount of the Stalking Horse Bidder's potential credit bid (which likely exceeds $45 million). Indeed, no party expressed an interest in submitting a Qualified Bid.

- Fourth, the transaction will enable the Debtors to expeditiously complete their chapter 11 restructuring without incurring additional operating expenses at a time when the Debtors have minimal cash on hand.

ii. The Prasari Bid Is Not a Credible or SuperiorAlternative to the Proposed Sale and Should Be Disregarded.

14. Because the Committee cannot demonstrate that the Debtors acted improperly in connection with their entry into the Stalking Horse Agreement, the Committee asserts that the Debtors should disregard the offer on the table from the Stalking Horse Bidder in favor of a bid (which is not a Qualified Bid) from an uncommitted bidder.

15. The Prasari Bid is deficient because (i) it does not satisfy the minimum bid requirement, (ii) contains a due diligence contingency with an unspecified duration, and (iii)

Prasari has not demonstrated its ability to consummate the sale transaction. Prasari's counsel has informed the Debtors that the Prasari Bid would not be modified.

The Prasari Bid Does Not Satisfy the Minimum Bid Requirement

16. The Bidding Procedures state that a Qualified Bid is one that "contains a purchase price that provides for payment in cash at Closing in an amount equal to the sum of: (x) $35,000,000 . . . *plus* (y) the Expense Reimbursement [of $250,000] *plus* (z) $150,000." The Prasari Bid provides that "[t]he aggregate purchase price for the Assets would be $9 million." Thus, the purchase price in the Prasari Bid is deficient by more than $26 million.

17. In response to this deficiency raised by the Debtors, Prasari's counsel first noted that the Stalking Horse Bidder purchased the Loan Commitments for $4.25 million. As the Court has noted, this fact is irrelevant. It certainly is not relevant to whether the Prasari Bid satisfies the minimum bid requirement in the Bidding Procedures. As discussed in more detail below, the Stalking Horse Bidder, as a secured lender, is entitled to credit bid the full amount of its debt pursuant to Section 363(k) of the Bankruptcy Code. Additionally, accepting the Prasari Bid in lieu of the Stalking Horse Bidder's bid would result in an increase of approximately $35 million of unsecured claims, and any proceeds from a sale to Prasari would be distributed to the Stalking Horse Bidder in satisfaction of its secured claim. The Debtors do not think this result can be viewed as more favorable to the Debtors' estates.

18. Second, Prasari's counsel noted that the Prasari Bid does not require the termination of any employees, "thus eliminating the claims arising from the termination of the many employees as proposed in the SpecialtyCare bid." The Stalking Horse Bidder made employment offers, on terms substantially similar to or better than the Debtors' current employment terms, to all of the Debtors' technicians and readers and has agreed to continue to

pay the salaries of all but one of the Debtors' administrative employees during a transition period, with the remaining employee receiving a severance and release package from the Debtors. Thus, the Prasari Bid is not superior to the Stalking Horse Bidder's bid in this respect.

19. Third, Prasari's counsel noted that the Prasari Bid contemplates taking assignment of all executory contracts with vendors and suppliers of goods and services used by the company and unexpired leases for personal property. The proposed APA submitted by Prasari, however, does not reflect this. Instead, Prasari has the same rights that are contained in the Stalking Horse Agreement to exclude assumed contracts at any time up until closing. Even if the APA submitted by Prasari was amended (which Prasari's counsel has informed the Debtors that it would not be) and this would satisfy a large portion of unsecured claims, this neglects the fact that the unsecured claim pool would be increased by an approximately $35 million deficiency claim held by the Stalking Horse Bidder. Again, the Debtors do not think this result can be viewed as more favorable to the Debtors' estates.

20. Finally, Prasari's counsel noted that Prasari is "willing to step into the shoes of the [Stalking Horse Bidder] to provide DIP financing." The Debtors do not believe that this enhances the Prasari Bid in any meaningful way. In fact, this would likely cause the Debtors to incur additional legal fees and expenses, thereby reducing any recovery to creditors.

The Prasari Bid Contains a Due Diligence Contingency With an Unspecified Duration

21. The Bidding Procedures state that "other than with respect to a due diligence contingency that may only be exercised until one (1) day prior to the Auction," a Qualified Bid must not be subject to "any conditions less favorable to the Debtors, as determined by the Debtors, than those provided for in the Stalking Horse Agreement."

