

UNITED STATES BANKRUPTCY COURT
Eastern District of California

Honorable Michael S. McManus
Bankruptcy Judge
Sacramento, California

April 2, 2018 at 10:00 a.m.

1. 17-26125-A-11 FIRST CAPITAL RETAIL, MOTION FOR
GL-1 L.L.C. RELIEF FROM AUTOMATIC STAY
5060 MONTCLAIR PLAZA LANE OWNER, L.L.C VS. 10-17-17 [62]

Tentative Ruling: The court will continue the hearing on this stay relief motion to a date to be determined at the April 2 hearing.

2. 17-26125-A-11 FIRST CAPITAL RETAIL, MOTION TO
GEL-17 L.L.C. SELL AND TO ASSUME LEASE OR
EXECUTORY CONTRACT
3-7-18 [304]

Tentative Ruling: This is the same ruling as posted for the hearing on March 29.

The motion will be denied.

The debtor in possession seeks approval of a sale of substantially all its assets, free and clear of all interests, to Pilot Real Estate Group, L.L.C., for \$1.2 million. In connection with the sale, it also seeks to assume and assign eight leases of its Cinnabon franchise stores to Pilot. Pilot was the prevailing bidder at the auction conducted by the debtor on March 20. Docket 333. The debtor also asks for:

- waivers of the 14-day periods of Fed. R. Bankr. P. 6004(h) (sales) and 6006(d) (assignments) because the sale and lease assignments are set to take place no later than April 12, 2018;
- a "good faith purchaser" finding under 11 U.S.C. § 363(m);
- a determination under 11 U.S.C. § 363(n) that the sale price was not controlled by an agreement among potential bidders at such sale; and
- a finding that the buyer is not a successor in interest to or subject to successor liability for the debtor or any of the retail store.

The assets being sold include, without limitation:

inventory, accounts receivables, executory contracts, cash and cash equivalents, deposits, franchise agreements (including franchise agreements), supply agreements, permits, licenses, software systems, fixtures, furniture, equipment, tools, supplies, intellectual property, all leasehold interests and tenant improvements, and all other assets used in connection with operating the debtor's various franchise businesses.

Six of the leases to be assumed and assigned are not terminated and the debtor is still operating those locations (Montclair Plaza, Galleria at Tyler, Solano Town Center, Montebello Town Center, Santa Rosa, Universal City Walk).

Two of the leases to be assumed and assigned were terminated, but the debtor is pursuing negotiations and/or avoidance of the forfeiture to reinstate the leases. The court cannot determine from the record which two leases the debtor is seeking to assume and assign.

The debtor also intends to reject four leases (Moreno Valley, Northridge Mall, Oakridge Mall, Imperial Valley).

Pilot will also assume some employee-related (e.g., sick and vacation days) and customer-related liabilities.

11 U.S.C. § 1107(a) provides that a debtor-in-possession shall have all rights, powers, and shall perform all functions and duties, subject to certain exceptions, of a trustee, "[s]ubject to any limitations on [that] trustee." This includes the trustee's right to sell property of the estate pursuant to section 363. Section 363(b) allows, then, a debtor-in-possession to sell property of the estate, other than in the ordinary course of business. The sale must be fair, equitable, and in the best interest of the estate. Mozer v. Goldman (In re Mozer), 302 B.R. 892, 897 (C.D. Cal. 2003). Sale of property outside the ordinary course of business requires the estate to show good faith and valid business justification for the sale. 240 N. Brand Partners, Ltd. v. Colony GFP Partners, LP (In re 240 N. Brand Partners, Ltd.), 200 B.R. 653, 659 (B.A.P. 9th Cir. 1996). Good faith "encompasses fair value, and further speaks to the integrity of the transaction." Id.

