



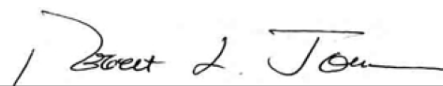
U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS

ENTERED

TAWANA C. MARSHALL, CLERK
THE DATE OF ENTRY IS
ON THE COURT'S DOCKET

The following constitutes the ruling of the court and has the force and effect therein described.

Signed July 30, 2013


United States Bankruptcy Judge

IN THE UNITED STATES BANKRUPTCY COURT
IN THE NORTHERN DISTRICT OF TEXAS
AMARILLO DIVISION

IN RE: §
FRIENDSHIP DAIRIES, §
a general partnership § BANKRUPTCY NO. 12-20405-11
Debtor § Chapter 11
§
§

INTERIM ORDER AUTHORIZING USE OF CASH COLLATERAL

On July 25, 2013, the First Amended Emergency Motion For Use of Cash Collateral (the “Motion”) filed by Friendship Dairies, the debtor and debtor-in-possession (the “Debtor”) came on for consideration by the Court.

The Court previously approved Debtor’s use of cash collateral on an interim basis on August 9, 2012 [Docket No. 31], August 24, 2012 [Docket Nos. 140, 141], on October 31, 2012, on November 14, 2012 [Docket No. 161], and on April 25, 2013 [Docket No. 385]. At the hearing on July 25, 2013, J. Bennett White appeared on behalf of the Debtor, John O’Brien and Scott Sandberg appeared on behalf of AgStar Financial Services, FLCA, loan servicer for

McFinney Agri Finance, LLC (“AgStar”), R. Byrn “Byrnie” Bass, Jr. appeared on behalf of Frontier Capital Group, Ltd. (“Frontier”) and Steven Jakubowski appeared on behalf of the Official Creditors Committee (“Committee”) (collectively the “Parties”).

The Court has considered the pleadings filed in this Chapter 11 case, the proceedings held before this Court, and the evidence and arguments of counsel presented. After due deliberation and consideration and pursuant to the stipulations stated on the record, the Court finds that good and sufficient cause exists to GRANT the Debtor’s use of post-petition cash on an interim basis pursuant to 11 U.S.C. § 363 as stated below:

A. The Debtor’s Chapter 11 case was commenced by the filing of its voluntary petition on August 6, 2012 (the “Petition Date”) under the Bankruptcy Code. The Debtor is operating its business and managing its property as debtor-in-possession pursuant to Sections 1107(a) and 1108 of the Bankruptcy Code.

B. This Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2). The statutory predicates for the relief sought herein are Sections 105, 361, 362, and 363 of the Bankruptcy Code and Bankruptcy Rule 4001(d). Venue of this Chapter 11 proceeding and this Motion in this district is proper pursuant to 28 U.S.C. §§ 1408 and 1409.

C. Proper notice of the hearing was provided pursuant to Bankruptcy Rule 4001(d) and applicable local rules. No other notice is necessary under the circumstances.

D. The Court finds that, for the purpose of determining adequate protection for the use of cash collateral:

- a. AgStar asserts a Petition Date claim in the approximate amount of \$18,400,000 (of which approximately \$1,900,000 is contingent) plus continuing interest and reimbursable charges;
- b. Frontier asserts a claim in the amount of \$27,041,479.91;
- c. Gavilon Ingredients, LLC asserts a claim in the amount of \$270,457.32; and
- d. Dimmitt Flaking, LP asserts a claim in the amount of \$514,240.80.

