



Honorable Mike K. Nakagawa
United States Bankruptcy Judge



Entered on Docket
March 09, 2015

UNITED STATES BANKRUPTCY COURT

DISTRICT OF NEVADA

* * * * *

In re:)	Case No.: 10-29932-MKN
)	Chapter 11
CAREFREE WILLOWS, LLC,)	
)	Date: January 14, 2015
Debtor.)	Time: 9:30 a.m.

**ORDER ON MOTION TO MODIFY ORDER
AUTHORIZING USE OF CASH COLLATERAL¹**

On January 14, 2015, the court heard the Motion to Modify Order Authorizing Use of Cash Collateral (“Modification Motion”) brought by Carefree Willows, LLC, the debtor in possession in the above-captioned case. The motion was opposed by creditor AG/ICC Willows Loan Owner, LLC (“AG”). The appearances of counsel were noted on the record. After oral arguments were presented, the matter was taken under submission.

BACKGROUND

On October 22, 2010, Carefree Willows, LLC (“Debtor”) filed a voluntary Chapter 11 petition along with its schedules of assets and liabilities. (ECF No.1). It is a single asset real estate entity whose property consists of a 300-unit senior housing complex located in Henderson, Nevada (“Property”). On its real property Schedule “A,” Debtor represented that the current value of the Property was \$30,000,000. AG is a creditor of the Debtor that holds the primary claim secured by a deed of trust against the Property that also includes, inter alia, an assignment

¹ In this Order, all references to “ECF No.” are to the numbers assigned to the documents filed in the case as they appear on the docket maintained by the clerk of the court. All references to “Section” are to the provisions of the Bankruptcy Code, 11 U.S.C. §§ 101-1532. All references to “FRBP” are to the Federal Rules of Bankruptcy Procedure.

1 of rents clause.

2 On November 12, 2010, an order was entered approving a stipulation between the Debtor
3 and Union Bank, N.A., predecessor in interest to AG, for the interim use of the proceeds of its
4 lien against the Property (“cash collateral”). (ECF No. 34).

5 On November 18, 2010, an order was entered approving a further stipulation between the
6 Debtor and AG for further use of cash collateral through February 1, 2011. (ECF No. 48).

7 On December 6, 2010, AG filed a motion seeking a determination that the Debtor is a
8 “single asset real estate” (“SARE”) entity within the meaning of Section 101(51B) (“SARE
9 Motion”). (ECF No. 61). On December 29, 2010, Debtor filed opposition. (ECF No. 72). On
10 January 5, 2011, AG filed a reply. (ECF No. 77).

11 On January 14, 2011, Debtor filed a motion (“Valuation Motion”) seeking to determine
12 the value of the Property at \$30,000,000 “for purposes of confirmation.” (ECF No. 88). The
13 Valuation Motion was based on two appraisal reports: one valuing the Property as of September
14 2, 2010, prepared by Timothy R. Morse & Associates and another valuing the Property as of
15 August 24, 2010, prepared by Anderson Valuation Group, LLC. On February 2, 2011, AG filed
16 opposition that requested an evidentiary hearing. (ECF No. 123).

17 On January 28, 2011, an order was entered granting the SARE Motion (“SARE Order”).
18 (ECF No. 110). In its opposition to the SARE Motion, AG had alleged that it charges rents
19 approximately 20% higher than otherwise due to the additional services and activities it provides
20 to the tenants. The court, however, considered the authorities cited by the Debtor, and rejected
21 Debtor’s position that the additional services and activities constitute substantial business
22 activity separate from operations of the Property. See SARE Order at 3:6 to 6:7.

23 On February 8, 2011, an order was entered approving a further stipulation between the
24 Debtor and AG for use of cash collateral under certain terms on an ongoing basis, and
25 authorizing both parties to file motions seeking to modify its terms any time after May 1, 2011
26 (“Cash Collateral Order”). (ECF No. 128).

27 Also on February 8, 2011, Debtor filed a reply in support of the Valuation Motion (ECF
28 No. 129) accompanied by the Declaration of Kenneth Templeton (ECF No. 130) attesting that a

1 confirmable plan could be proposed if the court establishes a value of the Property of at least
2 \$30,000,000. On February 15, 2011, AG withdrew its opposition to the Valuation Motion after
3 reviewing the two appraisal reports. (ECF No. 134).