22. The Prasari Bid is contingent upon "the Stalking Horse Bidder being allowed adequate time to complete its due diligence review of Seller." To the extent that "adequate time" means a date that is later than one (1) day prior to April 8, 2015 at 10:00am (ET) (i.e., the Auction), the Prasari Bid is not a Qualified Bid.

23. Additionally, the Prasari Bid is contingent upon "the entry of an order by the Bankruptcy Court reducing or eliminating the credit bid currently extant by SpecialtyCare for the Company's assets." The Debtors view this contingency as highly speculative given that this Court has stated on the record that it has "seen nothing in the papers that tells [the Court] this is a *Fisker* like situation or that [the Stalking Horse Bidder] has engaged in bad behavior as [the Court] likes to call those considerations. I see nothing in the papers that tells me that." Transcript of Hearing at 53 (Mar. 11, 2015). In any event, such a contingency does not constitute a Qualified Bid.

24. In response to this concern raised by the Debtors, Prasari's counsel stated that Prasari "believes that the time for due diligence is unfairly short and has made effective and meaningful diligence impossible." Jeffrey Thramann (who Prasari's counsel indicates is financially supporting the Prasari Bid) had significant involvement with the Debtors prior to the commencement of these Chapter 11 Cases. Mr. Thramann (i) is the founder of the Debtors, (ii) is a former Board member (until January of this year), (iii) has, at certain times, held nearly half of the Debtors' equity, and (iv) was part of the prepetition sale process (Mr. Thramann submitted the $6.75 million expression of interest discussed above). Under the Bidding Procedures, bids were due 26 days after entry of the Bidding Procedures Order. The Stalking Horse Bidder conducted due diligence, negotiated and drafted the Stalking Horse Agreement (with related schedules), reached out to all of the Debtors' technicians and readers, and negotiated and drafted

a DIP credit agreement in 27 days. The Debtors believe that, of all potential bidders, Mr. Thramann cannot complain that he has had more than sufficient time to conduct any due diligence that he believes is necessary.

25. Additionally, as discussed above, the Debtors' financial situation and liquidity constraints justify the need for an expedited sale process. There is no additional time for due diligence.

Prasari Has Not Demonstrated its Ability to Consummate the Sale Transaction

26. The Bidding Procedures state that a Qualified Bidder must "provide such other information that will allow the Debtors and their advisors to make a reasonable determination as to such Qualified Bidder's ability to consummate the transactions contemplated by the marked copy of the Stalking Horse Agreement, including the Adequate Assurance Package."

27. The Prasari Bid states that Prasari (i) "is financially capable of consummating the transactions," and (ii) "has cash available on hand, permitted borrowing capacity under existing facilities or firm financing commitments that together are sufficient to enable payment of all amounts required in connection with the transactions contemplated by this Bid." These statements were not supported with any documentation.

28. In response to this concern, Prasari's counsel sent the Debtors a letter from Lateral Investment Management (the "Lateral Letter"). This letter falls well short of constituting a "firm commitment" for financing any transaction. For example, Section 1 of the Lateral Letter states, "Lateral *intends to work* towards providing a Credit Facility . . . ." (emphasis added). And Section 2 of the Lateral Letter contains a number of speculative conditions, including necessary time to conduct due diligence. Further, the Lateral Latter is unexecuted, and thus the Debtors have no way to verify its authenticity.

29. Additionally, Prasari's counsel indicated that the Prasari Bid "is financially supported by Jeffrey Thramann, MD." Although Prasari's counsel provided the Debtors with information about Mr. Thramann's history, including the fact that "[h]e has never been unsuccessful in financing a deal," the Debtors have not received any evidence that Mr. Thramann currently has sufficient cash available to consummate the transaction. Based on the information received to date, the Debtors have no reason to believe that Prasari has the ability to consummate the sale transaction.

30. The bid letter received from Prasari indicates that Prasari will take assignment of "contracts necessary for the ongoing business of the Company to continue as agreed to be assumed by the Stalking Horse Bidder, tentatively including and subject to further due diligence as to any individual contract, contracts with hospitals, as well as employment agreements with clinical employees, including reading doctors and technologists . . . ." In follow-up correspondence, Prasari's counsel informed the Debtors that "Prasari intends to assume all executory contracts related to goods and services provided to the Debtors, and all unexpired leases for personal property." Despite this statement, neither the Prasari bid letter nor the marked APA submitted by Prasari reflects anything more than what the Stalking Horse Bidder has agreed to do. Both Prasari and the Stalking Horse Bidder, under their respective APAs, would have the right, up until the Closing Date, to determine which contracts they do not want to take assignment of and pay cure costs. Thus, the Prasari Bid is no different than the bid from the Stalking Horse Bidder's bid in this respect.

