

Eastern District of California

July 24, 2014 at 2:00 p.m.

- Tentative Ruling:** Oral argument may be presented by the parties at the scheduled hearing, where the parties shall address the issues identified in this tentative ruling and such other issues as are necessary and appropriate to the court's resolution of the matter.

The Approval of Disclosure Statement is denied.

Background: Judy and Michael House, Debtors-in-Possession, operate two ranches in the Modesto area: Triumph Ranch and Smith Ranch, consisting of raw land and buildings used for poultry grow-out facilities and residential improvements. Debtors-in-Possession lease out the properties under long-term commitment with Petaluma Acquisition, LLC, a large poultry producer for about \$26,000.00 a month. Debtors-in-Possession financed their operation with five different loans against the real estate and their personal debt loan continually increased. Mrs. House also runs a small photography business in the area that grosses about \$4,000 a month.

Creditor/Class	Treatment	
Administrative Claims	Claim Amount	Estimated at \$107,325
	Impairment	

	Professional fees: \$100,000 Clerk's Office fees: \$500 US Trustee fees: \$325 Accountant fees: \$4,000 IRS for form 1040, 2013: \$2,500 FTB Form 540, 2013: \$500 Claims paid in full on the effective day or upon entry of court order.	
Priority Tax Claims	Claim Amount	Estimated \$3000
	Impairment	
	FTB Form 540 for 2012: allowed amount estimated at \$500 will be paid on the effective date IRS Form 1040 for 2012: allowed amount estimated at \$2,500 with interest paid as provided by the statute at 4%, monthly payment estimated to be \$56.40.	
Class 1: American Ag Credit FLCA	Claim Amount	\$389,870.99
	Impairment	Impaired
	This creditor holds a note secured by a first deed of trust against the Triumph Ranch. This creditor is fully secured. The present note expires on approximately September 1, 2022; however, as the Petaluma Lease expires on December 1, 2023 the Debtor desires to realign the maturity dates of the notes against the property with the expiration of the Lease and, therefore, seeks to extend the maturity date to November 1, 2023. The monthly payment will be reduced from approximately \$4,224 to \$4,055.81 to reflect the extended maturity. All other aspects of the Loan; including the validity, extent and priority of the security interest, will remain the same. The claim is undisputed.	

Class 2: Karen House (on Triumph)	Claim Amount	Disputed
	Impairment	Unimpaired
	This creditor holds a note secured by a second deed of trust against the Triumph Ranch. This creditor is fully secured. The claim is disputed as to the amount and to the validity of an unrecorded interest in the real property apparently held by the "Stouts". As of the Petition Date the creditor claims that the amount due is \$571,713; the Debtor claims that the amount due on the Petition Date was \$447,171.77. If the Debtor's belief in the amount due is upheld, the monthly payment will be adjusted to approximately \$4,364. Once the monetary issues are resolved, the Debtors will make the payments as per the Agreement. This creditor is unimpaired. The claim is otherwise undisputed. The dispute will either be resolved in a motion to be brought to the court, or will be embodied in an objection to the Proof of Claim, number 12-1.	
Class 3: Oak Valley Bank (on Smith Ranch)	Claim Amount	\$105,226.23
	Impairment	Impaired
	This creditor holds a note secured by a first deed of trust against the Smith Ranch. This creditor is fully secured. The present note expires on approximately February 1, 2019; however, as the Petaluma Lease expires on December 1, 2023 the Debtor desires to realign the maturity dates of the notes against the property with the expiration of the Lease and, therefore, seeks to extend the maturity date to November 1, 2023. The monthly payment will be reduced from approximately \$1,693 to \$1,131.73 to reflect the extended maturity. All other aspects of the Loan; including the extent and priority of the security interest, will remain the same. The claim is undisputed.	
Class 4: Karen House (on Smith Ranch)	Claim Amount	Disputed
	Impairment	Unimpaired
	This creditor holds a note secured by a second deed of trust against the Smith Ranch. This creditor is fully secured. The claim is disputed as to the amount. As of the Petition Date the creditor claims that the amount due is \$113,700.06; the Debtor does not know the amount due on the Petition Date. The only reconciliation provided by the creditor starts in December 2010; there is no accounting for the years from 1984 to 2010. Once the issue is resolved, the Debtors will make the payments as per the Agreement.	

