UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF KENTUCKY
PIKEVILLE DIVISION

IN RE:

CASE NO. 18-70219

PAINTSVILLE INVESTORS, LLC

CHAPTER 11

DEBTOR AND DEBTOR IN POSSESSION

DISCLOSURE STATEMENT FOR DEBTOR'S' PLAN OF REORGANIZATION UNDER CHAPTER 11 OF THE UNITED STATES BANKRUPTCY CODE

Respectfully submitted,

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Dated: October 9, 2018

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Comes Paintsville Investors, LLC (the "Debtor"), as debtor and debtor in possession in this bankruptcy case, and pursuant to 11 U.S.C. § 1125 and Fed. R. Bankr. P. 3016, submits the following Disclosure Statement (the "Disclosure Statement") to provide holders of Claims against and Interests in the Debtor with adequate information in order to allow them to make an informed decision regarding their rights to vote on the Debtor's Plan of Reorganization (the "Plan") filed contemporaneously herewith.

ARTICLE I

PRELIMINARY STATEMENTS AND DISCLAIMERS

1.1 **Introduction.** The Debtor is seeking approval of its Plan of Reorganization. The confirmation of a plan is the overriding purpose of a Chapter 11 case. Although referred to as a "plan of reorganization," a plan may provide for anything from a complex restructuring of a debtor's business and its related obligations to a simple liquidation of assets. In either event, upon confirmation of a plan, the plan becomes binding on the debtor and all of its creditors and other parties in interest, and the obligations owed by the debtor to those parties are substituted for those outlined in the confirmed plan. In this Bankruptcy Case, the Plan contemplates a reorganization of the Debtor's business in order to protect the well-being of residents, preserve the facility and its jobs in the community, and to maximize the ultimate recoveries for all Creditors.

To assist all known Creditors, Interest Holders, and other parties in interest of the Debtor with their review of the Plan, the Debtor provides this Disclosure Statement for the purpose of disclosing all information the Debtor deems material, important, and necessary to the parties' ability to make a reasonably informed decision regarding their rights and to vote on the Plan. By an Order of the United States Bankruptcy Court for the Eastern District of Kentucky entered on _____ __, 2018 [ECF No. ___], this Disclosure Statement has been approved as containing "adequate information" in accordance with 11 U.S.C. § 1125. The Bankruptcy Code defines "adequate information" as "information of a kind, and in sufficient detail, as far as is reasonably practicable in light of the nature and the history of the debtor and the condition of the

debtor's books and records . . . that would enable . . . a hypothetical investor of the relevant class to make an informed judgment about the plan . . . ." 11 U.S.C. § 1125(a)(1).

All Creditors, Interest Holders, and Parties in Interest are encouraged to read and carefully consider this entire Disclosure Statement and to refer to the Plan during their review. THE PROVISIONS CONTAINED IN THE PLAN CONTROL OVER ANY STATEMENTS CONTAINED IN THIS DISCLOSURE STATEMENT.

1.2 **Debtor's Preliminary Statement.** The Debtor believes that the Plan is in the best interests of all Creditors. As a Creditor, your vote on the Plan is important. All Creditors entitled to vote are urged to vote in favor of the Plan. A summary of the voting instructions is set forth in Section 8.2 below, and more detailed instructions are contained on the ballots distributed to each Creditor entitled to vote on the Plan. ***For your vote to be counted, your ballot must be duly completed, executed, and received by 5:00 p.m. Eastern Time, on _____ __, 2018*** (the "Voting Deadline"), unless the Voting Deadline has been extended by the Debtor or the Court in writing prior to that time.

The Plan will be confirmed by the Bankruptcy Court if it is accepted by the holders of two-thirds (2/3) in dollar amount and more than one-half (1/2) in number of the Creditors' Claims in each class voting on the Plan. However, the Debtor has the right under 11 U.S.C. § 1129(b) to ask for approval of the Plan even though a class or classes reject the Plan, if the Bankruptcy Court finds that the Plan provides fair and equitable treatment for the rejecting class.

1.3 **Disclaimers.**

1.3.1 **Legal Effect of Statements in this Document.** The information contained in this Disclosure Statement—including, but not limited to, the information regarding the Debtor's history, business, and operations, the Debtor's financial information, and the Debtor's liquidation analysis—is included solely for the limited purpose of soliciting acceptances of the Plan. This information shall not be construed as an admission of any fact or liability, stipulation, or waiver by the Debtor in any contested matter, adversary proceeding, or other action or threatened action involving the Debtor, but rather as statements made in the course of settlement negotiations. Further, this information shall not be admissible in any non-bankruptcy proceeding involving the Debtor, nor shall it be construed to be conclusive advice on the tax or other legal effects of the Plan as to Creditors of the Debtor; provided, however, that in the event that the Debtor defaults under the Plan, the Disclosure Statement may be admissible in a proceeding relating to such default for the purpose of establishing the existence of such default.

1.3.2 **No Other Representations Authorized.** All representations in this Disclosure Statement are those of the Debtor, and no one else is authorized by the Debtor to give any additional information or to make any representations beyond those in this Disclosure Statement, the Plan, and the exhibits attached thereto, incorporated by reference, or referred to herein. If any such information is given or representations are made, such information or representations ***may not be relied upon*** as having been authorized by the Debtor. Further, any representations or inducements made to secure acceptance of the Plan which are *other than* as contained in this Disclosure Statement ***should not be relied upon*** by any person.

1.3.3 **No Involvement of Independent Public Accountant.** To the Debtor's knowledge, no information contained in this Disclosure Statement has been prepared by an independent public accountant, except as specifically noted.

1.3.4 **Forward-Looking Statements**. This Disclosure Statement contains forward-looking statements based primarily on the current expectations of the Debtor and projections about future events and financial trends affecting the Debtor's business. The words "believe," "may," "estimate," "continue," "anticipate," "intend," "expect," and similar expressions identify these forward-looking statements. Forward-looking statements have a number of risks, uncertainties, and assumptions, including those described in Article VII. Accordingly, the forward-looking events and circumstances discussed in this Disclosure Statement may not occur, and actual results could differ materially from those anticipated in the forward-looking statements. The Debtor may, but has no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

Neither the Plan nor this Disclosure Statement attempt to forecast consequences which follow from a general rejection of the Plan, although an attempt is made later to state the consequences of a liquidation of the Debtor's assets.

1.3.5 **Effect of Representation by Counsel.** The Debtor is represented by the law firm of DelCotto Law Group PLLC, 200 North Upper Street, Lexington, Kentucky 40507. DelCotto Law Group has not expressed an opinion on any information set forth herein and has no actual knowledge of any information that would conflict with any information contained in the Plan or in this Disclosure Statement.

ARTICLE II

NOTICES AND DEADLINES

2.1 **Voting Deadline.** For your vote to accept or reject the Plan to be counted, you must: (1) complete all required information on the ballot; (2) execute the ballot; and (3) return the completed ballot to the Debtor's counsel at DelCotto Law Group PLLC, c/o Tresine Callahan, 200 North Upper Street, Lexington, Kentucky 40507 so that it is ***received by 5:00 p.m., Eastern Time, on the Voting Deadline, _____ __, 2018***. Any failure to follow the voting instructions included with the ballot or to return a properly completed ballot so that it is received by the Voting Deadline may disqualify your ballot and your vote.

2.2 **Date of Confirmation Hearing.** A hearing to consider the confirmation of the Plan will be held before the United States Bankruptcy Court for the Eastern District of Kentucky, 100 East Vine Street, Second Floor, Lexington, Kentucky 40507, on _____ __, 2018 at the hour of 9:00 a.m., Eastern Time. Parties are not required to attend the confirmation hearing, but may do so if they wish. Attendance at the Confirmation Hearing does not include the ability to vote, so you are urged to fill in, date, sign, and promptly return your ballot to the Debtor's counsel by the Voting Deadline.

2.3 **Deadline to Object to Confirmation of the Plan.** Objections, if any, to confirmation of the Plan must: (a) be in writing; (b) state the name and address of the objecting party and the nature of the Claim or Interest of the party; (c) state with particularity the basis and nature of any objection; and (d) be filed with the Court and served so that they are ***received no later than 5:00 p.m., Eastern Time, on _____ __, 2018*** by the U.S. Trustee and the Debtor's counsel.

2.4 **Deadline to Object to Claims.** Unless otherwise ordered by the Bankruptcy Court, all objections to Claims, including determinations regarding the secured status of any claim, shall be filed on or before one hundred and twenty (120) days following the Effective Date, or forty five (45) days following the filing of any Claim, whichever is later (the "Claim Objection Bar Date"), without prejudice to the extension of such period upon proper application therefor. The objecting party shall serve a copy of each such objection upon the holder of the Claim in accordance with Fed. R. Bankr. P. 3007. Under the Plan, any Claim for which a timely objection is not filed shall be deemed Allowed as filed or scheduled.

2.5 **Requests for Copies of Disclosure Statement and Plan.** Requests for copies of the Disclosure Statement and the Plan by parties in interest may be made in writing to the Debtor's counsel by mail at DelCotto Law Group PLLC, c/o Tresine Callahan, 200 North Upper Street, Lexington, Kentucky 40507, or by email to tcallahan@dlgfirm.com. Please call Ms. Callahan at (859) 231-5800 with any questions.

ARTICLE III

GENERAL INFORMATION ABOUT THE DEBTOR

3.1 **Formation and Historical Background.** The Debtor is a Kentucky limited liability company formed in 2000 by the merger of Paintsville Investors, Inc. and Paintsville Investors II, LLC. However, the Debtors' predecessor companies have operated a skilled nursing facility at its current location in Paintsville, Kentucky since the mid-1990's. The company is manager-managed, and the managers are designated as directors of the company. The current managers are Patricia Akers and Franklin D. Fitzpatrick, as trustee of the H.D. Fitzpatrick, Jr. Irrevocable Trust. Ms. Akers and the Fitzpatrick Irrevocable Trust each own one-half of the equity of the Debtor. The Debtor entered into a 99-year lease for the property where its facilities are located on September 21, 1992, for the specific purpose of constructing and operating a "nursing and convalescence home". Construction of the facilities was financed with a July 21, 1994 loan from The Phares Company in the amount of $4,238,200, guaranteed by the U.S. Department of Housing and Urban Development ("HUD"). The Debtor uses the assumed names of Mountain Manor of Paintsville for its skilled nursing facility, and Buckingham Place for its independent living facility. The Debtor holds a license for 126 skilled nursing beds and has historically cared for over 100 patients. Buckingham Place has 20 units consisting of studio, one and two bedroom apartments.

3.2 **Debtor's Business Operations.** The Debtor has historically had an average occupancy rate of 90%, with revenue sources derived as follows: 17% from Medicare, 60% from Medicaid; 4% from VA patients, and 19% from private pay patients. The Debtor employees over

120 individuals and administers employee benefit plans for its employees which include health, dental and vision insurance, life and disability insurance, as well as a 401(k) retirement plan. Emily Jones-Gray, MSW, CSW is the licensed administrator of the skilled nursing facility. In an effort to streamline its operations, increase its billing efficiency, and assist with compliance issues, in November, 2015, the Debtor retained Health Systems of Kentucky, LLC to provide management, fiscal and operations consulting services.