31. Additionally, Prasari's counsel indicated that Prasari would satisfy all prepetition vendor claims that are not otherwise subject to contracts. Again, this obligation can be found nowhere in the APA. Prasari does not explain how such an offer dovetails with Prasari's

continued due diligence requirement. At what count could the claims exceed what Prasari is willing to pay or, more importantly, what Prasari's purported lenders are willing to finance? Moreover, it is unclear how this could be effected in accordance with the absolute priority rule. Nothing in the Bankruptcy Code authorizes the Debtors or the Bankruptcy Court to ignore the rights of a secured lender so that unsecured creditors may receive a greater recovery.

b. SpecialtyCare is Entitled to Credit Bid the Full Amount of the Loan Commitments.

25. In an effort to make the $9 million Prasari Bid competitive against the Stalking Horse Bidder's $35 million bid, the Committee requests that the Court deny, or at least limit, the Stalking Horse Bidder's right to credit bid the value of the Loan Commitments under section 363(k) of the Bankruptcy Code. This is a repeat of the Committee's request (denied by the Court) at the Bidding Procedures Hearing, and the Committee offers no new facts in support of its request that the Court reverse its decision.

26. Section 363(k) of the Bankruptcy Code provides as follows:

> At a sale under subsection (b) of this section of property that is subject to a lien that secures and allowed claim, unless the court for cause orders otherwise the holder of such claim may bid at such sale, and, if the holder of such claim purchases such property, such holder may offset such claim agains the purchase price of such property.

11 U.S.C. § 363(k). It is well established that a credit bid "is the equivalent of a cash purchase." <u>In re Spillman Dev. Grp., Ltd.</u>, 401 B.R. 240, 253 (Bankr. W.D. Tex. 2009). As such, a secured creditor is entitled to credit bid the full value of its claims unless the Court orders otherwise "for cause," <u>see</u> 11 U.S.C. § 363(k), such as where a lender's liens are in bona fide dispute. <u>See, e.g.</u>, <u>In re Merit Group, Inc.</u>, 464 B.R. 240, 252 (Bankr. D.S.C. 2011) (rejecting objection by creditors' committee to credit bid where there were no pending objections to the creditor's claims and no pending proceedings challenging validity, priority, or extent of its liens).

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27. Here, the Committee's effort to limit the Stalking Horse Bidder's right to credit bid must be rejected because it is irreconcilable with the well-established right, and, indeed, presumption, in this Circuit that a secured lender is entitled to vote the full amount of its secured claims. Nor is there any legitimate dispute regarding the Stalking Horse Bidder's liens that could or should prevent the Stalking Horse Bidder from exercising its rights in this regard.

- First, the price at which an entity purchased a secured claim is wholly irrelevant to whether the entity should be entitled to credit bid the full amount of its claim.

- Second, the Stalking Horse Bidder has a lien on all of the Acquired Assets and is entitled to credit bid for these assets. Among other things, the Bidding Procedures Order permits the Stalking Horse Bidder to credit bid its $2.5 million DIP claim, and there is no dispute that the Stalking Hose Bidder, as the DIP lender, has a lien on all of the Debtors' assets. In any event, even if the Stalking Horse Bidder did not have a lien on some of the Acquired Assets, the Stalking Horse Bidder is contributing substantial consideration in the form of its agreement to fund $1.69 million in wind-down costs plus an additional estimated $1.37 million in certain pre-closing administrative expenses. These forms of consideration are equivalent to the Stalking Horse Bidder paying cash for any Acquired Assets that are not part of its collateral package.

- Third, the fact that the Committee objects to the Stalking Horse Bidder's proposed Sale is wholly insufficient to manufacture a bona fide dispute. Indeed, neither the Stalking Horse Purchaser nor its affiliates engaged in inequitable conduct with respect to the Debtors, and the Committee does not even allege such conduct. Indeed, the Stalking Horse Bidder provided a critical financial lifeline to the Debtors to fund these Chapter 11 Cases when no funding was otherwise available to the Debtors. These and other factors evidence the Stalking Horse Bidder's good-faith commitment to the Debtors and undermine any suggestion that the Stalking Horse Bidder or its affiliates have acted in bad faith.