4 On February 28, 2011, AG filed a proof of claim, assigned Claim No. 10-1 (“POC 10-
5 1”). The total amount of the claim is for \$32,562,189.24. Of that amount, the claim states that
6 \$30,000,000 is secured based on a value of \$30,000,000 for the Property and that the remaining
7 amount of \$2,562,189.24 is unsecured. Although POC 10-1 was filed on February 28, 2011, it
8 did not include any postpetition interest that might have accrued pursuant to the underlying loan
9 documents.

10 On February 28, 2011, AG also filed a proposed plan of reorganization (ECF No. 138)
11 along with a proposed disclosure statement (ECF No. 137).

12 On March 2, 2011, Debtor filed its proposed plan of reorganization (ECF No. 145)
13 accompanied by a proposed disclosure statement (ECF No. 146).

14 On March 14, 2011, an order submitted by Debtor’s counsel was entered on the
15 Valuation Motion stating that the value of the Property “for purposes of the Debtor’s proposed
16 Plan of Reorganization **is at least** Thirty Million Dollars (\$30,000,000).” (ECF No. 156).

17 On March 17, 2011, an amended order submitted by counsel was entered on the
18 Valuation Motion stating that the value of the Property “for purposes of plan confirmation **is**
19 Thirty Million Dollars (\$30,000,000).” (“Valuation Order”). (ECF No. 163). (Emphasis added).

20
21 On March 25, 2011, Debtor filed an objection to POC 10-1. (ECF No. 178). On May 3,
22 2011, AG filed a response. (ECF No. 268). On May 10, 2011, Debtor filed a reply. (ECF No.
23 279). On May 24, 2011, an order was entered overruling Debtor’s objection to POC 10-1. (ECF
24 No. 323).

25 Debtor’s use of cash collateral continued under the Cash Collateral Order while the
26 Debtor and AG contested virtually every step along the way during the plan confirmation
27 process.

28 On February 29, 2012, Debtor filed a proposed Fourth Amended Plan. (ECF No. 578).

1 On April 3, 2012, an order was entered conditionally approving the disclosure statements
2 filed by both AG and the Debtor, and scheduling a confirmation hearing on both plans to
3 commence on May 31, 2012. (ECF No. 599). That order also provided that any modifications
4 of the plans and disclosure statements must be made before April 27, 2012.

5 On April 26, 2012, AG filed a proposed Second Amended Plan. (ECF No. 617). Under
6 its proposed plan, AG will receive either (1) all right, title, and interest in or to the Property, in
7 partial satisfaction of its secured claim, or (2) all right to control the Property and proceed with
8 foreclosure proceedings, in partial satisfaction of its secured claim.

9 On May 26, 2012, Debtor filed a first amendment to its Fourth Amended Plan. (ECF No.
10 745). Under its proposed plan, the Debtor will retain the Property, pay creditors over time, and
11 have existing equity holders maintain control of the business operations. AG's secured claim
12 would be paid in full over four years. The equity holders would contribute \$9 million to finance
13 the reorganization.

14 On May 31, 2012, the evidentiary hearing commenced on confirmation of the competing
15 plans. The hearing ("Plan Confirmation Hearing") took place over nine days, with the final day
16 of testimony taking place on August 27, 2012.² Along with plan confirmation, the same
17 evidence also was presented in connection with separate motions brought by AG to designate the
18 votes of alleged creditor Willows Account, LLC ("Willows Account")³ or to recharacterize⁴ the
19

20 ² The hearing took place on May 31, June 1, July 12, July 13, July 23, July 24, August 13,
21 August 14, and August 27, 2012. The following individuals testified during the evidentiary
22 hearing: Alex Roudi, Edward McDonough, John White, Edward Erganian, Edward Burr, Deron
23 Bocks, Grant Lyon, Elliott Burrell, Claudia Widhalm, Glenn Anderson, Thomas Anderson,
Beverly Elrod, Harry Kogan, Kevin Close, Stanley Paher, Phillip Aurbach, and Kenneth
Templeton.