Pursuant to 11 U.S.C. § 363(f), the debtor in possession may sell the personal property free and clear of liens only if: 1) applicable nonbankruptcy law permits sale of such property free and clear of such liens; 2) the entity holding the lien consents; 3) the proposed purchase price exceeds the aggregate value of the liens encumbering the property; 4) the lien is in bona fide dispute; or 5) the entity could be compelled to accept a money satisfaction of the lien.

11 U.S.C. § 365(a) and (b) (1) provides that:

"(a) Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor.

"(b) (1) If there has been a default in an executory contract or unexpired lease of the debtor, the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee--

"(A) cures, or provides adequate assurance that the trustee will promptly cure, such default other than a default that is a breach of a provision relating to the satisfaction of any provision (other than a penalty rate or penalty provision) relating to a default arising from any failure to perform nonmonetary obligations under an unexpired lease of real property, if it is impossible for the trustee to cure such default by performing nonmonetary acts at and after the time of assumption, except that if such default arises from a failure to operate in accordance with a nonresidential real property lease, then such default shall be cured by performance at and after the time of

assumption in accordance with such lease, and pecuniary losses resulting from such default shall be compensated in accordance with the provisions of this paragraph;

"(B) compensates, or provides adequate assurance that the trustee will promptly compensate, a party other than the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default; and

"(C) provides adequate assurance of future performance under such contract or lease."

11 U.S.C. § 365(b) (3) provides:

"(3) For the purposes of paragraph (1) of this subsection and paragraph (2) (B) of subsection (f), adequate assurance of future performance of a lease of real property in a shopping center includes adequate assurance—

"(A) of the source of rent and other consideration due under such lease, and in the case of an assignment, that the financial condition and operating performance of the proposed assignee and its guarantors, if any, shall be similar to the financial condition and operating performance of the debtor and its guarantors, if any, as of the time the debtor became the lessee under the lease;

"(B) that any percentage rent due under such lease will not decline substantially;

"(C) that assumption or assignment of such lease is subject to all the provisions thereof, including (but not limited to) provisions such as a radius, location, use, or exclusivity provision, and will not breach any such provision contained in any other lease, financing agreement, or master agreement relating to such shopping center; and

"(D) that assumption or assignment of such lease will not disrupt any tenant mix or balance in such shopping center."

11 U.S.C. § 365(f) further provides that:

"(f) (1) Except as provided in subsections (b) and (c) of this section, notwithstanding a provision in an executory contract or unexpired lease of the debtor, or in applicable law, that prohibits, restricts, or conditions the assignment of such contract or lease, the trustee may assign such contract or lease under paragraph (2) of this subsection.

"(2) The trustee may assign an executory contract or unexpired lease of the debtor only if--

"(A) the trustee assumes such contract or lease in accordance with the provisions of this section; and

"(B) adequate assurance of future performance by the assignee of such contract or lease is provided, whether or not there has been a default in such contract or lease.

"(3) Notwithstanding a provision in an executory contract or unexpired lease of the debtor, or in applicable law that terminates or modifies, or permits a

party other than the debtor to terminate or modify, such contract or lease or a right or obligation under such contract or lease on account of an assignment of such contract or lease, such contract, lease, right, or obligation may not be terminated or modified under such provision because of the assumption or assignment of such contract or lease by the trustee."

The standard for determining whether to approve the assumption of unexpired leases and/or executory contracts is the business judgment test. Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific R. Co., 318 U.S. 523 (1943); Robertson v. Pierce (In re Chi-Feng Huang), 23 B.R. 798, 800-01 (B.A.P. 9th Cir. 1982) (holding that the primary issue is whether rejection or assumption would benefit the general unsecured creditors, which may also involve a balancing of interests).

The court "should approve the rejection [or assumption] . . . unless it finds that the debtor-in-possession's conclusion that rejection [or assumption] would be 'advantageous is so manifestly unreasonable that it could not be based on sound business judgment, but only on bad faith, or whim or caprice.' [. . . .] Such determinations, clearly, involve questions of fact . . . which we review for clear error." Agarwal v. Pomona Valley Medical Group, Inc. (In re Pomona Valley Medical Group, Inc.), 476 F.3d 665, 670 (9th Cir. 2007).