Class 5: Petaluma Acquisition LLC (secured by both the Triumph Ranch and the Smith Ranch	Claim Amount	\$773,395.56
	Impairment	Impaired
	This creditor has a third deed of trust on both ranches. The creditor is fully secured. The Debtors desire to modify the note to provide for a constant payment stream to the creditor. Now the note calls for payments to be made in the amount of \$6,276. However, those payments increase up to \$12,000 and beyond by the 2020's. The Debtors propose to pay a level amount sufficient to pay off the loan at the current maturity date at the same interest rate. The new payment amount would be approximately \$7,575.78 per month starting on the Effective Date. All other aspects of the Loan; including the validity, extent and priority of the security interest, will remain the same. The claim is undisputed.	
Class 6: General Unsecured Claims	Claim Amount	\$181,211.49
	Impairment	Impaired
	20.45% paid over 60 months. Payments to be made quarterly starting on the 60th day after the effective date in the amount of the CLASS 6 MONTHLY PAYMENT times three, or a quarterly payment of \$2,400.	
Class 7: Emanuel O. Amaral	Claim Amount	
	Impairment	Unimpaired
	The claimant shall receive nothing. This claimant is the owner of the real property located at 6131 -6133 - 6135 Smith Road, Oakdale, California. The property in this estate known as the Smith Ranch is located at 6231 Smith Road, Oakdale, California and is the parcel just north of some of the claimant's holdings. This claimant claims that an access road across the southerly width of the Smith Ranch improperly is placed on the claimant's land. The allegedly offending strip of pavement is approximately 1000 feet long and ranges from 0' to 16' feet in width. The Debtor claims that: (a) the boundary line is in dispute and is otherwise unclear; (b) the strip of pavement has been in place since before Mike House's father first bought the property in 1972; and (c) either by prescriptive easement or by adverse possession title to the property under the pavement belongs to this estate. The claimant is not therefore entitled to any claim against this estate; and the estate is entitled to a judgment in its favor settling the title issue in favor of the Debtor.	

Class 8: Interest Holders	Claim Amount	
	Impairment	Unimpaired
	<p>Debtors shall retain all property of the estate and any other property to which Debtors had a right to prior to the Petition Date and as to which Debtors may obtain rights to receive in the future.</p> <p>APPLICATION OF THE ABSOLUTE PRIORITY RULE: Debtors assert that the absolute priority rule does apply to the confirmation of this plan based on the facts of the case. Debtors propose to apply all of their disposable income for the five-year duration of the case to make payments to unsecured creditors. Therefore, the restrictions of the absolute priority rule should not limit this Plan. However, the Debtors anticipate that they will deposit \$10,000 by the Effective Date as additional working capital should a "new value" consideration be required.</p>	
	Claim Amount	
	Impairment	
	Claim Amount	
	Impairment	

A. C. WILLIAMS FACTORS PRESENT

- Y Incidents that led to filing Chapter 11
- Y Description of available assets and their value
- Y Anticipated future of the Debtor
- Y Source of information for D/S
- Y Disclaimer
- Y Present condition of Debtor in Chapter 11
- Listing of the scheduled claims
- Y Liquidation analysis
- Identity of the accountant and process used
- Y Future management of the Debtor

Y The Plan is attached

In re A.C. Williams, 25 B.R. 173 (Bankr. N.D. Ohio 1982); see also *In re Metrocraft*, 39 B.R. 567 (Bankr. N.D. Ga. 1984).

OBJECTIONS:

Creditor American AgCredit, FLCA

Creditor American AgCredit, FLCA, objects to the Disclosure Statement because it fails to adequately notify the reader that the Petaluma lease was not to be renewed at the end of the current term, 2018, and without the funds generated therefrom, the plan would lack sufficient income to make the proposed plan payments resulting in failure. Creditor states the only mention concerning the risks of non-renewal is at the top of page 21 of the Disclosure Statement wherein it merely states that a risk is non-renewal without any elaboration on the impact of that. American AgCredit, FLCA further objects that the Disclosure Statement misstates on page 14 of the proposed Disclosure Statement that the Petaluma lease runs through December 1st of the year 2023, when that is only a fact if Petaluma renews the lease for an additional five (5) years in 2018, something that is still an unknown and the Disclosure Statement gives no information as to that critical issue.