24 ³ See Motion to (1) Deem Willows Account, LLC an Insider; (2) Designate the Claim of
25 Willows Account, LLC Pursuant to 11 U.S.C. § 1126(e); (3) Subordinate the Claim of Willows
26 Account, LLC; and Objection to Claim No. 3 of Willows Account, LLC Pursuant to 11 U.S.C. §
27 502(d) ("AG Designation Motion"). (ECF No. 625). The motion was accompanied by the
Declaration of Ali M.M. Mojdehi (ECF No. 628) to which was attached 33 different exhibits.

28 ⁴ See Motion to Recharacterize the Claim of Willows Account, LLC as Equity ("AG
Recharacterization Motion"). (ECF No. 623).

1 latter's claim. An additional motion by the Debtor to designate the claim of AG⁵ also was
2 heard.⁶ The appearances of counsel were noted on the record each day. Closing briefs were
3 filed on September 26, 2012. Reply briefs were filed on October 9, 2012. Thereafter, the
4 matters were taken under submission.

5 Confirmation of the competing plans was dependent on the outcome of the parties'
6 designation and recharacterization motions. Resolution of those matters was based on the
7 evidence presented at the Plan Confirmation Hearing in addition to live testimony previously
8 presented by the Debtor in connection with other matters presented to the court.⁷

9 After all of the matters were taken under submission, the parties attempted several times
10 to introduce additional issues or materials after the record was closed. On October 17, 2012, the
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12 ⁵ See Motion to Designate the Claim of AG/ICC and Affiliates ("Debtor's Designation
13 Motion"). (ECF No. 219).

14 ⁶ On August 24, 2012, before the Plan Confirmation Hearing was concluded, AG filed an
15 amended proof of claim that was assigned Claim No. 10-2 ("POC 10-2"). The claim states that
16 the original amount of the claim as of the petition date was \$32,565,392.63. POC 10-2 states
17 that \$36,240,000 is the secured amount based on a collateral value of \$36,240,000, and that there
18 is a remaining amount of \$269,757.92 that is unsecured. An attachment to POC 10-2 explains
19 that the amended value of the Property collateral is based on the Debtor's appraisal evidence of
20 value that was admitted at evidentiary hearings on plan confirmation. Unlike its initial proof of
21 claim, AG includes in POC 10-2 a claim for postpetition interest.

22 ⁷ On March 25, 2011, AG commenced an action against Carefree Holdings Limited
23 Partnership ("Carefree Holdings") in the Eighth Judicial District Court, Clark County, Nevada,
24 Case No. A-11-637829-C ("Guaranty Suit"), alleging breach of certain guaranties as a result of
25 the Debtor's non-payment of the Loan. AG seeks in excess of \$34,018,225.30 from Carefree
26 Holdings in that action. On September 19, 2011, Debtor commenced an adversary proceeding
27 against AG, Adversary No. 11-01262-MKN ("AECF No."), seeking, inter alia, to enjoin AG
28 from pursuing Carefree Holdings, Templeton Family Trust dated October 8, 1993, Ken II Trust
dated May 4, 1998, Kenneth L. Templeton ("Templeton"), and MLPGP, L.L.C., as guarantors
("Guarantors") of the loan obligation that is the basis for AG's primary claim. On November 29,
2011 and December 1, 2011, an evidentiary hearing was conducted on the Debtor's request for a
preliminary injunction ("Preliminary Injunction Motion") at which several witnesses called by
the Debtor testified under oath. Those witnesses included Kevin Close, Kenneth Templeton, and
Edward McDonough. On February 10, 2012, an order was entered denying a preliminary
injunction. (AECF No. 123). In the memorandum decision accompanying that order (AECF
No. 122), the court considered the evasive and contradictory testimony of Templeton, and
concluded that issuance of a preliminary injunction in favor of the Guarantors would not be in
the public interest. Id. at 26:6 to 28:3.

1 Guarantors filed a motion to redact portions of transcripts of the evidentiary hearing on the
2 Debtor's preliminary injunction request that had been held in November and December of the
3 prior year and which already were part of the public record. (ECF No. 914). On December 21,
4 2012, Debtor objected to AG's amended POC 10-2. (ECF No. 939). On January 23, 2013, a
5 hearing was conducted on Debtor's objection to POC 10-2 and the matter was taken under
6 submission.