"The Bankruptcy Court, in evaluating the debtor's decision, 'should presume that the debtor-in-possession acted prudently, on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the bankruptcy estate.' It should approve the decision to reject [or assume] . . . 'unless it finds that the debtor-in-possession's conclusion that rejection [or assumption] would be advantageous is so manifestly unreasonable that it could not be based on sound business judgment, but only on bad faith, or whim or caprice.'" In re Yellowstone Mountain Club, LLC, Case Nos. 08-61570-11, 0861571-11, 08-61572-11, 08-61573-11, CV-09-48-BU-SEH, 2010 WL 5071354, at *2 (D. Mont. Dec. 7, 2010) (quoting and citing to Pomona Valley Medical Group at 670).

The motion will be denied.

First, the motion describes no benefit to the estate or its creditors from the sale. It says nothing about the net sales proceeds generated for the benefit of the estate and its creditors. It says nothing about the claims that are secured by the debtor's assets. It says nothing about any agreements (e.g., carve-out) between the debtor and its secured creditors for the sharing of the sale proceeds.

After cure amounts to the franchisor and the lessors are paid from the \$1.2 million purchase price, what will be left over for the estate and the senior secured creditor, Byline Bank?

Second, the motion does not outline the encumbrances against each of the debtor's assets. As such, the court cannot analyze the sale under 11 U.S.C. § 363(f). For instance, the motion does not indicate whether Byline and any other secured creditors have consented to the sale. The motion speaks of liens and encumbrances in generalities without being specific as to identity of creditor, collateral, and claim amount. And, there is no indication that Byline Bank has consented to the sale.

Third, the court cannot approve relief under 11 U.S.C. § 363(m) as there is no declaration in the record from a responsible person associated with Pilot

regarding Pilot's good faith in connection with this sale.

Fourth, the court cannot approve relief under 11 U.S.C. § 363(n), which permits avoidance of a sale when the sale price was controlled by an agreement among the potential bidders. The court cannot pre-adjudicate the liabilities of buyers under section 363(n). No one has invoked the remedies under section 363(n). As such, there is no case or controversy under section 363(n) for the court to determine if relief under it is warranted. Nor will the court render an advisory opinions with regard to section 363(n).

"[I]t is quite clear that "the oldest and most consistent thread in the federal law of justiciability is that the federal courts will not give advisory opinions." Flast v. Cohen, 392 U.S. at 96 . . . (citing c. Wright, Federal Courts 34 (1963)). The doctrine of justiciability is a blend of constitutional and policy or prudential considerations. Id. at 97. . . ."

Krasnoff v. Marshack (In re General Carriers Corp.), 258 B.R. 181, 190 (B.A.P. 9th Cir. 2001).

Fifth, even if the court were to ignore the foregoing deficiencies, it cannot approve the assumption and assignment of the leases referenced in the motion.

To begin with, the motion is not clear which of the terminated leases will be assumed. The motion lists three terminated leases where the debtor is still operating, but it does not state which of these leases will be assumed. Docket 304 at 5.

Nor has the debtor clarified how it will be assuming leases that have been terminated. There is no report from the debtor concerning its negotiations with lessors with terminated leases or on the status of any attempt to set aside a lease forfeiture.

Sixth, the court cannot grant this motion given the numerous objections by lessors and the franchisor based on the debtor's under-estimation of cure amounts.

The cure amount claimed by Cinnabon Franchisor SPV, L.L.C., exceeds the debtor's estimate by approximately \$88,508 (per the debtor it is \$248,088, per Cinnabon it is \$336,589.18). This does not include a \$15,000 transfer fee with respect to each franchise location. Dockets 317 at 3; Docket 350.