3.3 **Debtor's Prepetition Assets and Liabilities.** The following subsections provide a summary of the Debtor's primary Assets and Liabilities according to the Debtor's books and records, its Bankruptcy Schedules, and a benchmark and valuation analysis conducted in April, 2018.[1] This summary does *not* take into consideration all of the Proofs of Claim filed herein. The Asset values are based on the Debtor's best estimates of market values, historic book values on the Petition Date, or as determined by professional analyses, and may *not*, and in all likelihood *do not*, accurately reflect liquidation values or what value may ultimately be obtained for these Assets.[2] ***Holders of Claims are encouraged to review the Schedules and related Amendments for a complete listing of the Debtor's Assets and Liabilities.***

3.3.1 **Prepetition Assets.** As of the Petition Date, the Debtor estimated the approximate fair market values of its respective prepetition Assets as follows, based on the assessed value[3] of real estate and the Debtor's knowledge of the health care industry:

Real property -	$	5,300,000
Personal property -	$	1,713,720

[*See* Schedules and Amendment, ECF No. 1]. This valuation does not include "current assets" such as bank accounts or accounts receivable and does not include furniture, fixtures and equipment, which were listed with an "unknown" value in the bankruptcy schedules. As of September 30, 2018, the Debtor had cash in bank accounts totaling $135,670.04 and estimated net accounts receivable of $_____. However, these amounts do not adequately portray the total "going concern" value of the Debtor's business as a whole, as they do not take into account any added goodwill value that the Debtor's business may have, nor do they account for the human capital provided by the Debtor's employees or the expertise and extensive knowledge of the Debtor's owners. These "soft" Assets are a vital and important component of the Debtor's business and its "going concern" value.

3.3.2 **Overview of Total Prepetition Liabilities.** As of the Petition Date, the Debtor's prepetition liabilities totaled approximately $9,809,753.66, which consists of: (a) secured claims totaling approximately $8,922,986.24; (b) priority unsecured claims totaling approximately $11,339.00; and (c) unsecured claim totaling approximately $875,428.42. *See* Schedules [ECF No. 1]. Based on additional developments and claims filed as of the date of this Disclosure Statement, the Debtor's Schedules understate the claims against it. In addition, certain prepetition

[1] The benchmark and valuation analysis is attached as **Exhibit A**.

[2] *See* Section 8.3.1 of this Disclosure Statement and **Exhibit D** attached hereto for the Debtor's Liquidation Analysis.

[3] This is the assessed value of the real property and improvements according to the 2017 ad valorem tax bill.

claims have been reduced by court-authorized payments from the Debtor since the case was filed and the Debtor has incurred regular trade debt since the Petition Date.

Secured Claims - $8,922,986.24, broken down as follows:

Creditor	Scheduled Amount	Claimed Amount
First Insurance Funding	$ 108,614.00	$ No claim filed – paid post-petition
X-Caliber Capital Corp.	$8,814,372.24	$ No claim filed – amount stipulated
U.S. Dept. of HUD	$ *0*	$ No claim filed – loan insurer
Totals:	$8,922,986.24	$

Priority Claims – $11,339.00, broken down as follows:

Creditor	Scheduled Amount	Claimed Amount[4]
Wages[5]	$ *0*	No claims filed
IRS	$ unknown	$ 5,273.29 - estimated
Ky. Dept. Rev.	$ 11,339.00	$ 49,579.74
Total:	$ 11,339.00	$ 54,853.03

Unsecured Claims - $875,428.42. As a result of a review of the Debtor's books and records and filed claims, the Debtor believes the actual amount of the unsecured claims held by its creditors may be higher than as listed in its bankruptcy schedules.

3.3.3 **Valuation of Real Property Interests and Liens against same.** The Debtor (as successor by merger to Paintsville Investors, Inc.) is the lessee of a 3.8 acre parcel of land known as 1025 Euclid Avenue in Paintsville, Johnson County, Kentucky (the "Property"). The Debtor entered in to a Lease and Agreement (the "Lease") and an Addendum to Lease (the "Addendum") in September, 1992. The Lease runs for a term of 99 years. The Lease and Addendum are of public record in Lease Book 213, Page 86 in the Johnson County Court Clerk's Office. After entering into the Lease, the Debtor constructed a 126 bed skilled nursing facility known as Mountain Manor of Paintsville. In October, 2008, the Debtor opened a 20 bed independent living facility known as Buckingham Place.

Under the terms of the Addendum, the Debtor's ability to sell the Lease is subject to a contingent right to purchase the underlying property in favor of the Federal Housing Commissioner. The Debtor's ability to assign the Lease is subject to the approval of the Federal Housing Commissioner. In the Debtor's opinion, the nature of its interest in the Property and the rights and restrictions in favor of the Federal Housing Commissioner have a negative impact on the value of its leasehold interest in the Property. As the Debtor owns only a long-term leasehold interest, the Debtor has not had the Property formally appraised and believes that the cost and

[4] The total of priority claims excludes any amounts designated as unsecured in filed claims.

[5] Employee wages were scheduled as zero because court authority was obtained to pay all prepetition wages.

delay associated with a formal appraisal limited to its leasehold interest would not benefit creditors or other parties evaluating the Debtor's Plan.

The Debtor is indebted to X-Caliber Capital Corporation pursuant to a Mortgage Note in the original principal amount of $9,165,900.00 dated as of November 21, 2013 (as amended, the "Note"). The Note was subsequently assigned to The Phares Company and is now held by X-Caliber. The Note is secured by: (a) a Mortgage (Leasehold) in favor of Bellwether Enterprises Real Estate Capital LLC (the "Original Mortgagee") dated November 21, 2013 and recorded in the Johnson County, Kentucky Clerk's Office at Mortgage Book 514, Page 532 (the "Mortgage"), and assigned to The Phares Company pursuant to that certain Assignment of Mortgage recorded in the Johnson County, Kentucky Clerk's Office at Mortgage Book 514, Page 558; (b) a Regulatory Agreement for Multifamily Housing Projects between the Debtor and the Secretary of Housing and Urban Development ("HUD") dated as of November 21, 2013 and recorded in the Johnson County, Kentucky Clerk's Office at Mortgage Book 514, Page 541. The outstanding balance owed under the Note as of the Petition Date was $8,814,372.24. There are no other consensual liens against the Debtor's leasehold interest in the Property to the best of the Debtor's knowledge.

3.3.4 **Additional Information about Prepetition Assets and Liabilities.** For more specific information about the Debtor's prepetition Assets and Liabilities, see the Debtor's Schedules and Amendments filed in its Bankruptcy Case, Case No. 18-70219.

3.4 **Debtor's Postpetition Liabilities.**

3.4.1 **Professional Fees.**

(a) **DelCotto Law Group PLLC.** As set forth more fully in Section 5.2.1 below, the Debtor was authorized to employ DelCotto Law Group PLLC ("DLG") as its counsel in the Bankruptcy Case. The Debtor also obtained several Cash Collateral Orders [ECF Nos. 50, 88, and 121] as defined and discussed more fully in Section 5.3 below. Pursuant to the Cash Collateral Orders, the Debtor agreed to adhere to approved Cash Collateral Budgets, which provided for payment of the fees of DLG, but did not include a carve-out from cash collateral for that purpose. DLG received a total of $40,000 pursuant to a prepetition retainer, and held the sum of $32,652.75 in escrow on the Petition Date. On September 24, 2018, DLG received interim approval to pay fees and expenses accrued through July 31, 2018 in the amount of $63,963.51. As of October 1, 2018, DLG's total fees and expenses incurred since the Petition Date for representation of the Debtor total approximately $95,063.75.

(b) **Providence Health Management, Inc.** As set forth more fully in Section 5.2.2 below, the Debtor was authorized to employ Providence Health Management, Inc. ("Providence") to replace Health Management Systems of Kentucky, LLC as its operations, fiscal and management consultant [ECF Nos. 120, 138, 178] at a flat rate of $12,000.00 per week. Pursuant to the Cash Collateral Orders, the Debtor agreed to adhere to approved Cash Collateral Budgets, which provided for payment of the fees of Providence as an ordinary operating expense of the Debtor. The Debtor has paid Providence's fees pursuant to the Cash Collateral Orders, and as of October 1, 2018, Providence has received a total of $168,000.00.

(c) **Deming, Malone, Livesay & Ostroff.** As set forth more fully in Section 5.2.3 below, the Debtor was authorized to employ Deming, Malone, Livesay & Ostroff ("DMLO") as its accountants for the purpose of preparing 2017 cost reports, all necessary tax returns for the Estate, and to provide general accounting advice to the Debtor [ECF No. 114]. DMLO was employed by the Debtor for general accounting, audit and tax preparation services prior to the Petition Date. On May 31, 2018, the Bankruptcy Court granted approval to pay DMLO the sum of $13,000 to prepare 2017 cost reports, and DMLO has been fully paid. The Debtor expects to incur additional fees for the preparation of a required audit and tax returns in the future.

3.5 **Current Litigation and Administrative Proceedings involving the Debtor.**

3.5.1 **Prepetition Litigation.** As of the Petition Date, the Debtor was involved in 10 state court civil actions, all alleging tort claims for personal injury or wrongful death, and all pending in the Johnson County, Kentucky, Circuit Court. An additional civil action was (improperly) filed after the Petition Date. A number of the lawsuits name additional defendants such as the management company (Health Systems of Kentucky, LLC) or the facility administrator (Emily Jones-Gray). No adverse judgments had been rendered against the Debtor as of the Petition Date and each of the civil suits was being defended on behalf of the Debtor under its liability insurance policy. The Debtor's insurance carrier was also providing a defense on behalf of additional named defendants. The Debtor's professional liability policy in place on the Petition Date provided coverage in the amount of $1,000,000 per claim, with a $3,000,000 aggregate limit, subject to a $50,000 deductible per claim. The policy is a "claims made" policy and covers the period from September 1, 2017 through August 31, 2018.

Kentucky established medical review panels in 2017, and personal injury claimants are required to present claims for review before initiating litigation. The constitutionality of the medical review panels was questioned, and they were found unconstitutional by the Franklin County Circuit Court. The Kentucky Supreme Court granted an expedited review, and the case was argued in August, 2018. In the meantime, claimants adopted a practice of filing a civil action simultaneously with claims filed with medical review panels. Most claims filed after the medical review panels came into existence have been stayed by the circuit court judge, pending a decision by the review panel or the Kentucky Supreme Court. Accordingly, specific information about each case listed below is limited to any unique issues related to their status.

(a) **Janice Bayes v. Paintsville Investors.** Case No. 17-CI-00371. Discovery commenced, but case in abeyance as of December 18, 2017.

(b) **Van Cope, Administrator of the Estate of Mavis Cope v. Mountain Manor of Paintsville**. Case No. 16-CI-00076. This case was resolved by an Agreed Order of Dismissal entered on March 21, 2017.

(c) **Jimmy D. Crum v. Paintsville Investors**. Case No. 16-CI-00087. The Debtor obtained a summary judgment in its favor in this case, which was appealed by the plaintiff on March 28, 2018.

(d) **Paul D. Witten, Administrator of the Estate of Shirley F. Davis v. Paintsville Investors.** Case No. 17-CI-00226. This case was set for trial in January, 2019, but is currently stayed and the trial date has been vacated.

(e) **Mickey Fyffe, Administrator of the Estate of Mavis Fyffe.** Case No. 17-CI-00218. This case was set for trial in October, 2018, but is currently stayed and the trial date has been vacated.

(f) **Willa Webb, by her Guardian, Renee Kretzer v. Paintsville Investors.** Case No. 17-CI-0145. This case was set for trial in October, 2018, but is currently stayed.

(g) **Gary Marshall and Chad Marshall as Administrator of the Estate of Betty L. Marshall v. Paintsville Investors.** Case No. 18-CI-00027. Case held in abeyance per order entered March 15, 2018.

