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Counsel to WELLS FARGO BANK, NATIONAL ASSOCIATION, as Trustee for the Registered Holders Of Colony Multifamily Mortgage Trust 2014-1, Commercial Mortgage Pass-Through Certificates, Series 2014-1, which is Serviced by its Special Servicer, COLONY AMC OPCO, LLC

Hearing Date: May 26, 2017[1]
Time: 10:00 a.m.

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

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In re:

CAYOT REALTY, INC.,

Debtor.

Chapter 11
Case No. 16-22664 (RDD)

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OBJECTION OF COLONY AMC OPCO, LLC TO DEBTOR'S DISCLOSURE STATEMENT AND RESERVATION OF RIGHTS [ECF NO. 48]

Colony AMC OPCO, LLC, as Special Servicer, for Wells Fargo Bank, National Association, as Trustee for the Registered Holders of Colony Multifamily Mortgage Trust 2014-1, Commercial Mortgage Pass-Through Certificates, Series 2014-1 ("Lender"), by its undersigned counsel, hereby objects to the Disclosure Statement and proposed chapter 11 Plan of Cayot Realty, Inc. dated April 6, 2017 (the "Disclosure Statement" and "Plan"), as follows:[2]

[1] On consent, the time for Lender to object to the Disclosure Statement was extended through May 22, 2017.
[2] The Debtor filed the proposed Disclosure Statement and Plan on April 7, 2017 (ECF No. 48). No notice of hearing or motion for approval of the Disclosure Statement has been filed. At a hearing held on April 28, 2017, counsel for the Debtor indicated on the record that the Debtor intended to amend or supplement the Disclosure Statement and Plan. No amended Disclosure Statement or Plan has been provided to Lender or filed with the Court. Lender reserves the right to amend or supplement its Objection in response to any supplemental filings by the Debtor.

Preliminary Statement

1. This voluntary chapter 11 case has been pending since May 16, 2016. A full year has gone by in chapter 11.

2. The Debtor has had the benefit of a full year in chapter 11, but still has not refinanced its non-residential real property located at 333 Route 202, Pomona, New York 10970 (the "Real Property") and other assets (collectively, the "Property"). What was included with the proposed Plan and Disclosure Statement is not a commitment for such financing.

3. This case is, by and large, a two-party dispute between the Debtor and Lender. Debtor owes Lender approximately $2.1 Million, and the Debtor's other debts combined are merely $27,000.00 (approximate). The Debtor valued all of its Property in its voluntary Chapter 11 petition as aggregating $3,024,785.00. *See* Petition, ECF No. 1, at p.7.

4. Creditors who have waited while the past year has gone by in chapter 11 should not have to wait any longer in a case where the Debtor claims that there is a sufficient asset base from which to pay all claims in full should those assets be sold.

Discussion

5. The Disclosure Statement and Plan, as presented, contain fundamental flaws that preclude approval of the Disclosure Statement for distribution to creditors.

6. The foundation of the Disclosure Statement and Plan is a refinancing of the Debtor's debt. But it is a shaky foundation, built upon unrealistic expectations. The Plan, in sum, calls for the transfer of the Debtors' Property to a new entity, backed by a loan from an entity called Northwind Financial Corporation (or one of its affiliates, "Northwind") in the amount of $2.6 Million. *See* Disclosure Statement at p.8. A "Loan Commitment" letter, dated

February 20, 2017 (the "Commitment Letter"), is annexed to the Disclosure Statement as Exhibit B.[3]

7. The Commitment Letter, however, is not a firm commitment. First, on its face it appears invalid. It is unsigned. Second, it expired by its terms as of February 27, 2017. Third, whether the financing discussed in the Commitment Letter will be provided, and the amount of financing that ultimately might be provided, remain subject to further diligence.

8. Beyond these basic problems, a review of the terms set out by Northwind in the Commitment Letter, alongside some of the Debtor's admissions in its Schedules, demonstrates that it is not likely that the financing contemplated by Northwind will come to pass. This is so, at least in part, because the Commitment Letter contemplates a loan of up to $2.6 Million, but by its terms requires a maximum loan to value ratio of 75%. The Debtor valued all of its Property as aggregating $3,024,785.00. *See* Petition, ECF No. 1, at p.7. With that asset base, $2.6 Million loan would have a Loan to Value of **85%** which is inconsistent with the terms of the Commitment Letter. The Disclosure Statement does not describe what would happen if a lesser amount were loaned. The Commitment Letter should be recognized as being what it is – something far less than a firm commitment to fund the amounts necessary to implement the Plan.