E. The Court assumes that, for the purpose of determining adequate protection for the use of cash collateral, as of the Petition Date:

- a. AgStar had a senior lien on substantially all of Debtor's real estate and a senior security interest in Debtor's irrigation equipment, milking equipment, and certain other assets;
- b. Gavilon Ingredients, LLC had a senior lien on Debtor's livestock¹;
- c. Dimmitt Flaking, LP had a lien on Debtor's livestock that is junior to the lien of Gavilon Ingredients, LLC, but is senior to the security interest of Frontier²;
- d. Frontier had a security interest in Debtor's livestock that is junior to the statutory liens of Gavilon Ingredients, LLC and Dimmitt Flaking, LP. Frontier had a senior security interest in Debtor's growing crops and in Debtor's feed inventory; and

¹ Debtor's counsel announced at the hearing that an agreement had been reached with Gavilon Ingredients, LLC for its claim to be unsecured; however, at present the claim is filed as a secured claim and will be treated as such in this Order.

² Debtor's counsel announced at the hearing that an agreement had been reached with Dimmitt Flaking, LP for its claim to be unsecured; however, at present the claim is filed as a secured claim and will be treated as such in this Order.

- e. As to the milk that had been sold prior to the Petition Date, but for which payment had not been received, and as to the milk on hand as of the Petition Date, AgStar had a security interest in the proceeds of such milk, so too did Gavilon Ingredients, LLC, Dimmitt Flaking, LP, and Frontier.

F. The Court finds that, as of the Petition Date, Debtor's assets may be assigned the following values:

- a. Debtor's livestock had a value of approximately \$12,551,350;
- b. Debtor's growing crops had a value between \$1,750,000 and \$3,428,400;
- c. Debtor's real estate, milking equipment, and dairy equipment had a fair market value of approximately \$24,810,000 if a seller is not under a compulsion to sell and based upon certain marketing period assumptions. There is evidence that a distressed sale domino effect and adjustment for the prepayment fee may lead to AgStar being less secured, but the Parties agree AgStar is oversecured; and
- d. Debtor's milk had a value of \$1,088,947.57.

G. The cash collateral generated by the sale of the milk that existed on the Petition Date has been spent by Debtor as previously authorized by this Court. Pursuant to 11 U.S.C. § 552, but for the replacement liens granted in conjunction with the interim authorization to use cash collateral previously approved by the Court, no party has a lien or security interest on Debtor's post-petition milk.

H. Assuming the validity of AgStar's claim and liens, AgStar's claim is fully secured by its liens and security interests in Debtor's real estate, milking equipment, dairy

equipment, and other assets. The Court makes no finding on the amount of any equity cushion at this time and notes that AgStar's secured position can change with the passage of time.

I. The Parties agree that Gavilon Ingredients' claim is fully secured by its statutory lien against Debtor's livestock. The value of the livestock provides Gavilon Ingredients with an equity cushion of approximately 4,600 percent (4,600%), even without taking into consideration the value of any other assets against which Gavilon Ingredients' statutory lien would have attached.

J. The Parties agree that Dimmitt Flaking's claim is fully secured by its statutory lien against Debtor's livestock. After reducing the livestock value by the amount of Gavilon Ingredient's claim, the remaining value of the livestock provides Dimmitt Flaking with an equity cushion of approximately 2,400 percent (2,400%), even without taking into consideration the value of any other assets against which Dimmitt Flaking's statutory lien would have attached.

K. Frontier is not fully secured. The value of Frontier's secured claim is limited to the value of its collateral. The Court was not presented with a complete analysis of all Frontier's collateral; therefore, there is no basis for the Court to make a determination of the exact amount of Frontier's secured claim. However, for the purpose of determining adequate protection for the use of cash collateral, the parties have agreed to use a stipulated amount of \$15,979,750.

L. The issues before the Court relate to (a) the Debtor's use of revenue from the sale of milk; (b) the Debtor's use of revenue from the sale of mature milk cows; and (c) the Debtor's consumption of its grown and harvested crop in the feeding of its livestock. Frontier asserts a claim to the cash collateral generated by the sale of mature milk cows. Frontier also asserts a claim that the consumption of grown crops represents a use of cash collateral for which it should be adequately protected. AgStar asserts a claim to the milk revenue and seeks a replacement

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lien as adequate protection for the Debtor's use of the cash collateral derived from the milk that existed on the Petition Date.