(h) **Estate of Betty Jo Parker v. Paintsville Investors.** Case No. 18-CI-00238. This case was filed post-petition on June 21, 2018 and the Debtor believes the filing is void or voidable.

(i) **Nell Pelfrey, Administrator of the Estate of Forest Pelfrey.** Case No. 17-CI-00222. This case was set for trial in October, 2018, but is currently stayed and the trial date has been vacated.

(j) **Julia Ratliff, by and through C. Eric Ratliff v. Paintsville Investors.** Case No. 17-CI-00140. This case was set for trial in October, 2018, but is currently stayed.

(k) **Estate of Buddy Boy Senters v. Paintsville Investors.** Case No. 17-CI-00083. This case was set for trial in July, 2018, but is currently stayed and the trial date has been continued generally.

(l) **Coddie Jude, as Power of Attorney for Paula Van Hoose v. Paintsville Investors.** Case No. 17-CI-00151. This case was set for trial in October, 2018, but is currently stayed and the trial date has been vacated.

3.5.2 **Prepetition Administrative Proceedings.** The Kentucky Cabinet for Health and Family Services, Office of Inspector General (the "OIG"), conducts regular surveys of long term care facilities in Kentucky, including the Debtor's facilities. The OIG noted deficiencies at the facility during abbreviated surveys on November 17 and December 21, 2017. The Debtor submitted a plan of correction to address the deficiencies, but a subsequent extended survey on March 7, 2018 resulted in an "immediate jeopardy" classification. The Debtor took appropriate action, submitted another plan of correction, and after a subsequent inspection on April 26, 2018, the facility was found to be in compliance with applicable regulations and requirements as of April 17, 2018.

As a consequence of the OIG surveys and deficiency citations, the United States Department of Health & Human Services, Centers for Medicare & Medicaid Services ("CMS")

imposed an enforcement remedy of a Denial of Payment for New Admissions ("DPNA"), effective as of January 12, 2018. As a consequence, admissions to the Debtor's long term care facility – and revenue that would have been generated by such admissions – declined. Once the facility regained compliance, the DPNA was lifted, effective as of April 16, 2018. In addition to the enforcement remedy of a DPNA for a period of three months, on May 23, 2018, CMS imposed a civil monetary penalty upon the Debtor in the amount of $366,709.85. The penalty represents a 35% reduction allowed as a result of the Debtor's waiver of its right to appeal the penalty. The parties are advised to review the Plan for the Debtor's proposed treatment of this civil monetary penalty.

ARTICLE IV

EVENTS LEADING UP TO THE FILING OF THE DEBTOR'S CHAPTER 11 CASE

4.1 **Events Contributing to the Chapter 11 Filing.** The Debtor experienced financial difficulties in 2017 due primarily to the costs associated with defense of the many personal injury lawsuits against it and the escalating cost of liability insurance. The cost of the Debtor's last liability insurance policy described above was almost $600,000, and the Debtor was incurring and/or paying for defense costs on the 10 pending lawsuits up to the $50,000 per claim deductible limit. When the DPNA issued by CMS went into effect in January, 2018, the Debtor realized it would ultimately face a cash shortage as revenues from Medicare and Medicaid patients would decline in the near future. The Debtor took steps to reduce expenses, such as closing a unit of the facility, but the combination of the loss of revenue from the DPNA and increased costs associated with liability insurance and personal injury lawsuits resulted in an inability to remain current in payments to vendors. The Debtor also recognized that a civil monetary penalty would be imposed, which CMS could collect by recoupment from payments otherwise due to the Debtor, crippling its ability to operate.

4.2 **Prepetition Restructuring Efforts.** As early as November, 2015, the Debtor retained an outside management company (Health Systems of Kentucky, LLC) to oversee and manage the day to day operations at the Debtor's facilities. Although the efforts of the management company helped to improve the overall financial performance of the business, the combination of excessive legal claims and loss of revenue from the DPNA exceeded any improvements. In addition to the attempts to reduce expenses to deal with a short-term drop in revenue, described above, the Debtor also sought a third-party opinion regarding the value of its business, with an eye towards finding a purchaser of the business as a going concern. Although the Debtor had informal discussions with potential purchasers prior to seeking bankruptcy relief, no firm offers to acquire the business were made.

ARTICLE V

COMMENCEMENT AND PROGRESS OF THE CHAPTER 11 CASE

5.1 **Commencement of Case.**

5.1.1 **Petition Date.** On April 9, 2018, the Debtor filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code, commencing its Bankruptcy Case.

5.1.2 **Chapter 11 Operating Order.** On April 10, 2018, the Bankruptcy Court entered a Chapter 11 Operating Order in the Debtor's Bankruptcy Case evidencing that the Debtor had requested and been granted relief under Chapter 11 of the Bankruptcy Code and had thereby become a Debtor in Possession. *See* ECF No. 15.

5.2 **Retention of Professionals.**

5.2.1 **Retention of Debtor's Counsel.** Pursuant to the Interim Order entered on April 13, 2018 [ECF No. 42], and the Final Order entered on May 10, 2018 [ECF No. 90], the Debtor was authorized to employ the law firm of DelCotto Law Group PLLC as its counsel in the Bankruptcy Case, effective as of the Petition Date.

5.2.2 **Retention of Debtor's Management Consultant.** Pursuant to the Interim Order entered on June 1, 2018 [ECF No. 120] and the Final Order entered on July 17, 2018 [ECF No. 138], the Debtor was authorized to employ Providence Health Group, LLC as its operations, fiscal and management consultant, effective as of June 1, 2018. On September 17, 2018, the Court amended the final order to substitute Providence Health Management, Inc. as the entity authorized to provide such services to the Debtor [ECF No. 178].

5.2.3 **Retention of Debtor's Accountants.** Pursuant to the Order entered on June 1, 2018 [ECF No. 114], the Debtor was authorized to employ Deming, Malone, Livesay & Ostroff as its accountants in the Bankruptcy Case, effective as of May 9, 2018.

5.2.4 **Official Committee of Unsecured Creditors.** No trustee or examiner has been appointed in this Chapter 11 case, and no creditors' committee or other official committee has been appointed. The Kentucky Long Term Care Ombudsman was appointed as the Patient Care Ombudsman in this case on April 25, 2018 [ECF No. 59].

5.3 **Cash Collateral/Adequate Protection.** On April 17, 2018, the Court entered an Order for Interim Use of Cash Collateral [ECF No. 50]. The Court subsequently entered a Second Interim Order for Use of Cash Collateral on May 4, 2018 [ECF No. 88], and a Final Order Authorizing Use of Cash Collateral and Authorizing Adequate Protection Payments on June 1, 2018 [ECF No. 121]. Collectively, these cash collateral orders are referred to herein as the "Cash Collateral Orders." The Final Cash Collateral Order provides a mechanism for the Debtor to obtain extensions of its terms by submitting subsequent budgets and providing an opportunity for interested parties to object. The Debtor's authority to use cash collateral currently extends through the week ending November 2, 2018, pursuant to the most recent budget filed with the Court [ECF No. 142]. To date, the Debtor has been operating in compliance with the Cash Collateral Orders.

The Court also entered Orders on April 25, 2018 [ECF No. 58] and July 30, 2018 [ECF No. 152] authorizing the use of cash collateral held by X-Caliber to pay liability insurance premiums and authorizing the Debtor, X-Caliber and the institution where the debtor-in-possession accounts are maintained to execute account control agreements.

5.4 **Orders relating to Executory Contracts**. On July 9, 2018, the Court entered an Agreed Order rejecting an executory contract between the Debtor and Health Systems of Kentucky, LLC [ECF No. 127]. The Debtor filed a Motion for an Order Extending Debtor's Time to Assume or Reject Unexpired Non-residential Real Property Lease [ECF No. 132], which was granted by an Order entered on July 25, 2018 [ECF No. 146], allowing the Debtor through and including November 6, 2018 to assume or reject the unexpired non-residential real property lease where the Debtor's facility is located. On October 2, 2018, the Debtor filed a motion seeking to assume its long-term non-residential lease [ECF No. 203], which is scheduled to be heard on October 18, 2018.

5.5 **Establishment of Bar Dates for Claims.** On July 12, 2018 the Court entered two orders: one which established a notice procedure and bar date of November 2, 2018 for unknown claims to be filed with the Court [ECF No. 170]; and one which established a bar date of November 2, 2018 for contingent, unliquidated or disputed claims [ECF No. 171].

5.6 **Order relating to Liability Insurance.** The Debtor's general and professional liability insurance expired on August 31, 2018. The Debtor sought replacement insurance at numerous coverage levels, but also filed a motion asking the Court to waive the requirement to maintain insurance contained in the Operating Order [ECF No. 155]. On September 21, 2018, the Court entered an Order [ECF No. 189] which temporarily relieved the Debtor of the requirement to maintain liability insurance, through and including November 20, 2018. The Debtor proposes to continue operating without liability insurance after Confirmation unless such insurance can be obtained at a reasonable cost.

5.7 **Plan Formulation Process**. The Debtor continued discussions with an existing prospective purchaser after the Petition Date, and provided information to other prospective purchasers to determine if a liquidating plan would maximize recovery for creditors. However, no firm offers to acquire the Debtor as a going concern were received. Following the internal formulation of its Plan of reorganization, the Debtor has communicated with its major secured lenders. The Debtor has discussed concepts for its Plan with these parties and others in advance of its filing.

The Debtor has worked diligently to prepare a plan of reorganization that is feasible, fair and equitable among all of its Creditors and parties in interest. The Debtor submits that the Plan filed with the Court and attached hereto represents the product of these efforts and provides the best possible recovery for all Creditors.

ARTICLE VI

OVERVIEW OF THE DEBTOR'S PLAN OF REORGANIZATION

6.1 **General Summary**. The Plan contemplates the continued operation of the Debtor's long term care and independent living facilities, and a gradual increase in the patient census for the long term care facility to prior occupancy levels. The Plan also contemplates the creation of a new entity to serve as a real property holding company ("RealCo") in order to allow the Reorganized Debtor to focus on operations, and to help insulate the real property interests from personal injury claims. Allowed Claims will be paid to the extent possible over a period of time from future income. To the extent creditors have liens against real property or tangible personal property, the Plan contemplates that such creditors will retain their liens whether property is transferred to RealCo or retained by the Reorganized Debtor. In general, all Claims other than Secured Claims will be paid to the greatest extent possible within five years after the Effective Date of the Plan. The Secured Claims will be paid in full over time, as set described more fully in Article VI, below.

The two largest factors contributing to the Debtor's financial distress are the large number of outstanding personal injury lawsuits and the civil monetary penalties imposed by CMS. The Debtor has structured the Plan and its obligations thereunder around the ability of CMS to recoup the civil monetary penalties from future revenues and the availability of insurance to resolve the pending personal injury lawsuits. The Debtor believes this provides a reasonable and conservative approach to its emergence from Chapter 11.

6.2 **Debtor's Recommendation.** The Debtor believed that the Plan is in the best interests of all of its constituencies and will permit the maximum recovery possible for all classes of Claims, greater than any possible recovery in a Chapter 7 or other liquidation setting.

6.3 **Description of Certain Key Plan Terms.** The Debtor provides this general summary and description of what it believes to be certain of the key terms of the Plan. This is not a full and complete description of everything contained in the Plan, only of various general and specific Plan provisions. THE PLAN AND THE EXACT LANGUAGE THEREIN CONTROL OVER THIS GENERAL DESCRIPTION AND SHOULD BE REVIEWED CAREFULLY.