9. The Plan makes no contingency for the failure of this financing,[4] and places no outer boundary upon the time in which the Debtor can continue to seek sources of refinancing.[5] After a year in chapter 11, creditors deserve better.

[3] Debtor's counsel has informed Lender's counsel that there supposedly is a revised commitment letter. However, no such document has been provided to Lender despite requests therefor.
[4] Debtor's counsel has advised Lender's counsel that there is a draft of an amended Plan that supposedly provides for the possible "reinstatement" and sale scenarios. However, Debtor has not produced any such amended Plan as of the date hereof.
[5] The Disclosure Statement contemplates that the refinancing transaction will close within thirty (30) days of confirmation, but makes no contingency for what will happen to the extent that the closing fails. *See* D. Stmt., p. 7.

10. If a refinancing option is pursued, Lender submits that the Plan and Disclosure Statement should permit a short window of time within which the Debtor can pursue this approach. If a refinancing has not closed within thirty (30) days of confirmation, Lender respectfully submits that Debtor's Plan should provide for an immediate auction sale of the Property, with bidding procedures in a form reasonably acceptable to Lender and subject to the statutory and agreed-upon right for Lender to credit bid its claims as set forth in the Final Stipulation and Order Approving Use of Cash Collateral [ECF No. 24]. It is only by putting in place a sunset provision addressing potential refinancing, followed by a sale process if necessary, that creditors can be protected (and that the Plan can be feasible).

11. In addition, although the Plan is a "no one can vote" proposition, the reality of the matter is that Lender's rights are impaired and Lender is entitled to vote, as are unsecured creditors (who are not receiving interest on their claims, in accordance with state law).

12. Beyond these truly fundamental, flawed-foundation problems with the Plan and Disclosure Statement, as filed the Disclosure Statement also falls short of providing sufficient information in a number of ways. For example:

> <u>No Disclosure of Post-Confirmation Management/Insider Compensation.</u> The Plan and Disclosure Statement contemplate the Debtor's sole shareholder retaining its interests; that the Property will be transferred to a newly formed entity in consideration for the $2.6 Million loan from new lender, with the loan proceeds used to pay the estate's creditors in full. Yet, as proposed, there is no certainty as to payment in full because the Commitment Letter remains subject to diligence and contingencies, including the amount of funds ultimately to be provided. With that in mind, post-confirmation oversight, activities, decision-making and payment of post-confirmation expenses remain relevant. Yet, there is no disclosure regarding management, which is likely to consist of an insider, or what their compensation will be. A disclosure statement must provide adequate information concerning future management of the debtor, including the amount of compensation to be paid to any insiders, directors, and/or officers of the debtor;

> <u>Inadequate Liquidation Analysis.</u> The Debtor's liquidation analysis is little more than a general statement that there will be additional costs attendant with liquidation, and that additional costs are not desirable, but there is no real indication that creditors would risk not being paid in full under the facts and circumstances of this case. Indeed, the Debtor's own asset valuation – and the amount required under the Commitment Letter in order to reach the requested funding threshold without violating Northwind's loan-to-value ratio – indicates that there are more than sufficient assets available from which to pay all claims in full upon liquidation. The Debtor has not demonstrated that the proposed Plan is "better" for creditors than liquidation.

13. As is set forth in more detail below, the proposed Plan is fatally flawed. Beyond the fundamental problems with the Plan that render it patently unconfirmable, there are a number of inadequacies in disclosure that should be addressed through revisions before a Disclosure Statement can be approved. The Debtor's exclusive periods within which to promulgate a plan and solicit acceptances thereto have long since expired, but Lender has not at this point proceeded on the basis of a competing plan. Lender is prepared to continue to try and work with the Debtor to put forth an acceptable Plan, but reserves its right to file its own Plan if this Debtor is unwilling or unable to promulgate and put forward a confirmable and feasible plan.