M. AgStar asserts a lien in the \$1,088,947.57 of milk proceeds existing on the Petition Date. The Court finds that the cash collateral to which that lien attached has been spent as previously authorized by the Court. (The Court notes further, however, that the Debtor has, in accordance with the Court's prior interim order authorizing the use of cash collateral [Docket No.141], made three adequate protection payments to AgStar in the amount of \$85,938 each.) The Court finds that if AgStar is not granted a replacement lien on post-petition milk proceeds, the effect would be the same as stripping AgStar of its lien on pre-petition milk proceeds. The Court is of the opinion that the use of cash collateral must protect a secured creditor's pre-petition lien. The Court is also of the opinion that approval of the use of cash collateral pursuant to 11 U.S.C. § 363 does not authorize the Court to strip a secured creditor of a lien existing on the petition date. Therefore, regardless of whether AgStar's secured claim is adequately protected by its liens and security interests in its other collateral, the Court finds that it is entitled to a replacement lien.

N. The Debtor currently holds \$506,323 in casualty insurance proceeds in which AgStar asserts a security interest (the "Insurance Proceeds Cash Collateral"). Thus, these Insurance Proceeds Cash Collateral constitute cash collateral in which AgStar has an interest.

O. The Court finds that Gavilon Ingredient's secured claim is adequately protected by its statutory lien against Debtor's livestock. The Court finds that the Debtor's use of cash collateral from the sale of livestock is not likely to cause any decrease in the amount of Gavilon Ingredient's secured claim; therefore, the Court finds that Gavilon Ingredients is not entitled to any adequate protection for the Debtor's use of livestock proceeds.

P. The Court finds that Dimmitt Flaking's secured claim is adequately protected by its statutory lien against Debtor's livestock. The Court finds that the Debtor's use of cash collateral from the sale of livestock is not likely to cause any decrease in the amount of Dimmitt Flaking's secured claim; therefore, the Court finds that Dimmitt Flaking is not entitled to any adequate protection for the Debtor's use of livestock proceeds.

Q. The Court finds that Frontier has agreed to cash out AgStar's interest in milk and milk products as described below and that the Debtor and Frontier have agreed to the Debtor's use of milk and milk proceeds after Frontier cashes out AgStar's lien on the milk and milk proceeds. The Debtor and AgStar have also stipulated to the use of the Insurance Proceeds Cash Collateral as described below. Accordingly, the Court hereby approves the stipulation, as incorporated below, made between the Debtor, AgStar, and Frontier.

R. The Court finds that Frontier and the Debtor have agreed and stipulated to conditions in exchange for which Frontier will consent to the use of its cash collateral, including cash collateral from the sale of milk, cash collateral from the sale of livestock, and cash collateral from the consumption of silage. The Court finds that the terms of that agreement are fair and equitable. Accordingly, the Court hereby approves the stipulation, as incorporated below, made between Debtor and Frontier.

THEREFORE, IT IS HEREBY ORDERED, ADJUDGED, AND DECREED AS FOLLOWS:

1. Identification Of Cash Collateral. As used herein, "Cash Collateral" shall consist of (a) cash proceeds from the sale of milk after August 6, 2012; (b) cash proceeds received by the Debtor from the sale of mature milking cows after August 6, 2012; and (c) silage harvested by Debtor from its growing crops after August 6, 2012, including silage harvested by Debtor

from any crops planted after August 6, 2012, along with any sales proceeds received by Debtor from the sale of any silage. Silage generally consists of corn, sorghum, and wheat silage.

2. Authority to Use Cash Collateral. The Debtor is authorized to use Cash Collateral to pay the Debtor's bona fide business expenses in accordance with the Budget attached hereto as Exhibit 1 for the period through September 30, 2013 (See ECF Doc. No. 538) (the "Budget"). The Budget includes two \$25,000 adequate protection payments to AgStar due on August 1 and September 1, 2013. The Debtor shall not use Cash Collateral other than as set forth in the Budget or following written consent of Frontier.