6.3.1 **Continued Existence of the Debtor**. The Plan provides for the Debtor to continue to operate post-Confirmation as the "Reorganized Debtor" in the ordinary course of its business, receiving ongoing income from its operations in order to fund Plan payments to its Creditors. In addition, real property owned by the Debtor may be transferred to RealCo, and RealCo will own and operate the real property separate and apart from the day to day business operations of the Reorganized Debtor. After Confirmation, RealCo and the Reorganized Debtor may, but shall not be required to, sell some or all of their assets pursuant to the terms of the Plan

6.3.2 **Funding the Plan.** The Reorganized Debtor and RealCo will fund the Plan payments to Creditors in the ordinary course and according to the Plan treatment terms from post-Confirmation net profits, as well as from payments from the equity holders of the Debtor. As of the Effective Date, and as long as the RealCo and the Reorganized Debtor continue operations,

they shall have the right to collect and use all of their revenues for operations, provided however, that the Reorganized Debtor will segregate funds each month in order to fund Plan payments to Unsecured Creditors and may agree to permit CMS to satisfy the civil monetary penalties via recoupment over time.

6.3.3 **Vesting of the Debtor's Assets.** At the Confirmation Date, all Assets of the Debtor and its Estate, including all Avoidance Actions and Causes of Action (if any), will revest in and remain with the Reorganized Debtor, free and clear of all liens, claims, interests, and encumbrances, except for those liens specifically provided for in the Plan. If the Reorganized Debtor liquidates any of its assets which remain subject to a lien post-confirmation at a price in excess of $5,000.00, then it will seek the consent of any Creditor holding a lien upon the particular Asset. If the Secured Creditor and the Reorganized Debtor cannot agree to the terms for a private, ordinary-course sale, then the Reorganized Debtor may seek authority for any such sale from this Court. The Reorganized Debtor and its Assets will remain subject to the jurisdiction of this Court until the Bankruptcy Case is closed or dismissed.

6.3.4 **Post-Confirmation Liabilities.** Neither RealCo nor the Reorganized Debtor will have any liability for the Debtor's obligations which existed on the Petition Date, except those expressly assumed and/or addressed under the Plan. RealCo will be responsible for expenses and payments to Creditors secured by real property, while the Reorganized Debtor will be responsible for all ongoing business expenses and payments due and owing or contemplated under the Plan related to the nursing home and independent living businesses.

6.3.5 **Injunctions.** Except as may be otherwise provided in the Confirmation Order, entry of the Confirmation Order and the satisfaction, releases and discharge pursuant to Article VI of this Plan shall also act as an **injunction** against any Person taking any action to commence or continue any action, employ any process, or act to collect, offset, or recover any claim or cause of action satisfied, released or discharged under this Plan to the fullest extent authorized or provided by the Bankruptcy Code, including to the fullest extent provided by Sections 524 and 1141 thereof. From and after the Confirmation Date, there shall be in place with regard to the Assets and any Claims, an injunction to the same extent and with the same effect as the stay imposed by Section 362 of the Bankruptcy Code and such injunction will remain in effect until the final Distribution is made by the Debtor. Except as provided in this Plan or as expressly approved in writing by the Reorganized Debtor, all Claimants shall be precluded and enjoined from asserting against the Reorganized Debtor, the Estate, or the Reorganized Debtor's Assets, any other or further Claim based upon any act or omission, transaction or other activity of any kind or nature that occurred prior to the Confirmation Date, whether or not the Claimant filed a proof of claim.

6.3.6 **Releases.** On the Effective Date, the Debtor, the Reorganized Debtor and such parties' respective members, officers, directors, attorneys, affiliates, representatives, agents or employees (the "Released Parties") shall not have or incur, and are hereby released from, any claim, obligation, cause of action, or liability to one another, to any other party in interest, or to any of their respective agents, employees, representatives, attorneys or affiliates for any act or omission before or after the Petition Date through and including the Effective Date in connection with, relating to, or arising out of the operation of the Debtor's business (other than liabilities

incurred in the ordinary course of the Debtor's business), this chapter 11 case, the filing of this case, the formulation, preparation, dissemination, approval, confirmation, administration, implementation or consummation of this Plan, the Disclosure Statement, or the property to be distributed under this Plan.

Notwithstanding any other provision of this Plan, no other party in interest, none of their respective agents, employees, representatives, attorneys, or affiliates, shall have any right of action against the Released Parties for any act or omission before or after the Petition Date through and including the Effective Date in connection with, relating to, or arising out of the operation of the Debtor's business (other than liabilities incurred in the ordinary course of the Debtor's business), this chapter 11 case, the filing of this case, the formulation, preparation, dissemination, approval, confirmation, administration, implementation or consummation of this Plan or the Disclosure Statement (and after the Effective Date with respect to any claims relating to the implementation of consummation of this Plan).

6.3.7 **Exculpation.** The Debtor, Reorganized Debtor and such parties' respective members, officers, directors, attorneys, affiliates, representatives, agents or employees, shall have no liability to any Claimant or any other Person for any act taken or omission made in connection with, or arising out of, the preparation, dissemination, implementation or administration of this Plan, any contract, instrument or agreement created or entered into in connection with this Plan, any other act taken or omitted to be taken in connection with, or in contemplation of, any of the restructuring or other transactions contemplated by this Plan, and the property to be distributed or otherwise transferred under this Plan. Nothing in this section or elsewhere in this plan shall release, discharge or exculpate any non-Debtor party from any liability to the United States government or its agencies arising under the Internal Revenue Code or criminal laws of the United States.

6.3.8 **Discharge of Claims.** The Plan provides that the payments, distributions, and other treatment provided in respect to each Allowed Claim in the Plan shall be in complete satisfaction of such Allowed Claim, and said Claim shall be discharged in accordance with the provisions of 11 U.S.C. § 1141. The Confirmation Order shall discharge the Debtor from all Claims and other debts that arose before the Confirmation Date, whether or not: (i) a Claim based on such debt is allowed pursuant to 11 U.S.C. § 502, or (ii) the holder of a Claim based on such debt has accepted the Plan.

6.3.9 **Objections to Claims.** Unless otherwise ordered by the Bankruptcy Court, all objections to Claims, including determinations regarding the priority/type of any Claim, shall be filed on or before one hundred and twenty (120) days following the Effective Date, or forty-five (45) days following the filing of any Claim, whichever is later, without prejudice to the extension of such period upon proper application therefor.

6.3.10 **Valuation of Secured Claims.** Under 11 U.S.C. § 506, a secured creditor has a "secured claim" to the extent of such creditor's interest in a Debtor's interest in collateral, and an unsecured claim for the balance, if any. The "allowed" amount of the creditor's secured claim will be the lesser of value of the creditor's interest in the Debtor's interest in the property as determined under 11 U.S.C. § 506, or the allowed amount of the creditor's claim. Under the Plan,

if any dispute over valuation occurs with any Secured Creditor, the Debtor reserves the right to request that the Court determine the value of the Creditor's interest in the collateral that secures the Creditor's Claim. More information about the Debtor's proposed valuation of claims of Secured Creditors may be found in the portion of the Plan which classifies claims.

6.3.11 **Procedure for Allowance of Contingent, Disputed and Unliquidated Claims.** The Court previously established a bar date of November 2, 2018 for contingent, disputed or unliquidated claims [ECF No. 171]. The Plan provides that Creditors who timely file claims for contingent, disputed or unliquidated Claims shall have sixty (60) days from the Confirmation Date to file a motion or adversary action with the Court to have their Claim allowed. Upon the allowance of a contingent or unliquidated Claim, the Plan provides that said Claim shall be entitled to distribution under the Plan consistent with the treatment of other Claims in the Class in which the contingent or unliquidated Claim is ultimately allowed. The contingent or unliquidated Claim of any Creditor who fails to initiate timely action pursuant to this provision for the allowance of its Claim shall have its Claim disallowed and be forever barred from seeking any recovery from the Reorganized Debtor, the Estate, or the Assets. A chart indicating which Claims the Debtor believes are contingent, disputed or unliquidated is attached hereto as **Exhibit B**.

6.3.12 **Procedure for Unknown Claims.** The Court previously established November 2, 2018 as the Unknown Claims Bar Date [ECF No. 170], and a Creditor holding an Unknown Claim must file a Claim before the Unknown Claims Bar Date or its Claim shall be disallowed and said Creditor shall be forever barred from seeking any recovery from the Debtor, the Estate and the Assets. Any timely filed Claim on behalf of an unknown claimant shall be treated as a contingent, disputed or unliquidated Claim and allowed only upon a Claimant's compliance with Section 6.3.11 of the Plan.

6.3.13 **Executory Contracts and Unexpired Leases.**

(a) **Generally.** Under the Plan, the Debtor reserves the right to apply to the Court at any time prior to Confirmation for authority to assume, assign, or reject any Executory Contracts and Unexpired Leases not expressly addressed in the Plan in whole or in part as provided in 11 U.S.C. §§ 365 and 1123. The Plan further provides that all remaining Executory Contracts and Unexpired Leases for which the Debtor has not so moved on or before the Confirmation Date shall be deemed rejected as of said date (the "Rejection Date"); provided, however, that any such motions, requests, proceedings, or actions to assume or reject, or to determine Allowed Cure Claims, pending at the Confirmation Date shall be continued until determined by Final Order of the Bankruptcy Court.

A chart describing the Debtor's Executory Contracts and Unexpired Leases, along with the Debtor's proposed treatment for each contract or lease, is attached as **Exhibit C**. The Debtor reserves the right to amend Exhibit C and/or move to assume, assign, or reject any other Executory Contracts or Unexpired Leases as described in this Section should they subsequently become aware of any such agreements.

(b) **Bar Date for Rejection Damages Claims.** The Plan and the Order Setting Bar Dates [ECF No. 171] provide that any proof of claim that any third party has with respect to

the rejection of any Unexpired Lease or Executory Contract must be filed no later than thirty (30) days after the later of: (i) entry of a Final Order of this Court authorizing such rejection, or (ii) the Rejection Date. Any such Claim for rejection damages shall be treated as a Class 6 Unsecured Claim.

(c) **Allowed Cure Claims on Assumed Unexpired Leases and Executory Contracts. If the Debtor applies for and receives the Court's authorization to assume an Unexpired Lease or Executory Contract as provided under 11 U.S.C. § 365, other than those Unexpired Leases and Executory Contract specifically addressed in the Plan, the Plan provides that the landlord under said Lease shall have thirty (30) days to seek allowance of a Cure Claim from the Bankruptcy Court, provided that the Court has not already entered an order specifying the Cure Claim terms. If no such allowance of a Cure Claim is sought within that time period, all such Claims shall be barred. However, if a Cure Claim is timely sought and thereafter allowed by the Court, the Plan requires that the Debtor will then consult with the Claimant to negotiate a repayment of the Allowed Cure Claim over a reasonable period, not to exceed two (2) years.**

6.3.14 **Causes of Action.** The Plan provides that at the Confirmation Date, all Assets of the Debtor and its Estate, including all Avoidance Actions or other Causes of Action (if any), will revest in and remain with the Reorganized Debtor. As set forth below, the Debtor has conducted a preliminary analysis of potential Avoidance Actions and has determined that many transferees appear to have valid defenses. However, the Debtor reserves its rights to bring such an Avoidance Action or other Cause of Action (if any) prior to or following the Confirmation Date if it subsequently determines otherwise.

(a) **Prepetition Vendor Payments.** The Debtor has identified approximately $663,500.00 in prepetition payments to vendors in its Statement of Financial Affairs, excluding secured debts and taxes. Numerous vendors required COD payments from the Debtor prior to the Petition Date. The Debtor continues to review its payment records to evaluate potential preference claims against vendors.