Creditor House Trust

Creditor Karen D. House, Trustee of the Arthur C. House and Karen D. House 1998 Living Trust ("House Trust"), objects to the Disclosure Statement because it fails to provide both correct and adequate information about the treatment of the House Trust's claim as referenced as a Class 2 and Class 4 creditor.

First, House Trust states that the Disclosure Statement incorrectly classifies their treatment of the second deed of trust on Triumph Ranch as "unimpaired" while attempting to modify the claim by rejecting a leasehold interest. Additionally, House Trust states there is no reference in either treatment of Class 2 or Class 4 to the fact that the House Trust is an oversecured creditor, which by virtue of 11 U.S.C. § 506 and established case law, is entitled to its fees and costs in these proceedings.

House Trust argues that the House Trust Class 2 Claim Involving the Triumph Ranch Is Not an Executory Contract. Moreover, House Trust states the lease agreements are between the House Trust, not Debtors, and Stoats and Krause as referenced in Debtors' Disclosure Statement or Plan. House Trust states if the Sale Agreement was an executory contract, Debtors would have to disclose that the Trust would be entitled to damages by virtue of lease rejection under 11 U.S.C. § 365 of the Bankruptcy Code. House Trust argues that Debtors must either advise this Court, creditors and the House Trust that they will abide by the terms and conditions of the agreement or advise that they intend to breach same.

U.S. Trustee

Tracy Hope Davis, the United States Trustee for the Northern

Districts of California and Nevada ("UST") objects to the disclosure statement on the basis that it fails to contain adequate information describing the Debtors' ability to fund the plan. UST states the historical data in the Debtors' monthly operating reports contradict the Debtors' projection of positive, annual cash flow. In the Disclosure Statement, the Debtors provide a 5-year projection of business profits. It describes over \$102,000 in business profit, per year. However, the Debtors' own monthly operating reports show that the Debtors have not generated a consistent stream of positive cash flow, while this case has been pending. These monthly operating reports show: the Debtors' post-petition, business operations from July 2013 through May 2014 resulted in an average loss of <3,457.45> , per month; in that same period, the Debtors' business operations resulted in a cumulative net loss of <38,032>.

UST argues the Disclosure Statement contains only general comments about "the consistency of the Debtors' income over the case..." and how the Debtors' income and expenses over "several years" have been "relatively steady." See Docket No. 116, p.9, line 21; p.10, line 5. Instead, the Disclosure Statement should clearly disclose the Debtors' apparent lack of cash flow during the bankruptcy case. The Disclosure Statement should also explain any changes or improvements to the Debtors' business operations during the bankruptcy case, any additional sources of income, and/or other concrete factors, to support the Debtors' projected business profits exceeding \$102,000 per year, for the next 5 years.

Additionally, the UST states the Disclosure Statement does not provide "adequate information" concerning the Debtors' ability to pay claimants and creditors, as of the effective date of the Plan. It appears from the Disclosure Statement that the Debtors intend to disburse over \$125,000 to administrative and other claims, on the effective date of the Plan. However, the most recently filed monthly operating report, for the month ending May 31, 2014, showed a cash balance of \$23,875. See Docket No. 121. The Disclosure Statement should provide information to describe and support how the Debtors will fund the estimated payments to claimants and creditors, that will become due on the effective date of the Plan, because the Debtors' current cash reserves appear insufficient.

Emanuel Amaral

Creditor Emanuel Amaral filed a late objection to the Disclosure Statement, stating that he was not served with the pleadings. Mr. Amaral states that there is a patent ambiguity in the disclosure statement in that under the impairment column for treatment of the claim, his claim is described as "unimpaired" as well as impaired an agreeing to vote for the plan. Mr. Amaral states he has not agreed to vote for the plan and that Debtors cannot obtain a declaratory judgment settling the title issue absent an adversary proceeding.

RESPONSE:

Debtors-in-Possession filed a response to each of the objecting creditors.

First, Debtors argues that Creditor American AgCredit, FLCA

objection is regarding eligibility, and as such, should be dealt with at the hearing on confirmation. Debtor also states he filed an amended disclosure statement, Part III(C) expanding the discussion of risk factors to answer the questions posed in the objection.