3. From the proceeds of the sale of mature milking cows, Debtor shall be permitted to use \$1,300.00 for each young cow that the Debtor adds as a milking cow. Debtor shall also be permitted to use the proceeds of the sale of mature milking cows to purchase milk cows.

4. Debtor shall be permitted to retain \$135,000 of the Insurance Proceeds Cash Collateral to purchase and install pumping equipment on previously drilled, but currently non-operating, water well on its property and such pumping equipment shall become a part of AgStar's real property collateral. The balance of the Insurance Proceeds Cash Collateral in the amount of \$371,323 shall be paid to AgStar within two (2) business days after the entry of this Order (the "Insurance Proceeds Cash Collateral Payment").

5. Frontier shall pay to AgStar the sum of \$700,000 within two (2) business days after entry of this Order (the "Cash Out Payment"). Upon AgStar's receipt of the Cash Out Payment Frontier shall have a senior lien on the Debtor's milk and milk proceeds, and AgStar shall no longer have a lien on the Debtor's milk and milk proceeds. Upon AgStar's receipt of the Cash Out Payment AgStar shall file amendments to its financing statements to release its lien on milk and milk proceeds, both pre-petition and post-petition, and Frontier is authorized to file

financing statements to evidence its senior lien on milk and milk proceeds. Upon receipt of the \$700,000 cash out payment AgStar will have no further interest in cash collateral currently in the Debtor's possession except for the Insurance Proceeds Cash Collateral.

6. The \$700,000 Cash Out Payment and the \$371,323 Insurance Proceeds Cash Collateral Payment paid to AgStar pursuant to this agreement, stipulation, and Order (the "AgStar Payments") shall be credited against the principal portion of the debt owed AgStar by the Debtor. The AgStar Payments shall first be applied to the principal payments that would have been made post-petition as specified in the loan amortization schedule that would have existed as of the petition date if the loan had not been accelerated. If the amounts paid in accordance with this Order exceed the unpaid amount of the payments described in the preceding sentence, this excess amount shall be held in escrow by AgStar until September, 2013, at which time the excess amount shall be applied to the principal portion of the indebtedness. The Parties have selected this payment schedule in order to avoid any possibility that any portion of the payments made in accordance with this Order be subjected to any prepayment or SWAP fee contained in the promissory note evidencing Debtor's indebtedness to AgStar. To protect AgStar and Frontier the AgStar Payments shall be unavoidable and irreversible such that it will not be necessary or allowable for the Debtor or any successor to the Debtor, including any Chapter 7 Trustee, Chapter 11 Trustee, or examiner to assert claims in the future for any reversal of the AgStar Payments which shall be credited to the principal of the Debtor's loan to AgStar as stated herein, including, but not limited to claims under 11 U.S.C. § 544, 547, 548, 549, 550, 553 or under the Texas fraudulent conveyance laws, and Frontier's replacement lien on the Debtor's post-petition milk and milk proceeds granted in exchange for the \$700,000 Cash Out Payment shall be similarly unavoidable and irreversible.

7. Each week, Debtor shall provide Frontier and AgStar with a report setting out its use of silage during the previous week. For each ton of silage used by the Debtor, Debtor shall earmark a portion of its revenue to be used only for farming expenses. Farming expenses shall include all costs incurred in conjunction with a future crop, i.e. planting, growing, and harvesting, and includes (without limitation) seed, fertilizer, chemicals, irrigation, labor, and utilities. The amount that shall be earmarked for future farming expenses shall be \$70 per ton for corn silage used, \$45 per ton for sorghum used, and \$50 per ton for wheat silage used. Frontier shall continue to inspect Debtor's growing crops in the same manner as it has done in the past. The Debtor will receive a credit against its use of silage for the value of its growing crop. Lone Star Milk Producers shall continue to supply to interested parties the periodic reports concerning milk purchases as stated in the Court's Interim Order Authorizing Use of Cash Collateral dated November 2, 2012 [Docket No. 141].