The cure amount of the leases of Starwood Retail Partners, L.L.C. and The Macerich Company and Westfield, L.L.C. exceeds the debtor's cure amount on those leases by hundreds of thousands of dollars. The court cannot tell from the parties' pleadings which leases in the objection will be assumed and which will be rejected. Docket 304 at 5; Docket 318 at 3-4.

The cure amount of the leases of GGP Northridge Fashion Center, L.P. and Tyler Mall Limited Partnership exceeds the debtor's cure amount on those leases by more than \$2,000. Docket 319 at 4.

Seventh, regardless of how the debtor has classified it (but subject to possible relief from the lease forfeiture), the Montclair Plaza lease cannot be assumed and assigned because that lease was terminated pre-petition and the landlord intends to obtain relief from stay at the upcoming April 2 hearing on its stay relief motion. Docket 324.

Eight, the court does not have sufficient evidence as to the debtor's compliance with section 365(b)(1). For instance, given the additional cure amounts identified by the franchisor and the lessors, the court cannot find in the record an adequate assurance that these amounts will be cured. Perhaps these amounts can be satisfied from the sale proceeds but does Byline Bank agree to the payment of these cures from the purchase price? After cure amounts to the franchisor and the landlords are paid from the \$1.2 million purchase price, what will be left over for the estate and, more specifically, the senior secured creditor, Byline Bank?

Nor is there evidence of adequate assurances of future performance from Pilot. The debtor should note that the requirement of such assurances is particularly important given the leases are for space in shopping centers. See 11 U.S.C. § 365(b)(3).

Specifically, GGP Northridge Fashion Center, L.P., and Tyler Mall Limited Partnership have raised issues concerning adequate assurances of future performance as to operating expenses billed on an estimated basis, subject to annual reconciliation and adjustment, as well as to assurances with respect to indemnification obligations. Docket 319 at 6-8.

Another issue not addressed by the motion is whether Pilot is able to provide additional security, as requested by some landlords (e.g., GGP Northridge Fashion Center, L.P. and Tyler Mall Limited Partnership (Docket 319 at 8-9)) under section 365(1).

Ninth, the motion does not address the debtor's ability to cure non-monetary obligations under its franchise agreements, more specifically its obligations to complete remodeling of some of the locations. Docket 317 at 3.

Tenth, there is no apparent justification for the debtor preventing Project Westbound, L.L.C., from participating in the auction. The debtor admits that Project met the bidding requirements. "Debtor determined that the alternate bid of Project Westbound, LLC met the Bid Requirements." Docket 333 at 2.

The court expects complete and unequivocal candor from the debtor and Pilot regarding their consultations concerning Project's participation in the auction and regarding Pilot's offer of employment to the debtor's principal.

Eleventh, while the court takes note of the *sub rosa* plan objection proffered by MCA Recovery, L.L.C. and Yellowstone Capital West, L.L.C., the court entertained this same objection at the February 27 hearing and it authorized the auction to proceed. Those arguments were adequately addressed by the court and the court entered an order on March 2, 2018, approving the bidding procedures and rejecting this objection. Docket 302.

Further, the court is not persuaded that it should deny approval of the proposed sale on this ground. The court has considered the interests of all parties, including the debtor, administrative creditors, secured creditors including specifically senior secured creditor Byline Bank and the landlords, the franchisor, unsecured creditors, and equity holders. If the sale does not take place, there will be nothing for the debtor to sell and the secured creditors will receive nothing. The franchisor will not permit continued operation of the debtor's business beyond April 12, 2018. The debtor does not have real property assets and its personal property assets, besides the franchise agreements and leases, are minimal and fully encumbered, the most valuable of which is about \$200,000 in cash that is being depleted fast and a

disputed claim to \$288,381 in funds held by First Data. To realize any value in the debtor's business as a going concern, the debtor would have to convince the court that a sale can be approved prior to April 12. After that date, there will be nothing for the debtor to operate or sell. The landlords involved with the leases that the debtor is seeking to assume and assign are prepared to take possession of the leased premises if the debtor stops operating. The court will have no choice but to grant their stay relief motions, given that the debtor would be no longer operating. This satisfies the "emergency" considerations given in The Comm. of Equity Sec. Holders v. The Lionel Corp. (In re The Lionel Corp.), 722 F.2d 1063, 1068-69 (2nd Cir. 1983).