(b) **Prepetition Insider Payments.** The Debtor has reviewed its payment history with insiders in the year prior to the Petition Date, and has identified approximately $38,000.00 in such payments in its Statement of Financial Affairs. The Debtor continues its investigation of the basis for such payments, but in its preliminary judgment, it appears that all insiders have valid defenses to any potential avoidance actions and/or that any such actions would not yield value for the Estate.

(i) **Payments and Benefits Paid.** As discussed in Section 3.1 above, Patricia Akers and Franklin D. Fitzpatrick, as trustee of the H.D. Fitzpatrick, Jr. Irrevocable Trust are equal co-owners of the Debtor (the "Owners"). Both Ms. Akers and Mr. Fitzpatrick devoted substantial time to the operations of the Debtor on and after the Petition Date, with Ms. Akers in charge of "back office" and personnel matters and Mr. Fitzpatrick in charge of physical plan, finance and cash flow issues. As compensation for their services, Ms. Akers and Mr. Fitzpatrick historically received a compensation package including an annual salary of approximately $58,500 each and various other benefits afforded to all employees of the Debtor. As a consequence of an

objection to use of cash collateral filed on behalf of HUD, the Court prohibited the Debtor from continuing to pay the Owners or provide them with benefits. The Owners have continued to provide services to the Debtor during the pendency of this case, without compensation or benefits. The Plan proposes to immediately restore insurance benefits for the Owners after the Effective Date of the Plan, and to restore an annual salary to the Owners, up to the amount of their prior salaries, no sooner than two years after the Effective Date, but only if "surplus cash" is available for that purpose, consistent with the terms of the Regulatory Agreement.

No relatives of the Owners are employed by the Debtor.

6.4 **General Summary of Plan Treatment of Unclassified Claims.** *The Plan provisions control over the following generalized summary.*

6.4.1 **Administrative Claims.**

(a) **Ordinary Course Administrative Claims.** The Plan provides that all Allowed Administrative Claims arising from obligations incurred by the Debtor in the ordinary course of its business prior to the Confirmation Date, including Administrative Trade Claims, will be paid and performed by the Reorganized Debtor in the ordinary course of its business in accordance with the terms of any agreements governing, instruments evidencing, or other documents relating to such transactions. The Debtor believes that all "ordinary course" Claims are generally current.

(b) **Other Allowed Administrative Claims.** The Plan states that all other holders of Allowed Administrative Claims, including, but not limited to Professional Claims and Allowed Claims under 11 U.S.C. § 503(b)(9), if any, shall be paid in full on the Effective Date or as agreed by any such Creditor. All Professionals shall retain any respective carve-out rights as provided for by Cash Collateral Orders of the Court. At present, the Debtor does not anticipate that there will be any other Allowed Administrative Claims, beyond those noted above.

6.4.2 **Bar Date for Administrative Claims.** The Plan provides certain time deadlines for certain administrative claimants to seek application for allowance and should be closely reviewed, as any untimely-filed claim will be disallowed.

6.4.3 **Post-Confirmation Professional Claims.** Post-Confirmation Date Professional Claims will not require Bankruptcy Court approval and will be paid post-Confirmation from either or both of new value payments from the Owners or Avoidance Action recoveries, but not from the ongoing revenue from the business operations of RealCo or the Reorganized Debtor.

6.4.4 **United States Trustee Fees.** The Plan provides that all fees accrued and payable to the United States Trustee pursuant to 28 U.S.C. § 1930 shall be paid on or before the Effective Date of the Plan. Following Confirmation, the obligation to pay United States Trustee fees shall continue until the Bankruptcy Case is converted, dismissed, or closed, whichever occurs first, and said fees will be paid by RealCo and the Reorganized Debtor in the ordinary course as they are incurred, with all fees to be paid before the Bankruptcy Case may be closed. The

Reorganized Debtor and/or RealCo shall also timely file and serve all reports required by the U.S. Trustee.

6.4.5 **Priority Tax Claims.** As set forth more fully in the Plan, unless otherwise agreed by the holder of a Priority Tax Claim and RealCo or the Reorganized Debtor, each governmental unit which is the holder of an Allowed Priority Tax Claim will receive, in full satisfaction of its Allowed Priority Tax Claim, deferred cash payments totaling the Allowed amount of such Claim over a period not exceeding five (5) years from the Petition Date, as required by the Bankruptcy Code, which period shall conclude on April 9, 2023. The Plan provides that payments on the Allowed Priority Tax Claims will be made on a quarterly basis, beginning on April 1, 2019, and shall continue to be paid each quarter until the Priority Tax Claims are paid in full. The payments on the Allowed Priority Tax Claims shall be made in equal monthly installments of principal and simple interest accruing from the Effective Date at the current rate of interest required by law on the unpaid portion of each Allowed Priority Tax Claim (or upon such other terms determined by the Bankruptcy Court to provide the holders of Priority Tax Claims with deferred cash payments having a value, as of the Effective Date, equal to the Allowed amount of such Priority Tax Claims). No payments will be made on account of any penalty arising with respect to or in connection with an Allowed Priority Tax Claim. RealCo and the Reorganized Debtor will have the right and discretion to pay any Allowed Priority Tax Claim, or any remaining balance of such Priority Tax Claim, in full, at any time on or after the Effective Date, without premium or penalty and without further order of the Court if cash is available to do so

6.4.6 **Other Allowed Priority Non-Tax Claims.** Under the Plan, as soon as practicable after the later of the Effective Date and the date the Claim becomes an Allowed Claim, each holder of an Allowed Priority Non-Tax Claim against the Reorganized Debtor will receive in full satisfaction, settlement, release, and discharge of and in exchange for such Allowed Priority Non-Tax Claim a Distribution from RealCo or the Reorganized Debtor: (i) in Cash equal to the unpaid portion of such Allowed Priority Non-Tax Claim against the Debtor, or (ii) in such amounts and on such other terms as may be agreed between the holder of the Allowed Priority Non-Tax Claim and the Debtor, or (iii) in accordance with the terms of the particular agreement under which such Priority Non-Tax Claim arose. To the extent that any Creditor's total Allowed Priority Non-Tax Claim exceeds the amount entitled to Priority treatment under 11 U.S.C. § 507, the remaining amount of such Claim shall be treated as a Class 6 Allowed Unsecured Claim. The Debtor does not believe that there are any unpaid Priority Non-Tax Claims.

6.5 **General Summary of Plan Treatment of Classified Claims.** *The Plan provisions control over the following generalized summary.*

6.5.1 **Class 1: Allowed Secured Claim of X-Caliber Capital Corp.** Class 1 shall consist of the Allowed Secured Claim of X-Caliber Capital Corp. ("X-Caliber") in the total amount of $8,814,372.24 as of the Petition Date. The Class 1 Claim against the Debtor will be hereinafter referred to as the "X-Caliber Claim." As set forth more fully in the Plan, the Class 1 Claim will be secured by essentially all of the Debtor's Assets (including Assets transferred to RealCo), with its security interests remaining in place after Confirmation. The Debtor will continue payments of principal, interest, taxes and insurance (except liability insurance) to X-Caliber after the Confirmation Date, will delay the resumption of payments to a replacement

reserve account held by X-Caliber, and add any delinquent payments to the end of the term of the X-Caliber loan . Any obligation of the Debtor to obtain or maintain liability insurance under the X-Caliber loan documents shall be modified to require such insurance only to the extent it provides for a per claim deductible of $10,000 or less, and is available for an annual premium of $125,000 or less. The Class 1 Claim is Impaired.

6.5.2 **Class 2: Secured Claim of HUD.** Class 2 consists of the Secured Claim of HUD, including its rights under the Regulatory Agreement. No funds were owed to HUD as of the Petition Date. HUD will retain its security interests which existed on the Petition Date. RealCo and the Reorganized Debtor will execute documents necessary to maintain, create or extend HUD's security interests to any property which is transferred to RealCo. Any action or omission by the Debtor prior to the Confirmation Date which might constitute a violation of, or default under, the Regulatory Agreement shall be deemed waived by HUD, provided that none of the professional fees or U.S. Trustee fees incurred solely in connection with the bankruptcy shall be paid from the Debtor's operating revenues. Any obligation of the Debtor to obtain or maintain liability insurance under the Regulatory Agreement shall be modified to require such insurance only to the extent it provides for a per claim deductible of $10,000 or less, and is available for an annual premium of $125,000 or less. The Class 2 Claim is Impaired.

6.5.3 **Class 3: Allowed Secured Claims of First Insurance Funding Corp.** Class 3 consists of the Allowed Secured Claim of First Insurance Funding Corp. ("First Insurance"), in the amount of $108,614.00 as of the Petition Date. The First Insurance Claim was secured by any unearned premium for the Debtor's liability insurance policy which expired on August 31, 2018. The First Insurance Claim was paid in full after the Petition Date, and no additional sums are due to First Insurance. The Class 3 Claim is not Impaired.

6.5.4. **Class 4: Allowed Other Secured Claims.** Class 4 shall consist of all other Secured Claims, if any, excluding the Class 1 - 3 Secured Claims. The Plan provides that, in satisfaction of the Allowed Secured Claim of any Class 4 Claimant, if any, the Debtor shall, on the Effective Date, or such other date as may be agreed on, at the Debtor's option, either: (i) surrender the collateral to the Claimant to allow it to liquidate said collateral at its discretion; or (ii) pay the amount of such Allowed Secured Claim to the Class 4 Creditor over time during the life of the Plan. Any Allowed Deficiency Claim shall be treated as a Class 6 Claim. The Class 4 Claims are not Impaired. There are no known claims in this Class.

6.5.5 **Class 5: Allowed Claim of CMS.** Class 5 shall consist of the Claim of the United States Department of Health & Human Services, Centers for Medicare & Medicaid Services ("CMS"), consisting of a civil monetary penalty in the amount of $366,709.85, assessed after the Petition Date, but based on event occurring prior to the Petition Date. Under existing federal regulations,[6] CMS may deduct the penalty from any sums CMS or Kentucky Medicaid owe the Debtor. Although the CMS Claim is not secured, its regulatory authority to recover the penalty from sums owed distinguishes its Claim from other Unsecured Claims. In full satisfaction of the CMS Allowed Claim, the Debtor will pay the penalty in monthly deferred cash payments

[6] 42 C.F.R. 488.442(c).

totaling the Allowed amount of such Claim over a period not exceeding five (5) years from the Petition Date. No interest will accrue on the CMS Claim. The Class 5 Claim is Impaired.

6.5.6. **Class 6: Allowed Unsecured Claims.** Except as otherwise set forth herein, the Plan provides that each holder of an Allowed Claim in Class 6 shall receive Distribution(s) to the greatest extent possible from the net cash flow of the Reorganized Debtor for a period of 60 months following the Effective Date. Allowed Unsecured Claims include any unknown, contingent, disputed or unliquidated Claims that are Allowed pursuant to the provisions of the Plan. Within 30 days of the Effective Date, the Plan requires that the Reorganized Debtor establish a separate escrow account to be used solely for funding Distributions to Class 6 Claimants (the "Class 6 Escrow"). Beginning thirty (30) days after the Effective Date and continuing for 60 months, the Reorganized Debtor shall deposit the monthly sum of $1,000.00 into the Class 6 Escrow for the purposes of paying Class 6 Allowed Unsecured Claims. In addition, the Debtor shall deposit Net Profits generated during each full calendar year after the Effective Date into the Class 6 Escrow, to be distributed pursuant to the Plan afrer payment of the Convenience Claims. The Reorganized Debtor shall make Distributions from the Class 6 Escrow to each holder of an Allowed Class 6 Claim annually, beginning on March 1, 2020 and ending on March 1, 2024, in the amount of each Claimant's *pro rata* share of the Class 6 Escrow on that date. The Class 6 Claims are Impaired.