8. Actual To Budget Reports. By the 20th day of each month (which is also the date that the Debtor's monthly operating reports need to be filed with the office of the U.S. Trustee), the Debtor will provide Frontier and AgStar with a report comparing actual disbursements to the Budget for the prior month for each line item stated in the Budget.

9. Permitted Deviations From Budget. Debtor may not deviate from its Budget by more than 10% without Frontier's consent or an order of the Court. The permitted 10% deviation shall apply on a cumulative basis over the two (2) month period approved by this Order; however, the cumulative variance will not result in a reduction to the net cash flow in excess of \$225,000. For example, the total disbursements over the two (2) month period could exceed the projections by \$189,550 without violating this provision regardless of which individual month or months produced the overspending.

10. Adequate Protection Payments. As provided in the Budget, the Debtor shall pay monthly adequate protection to Frontier in the amount of \$83,000.00 payable on the last day of each calendar month through and including September 30, 2013.

11. Replacement Adequate Protection Post-Petition Milk Lien. Frontier is hereby granted a post-petition replacement senior lien on the milk and milk proceeds.

12. Replacement Adequate Protection Post-Petition Livestock Lien. Frontier is hereby granted a post-petition replacement lien on the livestock acquired by Debtor post-petition and the products and proceeds therefrom in the same nature, extent, and validity as its claims and security interests existed pre-petition, but subject to the limitation in Section 552 and to any avoidance actions and lien contests should such actions be brought, for any diminution in the value of the Cash Collateral caused by the Debtor's use of the Cash Collateral or the effect of the automatic stay in the Debtor's case. In accordance with Section 361, the extent to which any replacement lien in livestock is granted by this Order shall be limited to the amount necessary to protect such holder against a decrease in the value of such holder's interest in Cash Collateral resulting from the Debtor's use thereof.

13. Replacement Adequate Protection Post-Petition Crop Lien. Frontier is hereby granted a post-petition replacement lien on crops planted by Debtor post-petition, crop insurance proceeds, and proceeds from the sale of any crops in the same nature, extent, and validity as its claim and security interest existed pre-petition in Cash Collateral, but subject to the limitation in Section 552 and to any avoidance actions and lien contests should such actions be brought, for any diminution in the value of the Cash Collateral caused by the Debtor's use of the Cash Collateral or the effect of the automatic stay in the Debtor's case. In accordance with Section 361, the extent to which any replacement lien on future crops (including proceeds and crop

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insurance proceeds) is granted by this Order to Frontier shall be limited to the amount necessary to protect Frontier against a decrease in the value of its interest in Cash Collateral resulting from the Debtor's use thereof.

14. Default; Termination of Consent. In the event Debtor defaults under any of the foregoing provisions of this Order concerning Cash Collateral usage, Frontier may withdraw its consent to the Debtor's use of Cash Collateral and the Debtor will not be authorized to use Cash Collateral without an order the Court. If Frontier and Debtor fail to timely make the AgStar Payment to AgStar as required by this Order Debtor's right to use Cash Collateral shall terminate.

15. No Waiver. The Court finds that none of the affected Parties have waived any claim that was brought or could have been brought at the time of the filing of this case or the Emergency Motion for Use of Cash Collateral (as amended), and all Parties have reserved the right to assert such claims or defenses as they may have had then or that may have arisen since this case was filed. Nothing herein shall prejudice the rights of any party to subsequently argue that any secured creditor should be required to marshal its collateral.

16. Next Interim Hearing. This Court hereby sets a hearing for _____ a.m., _____, 2013, to be held in Lubbock, Texas to consider whether the provisions for the use of Cash Collateral should be extended after September 30, 2013.

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insurance proceeds) is granted by this Order to Frontier shall be limited to the amount necessary to protect Frontier against a decrease in the value of its interest in Cash Collateral resulting from the Debtor's use thereof.