- Fourth, the Committee attempts to argue that the Stalking Horse Bidder does not have a perfected lien on assets of the non-debtor Affiliated Practices. The Committee has no standing or ability to challenge the liens of creditors against non-debtor entities. Therefore, even if there were an issue with such liens (and there is not), it would be wholly irrelevant to the issue of the Stalking Horse Bidder's right to credit bid with respect to its secured claim on the Debtors' assets.

- Finally, limiting the Stalking Horse Bidder's right to credit bid will not foster a competitive auction. Instead, it increases the possibility that the Stalking Horse Bidder will terminate the Stalking Horse Agreement, leaving the Debtors at the mercy of Prasari, which has not demonstrated any ability to consummate a transaction.

i. The Price at Which SpecialtyCare Acquired the Loan Commitments Is Irrelevant to Its Eligibility to Credit Bid.

28. The Committee's assertion that the Court should limit SpecialtyCare's right to credit bid the value of the Loan Commitments is at odds with the settled law in this Circuit regarding credit bidding and the significant public policies underpinning section 363(k) of the Bankruptcy Code.

29. It is hornbook law that "the plain language of [section 363(k)] makes clear that the secured creditor may credit bid its entire claim, including any unsecured deficiency portion thereof," and that "logic demands that § 363(k) be interpreted in this way; interpreting it to cap credit bids at the economic value of the underlying collateral is theoretically nonsensical." Cohen v. KB Mezzanine Fund II LP (In re SubMicron Sys. Corp.), 432 F.3d 448, 459-60 (3d Cir. 2006) (quoting In re Morgan House Gen. P'ship, 1997 WL 50419, at *1 (E.D. Pa. Feb. 7, 1997). The price at which the Stalking Horse Bidder acquired the Loan Commitments, therefore, is irrelevant and not a basis for limiting its statutory right to credit bid.

ii. SpecialtyCare is Entitled to Credit Bid for the Acquired Assets or, Alternatively, to Pay Cash for the Acquired Assets That are Not Part of Its Collateral Package.

30. In an effort to undermine the Stalking Horse Bidder's right to credit bid, the Committee asserts that certain assets are not part of the Stalking Horse Bidder's collateral package and, therefore, cannot be acquired by the Stalking Horse Bidder through its credit bid. This argument should be rejected for two reasons: (a) first, this argument mischaracterizes the ability to perfect a lien in government receivables (which, in any event, are assets of the non-debtors); and (b) second, this argument ignores the material forms of consideration provided by the Stalking Horse Bidder in addition to its credit bid, including $3.06 million of cash.

1. The Committee Mischaracterizes the Scope of the Assets Subject to SpecialtyCare's Liens.

31. The Committee contends, as it did at the final hearing for approval of the DIP Credit Agreement, that questions remain outstanding regarding the validity of SpecialtyCare's liens. See Committee Objection, ¶¶ 3,45, 47. The Committee asserts that as a result of section 4.11 of the Prepetition Credit Agreement ("Section 4.11"), SpecialtyCare, as successor lender, has disclaimed its interest in the government receivables received by the Affiliated Practices. The Committee, however, did not articulate a cogent argument why it believes that UCC-1 filings are not sufficient to perfect a security interest in government receivables.

32. First, SpecialtyCare holds a valid security interest over all the property of the Affiliated Practices. The Guaranty and Security Agreement dated as of December 20, 2012 grants security interests over all "Collateral" of the "Grantors." "Collateral" is defined broadly to include all property of the "Grantors" other than "Excluded Property." The Affiliated Practices are included under the definition of "Grantor." Excluded Property means, generally, property over which applicable law prohibits the grant of a security interest. The government receivables, which are received by and property of the Affiliated Practices ***are not*** Excluded Property because applicable law does not prohibit the grant of a security interest over the government receivables, but merely prohibits a secured party from directly receiving the proceeds of such receivables. *See, e.g.*, *Missionary Baptist Foundation of America, Inc. v. Wilson* (*In re Missionary Baptist Foundation of America, Inc.*), 796 F.2d 752, 759 (5th Cir. 1986) (holding as allowable the granting of a security interest in Medicaid receivables but not the assignment of such to a non-provider). In connection with the Guaranty and Security Agreement, General Electric Capital Corporation ("GECC"), SpecialtyCare's predecessor under the Loan Commitments, validly filed UCC-1 statements to perfect its security interest in the

assets of the Affiliated Practices, including the government receivables. Thus, as a threshold matter, the government receivables are covered by SpecialtyCare's broad liens over the property of the Affiliated Practices.