The court also has given the parties sufficient other procedural safeguards, outside of plan confirmation, regarding the instant sale. The hearing on the motion to approve the bidding procedures for this sale was held on February 27, 2018, about one month before the hearing on the actual sale, March 29. Docket 295. The motion for the February 27 hearing was filed on February 16. Docket 263.

Notwithstanding the foregoing, because the safeguards of the plan confirmation process are being bypassed, the court expects complete candor from the debtor and Pilot regarding their exclusion of Project from the auction and Pilot's offer of employment to the debtor's principal in the new company.

Twelfth, the objection of First Data Merchant Services, L.L.C. will be overruled. First Data holds \$214,932.33 in funds that are claimed by both the debtor and MCA Recovery, L.L.C., as assignee of Yellowstone Capital West, L.L.C. Entitlement to the funds is still in dispute between the debtor and MCA. First Data complains that the purchase agreement includes a provision that "*calls for the sale of 'any cause of action, lawsuit, judgment, claim, refund, right of recovery, right of set-off, counterclaim, defense, demand, warranty claim, right to indemnification, contribution, advancement of expenses or reimbursement, or similar rights' held by Debtor against First Data.*" Docket 340 at 5.

First Data has filed an interpleader action (Adv. Proc. No. 18-2030), attempting to protect itself from claims by the debtor and MCA over the funds.

First Data is asking the court to compel the debtor and Pilot to modify the instant purchase agreement "to reflect that there are no claims or causes of action to be asserted against First Data." Docket 340 at 5.

First Data's objection will be overruled. The court will not compel the debtor and Pilot to modify the purchase agreement with respect to the reference to claims the debtor has against First Data. The reference in the agreement to claims against First Data is to any potential claim against First Data. Having or not having this provision in the agreement is not determinative or conclusive as to whether the debtor actually has claims against First Data. The debtor's claims against First Data are whatsoever they are.

The court cannot do what First Data is asking because the objection seeks some sort of a comfort ruling to the effect that First Data is not liable to the debtor for anything. The court will not make such determinations except in the context of an adversary proceeding. See Fed. R. Bankr. P. 7001(1), (2), (7), (9).

Finally, the objection of CBL & Associates Management, Inc., will be overruled as moot. The debtor intends to reject its unexpired lease. CBL does not have

contractual privity with the debtor. Rather, the debtor appears to be a sublessee from CBL's lessee. Docket 304 at 5; Docket 327.

3. 17-26125-A-11 FIRST CAPITAL RETAIL, MOTION FOR
18-2017 L.L.C. GEL-1 PRELIMINARY INJUNCTION
FIRST CAPITAL RETAIL, L.L.C. V. 2-19-18 [7]
FIRST CAPITAL REAL ESTATE

Tentative Ruling: The motion will be denied as moot.

The plaintiff in this proceeding, First Capital, L.L.C., the debtor in the underlying bankruptcy case, seeks an injunction with respect to the proposed sale of the plaintiff's member's 100% interest in the plaintiff at a foreclosure auction. The auction allegedly was set by the defendant, First Capital Real Estate Investments, L.L.C. The defendant's principal is Suneet Singal, the prior owner of the debtor who sold his interest in the debtor to the current owner, Rameshwar Prasad. It is alleged that if Mr. Prasad is displaced, the debtor's efforts to sell its assets will be frustrated.

The motion will be denied as moot because the plaintiff has had the opportunity to conduct a sale. While the sale has not been approved, no other sale is likely in the short time the debtor has remaining to assume and assign its leases and continue to operate under its franchise agreement. As such, there is no viable reason to continue the temporary injunctive relief any longer.