6.5.7 **Class 7: Allowed Convenience Claims.** Class 7 shall consist of Convenience Claims, which are Allowed Unsecured Claims in the amount of $1,000.00 or less. The minimum required payments to the Class 6 Escrow during the first year of the Plan (total $12,000.00) are designated to pay Allowed Claims within the Convenience Class to the greatest extent possible, in full satisfaction, settlement, release and extinguishment of such Claims. A Creditor holding an Allowed Secured Claim in excess of $1,000.00 may elect to reduce its Claim to $1,000.00 and be included in the Class 7 Convenience Claims. The Class 7 Claims are Impaired.

6.5.8. **Class 8: Allowed Unsecured Tort Claims.** The Debtor's Statement of Financial Affairs identifies numerous pending claims against it based on allegations of negligent, reckless or intentional acts or omissions. In addition, there may be tort claims which accrued prior to August 31, 2018 which are unknown to the Debtor. Pursuant to prior orders [ECF Nos. 170, 171], the Court established a method for notifying known and potential claimants of the bar date of November 2, 2018 for filing such claims. The Debtor disputes any tort claims which may exist against it. However, for any timely filed Allowed Claims based on allegations of negligent, reckless or intentional acts or omissions, recovery and payment on such Claims shall be limited to existing insurance coverage, if any. After the Effective Date, upon request of the holder of an Allowed Class 8 Claim, the Reorganized Debtor will stipulate that any injunction imposed by the Confirmation Order does not apply to the extent a Class 8 Creditor seeks to liquidate its Claim via pending litigation. Class 8 Claims are impaired.

6.5.9 **Class 9: Equity Interests in the Debtor.** Class 9 consists of those Persons or entities holding equity or membership Interests in the Debtor – Patricia Akers (50%) and Franklin D. Fitzpatrick, as trustee of the H.D. Fitzpatrick, Jr. Irrevocable Trust (50%). The Plan provides that on the Effective Date, the equity interests in the Debtor will be retained by the existing members, and new equity interests in RealCo shall be issued to the existing members of

the Debtor, in exchange for total capital contributions of $330,000.00 (the "New Value"). The New Value payments consist of a) $280,000.00 contributed to the Debtor prior to October 1, 2018; and b) $50,000 to be contributed to the Reorganized Debtor or RealCo after October 1, 2018, but no later than 60 days after the Effective Date. In addition to payment of the New Value, the Owners will waive any claims they may have against the Debtor as of the Effective Date. The Class 9 Interests are Impaired.

6.6 **Executory Contracts and Leases** The Debtor previously entered into an Agreed Order rejecting its executory contract with Health Systems of Kentucky, LLC effective May 31, 2018. [ECF No. 127]. The Debtor has filed a motion to assume the non-residential real property lease where the Debtor's facilities are located [ECF No. 203], and that motion is scheduled for a hearing on October 18, 2018. The Debtor reserves the right to apply to this Court at any time prior to Confirmation for authority to assume, assume and assign, or reject any other Executory Contracts and/or Unexpired Leases in whole or in part as provided in 11 U.S.C. §§ 365 and 1123. All remaining Executory Contracts and Unexpired Leases for which the Debtor has not specifically so moved on or before the Confirmation Date shall be deemed rejected as of said date (the "Rejection Date"); provided, however, that any such motions, requests, proceedings or action to seek to assume or reject, or to determine Allowed Cure Claims, pending at the Confirmation Date shall be continued until determined by Final Order of the Bankruptcy Court or other court of competent jurisdiction.

6.7 **Plan Implementation**

6.7.1 **Parties Responsible for Implementation of the Plan.** Upon confirmation, the Plan provides that Providence Health Management, Inc. will continue to manage the Reorganized Debtor's operations, with input from the Owners. The Owners will be responsible for the creation of RealCo, the transfer of real property assets to it, subject to the terms of the Plan. The Owners will have the authority to take all actions desirable in their business judgment to continue the operations of RealCo and the Reorganized Debtor, including implementation and administration of the Plan. In exchange for providing these services to the Debtor, the Plan proposes to restore insurance benefits for the Owners after the Effective Date of the Plan, and to restore an annual salary to the Owners, up to the amount of their prior salaries, no sooner than two years after the Effective Date, but only if "surplus cash" is available for that purpose, consistent with the terms of the Regulatory Agreement. The Reorganized Debtor will pay all United States Trustee fees and will file all post-Confirmation reports required by the United States Trustee's Office. The Reorganized Debtor will also file the necessary final reports and will request closing the Bankruptcy Case as soon as practicable after Plan payments have begun.

6.7.2 **Means of Implementation.** RealCo will operate the real property leased by the Debtor post-Confirmation, and the Reorganized Debtor will operate the long term care and independent living business previously conducted by the Debtor in the ordinary course of business, receiving ongoing income from operations, and using all income to pay its customary operating expenses and necessary capital expenditures and Plan payments. The Debtor has projected and assumed income growth through a conservatively-projected growth in its business following recovery from the DPNA reduction in admissions and resulting reduction in revenues.

6.7.3 **Continued Engagement of Professionals**. RealCo and the Reorganized Debtor shall continue the engagement of DelCotto Law Group PLLC, Providence Health Management, Inc., Deming Malone Livesay & Ostroff, and such other professionals as may be necessary for the purposes of rendering services in connection with implementing the Plan, resolving Claims, and performing routine post-Confirmation Chapter 11 administration, such as final reporting and moving to have the Case closed upon Plan completion. Post-Confirmation, any professional services will not require Court approval.

ARTICLE VII

RISK FACTORS

7.1 **Risks of Non-Confirmation.**

If no Plan can be confirmed, the Chapter 11 Bankruptcy Case may be converted to a case under Chapter 7 of the Bankruptcy Code, in which case a trustee would be elected or appointed to liquidate the Debtor's Assets for distribution to Creditors in accordance with the priorities established by the Bankruptcy Code. The Debtor believes that Confirmation is preferable to Chapter 7 liquidation because the Plan maximizes the distributions to all Classes of Creditors, and any alternative to Confirmation would result in substantial delays and potentially lesser recoveries as persons unfamiliar with the Debtor's Assets would assume administration of the Case. It is projected that only the secured creditors would have any recovery in any type of liquidation, and even this recovery could be substantially less, since the Debtor's operations could "go dark" prior to sale or an "auction" sale could produce lower results than any going concern, ordinary-course sale.

7.2 **Risks of Non-Consensual Confirmation.** Pursuant to the "cramdown" provisions of 11 U.S.C. § 1129, the Bankruptcy Court can confirm the Plan at the Debtor's request if at least one impaired Class has accepted the Plan (with such acceptance being determined without including the acceptance of any "insider" in such Class) and, with respect to each Impaired class that has not accepted the Plan, the Bankruptcy Court determines that the Plan "does not discriminate unfairly" and is "fair and equitable" with respect to impaired Classes. In accordance with 11 U.S.C. §§ 1129(a)(8) and (b), the Debtor will request Confirmation of the Plan without the acceptance of all impaired Classes entitled to vote.

The Debtor reserves the right to modify the terms of the Plan as necessary for Confirmation without the acceptance of all impaired Claims. Such modification could result in less favorable treatment for any non-accepting Classes than the treatment currently provided for in the Plan. Such less favorable treatment could include a distribution of property of a lesser value than that currently provided for in the Plan or no distribution of property whatsoever.

7.3 **Risks of Delays in Confirmation.** Any delay in Confirmation and effectiveness of the Plan could result in, among other things, increased Administrative Claims or contested fights with secured creditors. These or any other negative effects of delays in Confirmation of the Plan could endanger the ultimate approval of the Plan by the Bankruptcy Court.

7.4 **Risks of Shut Down of Operations.** In its business judgment, the Debtor has determined that maintaining and reorganizing its business operations pursuant to the Plan will provide a better return for all parties in interest. Due to the nature of the Debtor's business, a majority of its assets are worth much more as part of a going concern than they are if sold on a piecemeal basis. As a result, if the Debtor is forced to discontinue its business operations, all of its Creditors stand to receive far smaller distributions, if any, in satisfaction of their Claims than they would if the Debtor's business continued operating.

ARTICLE VIII

PLAN CONFIRMATION

8.1 **Generally.** To confirm the Plan, the Bankruptcy Code requires that the Bankruptcy Court make a series of findings concerning the Plan and the Debtor, including that the:

(1) Plan has classified Claims and Interests in a permissible manner;

(2) Plan complies with the applicable provisions of the Bankruptcy Code;

(3) Debtor complies with the applicable provisions of the Bankruptcy Code;

(4) Debtor, as proponent of the Plan, has proposed the Plan in good faith and not by any means forbidden by law;

(5) Disclosure required by 11 U.S.C. § 1125 has been made;

(6) Plan has been accepted by the requisite votes of creditors and equity interest holders (except to the extent that cramdown is available under 11 U.S.C. § 1129(b));

(7) Plan is feasible;

(8) Plan is in the "best interests" of all holders of Claims or Interests in an impaired Class by providing to creditors or interest holders, on account of such Claims or Interests, property of value, as of the Effective Date, that is not less than the amount that such holder would receive or retain in a Chapter 7 liquidation unless each holder of a Claim or Interest in such Class has accepted the Plan;

(9) Fees and expenses payable under 28 U.S.C. § 1930, as determined by the Bankruptcy Court at the Confirmation Hearing, have been paid or the Plan provides for the payment of such fees on the Effective Date;

(10) Plan provides for the continuation after the Effective Date of all retiree benefits, as defined in 11 U.S.C. § 1114, at the level established at any time prior to Confirmation pursuant to 11 U.S.C. §§ 1114(e)(1)(B) or 1114(g), for the duration of the period that the Debtor has obligated itself to provide such benefits; and

(11) Disclosures required under 11 U.S.C. § 1129(a)(5) concerning the identity and affiliations of persons who will serve as officers, directors, and voting trustees of the successors to the Debtor have been made.

8.2 **Voting Requirements for Confirmation under the Bankruptcy Code.**

8.2.1 **General Voting Information.**

PLEASE CAREFULLY FOLLOW ALL OF THE INSTRUCTIONS CONTAINED ON THE BALLOT PROVIDED TO YOU. ALL BALLOTS **MUST** BE COMPLETED AND RETURNED IN ACCORDANCE WITH THE INSTRUCTIONS PROVIDED.

TO BE COUNTED, YOUR BALLOT MUST BE ACTUALLY RECEIVED BY THE DEADLINE SET BY THE COURT AND AT THE ADDRESS SET FORTH ON YOUR BALLOT. IT IS OF THE UTMOST IMPORTANCE TO THE DEBTOR THAT YOU VOTE PROMPTLY TO ACCEPT THE PLAN. IF YOU HAVE ANY QUESTIONS, PLEASE CONTACT THE DEBTOR OR ITS COUNSEL.

IF YOU HOLD CLAIMS IN MORE THAN ONE CLASS, IF YOU HOLD MULTIPLE GENERAL UNSECURED CLAIMS, OR UNDER CERTAIN OTHER CIRCUMSTANCES, YOU MAY RECEIVE MORE THAN ONE BALLOT. YOU SHOULD COMPLETE, SIGN, AND RETURN EACH BALLOT YOU RECEIVE.