ARGUMENT

POINT I

THE DISCLOSURE STATEMENT, AS FILED, SHOULD NOT BE APPROVED FOR DISTRIBUTION TO CREDITORS

14. Section 1125(a) of the Bankruptcy Code requires that a disclosure statement contain "adequate information, " which is defined as "information of a kind, and in sufficient detail, as far as is reasonably practicable in light of the nature and history of the debtor and the condition of the debtor's books and records, that would enable a hypothetical reasonable investor typical of holders of claims or interest of the relevant class to make an informed judgment about

the plan . . ." 11 U.S.C. §1125(a)(1). *See In re Prudential Energy Co.*, 58 B.R. 857, 867 (Bankr. S.D.N.Y. 1986) (providing that adequate information to interested parties "is at 'the heart' of the reorganization process" because it enables holders of claims and interests "to make an informed judgment about the plan."). "[A] disclosure statement concerning a plan may not be distributed for consideration unless the supervising bankruptcy judge is satisfied that the statement contains 'adequate information.'" *Kirk v. Texaco Inc.*, 82 B.R. 678, 681 (S.D.N.Y. 1988).

15. While the determination of adequate information is case-specific, *see, e.g., In re Copy Crafters Quickprint, Inc.*, 92 B.R. 973, 979 (Bankr. N.D.N.Y. 1988), courts in the Second Circuit have held that certain information is mandatory. *In re Weiss-Wolf, Inc.*, 59 B.R. 653, 656 (Bankr. S.D.N.Y. 1986) ("it is not enough for a debtor to say, in effect, trust me, this is a good deal for creditors").

16. Courts in this Circuit have also relied on the 19-point list enumerated in *In re Scioto Valley Mortgage Co.*, 88 B.R. 168, 170-71 (Bankr. S.D. Ohio 1988). The 19-point list of materials required to be fully disclosed in a disclosure statement is as follows:

1. The circumstances that gave rise to the filing of the bankruptcy petition;
2. A complete description of the available assets and their value;
3. The anticipated future of the debtor;
4. The source of the information provided in the disclosure statement;
5. A disclaimer, which typically indicates that no statements or information concerning the debtor or its assets or securities are authorized, other than those set forth in the disclosure statement;
6. The condition and performance of the debtor while in Chapter 11;
7. Information regarding claims against the estate;
8. A liquidation analysis setting forth the estimated return that creditors would receive under Chapter 7;
9. The accounting and valuation methods used to produce the financial information in the disclosure statement;

10. Information regarding future management, including compensation to be paid to any insiders, directors, and/or officers of the debtor;
11. A summary of the plan of reorganization;
12. An estimate of all administrative expenses;
13. The collectability of any accounts receivable;
14. Financial information, valuations or *pro forma* projections relevant to creditors' determinations of whether to accept or reject the plan;
15. Information relevant to risks being taken by creditors and interest holders;
16. Actual or projected value that can be obtained from avoidable transfers;
17. Existence, likelihood and possible success of non-bankruptcy litigation;
18. The tax consequences of the plan; and
19. The relationship of the debtor with affiliates.

Scioto Valley Mortgage Co., 88 B.R.at 170-71.

A. The Disclosure Statement Should not be Approved for Distribution Because It Describes a Plan that is "Patently Unconfirmable."

17. For each of three separate and distinct reasons, the Plan is patently unconfirmable and should not be distributed to creditors. First, the Plan contemplates financing that has not been put in place. Second, the Plan does not contemplate alternatives in the event that the as-yet-not-obtained financing is not put in place in a reasonable time period. Third, the Plan fails to give creditors the right to vote, when claims are impaired. For each of these reasons, the relief sought through the Motion should be denied.

i. The Financing that Forms the Backbone of the Plan, is not in Place.

18. The Plan calls for the transfer of the Debtors' Property to a new entity and a new loan from Northwind in the amount of $2.6 Million, which loan proceeds will be used to pay creditors in full. *See* Disclosure Statement at p.8. Without this financing, the Plan falls apart.

19. The Commitment Letter, on its face, has expired. There is no commitment to refinance on the record present. Absent financing, the Plan is not feasible.