33. Second, the Committee assails SpecialtyCare's liens on the basis of its interpretation of Section 4.11 of the Prepetition Credit Agreement and argues that as a result of Section 4.11, SpecialtyCare has disclaimed any interests in the government receivables. Section 4.11, however, simply reflects the well-established mechanism by which a secured lender obtains valid security interests over government receivables in accordance with the applicable Medicare and Medicaid statutes. *See, e.g.*, Medicare Claims Processing, CMS Manual System Pub. 100-04 (June 25, 2004) (finding implicitly the double-lockbox structure to conform with federal reassignment provisions). The Committee objection only focuses on one sentence in Section 4.11, but, read as a whole, the section provides a series of steps to enable a secured party to validly obtain a security interest in the government receivables without directly receiving the proceeds of such receivables in compliance with the applicable regulations. Section 4.11 waives the secured lenders' ***control*** over the Segregated Governmental Accounts, but it does not waive the secured lenders' security interest in the proceeds that are deposited into that account. In short, the secured lenders do not have a security interest in the Segregated Governmental Accounts, but, in accordance with the UCC, their perfected security interest continues in the proceeds that are deposited in those account. The applicable steps are as follows:

> ***Segregation of government receivables*** – The relevant regulations require a healthcare provider to segregate its receivables into two different lockboxes – one to hold government receivables and another to hold all other types of receivables. Section 4.11 complies with these regulations by providing that "in order to segregate and to facilitate the perfection of the Agent's security interest in funds received . . . under Medicare or Medicaid, the Credit Parties, which includes ProNerve, LLC and the Affiliated Practices, must segregate their collections. This is accomplished by the Affiliated Practices having deposit accounts into which the government receivables are paid.

Government payors make payments to the segregated government account – The relevant regulations also require that all government proceeds must be paid in the first instance to a deposit account with respect to which only the healthcare provider can give instructions. Section 4.11 complies with these regulations by providing that "Credit Parties shall . . . notify all Governmental Payors making payments under Medicare and Medicaid to make payments to a Segregated Governmental Account."

Affiliated Practices enter into the Master Services Agreement and Sweep Agreement to transfer funds from the Segregated Governmental Accounts to the deposit account of ProNerve, LLC – Each of the Affiliated Practices entered into a Management Services Agreement with ProNerve, LLC, pursuant to which the Affiliated Practices agreed to remit funds received to ProNerve LLC. ProNerve, LLC, in turn, granted to GECC an express security interest in the contract rights and intangibles arising under the Management Services Agreement. In furtherance of the Affiliated Practices' obligation to remit funds out the Segregated Governmental Accounts to ProNerve, LLC, Section 4.11 provides that "Credit Parties shall . . . enter into, and cause each applicable depository to enter into, a "sweep agreement" (a "Sweep Agreement") with respect to each Segregated Governmental Account pursuant to which such depositary will agree to sweep amounts deposited therein on [a] daily basis to a deposit account of the Credit Parties . . . . ." Under this Sweep Agreement, all available balances in the deposit accounts of the Affiliated Practices (including the Segregated Governmental Accounts) are swept to the Concentration Account at Regions Bank held in the name of ProNerve, LLC (the ***Regions Concentration Account***").

Amounts deposited to deposit account of ProNerve, LLC, which is subject to control agreement in favor of GECC (now SpecialtyCare) – Section 4.11 provides that the swept amounts "deposited on [a] daily basis to a deposit account of the Credit Parties . . . [shall be] subject to a Control Agreement in favor of the Agent . . . ." The Regions Concentration Account is subject to a control agreement in favor of GECC.

As a result of this structure, SpecialtyCare's security interest in any governmental receivables is maintained every step of the way:

- SpecialtyCare has a perfected security interest in the receivables of the APEs, including any governmental receivables, by virtue of its security agreements and UCC-1 filings.
- The proceeds of the governmental receivables are deposited into the applicable Segregated Governmental Account for each APE.
- Although SpecialtyCare has waived any control rights with respect to the Segregated Governmental Account (and therefore, has no security interest in the account and no right to control release of funds in the account), SpecialtyCare maintains its perfected security interest in the proceeds of the governmental receivables.

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- The governmental receivables are transferred to the Regions Concentration Account in furtherance of the APEs' obligations under the Management Services Agreements.
- SpecialtyCare has a perfected lien on all contract rights and intangibles under the Management Services Agreements by virtue of its agreements with the Debtors and UCC-1 filings.
- SpecialtyCare also has a perfected lien on the Regions Concentration Account by virtue of its control agreement relating to such account.