ACCEPTANCE OR REJECTION OF THE PLAN WILL BE DETERMINED, PURSUANT TO THE BANKRUPTCY CODE, BASED UPON THE BALLOTS OF THE CREDITORS HOLDING ALLOWED CLAIMS THAT *ACTUALLY VOTE* ON THE PLAN. THEREFORE, IT IS IMPORTANT THAT CLAIMANTS EXERCISE THEIR RIGHT TO VOTE TO ACCEPT OR REJECT THE PLAN.

IF ANY OF THE CLASSES OF HOLDERS OF IMPAIRED CLAIMS VOTE TO REJECT THE PLAN: (A) THE DEBTOR MAY SEEK TO SATISFY THE REQUIREMENTS FOR CONFIRMATION OF THE PLAN UNDER THE CRAMDOWN PROVISIONS OF 11 U.S.C. § 1129(b) AND, IF REQUIRED, MAY AMEND THE PLAN TO CONFORM TO THE STANDARDS OF SUCH SECTION; OR (B) THE PLAN MAY BE MODIFIED OR WITHDRAWN WITH RESPECT TO A PARTICULAR CREDITOR, OR (C) THE PLAN MAY BE WITHDRAWN IN ITS ENTIRETY. *See* Section 7.2.

8.2.2 **Classes Entitled to Vote on the Plan.**

(a) **Generally.** Pursuant to the Bankruptcy Code, only classes of claims against or equity interests in a debtor that are "impaired" under the terms of a plan of liquidation or reorganization are entitled to vote to accept or reject a plan. A class is "impaired" if the legal, equitable, or contractual rights attaching to the claims or interests of that class are modified, other than by curing defaults and reinstating maturity. Classes of Claims and Interests that are not impaired are *not* entitled to vote on the Plan and are conclusively presumed to have accepted the Plan. In addition, Classes of Claims and Interests that receive no distributions under the Plan are not entitled to vote on the Plan and are deemed to have rejected the Plan unless such Class otherwise indicates acceptance. *The classification of Claims and Interests under the Plan is summarized, together with an indication of whether each Class of Claims or Interests is impaired, in Section 6.5.*

(b) **Contested and Unliquidated Claims.** Contested, disputed, contingent, and/or unliquidated Claims are *not* entitled to vote to accept or reject the Plan. If your Claim has been estimated for voting purposes by Court Order, you will be allowed to vote your Claim in the amount estimated by said Order. If ballots are erroneously sent to a Creditor not entitled to vote, then the ballot will not be counted in the calculation of the Creditors voting to accept or reject the Plan. If you are a Creditor holding a contested or disputed claim, you may ask the Court to have your Claim temporarily allowed for the purpose of voting pursuant to Fed. R. Bankr. P. 3018.

8.2.3 **Voting Procedures and Requirements.**

(a) **Ballots and Voting.** Creditors holding Allowed Claims entitled to vote on the Plan will be sent a ballot and instructions for voting along with this Disclosure Statement. Creditors should read the ballot carefully and follow the instructions. In voting to accept or reject the Plan, you must use *only* the ballot sent to you with this Disclosure Statement. Creditors entitled to vote must complete, sign, and return their ballots to counsel for the Debtor on or before the Voting Deadline. Fed. R. Bankr. P. 3018(a) permits a Creditor, for cause, to petition the Court to permit it to change or withdraw its vote on a plan. Any such petition must be made before the Confirmation Hearing, unless otherwise permitted by the Court. The Debtor will present the results of the voting to the Bankruptcy Court prior to the Confirmation Hearing.

(i) **Lost or Damaged Ballots.** If you are entitled to vote and you did not receive a ballot, received a damaged ballot, or lost your ballot, please contact Tresine Callahan at DelCotto Law Group PLLC at (859) 231-5800 or tcallahan@dlgfirm.com. Also, this Disclosure Statement, the Plan, and all of the related Exhibits and Schedules are available upon request to any party in interest by contacting the Debtor's counsel.

(ii) **Effective Transmittal of Ballots.** Votes cannot be transmitted orally. Accordingly, you are urged to return your signed and completed ballot by hand delivery, overnight service, facsimile, email, or regular U.S. mail, promptly.

(b) **Requirements for Class Acceptance.** As a condition of Confirmation, the Bankruptcy Code requires that each class of Claims that is impaired vote to accept the Plan, subject to the exception of 11 U.S.C. § 1129(b), which still requires one class of Claims that is impaired to have voted to accept the Plan. A class of Claims accepts the Plan if: (i) holders of at least two-thirds in the total dollar amount of Allowed Claims in that class, and (ii) a majority in number of holders of Claims in that class, vote to accept the Plan.

8.3 **General Requirements for Confirmation under the Bankruptcy Code.**

8.3.1 **Best Interests of Creditors/Liquidation Analysis.** Notwithstanding acceptance of the Plan by each impaired Class, to confirm the Plan, the Bankruptcy Court must determine that the Plan is in the best interests of each holder of a Claim or Interest in any such impaired Class who has not voted to accept the Plan. Accordingly, if an impaired Class does not unanimously accept the Plan, the "best interests" test requires that the Bankruptcy Court find that the Plan provides to each member of such impaired Class a recovery on account of the member's Claim or Interest that has a value, as of the Effective Date, at least equal to the value of the distribution that each such member would receive if the Debtor was liquidated under Chapter 7 of the Bankruptcy Code on such date.

To estimate what members of each impaired Class of Claims or Interests would receive if the Debtor was liquidated under Chapter 7 of the Bankruptcy Code, the Bankruptcy Court must first determine the aggregate dollar amount that would be available if the Chapter 11 Bankruptcy Case was converted to a Chapter 7 case under the Bankruptcy Code and the Debtor's Assets were liquidated by a Chapter 7 trustee (the "Liquidation Value"). The Liquidation Value would consist of the net proceeds from the disposition of the assets of the Debtor, augmented by any unencumbered cash held by the Debtor.

The Liquidation Value available to holders of Unsecured Claims and Interests would be reduced by, among other things: (a) the Claims of secured creditors to the extent of the value of their collateral; (b) the costs, fees, and expenses of the liquidation, as well as other administrative expenses of the Debtor's Chapter 7 case; (c) unpaid Administrative Claims of the Chapter 11 Case; and (d) Priority Claims and Priority Tax Claims. The Debtor's costs of liquidation in Chapter 7 would include the compensation of a trustee, as well as of counsel and of other professionals retained by a trustee, asset disposition expenses, applicable taxes, litigation costs, claims arising from any operations of the Debtor during the pendency of the Chapter 7 case, and all unpaid Administrative Claims incurred by the Debtor during the Chapter 11 case that are allowed in the Chapter 7 case. The liquidation itself would likely accelerate the payment of certain Priority Claims and Priority Tax Claims that would otherwise be payable in the ordinary course of business. These Priority Claims and Priority Tax Claims would be paid to the extent possible out of the net liquidation proceeds, after payment of Secured Claims, before the balance would be made available to pay Unsecured Claims or to make any distribution in respect of Interests. The Debtor believes that the liquidation also would generate an increase in Unsecured Claims, such as rejection damages Claims, and Tax and other governmental Claims.

The information contained in **Exhibit D** attached hereto provides a summary of the Liquidation Values of the Debtor's Assets, assuming a hypothetical Chapter 7 liquidation in which a trustee appointed by the Bankruptcy Court would liquidate the Debtor's Assets.

In summary, the Debtor believes that Chapter 7 liquidation of the Debtor would result in diminution in the value to be realized by holders of Claims, as compared to the proposed distributions under the Plan, because of, among other factors: (a) the negative impact of conversion to a Chapter 7 case and subsequent expedited liquidation on the Debtor's residents and employees; (b) additional costs and expenses involved in the appointment of a trustee, attorneys, accountants, and other professionals to assist such trustee in the Chapter 7 case; and (c) additional expenses and Claims, some of which would be entitled to priority in payment, that would arise by reason of a liquidation. Consequently, the Debtor believes that the Plan will provide a greater ultimate return to holders of Claims than a Chapter 7 liquidation.

8.3.2 **Feasibility of Plan.** Section 1129(a)(11) of the Bankruptcy Code requires that confirmation of a plan not be likely to be followed by the liquidation of the Debtor or any successor to the Debtor, or the need for further financial reorganization, unless such liquidation or reorganization is proposed in the Plan. Based on the Debtor's analysis, the Reorganized Debtor and RealCo will have sufficient assets and business operations to accomplish their tasks under the Plan. Therefore, the Debtor believes that its reorganization pursuant to the Plan will meet the feasibility requirements of the Bankruptcy Code. To support this contention, the Debtor's financial projections for the term of the Plan term are attached hereto as **Exhibit E**.

8.3.3 **Compliance with Applicable Provisions of the Bankruptcy Code.** Section 1129(a)(1) of the Bankruptcy Code requires that the Plan comply with the applicable provisions of the Bankruptcy Code. The Debtor has considered each of these issues in the development of the Plan and believe that the Plan complies with all applicable provisions of the Bankruptcy Code.

8.4 **Confirmation.**

8.4.1 **Confirmation Hearing.** The Bankruptcy Code requires the Bankruptcy Court, after notice, to hold a hearing on whether the Debtor has fulfilled the Confirmation requirements of 11 U.S.C. § 1129. The Confirmation Hearing has been or will be scheduled by Order of the Court and you will or have received notice of the hearing by separate notice/order. If you have any questions concerning the hearing, please contact the undersigned counsel.

8.4.2 **Objections to Confirmation.** Any objection to Confirmation must be made in writing and must specify in detail the name and address of the objector, all grounds for the objection, and the amount of the Claim or Interest held by the objector. Any such objections must be filed and served upon the persons designated in the notice of the Confirmation Hearing and in the manner and by the deadline described therein.

8.4.3 **Methods of Confirmation.**

(a) **Confirmation Based on Plan Acceptance.** A plan is accepted by an impaired class of claims if holders of at least two-thirds in dollar amount and a majority in number of claims of that class vote to accept the plan. Only those holders of claims who actually vote (and are entitled to vote) to accept or to reject a plan count in this tabulation. In addition to this voting requirement, 11 U.S.C. § 1129 requires that a plan be accepted by each holder of a claim or interest in an impaired class or that the plan otherwise be found to be in the best interests of each holder of a claim or interest in an impaired class by the Bankruptcy Court.

(b) **Confirmation through Cramdown.** The Bankruptcy Code contains provisions for confirmation of a plan even if it is not accepted by all impaired classes, so long as at least one impaired class of claims has accepted it. These "cramdown" provisions are set forth in 11 U.S.C. § 1129(b). As indicated above, the Plan may be confirmed under the cramdown provisions if, in addition to satisfying the other requirements of 11 U.S.C. § 1129(a), it: (a) is "fair and equitable;" and (b) "does not discriminate unfairly" with respect to each Class of Claims or Interests that is impaired under, and has not accepted, the Plan. The "fair and equitable" standard, also known as the "absolute priority rule," requires, among other things, that unless a dissenting class of unsecured claims or a class of interests with respect to a debtor receives full compensation for its allowed claims or allowed interests, no holder of allowed claims or interests with respect to such debtor in any junior class may receive or retain any property on account of such claims or interests. With respect to a dissenting class of secured claims, the "fair and equitable" standard requires, among other things, that holders either: (a) retain their liens and receive deferred cash payments with a value as of the effective date equal to the value of their interest in property of the debtor's estate; or (b) receive the indubitable equivalent of their secured claims. The "fair and equitable" standard has also been interpreted to prohibit any class senior to a dissenting class from receiving under a plan more than 100% of its allowed claims or allowed interests. The Debtor believes that, if necessary, the Plan may be crammed down over the dissent of certain Classes of Claims, in view of the treatment proposed for such Classes.