20. Beyond the fact that the Commitment Letter has expired, reference to the Debtor's schedules indicates that the financing contemplated by the Commitment Letter could not come to pass in that the maximum allowable loan to value ratio is 75%. *Id.*, Ex. B at p. 5. Given that the Debtor has valued its Property at $3,024,785.00, *see* Petition, ECF No. 1, at p.7, the loan to value ratio on a $2.6 Million loan is 85%. Thus, even had the "commitment" not expired, the financing contemplated by Northwind could not be obtained in an amount sufficient to fund the distributions on which the Plan is built. By its terms, the Plan and Commitment Letter demonstrate that the Plan is speculative at best, and as a result, are not feasible.[6]

21. Without certainty regarding the actual ability of the Debtor to obtain the financing necessary to confirm the Plan, the Disclosure Statement should not be approved for distribution to creditors because to do so would be a waste of judicial resources and futile. "If the plan is patently unconfirmable on its face, the application to approve the disclosure statement must be denied, as solicitation of the vote would be futile." *In re Quigley Co., Inc.*, 377 B.R. 110, 115 (Bankr. S.D.N.Y. 2007) (citing cases); *In re 266 Washington Associates*, 141 B.R. 275, 288 (Bankr. E.D.N.Y. 1992) (denying approval of a disclosure statement that describes a plan which is fatally flawed and thus incapable of confirmation). *Accord, In re Flour City Bagels, LLC*, 16-20213 (PRW), 2017 WL 456421 at *2 (Bankr. W.D.N.Y. February 2, 2017) (finding it "appropriate to deal with potential plan-killer issues in connection with the hearing on adequacy of the disclosure statements, to avoid the costs associated with circulating disclosure statements and soliciting ballots for potentially unconfirmable Chapter 11 plans.").

[6] In a case where there is more than sufficient value to pay creditors in full should the Property be sold.

ii. <u>The Plan Could be a Never-Ending Proposition, and it Should not be.</u>

22. The Plan's shortcomings as to feasibility make it all the more clear that, as a matter of plan structure, what has been proposed should not be approved for distribution to creditors.

23. The Plan provides no alternatives. Within what timeframe can a refinancing be sought? The Disclosure Statement suggests that the refinancing with Northwind will take place within thirty (30) days of confirmation, but what happens if that closing fails? An open-ended proposition is not feasible, yet, under the Plan, there is no end date for the possibility of refinancing to take place. Although ample time already has gone by, to the extent that a financing option is contemplated an additional short period of time could be considered. But, it should be a short period of time (30 days).

24. The Plan also does not provide for "what happens next" in the event that the Debtor cannot obtain the proposed refinancing (within a thirty (30) day window from confirmation). To the extent that the refinancing cannot be accomplished, it is respectfully submitted that a sale process must be part of the Plan. There needs to be an endgame. The Plan, as drafted, is an open door with no horizon in the event that the contemplating refinancing fails.

iii. <u>Creditors, who Have Waited for More Than a Year, are Not Given the Right to Vote</u>

25. Finally, another critical shortcoming of the Plan, sufficient to render the Plan patently unconfirmable, arises out of its "no one can vote" approach.

26. Pursuant to 11 U.S.C. § 1124, a class of claims is "impaired," and thus entitled to vote on confirmation, unless the proposed plan "leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interest."

See 11 U.S.C. § 1124(1). *Any* alteration of rights – even something that could be viewed by some as an *enhancement* of a creditor's position in one way or another – constitutes an impairment. *See, e.g., In re GSC, Inc.*, 453 B.R. 132, 177 (Bankr. S.D.N.Y. 2011); *Downtown Athletic Club of New York v. CASPI Dev. Corp. (In re Downtown Athletic Club of New York, Inc.)*, Case No. 98 B 41419 JLG, 1998 WL 898226, at *6 (Bankr. S.D.N.Y. Dec. 21, 1998).