7 On February 11, 2013, Debtor filed a request for judicial notice regarding the status of
8 certain appellate matters in the Guaranty Suit. (ECF No. 955). On March 6, 2013, AG filed a
9 notice of "supplemental authority" regarding a decision reached by the Seventh Circuit in
10 support of AG's objection to confirmation of the Debtor's proposed Plan. (ECF No. 959). On
11 May 30, 2013, AG filed another notice of "supplemental authority" regarding a decision reached
12 by the Ninth Circuit relevant to the AG Recharacterization Motion. (ECF No. 973). On June 12,
13 2013, Debtor filed a supplemental opposition to the AG Recharacterization Motion. (ECF No.
14 975). On December 10, 2013, AG filed a request for judicial notice regarding a loan payoff
15 demand that it had received from the Carefree Holdings. (ECF No. 1013). On December 27,
16 2013, Debtor filed a request for judicial notice regarding AG's purchase of other senior living
17 facilities in Southern Nevada. (ECF No. 1017).

18 Finally, on February 5, 2014, AG filed a motion to reopen the record regarding the
19 confirmation hearings and related matters so that it could introduce evidence that the value of the
20 Property has increased significantly since the Valuation Order was entered ("AG Reopening
21 Motion"). (ECF No. 1040).⁸ On February 19, 2014, Debtor filed opposition to that motion.
22 (ECF No. 1049). The AG Reopening Motion was initially noticed to be heard on March 5, 2014
23 (ECF No. 1042), but the hearing was continued to March 20, 2014.

24 Separate memorandum decisions and accompanying orders denying the Debtor's
25 Designation Motion, as well as granting the AG Recharacterization Motion and AG Designation
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27 ⁸ The AG Reopening Motion was accompanied by the Declaration of Peter Evans (ECF
28 No. 1041), to which was attached an appraisal of the Property as of January 24, 2014. As of that
date, AG's appraiser valued the Property at \$39,000,000.

1 Motion, were entered on March 14, 2014, March 17, 2014, and March 18, 2014, respectively.
2 (ECF Nos. 1058, 1060, 1063, 1064, 1067, 1068). Because the resolution of those motions was
3 favorable to AG, on March 20, 2014, it withdrew its request to reopen the evidentiary record.

4 Debtor appealed the order denying its designation motion. (ECF No. 1078). Willows
5 Account appealed the order granting the AG Recharacterization Motion. (ECF No. 1085).
6 Debtor and Willows Account appealed the order granting the AG Designation Motion. (ECF
7 Nos. 1088 and 1090). All of the appeals were directed to the United States District Court for the
8 District of Nevada (“District Court”). Willows Account further filed a motion seeking a stay
9 pending appeal of the order granting the AG Recharacterization Motion. (ECF No. 1114). An
10 order denying the motion for stay pending appeal was entered on May 20, 2014. (ECF No.
11 1174).

12 Debtor then filed a proposed Fifth Amended Plan of Reorganization on June 4, 2014.
13 (ECF No. 1186). An order was entered staying proceedings on that further amended plan (“Stay
14 Order”) on July 18, 2014. (ECF No. 1219). Debtor appealed the Stay Order. (ECF No. 1226).
15 Debtor then sought a stay of the Stay Order. An order was entered denying that requested stay
16 on August 15, 2014. (ECF No. 1254). Thereafter, an order was entered by the District Court
17 denying leave to appeal the Stay Order on October 23, 2014. (ECF No. 1284). No stay pending
18 appeal of the courts orders on the designation motions or recharacterization motion has been
19 obtained from the District Court or any other court.

20 On November 17, 2014, Debtor filed the instant Modification Motion (ECF No. 1304),
21 accompanied by the Declaration of Kevin Close (“Close Declaration”). (ECF No. 1305). The
22 motion was noticed to be heard on January 7, 2015 (ECF No. 1306), but by stipulation was
23 rescheduled for hearing on January 14, 2015, along with other motions brought by the Debtor.
24 (ECF No. 1317).⁹ On December 31, 2014, AG filed an opposition to the instant motion (“AG
25 Opposition”) (ECF No. 1322), accompanied by the Declaration of Alex Roudi (“Roudi
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27 ⁹ The other matters brought by the Debtor are its Motion for Order to Clarify Order
28 Staying Proceedings (ECF No. 1287) and its Motion to Reopen Record (ECF No. 1295). Those
matters are the subject of separate orders entered contemporaneously herewith.