The requirement that the Plan not "discriminate unfairly" means, among other things, that a dissenting class must be treated substantially equally with respect to other classes of equal rank. The Debtor does not believe that the Plan unfairly discriminates against any Class that may not accept or otherwise consent to the Plan. Subject to the conditions set forth in the Plan, a determination by the Bankruptcy Court that the Plan, as it applies to the Debtor, is not confirmable pursuant to 11 U.S.C. § 1129 will not limit or affect: (a) the confirmability of the Plan as it applies to the Debtor; or (b) the Debtor's ability to modify the Plan, as it applies to the Debtor, to satisfy the provisions of 11 U.S.C. § 1129(b).

8.5 **Alternatives to Confirmation.** If the Plan is not confirmed and consummated, the alternatives include preparation and presentation of an alternative plan of reorganization or a conversion of this case to one under Chapter 7 of the Bankruptcy Code. If the Court denies confirmation, the Debtor or any other party in interest could propose a different Plan. The Debtor believes such an alternative plan would result in less return to creditors than the distributions to creditors pursuant to the Plan. Before proposing the present Plan, the Debtor explored other alternatives and engaged in negotiations with its major Secured Creditor. The Debtor believes not

only that the Plan, as described herein, fairly adjusts the rights of various classes of Creditors and enables Creditors to realize the most possible under the circumstances, but also that rejection of the Plan in favor of some alternative arrangement will require, at the very least, an extensive and time-consuming process and will not result in a better recovery for any Class.

ARTICLE IX

CERTAIN FEDERAL TAX CONSEQUENCES

IRS Circular 230 Disclosure: To ensure compliance with requirement imposed by the IRS, we inform you that any U.S. federal tax advice contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing, or recommending to another party any transaction or matter addressed herein.

9.1 **General**.

A DESCRIPTION OF CERTAIN U.S. FEDERAL INCOME TAX CONSEQUENCES OF THE PLAN IS PROVIDED BELOW. THE DESCRIPTION IS BASED ON THE INTERNAL REVENUE CODE, TREASURY REGULATIONS, JUDICIAL DECISIONS, AND ADMINISTRATIVE DETERMINATIONS, ALL AS IN EFFECT ON THE DATE OF THIS DISCLOSURE STATEMENT. CHANGES IN ANY OF THESE AUTHORITIES OR IN THEIR INTERPRETATION MAY HAVE RETROACTIVE EFFECT, WHICH MAY CAUSE THE FEDERAL INCOME TAX CONSEQUENCES OF THE PLAN TO DIFFER MATERIALLY FROM THE CONSEQUENCES DESCRIBED BELOW. NO RULING HAS BEEN REQUESTED FROM THE IRS, NO LEGAL OPINION HAS BEEN REQUESTED FROM COUNSEL CONCERNING ANY TAX CONSEQUENCE OF THE PLAN, AND NO TAX OPINION IS GIVEN BY THIS DISCLOSURE STATEMENT.

THIS DESCRIPTION DOES NOT COVER ALL ASPECTS OF FEDERAL INCOME TAXATION THAT MAY BE RELEVANT TO THE DEBTOR OR HOLDERS OF CLAIMS. FOR EXAMPLE, THE DESCRIPTION DOES NOT ADDRESS ISSUES OF SPECIAL CONCERN TO CERTAIN TYPES OF TAXPAYERS, SUCH AS DEALERS IN SECURITIES, LIFE INSURANCE COMPANIES, FINANCIAL INSTITUTIONS, TAX-EXEMPT ORGANIZATIONS, AND FOREIGN TAXPAYERS, NOR DOES IT ADDRESS TAX CONSEQUENCES TO HOLDERS OF INTERESTS IN THE DEBTOR. THIS DESCRIPTION DOES NOT DISCUSS THE POSSIBLE STATE TAX OR NON-U.S. TAX CONSEQUENCES THAT MIGHT APPLY TO THE DEBTOR OR TO HOLDERS OF CLAIMS.

FOR THESE REASONS, THE DESCRIPTION THAT FOLLOWS IS NOT A SUBSTITUTE FOR CAREFUL TAX PLANNING AND PROFESSIONAL TAX ADVICE BASED UPON THE INDIVIDUAL CIRCUMSTANCES OF EACH HOLDER OF A CLAIM. HOLDERS OF CLAIMS ARE URGED TO CONSULT WITH THEIR OWN TAX ADVISORS REGARDING THE FEDERAL, STATE, LOCAL, AND FOREIGN TAX CONSEQUENCES OF THE PLAN.

9.2 **Tax Consequences of Payment of Allowed Claims Pursuant to Plan Generally.** The federal income tax consequences of the implementation of the Plan to the holders of Allowed Claims will depend, among other things, on the consideration to be received by the holder, whether the holder reports income on the accrual or cash method, whether the holder receives distributions under the Plan in more than one taxable year, whether the holder's Claim is Allowed or disputed on the Effective Date, and whether the holder has taken a bad debt deduction or worthless security deduction with respect to its claim.

9.2.1 **Recognition of Gain or Loss.** In general, a holder of an Allowed Claim should recognize gain or loss equal to the amount realized under the Plan in respect of its Claim, less the holder's tax basis in the Claim. Any gain or loss recognized in the exchange may be long-term or short-term capital gain or loss or ordinary income or loss, depending upon the nature of the Allowed Claim and the holder, the length of time the holder held the Claim, and whether the Claim was acquired at a market discount. If the holder realizes a capital loss, the holder's deduction of the loss may be subject to limitation. The holder's tax basis for any property received under the Plan generally will equal the amount realized. The holder's amount realized generally will equal the sum of the cash and the fair market value of any other property received by the holder under the Plan on the Effective Date or a subsequent distribution date, less the amount (if any) treated as interest, as discussed below.

9.2.2 **Post-Effective Date Distributions.** Because certain holders of Allowed Claims, including Disputed Claims that ultimately become Allowed Claims, may receive cash distributions after the Effective Date, the imputed interest provisions of the Internal Revenue Code may apply and cause a portion of the subsequent distribution to be treated as interest. Additionally, because holders may receive distributions with respect to an Allowed Claim in a taxable year or years following the year of the initial distribution, any loss and a portion of any gain realized by the holder may be deferred. All holders of Allowed Claims are urged to consult their tax advisors regarding the possible application of (or ability to elect out of) the "installment method" of reporting with respect to their Claims.

9.2.3 **Receipt of Interest.** Holders of Allowed Claims will recognize ordinary income to the extent that they receive cash or property that is allocable to accrued but unpaid interest which the holder has not yet included in its income. If an Allowed Claim includes interest, and if the holder receives less than the amount of the Allowed Claim pursuant to the Plan, the holder must allocate the Plan consideration between principal and interest. The holder may take the position that the amounts received pursuant to the Plan are allocable first to principal, up to the full amount of principal, and only then to interest. However, the proper allocation of Plan consideration between principal and interest is unclear, and holders of Allowed Claims should consult their own tax advisors in this regard. If the Plan consideration allocable to interest with respect to an Allowed Claim is less than the amount that the holder has previously included as interest income, the previously included but unpaid interest may be deducted, generally as a loss.

9.2.4 **Bad Debt or Worthless Securities Deduction.** A holder who receives, in respect of an Allowed Claim, an amount less than the holder's tax basis in the Claim may be entitled in the year of receipt (or in an earlier or later year) to a bad debt deduction in some amount under 26 U.S.C. § 166(a) or a worthless securities deduction under 26 U.S.C. § 165(g). The rules governing the character, timing, and amount of bad debt and worthless securities deductions place

considerable emphasis on the facts and circumstances of the holder, the obligor, and the instrument with respect to which a deduction is claimed. Holders of Allowed Claims, therefore, are urged to consult their tax advisors with respect to their ability to take such a deduction.

9.2.5 **Information Reporting and Withholding.** Under the Internal Revenue Code's backup withholding rules, the holder of an Allowed Claim may be subject to backup withholding with respect to distributions or payments made pursuant to the Plan, unless the holder comes within certain exempt categories (which generally include corporations) and, when required, either demonstrates that categorization or provides a correct taxpayer identification number and certifies under penalty of perjury that the taxpayer identification number is correct and that the holder is not subject to backup withholding because of a failure to report all dividend and interest income. Backup withholding is not an additional tax, but merely an advance payment that may be refunded to the extent it results in an overpayment of tax. Holders of Allowed Claims may be required to establish exemption from backup withholding or to make arrangements with respect to the payment of backup withholding.

9.3 **Certain U.S. Federal Income Tax Consequences to the Debtor.** In the event that the Debtor sells any of its Assets, the Debtor will generally recognize a gain or loss on the sale of those Assets, equal to the difference between the amount realized on the sale and the adjusted tax basis of the Assets being sold. Additionally, if the Debtor conveys appreciated (or depreciated) property (i.e. property having an adjusted tax basis less (or greater) than its fair market value) to a creditor in cancellation of full recourse debt, the Debtor must recognize taxable gain or loss equal to the excess or shortfall, respectively, of such fair market value over that adjusted basis. This gain or loss may be ordinary income or loss, capital gain or loss, or a combination of each, and may be offset against any applicable net operating loss carry-forwards from previous tax years.

Further, the discharge of a recourse debt obligation by the Debtor in exchange for the Debtor's payment of cash and/or transfer of property with a fair market value that is less than the adjusted issue price of the debt obligation (as determined for U.S. federal income tax purposes) may give rise to cancellation of indebtedness ("COD") income. COD income must generally be included in the Debtor's gross income, subject to certain statutory or judicial exceptions that may limit the amount of COD income required to be included. One such statutory exception applies to certain debtor whose discharge of indebtedness is granted in a case brought under Title 11 of the United States Code (relating to bankruptcy), pursuant to a court-approved plan of reorganization.

For the foregoing reasons, the precise amount of taxable gain or loss, COD income, or both that the Debtor may realize as a result of effectuation of the Plan cannot be determined until the date of the exchange.

ARTICLE X

ADDITIONAL INFORMATION, RECOMMENDATIONS, AND CONCLUSION

10.1 **Additional Information.** Any statements in this Disclosure Statement concerning the provisions of any document are not necessarily complete, and in each instance, reference is made to such document for the full text thereof. Certain documents described or referred to in this Disclosure Statement have not been attached as exhibits because of the impracticability of

furnishing copies of these documents to all recipients of this Disclosure Statement. The Debtor will file all exhibits to the Plan with the Bankruptcy Court, and the exhibits also will be available upon request from the Debtor's counsel.

10.2 **Recommendations and Conclusion.** The materials provided in this Disclosure Statement are intended to assist you in reviewing the Plan in an informed manner. If the Plan is confirmed, you will be bound by the terms of the Plan. You are urged to study these materials and make such further inquiries as you may deem appropriate.

For all of the reasons set forth in this Disclosure Statement, the Debtor believes that the Confirmation and consummation of the Plan is preferable to all other alternatives. Consequently, the Debtor urges all holders of Claims in voting Classes to vote to accept the Plan and to evidence their acceptance by duly completing and returning their ballots so that they will be received on or before the Voting Deadline.

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Dated: October 9, 2018

Respectfully submitted,

PAINTSVILLE INVESTORS, LLC

By: /s/ Bryan Fitzpatrick

Title: Designated Representative

Tendered by:

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