27. Here, the Plan contemplates that the debt to Lender will be refinanced and paid out in full. Even that, however, renders Lender's claims "impaired" in that payment in full contemplates payment before maturity, which would be an alteration of Lender's rights. Indeed, as is discussed in more detail below, "reinstatement" of the underlying loan is not possible here (either as a practical matter or as a matter of law). Without reinstatement and all rights of Lender being left unaltered, there is, by definition, impairment (unless Debtor wishes to surrender the Property to Lender, which Debtor has not indicated it is willing to do). *See* 11 U.S.C. §§ 1124 (1); (2)(A), (B), (E); *see also In re GSC, Inc.*, 453 B.R. at 177 (even improvement in position is impairment); *In re Downtown Athletic Club of New York, Inc.*, 1998 WL 898226, at *6 (same). Precisely what is meant by "paid in full" is also an open item – default rate interest continues to accrue, and must be paid. The Disclosure Statement does not address the rate of interest to be used in determining what constitutes "paid in full" under the Plan.

28. Moreover, unsecured creditors are likely entitled to interest on their claims pursuant to state law. The Disclosure Statement does not address this point, and the Plan makes no provision for the payment of interest to general unsecured creditors. As a result, unsecured creditors, too, are "impaired" and entitled to vote.

29. Last, because the open-ended refinancing approach is neither realistic nor feasible, it is clear that a timeline and alternative approach must be put in place. Alternatives would render Lender and unsecured creditors impaired. Because of the fact that the refinancing being proposed is not a "sure thing," alternatives have to be included in the Plan, and with alternatives comes the need to have creditors vote owing to the fact that in at least one of if not all of the alternatives on which the Plan might ultimately be implemented, creditors such as Lender and all unsecured creditors, will be impaired. A "wait and see" approach as to which alternative works out, simply won't work, in that by then, it will be too late.

30. Because the Plan's "no vote" approach is fatally flawed, Lender respectfully submits that the Disclosure Statement and Plan should not be distributed to creditors.

B. Additional Issues With Respect to Adequacy of the Disclosure Statement

31. The Debtor has also omitted other fundamentally required points of information in the Disclosure Statement, failing to provide appropriate disclosure per the requirements set forth in *Scioto Valley*. For example:

a. No information has been provided regarding post-confirmation oversight, activities, decision-making or payment of post-confirmation administrative expenses. There is no disclosure of the management of the Debtor, which appears to be an insider or what their compensation will be. A disclosure statement must provide adequate information concerning future management of the debtor, including the amount of compensation to be paid to any insiders, directors, and/or officers of the debtor. *Scioto Valley Mortgage Co.*, 88 B.R. at 170-71; and

b. The Debtor's liquidation analysis is nothing more than a generalized statement that there will be additional costs attendant with liquidation, but there is no real indication that creditors would risk not being paid in full under the facts and circumstances of this case. The Debtor has provided no actual financial comparison of treatment and risks to creditors from the Plan versus a Chapter 7 liquidation. A debtor's disclosure statement will be found inadequate if it does not provide sufficient information regarding its liquidation analysis,

> which certainly cannot be tested if the analysis is not provided at all. *See In re Crowthers McCall*, 120 B.R. 279 at 300-01 (finding debtor's disclosure statement inadequate).

POINT II

LIMITATIONS ON WHAT CAN BE DONE THROUGH AN AMENDED PLAN

32. To the extent that the Debtor intends to revise or amend the Plan and Disclosure Statement to address the points identified above, there are limitations on the Debtor's alternatives that should be considered in advance, recognizing that creditors have been waiting for more than a year while the Debtor operated under the protection of chapter 11.

33. At a hearing held on April 28, 2017, Debtor's counsel indicated the Debtor's intent to amend the Plan and Disclosure Statement to provide for the reinstatement of Lender's loan. This is likely an effort by Debtor to prevent Lender from voting on confirmation. Lender respectfully submits that there are a number of fundamental flaws with this potential approach.

34. First, the obvious – this approach requires the Debtor to find subordinate financing in a case where it has been unable to find any source of financing during a full year in chapter 11 (plus additional months in the prepetition period). This is not a realistic expectation.