14. Default; Termination of Consent. In the event Debtor defaults under any of the foregoing provisions of this Order concerning Cash Collateral usage, Frontier may withdraw its consent to the Debtor's use of Cash Collateral and the Debtor will not be authorized to use Cash Collateral without an order the Court. If Frontier and Debtor fail to timely make the AgStar Payment to AgStar as required by this Order Debtor's right to use Cash Collateral shall terminate.

15. No Waiver. The Court finds that none of the affected Parties have waived any claim that was brought or could have been brought at the time of the filing of this case or the Emergency Motion for Use of Cash Collateral (as amended), and all Parties have reserved the right to assert such claims or defenses as they may have had then or that may have arisen since this case was filed. Nothing herein shall prejudice the rights of any party to subsequently argue that any secured creditor should be required to marshal its collateral.

16. Next Interim Hearing. This Court hereby sets a hearing for 1:30 p.m.,
Room 314, 1205 Texas Ave,
September 25, 2013, to be held in Lubbock, Texas to consider whether the provisions for the use of Cash Collateral should be extended after September 30, 2013.

SNELL & WILMER L.L.P

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In Re: Friendship Dairies, Debtor
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####END OF ORDER###

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####END OF ORDER###

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Friendship Dairies
Proposed Budgets
August - September, 2013

		<u>August</u>	<u>September</u>
Sources	Projected Volume	100,000	108,500
	Projected Milk Price	17.80	18.25
	Milk Revenue	1,745,000	1,880,063
	Cull cows	80,000	80,000
	Bull calves	<u>20,000</u>	<u>20,000</u>
Total Sources		1,845,000	1,980,063
Disbursements			
Dairy			
	Accountant		
	Breeding	15,000	10,000
	Cow removal	1,000	1,000
	Draws (Partners)	25,000	25,000
	Electric	15,000	15,000
	Environmental cost	1,500	1,500
	Equipment	9,000	9,000
	Equity Purchase - Black Ridge Dairy		
	Feed	975,000	1,000,000
	Fuel & Gas	25,000	25,000
	Insurance	8,300	8,300
	Labor	120,000	120,000
	Medicine & Veterinary	25,000	25,000
	Miscellaneous	3,000	3,000
	Nutritionist		
	Rent - Feedlot	1,000	
	Repairs	30,000	30,000
	Supplies	45,000	45,000
	Taxes	38,000	38,000
	Telephone	3,000	3,000
	Testing & Trimming	15,000	15,000
	Trash removal	1,000	1,000
	Water treatment		
Total Dairy		1,355,800	1,374,800
Farming			
	Farming: Crop Insurance		
	Farming: Electric	90,000	95,000
	Farming: Equipment	11,613	11,613
	Farming: Fuel and Gas	7,500	15,000
	Farming: Harvesting	50,000	100,000
	Farming: Labor	6,000	6,000
	Farming: Manure Hauling	21,000	21,000
	Farming: Miscellaneous	3,000	3,000
	Farming: Repairs	25,000	25,000
	Farming: Seeding		
	Farming: Spraying/Fertilizing	40,000	60,000
	Farming: Supplies	<u>10,000</u>	<u>10,000</u>
Total Farming		284,113	346,613
Total Operating Disbursements		1,619,913	1,721,413
Reorganization			
	Legal fees - Debtor's Counsel	25,000	25,000
	Legal Fees - Other		
	Legal Fees - Creditors' Committee	<u>17,500</u>	<u>17,500</u>
	Professional Fees - Dairy Consultant		
	Trustee's Fees		
Total Reorganization		42,500	42,500
Adequate Protection Payments			
	AgStar	25,000	25,000
	Frontier	<u>83,000</u>	<u>83,000</u>
	Dimmitt Flaking		
	Gavilon Ingredients		
Total Adequate Protection Payments		108,000	108,000
Total Disbursements		1,770,413	1,871,913
Net Cash Flow		74,587	108,150
Cumulative Cash	Operating Cash	183,197	291,347
	Insurance Proceeds	<u>506,323</u>	<u>506,323</u>
	Total Cash on Hand	689,520	797,670