1 Declaration”). (ECF No. 1324). On January 7, 2015, Debtor filed a reply (“Reply”). (ECF No.
2 1326).

3 DISCUSSION

4 Attached as Exhibit “A” to the Cash Collateral Order is a budget for the Debtor’s
5 business operations on the Property. The monthly operating budget includes various authorized
6 expenditures, including a 4% management fee. The order also provides that “the Debtor is
7 authorized to expend up to 5% more than is shown on the Budget for expenses similar to those
8 stated in the Budget in any month without further Court order and the Debtor is prohibited from
9 spending more than 5% than the amount of the Budget without consent of the Lender or an order
10 of this court” Cash Collateral Order at 2:6-9.

11 The order further provides for monthly payments to be made to AG as “adequate
12 protection” for the use of its cash collateral. Two payments are required each month: (1)
13 minimum adequate protection payments of \$75,000 due on the tenth business day, and (2)
14 additional adequate protection payments of “the funds in excess of \$125,000 held by the Debtor
15 (the ‘Buffer’) at the end of each month, following payment of all Operating Expenses.” Cash
16 Collateral Order at 2:15-17.

17 Debtor now seeks to modify the Cash Collateral Order to reduce the amount of adequate
18 protection payments. It maintains that it currently pays \$230,000 per month as adequate
19 protection payments to AG, see Close Declaration at ¶ 4, that it has paid \$8,068,169 in adequate
20 protection payments during the case, id. at ¶ 8, that the value of the Property has significantly
21 increased, and that twenty percent of the income generated from the business is from services
22 provided by the Debtor to the residents, id. at ¶ 6 & Exhibit “A,” rather than the rent paid as cash
23 collateral of AG.¹⁰ It argues that it has substantial administrative expenses that must be paid,
24 including the purchase of at least one new bus to transport residents of the senior living facility.
25 See Close Declaration at ¶ 9. In lieu of the current payments under the existing Cash Collateral
26 Order, Debtor seeks a modification requiring it to pay a maximum of \$130,000 per month and
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28 ¹⁰ This argument previously was rejected in connection with the court’s determination of
the SARE Motion. See discussion at 2, supra.

1 granting AG a replacement lien on future cash collateral. See Modification Motion at 9:5-7.

2 AG maintains that Debtor has not met the requirements under FRBP 60(b) for relief from
3 the Cash Collateral Order. See AG Opposition at 8:26 to 10:23. It argues that its lien
4 encompasses all of the revenues generated from operations on the Property, not just the rents
5 received from the tenants. Id. at 11:6 to 12:10 and 15:21 to 17:11. Additionally, it asserts that
6 its interest in the Property as well as the cash collateral may not be adequately protected by the
7 increasing value of the Property. Id. at 17:14 to 19:13.¹¹ Finally, AG argues that there are no
8 substantial administrative expenses that need to be paid because Debtor's counsel is the only
9 retained professional in the case, but currently is being paid by Carefree Holdings, rather than by
10 the Debtor. Id. at 19:18 to 20:7.¹²

11 The court having considered the arguments presented, as well as the record in the case,
12 concludes that relief from the Cash Collateral Order must be denied without prejudice.

13 As a threshold matter, Debtor has not identified the administrative expenses that the Cash
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15 ¹¹ Exhibit "A" to the Roudi Declaration includes AG's calculation of interest and default
16 interest accruing since the bankruptcy petition date, and Exhibit "B" reflects the postpetition
17 adequate protection payments received from the Debtor through December 31, 2014. The total
18 amount of postpetition payments reflected in Exhibit "B" matches the amount set forth in the
19 Close Declaration. While both the Debtor and AG have asserted that the Property actually
20 increased in value from the petition date forward, neither have sufficiently addressed: (1)
21 whether AG was even entitled to adequate protection payments when the Property was
22 appreciating in value, and (2) whether there was a point in time when the Debtor's postpetition,
23 preconfirmation payments should have been applied to reduce the principal balance of AG's
24 secured claim and therefore the accruing interest. Compare First Federal Bank of California v.
25 Weinstein (In re Weinstein), 227 B.R. 284, 296-97 (B.A.P. 9th Cir. 1998).