35. Second, even to the extent that financing could be found on a subordinate basis, proceeding on that basis is not possible because doing so would violate the terms of Debtor's loan agreements with Lender. Paragraph 4 of the Mortgage executed and delivered to Lender from Debtor states, in pertinent part, as follows:

> Without Lender's prior written permission, Borrower shall not allow any lien inferior to this Instrument to be perfected against the Property. . . Borrower shall not allow any lien (other than the liens granted to Lender by this Deed of Trust) to be perfected against the Property and shall not otherwise execute any mortgage, security

> agreement, assignment of leases and rents or other agreement granting a lien (other than the liens granted to Lender by this Deed of Trust) with respect to the Property.

See Mortgage, annexed to Lender's Proof of Claim No. 4 at p. 13, ¶4.[7]

36. Thus, if Debtor seeks to reinstate its loan and debt to Lender, the only way in which Debtor could do so – by obtaining a subordinate loan – would put the newly-reinstated loan in default. Curing a default by taking action that creates a new default is not a recipe for a feasible exit from chapter 11. Indeed, the fact that reinstatement on the terms discussed would, in and of itself, create a new default under the "reinstated" agreement, demonstrates that reinstatement is not permissible. *See In re Young Broadcasting, Inc*., 430 B.R. 99, 115-118 (Bankr. S.D.N.Y. 2010) (denying reinstatement where proposed manner of doing so would violate change in control restrictions).

37. Debtor cannot modify its way around this problem. Although section 1124(2) of the Bankruptcy Code does permit a debtor to cure defaults and reinstate pre-default maturity, doing so comes at a price: the plan cannot alter any legal, equitable or contractual rights of Lender. *See* 11 U.S.C. §1124(2)(E); *In re Young Broadcasting Inc.*, 430 B.R. 99, 115 and N. 20 (Bankr. S.D.N.Y. 2010) (denying confirmation, finding that reinstatement of a loan as proposed by a Committee's plan was precluded, because the proposed structure would violate a section of the Debtor's Credit Agreement). Here, Lender will not consent to Debtor permitting a junior lien on the Property.[8]

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[7] For the convenience of the Court, a copy of Lender' s proof of claim and exhibits thereto is attached hereto as "Exhibit A."

[8] Even assuming if Debtor could further encumber its Property to reinstate Lender's loan over Lender's objection, Debtor does not appear to have sufficient and consistent net revenue to support debt service for two loans. Debtor's monthly operating reports show significant inconsistencies on a month to month basis with respect to net revenue. For example, the Debtor reported a net loss of $1,000.89 for April 2017. April Operating Report, ECF No. 54, at p.4. While the March Operating Report showed positive monthly revenue, the February 2017 Operating Report

38. Lender respectfully submits that the only viable alternative in the event the Debtor cannot refinance the Property *in toto*, is to conduct an auction sale of the Debtor's Property, subject to agreed-upon bid procedures and Lender's right to credit bid, which was previously agreed to by the parties and approved by this Court in the context of the Final Consent Order Authorizing Use of Cash Collateral entered on August 29, 2016. ECF No. 24, at ¶23. Lender respectfully reserves all of its rights to object to any amended or supplemented disclosure statement and to object to confirmation of this or any other plan of reorganization.

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disclosed a net loss of $5,185.47. February Operating Report, ECF No. 43 at p.4. Also, the guarantor under the loan with Lender has passed away, creating another issue for the Debtor and any attempt at reinstatement. To the extent that Mr. Cayot – the Debtor's principal – intends to become a substitute guarantor, this will not suffice in that Mr. Cayot's financial wherewithal is directly tied to the Debtor's asset value. A guaranty from Mr. Cayot would not be a credit enhancement, as was the prior guaranty.

CONCLUSION

Debtor has had ample time in chapter 11 to refinance its Property. Lender respectfully submits that Creditors who could be paid in full from a sale of the Property have waited long enough. The Disclosure Statement and Plan, fall short of demonstrating that the Debtor has or can obtain refinancing for the Property, and fail to put in place deadlines and alternatives that should reasonably have been anticipated and included in the proposed Plan. The Plan and Disclosure Statement should not be approved for distribution to creditors until these items are addressed. For each of the foregoing reasons, Lender respectfully requests that the Court deny approval of the Disclosure Statement and grant such other and further relief as this Court deems necessary and proper.

Dated: Uniondale, New York
May 22, 2017

WESTERMAN BALL EDERER
MILLER ZUCKER & SHARFSTEIN, LLP

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