Second, as to Creditor House Trust, Debtors state that the objection is just legal argument, setting out contentions regarding the view of the relationship between the House Trust and Debtors. Debtors argue this is to be argued at confirmation by way of separate memorandum.

Third, as to the objection by the UST, Debtors state this objection is essentially regarding feasibility and should be dealt with at the hearing on confirmation. Debtor states he also added a new Part III (D) to the amended disclosure statement to answer the questions posed in this objection. Debtors believe the plan is feasible because (1) there will be more income, (2) there will be less mortgage expense under the plan and (3) the UST analysis ignores the difference between cash and accrual accounting.

Lastly, the Debtors state that Mr. Amaral made an appearance two months ago with a claim to the land under one of Debtor's roads on the Triumph Ranch. Debtors state that he is wrongly described as "impaired" and that he has not agreed to vote for the plan. Debtor has fixed the language in the amended disclosure statement. Debtors state that an adversary proceeding needs to be filed to declare the rights of the parties to the underlying land.

DISCUSSION:

1. Before a disclosure statement may be approved after notice and a hearing, the court must find that the proposed disclosure statement contains "adequate information" to solicit acceptance or rejection of a proposed plan of reorganization. 11 U.S.C. § 1125(b).

2. "Adequate information" means information of a kind, and in sufficient detail, so far as is reasonably practicable in light of the nature and history of the debtor and the condition of the debtor's books and records, that would enable a hypothetical reasonable investor typical of the holders of claims against the estate to make a decision on the proposed plan of reorganization. 11 U.S.C. § 1125(a).

3. Courts have developed lists of relevant factors for the determination of adequate disclosure. *E.g., In re A.C. Williams, supra.*

4. There is no set list of required elements to provide adequate information per se. A case may arise where previously enumerated factors are not sufficient to provide adequate information. Conversely, a case may arise where previously enumerated factors are not required to provide adequate information. *In re Metrocraft Pub. Services, Inc.*, 39 B.R. 567 (Bankr. N.D.Ga. 1984). "Adequate information" is a flexible concept that permits the degree of disclosure to be tailored to the particular situation, but there is an irreducible minimum, particularly as to how the plan will be implemented. *In re Michelson*, 141 B.R. 715, 718-19 (Bankr. E.D.Cal. 1992).

5. The court should determine what factors are relevant and required in

light of the facts and circumstances surrounding each particular case. *In re East Redley Corp.*, 16 B.R. 429 (Bankr. E.D. Pa. 1982).

The court agrees that the Petaluma lease description in the plan has not been adequately addressed. If it is not to be renewed at the end of the current term, 2018, and without the funds generated therefrom, the plan appears to lack sufficient income to make the proposed plan payments. Debtor does not adequately address the risk of non-renewal of the impact of that factor.

Additionally, the court agrees that the Debtors' ability to fund the plan appears contradictory. The historical data in the Debtors' monthly operating reports appears to contradict the Debtors' projection of positive, annual cash flow. In the Disclosure Statement, the Debtors provide a 5-year projection of business profits, describing over \$102,000 in business profit, per year. However, the Debtors' own monthly operating reports show that the Debtors have not generated a consistent stream of positive cash flow, while this case has been pending, as described by the opposition of the UST. The court agrees that the general comments about the Debtors' income is not clear or adequate. The Disclosure Statement should also explain any changes or improvements to the Debtors' business operations during the bankruptcy case, any additional sources of income, and/or other concrete factors, to support the Debtors' projected business profits exceeding \$102,000 per year, for the next 5 years.

Additionally, the court agrees that the Disclosure Statement does not provide "adequate information" concerning the Debtors' ability to pay claimants and creditors, as of the effective date of the Plan. It appears from the Disclosure Statement that the Debtors intend to disburse over \$125,000 to administrative and other claims, on the effective date of the Plan. However, the most recently filed monthly operating report, for the month ending May 31, 2014, showed a cash balance of \$23,875. See Docket No. 121. The Disclosure Statement should provide information to describe and support how the Debtors will fund the estimated payments to claimants and creditors, that will become due on the effective date of the Plan, because the Debtors' current cash reserves appear insufficient.