2. The Proposed Sale Contemplates a Credit Bid and Additional Consideration Paid by the Stalking Horse Bidder in the Form of Plan Funding Commitments.

32. In any event, the Committee's objection incorrectly assumes that the Stalking Horse Bidder's bid is limited to its credit bid of the Loan Commitments. In fact, the Stalking Horse Purchaser is paying substantial consideration ($3.06 million) to the Debtors in addition to the credit bid, which is, in any event, "the equivalent of a cash purchase." In re Spillman Dev. Grp., Ltd., 401 B.R. 240, 253 (Bankr. W.D. Tex. 2009).

33. This other, non-credit bid form of consideration is equivalent to cash being paid by the Stalking Horse Bidder in exchange for any Acquired Assets to the extent that they are not subject to the liens securing the Loan Commitments.

3. The Bankruptcy Code's Core Policies are Served by Allowing the Stalking Horse Bidder to Credit Bid the Loan Commitments.

34. Finally, the Committee's requested relief would have the effect of undermining, rather than advancing core Bankruptcy Code policies. See In re Phila. Newspapers, LLC, 599 F.3d 298, 316 (3d Cir. 2010) (recognizing that a bankruptcy court may limit credit bidding where it is necessary to advance core bankruptcy policies). The proposed Sale would advance the Bankruptcy Code's core purpose, which is enabling distressed companies to maximize the value of their assets for the benefit of their creditors. See, e.g., In reGen. Motors Corp., 407 B.R. 463,

492 (Bankr. S.D.N.Y. 2009) (recognizing that preventing the "dismantling and liquidation of [the debtors] to the detriment of all involving ... serves the core purposes of the Bankruptcy Code and constitutes a strong business justification under section 363 of the Code to sell the debtors' assets outside of a plan process"). Furthermore, the proposed Sale sets a clear path for the Debtors to confirm the Liquidating Plan, which courts recognize is a fundamental purpose of the chapter 11 process. See In re CoServ, L.L.C., 273 B.R. 487, 497 (Bankr. N.D. Tex. 2002) (recognizing that debtors in possession are fiduciaries "holding the bankruptcy estate[s] and operating the business[es] for the benefit of [their] creditors and (if the value justifies) equity owners").

35. The Committee's requested relief, denying the Stalking Horse Bidder the right to credit bid the Loan Commitments, would have the effect of undermining these core policies. In fact, the Committee's requested relief, if granted, would materially increase the possibility that the Debtors are unable to consummate any restructuring transaction and would be forced to convert these cases to a liquidation under chapter 7 of the Bankruptcy Code, developments which would cause the value of the Debtors' assets to deteriorate and eliminate any possibility of a recovery for unsecured creditors (including administrative and priority creditors).

36. More specifically, the Committee's argument is predicated on the unfounded assumption that the Stalking Horse Bidder will continue to participate in these Chapter 11 Cases if the proposed Sale is not approved in accordance with the terms and conditions of the Stalking Horse Agreement. The Stalking Horse Agreement and DIP facility, however, expressly provide that the Stalking Horse Purchaser may terminate the Stalking Horse Agreement and its future DIP funding commitments if the Debtors do not close the Sale transaction within 60 days after the Petition Date (April 25, 2015). The Debtors are unaware of any reason that the Stalking

Horse Bidder will not terminate the Stalking Horse Agreement and the DIP facility, in which case the Debtors would be left without any alternative other than the contingent Prasari Bid.

Response to the Objection of Physiom Group, LLC

37. Pursuant to the Asset Purchase Agreement between PhysIOM Group, LLC ("PhysIOM") and Debtor ProNerve, LLC ("ProNerve"), PhysIOM agreed to sell to ProNerve substantially all of its assets, with the exception of certain Excluded Assets. Among the Excluded Assets were receivables billed to Federal Health Care Programs and their fiscal intermediaries (the "Government Receivables"). PhysIOM objects to the Sale Motion to the extent that the Sale Motion seeks authority for the Debtors to transfer the Government Receivables as part of the contemplated sale.

38. To the extent that the Stalking Horse Bidder purchases and collects any identifiable Government Receivables that are property of PhysIOM, or is found to have purchased cash that belongs to PhysIOM, it will turn over those funds to PhysIOM.

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Respectfully submitted,

/s/ Donald J. Detweiler

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