22 ¹² As to the purchase of a new bus for the residents of the senior facility, AG maintains
23 that it would be an expense out of the ordinary course of business that should be the subject of a
24 separate motion or a stipulation between the parties. Id. at 19 n. 14. At the hearing, AG also
25 argued that the Debtor has made expenditures exceeding the 5% variance from the operating
26 budget permitted by the Cash Collateral Order. Its counsel referred to the Debtor's monthly
27 operating report for November 2014 (ECF No. 1320) reflecting payment of management fees of
28 \$22,935, which is more than double the estimated monthly management fees included in the
original operating budget attached to the Cash Collateral Order. The management fee is paid to
Ken Templeton Realty & Investment, Inc. ("KTRI"), an entity that is an insider of the Debtor
and controlled by Templeton. At this juncture, however, AG has not requested that the Debtor
be prohibited from further use of cash collateral, but only that the relief requested in the
Modification Motion be denied.

1 Collateral Order prevents it from paying. The Cash Collateral Order includes a detailed
2 operating budget that appears to be sufficient to allow the Debtor's operations to generate
3 significant profits. As AG has noted, Debtor's counsel is the only retained professional in the
4 case and counsel's services apparently are being paid by Carefree Holdings, rather than the
5 Debtor. Even if the Debtor was paying fees of its counsel, such payment as an administrative
6 expense can be allowed only after a duly noticed application and a hearing. Absent any
7 information as to the administrative expenses that must be paid, Debtor simply has not
8 demonstrated that relief from the Cash Collateral Order is appropriate.

9 Moreover, it appears that the Debtor may not be in compliance with the operating budget.
10 AG correctly observed at the hearing that the management fee paid to KTRI, an insider of the
11 Debtor, appears to have doubled since the Cash Collateral Order was entered. Without some
12 explanation for this apparent violation of the express terms of the Cash Collateral Order, the
13 court is not inclined to grant relief at this time.

14 Finally, extraordinary capital expenses, such as the acquisition of a replacement bus to
15 transport tenants of the senior living facility, would not be encompassed by a monthly operating
16 budget.¹³ Debtor is free to seek AG's consent to use cash collateral for such purchases or to seek
17 court permission by separate motion.

18 For these reasons, the Modification Motion must be denied. Because Debtor has not
19 made even the threshold showings required for relief, it is unnecessary to address the remaining
20 issues raised by the parties.

21 **IT IS THEREFORE ORDERED** that the Motion to Modify Order Authorizing Use of
22 _____

23 ¹³ Debtor indicates that the cost of a replacement bus is approximately \$120,000. See
24 Close Declaration at ¶ 9. Ironically, the annual management fee in the original operating budget
25 was \$127,132, or slightly more than a \$10,500 monthly average. According to the Debtor's
26 monthly operating report for December 2013 (ECF No. 1031), the total management fee paid to
27 KTRI throughout the case was \$676,926. Debtor's previously mentioned that the monthly
28 operating report ending November 30, 2014, disclosed total management fees of \$890,879, i.e.,
an additional \$213,953 since the end of 2013, with an additional \$19,356 projected for December
2014. To the untrained eye, it appears that the amount paid in 2014 to KTRI in management fees
beyond the projections contained in the original operating budget was roughly equal to the cost
of a replacement bus for the senior tenants.

Cash Collateral, Docket No. 1304, be, and the same hereby is, **DENIED**.

and sent via FIRST CLASS MAIL BY THE COURT AND/OR BNC to:

CHRISTOPHER H. HART
SCHNADER HARRISON SEGAL & LEWIS LLP
ONE MONTGOMERY STREET, SUITE 2200
SAN FRANCISCO, CA 94104-5501

ALLISON M. REGO
4401 EASTGATE MALL
SAN DIEGO, CA 92121

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