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ATTORNEYS FOR FIRST
WESTERN SBLC, INC.

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

IN RE: §
§
VIGNAHARA, LLC, § CASE NO. 16-32261-11
§ (Chapter 11)
DEBTOR §

**FIRST WESTERN SBLC, INC.’S OBJECTION
TO DEBTOR’S DISCLOSURE STATEMENT**

TO THE HONORABLE BARBARA J. HOUSER, CHIEF UNITED STATES BANKRUPTCY
JUDGE:

First Western SBLC, Inc. (“First Western”), a secured creditor in the above-referenced chapter 11 bankruptcy case, files this objection to the *Debtor’s Disclosure Statement* (Dkt. No. 67, the “Disclosure Statement”) filed by Vignahara, LLC (the “Debtor”) as follows. For ease of reference, all citations in this Objection to articles, page numbers, and exhibits refer to the particular article, page number, or exhibit of the Disclosure Statement unless otherwise stated.

A. Relevant legal standards for approval of a disclosure statement.

Adequate Information

1. The Bankruptcy Code prohibits a plan proponent from soliciting acceptance or rejection of a chapter 11 plan until the court approves a written disclosure statement, after notice and hearing, as containing “adequate information.” 11 U.S.C. § 1125(b). “Adequate information” means “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, including a discussion of the potential material Federal tax consequences of the plan to the debtor, any successor to the debtor, and a hypothetical investor typical of the holders of claims or interests in the case, that would enable such a hypothetical investor of the relevant class to make an informed judgment about the plan, but adequate information need not include such information about any other possible or proposed plan and in determining whether a disclosure statement provides adequate information, the court shall consider the complexity of the case, the benefit of additional information to creditors and other parties in interest, and the cost of providing additional information[.]” 11 U.S.C. § 1125(a). The question of whether a disclosure statement contains “adequate information” depends upon the facts and circumstances of each case. *Oneida Motor Freight, Inc. v. United Jersey Bank*, 848 F.2d 414, 417 (3rd Cir.), *cert. denied*, 488 U.S. 967 (1988).

Unconfirmable Plan

2. Regardless of whether a disclosure statement contains adequate information sufficient to satisfy section 1125, approval should be denied if it describes a chapter 11 plan that cannot be confirmed. *In re American Capital Equip., LLC*, 688 F.3d 145, 154 (3rd Cir. 2012); *In re Harenberg*, 491 B.R. 706, 717 (Bankr. D. Md. 2013); *In re 18 RVC, LLC*, 485 B.R. 492, 495 (Bankr. E.D.N.Y. 2012); *In re Quigley Co.*, 377 B.R. 110, 115-16 (Bankr. S.D.N.Y. 2007); *In re U.S. Brass Corp.*, 194 B.R. 420, 422 (Bankr. E.D. Tex. 1996); *In re Gingerella*, 155 B.R. 3, 4 (Bankr. D.R.I. 1993); *In re 266 Washington Assocs.*, 141 B.R. 275, 288 (Bankr. E.D.N.Y.), *aff’d sub. nom on other grounds, In re Washington Assocs.*, 147 B.R. 827 (E.D.N.Y. 1992).

3. There is no point in approving a disclosure statement to permit voting on a defective plan that cannot be confirmed. *American Capital*, 688 F.3d at 154; *Harenberg*, 491 B.R. at 717-18. Approving a disclosure statement for an unconfirmable plan is a waste of the

time of the Court and the parties. *In re Valrico Square Ltd. Partnership*, 113 B.R. 794, 796 (Bankr.S.D. Fla.1990); *In re Kehn Ranch, Inc.*, 41 B.R. 832, 832-33 (Bankr. D.S.D. 1984).

B. Approval of the Disclosure Statement should be denied because the proposed plan is unconfirmable.

4. *Art. II.11, p. 16.* The Debtor's plan includes a blanket post-confirmation injunction that would prohibit First Western from enforcing the personal guaranties given by Denishkumar Patel and Mehul Patel. [Plan §§ 1.53 and 7.7] Neither of those two individuals is mentioned anywhere in the Disclosure Statement or plan except for being included in the plan's definition of "Guarantors." They are not members or managers of the Debtor [Art. II.1, p.4], will have no managerial role in the business after confirmation [Art. II.11, p. 16], and are not even employees of the Debtor [Art. II.1, p. 4; Dkt. No. 6]. Consequently, the proposed post-confirmation injunction, at least insofar as it protects those two individuals,¹ is not authorized by the Bankruptcy Code or applicable law and would violate section 1129(a)(3) of the Bankruptcy Code, making the plan unconfirmable.

5. This Court, in *In re Seatco, Inc.*, 257 B.R. 469, 477 (Bankr. N.D. Tex.2001), set the standard for the propriety of a temporary injunction looking to the two-factor test from *Feld v. Zale Corp. (In re Zale Corp.)*, 62 F.3d 746, 761 (5th Cir. 1995) and the traditional injunction factors, which, in order for an injunction to be proper, must all be met by the Debtor's proposal. *Seatco*, 257 B.R. at 476-77. The two-factor *Zale* requires that (1) the debtor and the non-debtor to benefit from the injunction "enjoy such an identity of interest that the suit against the non-debtor is essentially a suit against the debtor," and (2) that "the third-party action will have an adverse impact on the debtor's ability to accomplish reorganization." *Id.* A subsequent case in

¹ The objection stated in this paragraph is made only with respect to approval of the Disclosure Statement. First Western does not consent to the proposed injunction with respect to any of the "Guarantors" as defined in the plan and reserves all objections to confirmation of the plan based upon the proposed injunction.

this District approving a *Seatco* like injunction is the *In re Bernhard Steiner Pianos, USA, Inc.*, 292 B.R. 109, 116 (Bankr. N. D. Tex. 2002) (Hale, J.). In both *Seatco* and *Bernhard Steiner*, the non-debtor guarantor was essentially one and the same as the debtor and the success of the debtor was contingent upon the continued participation and efforts of the non-debtor guarantor. *Seatco*, 257 B.R. at 476; *Bernhard Steiner*, 292 B.R. at 117. By contrast, in *In re Couture Hotel Corp.*, 536 B.R. 712 (Bankr. N.D. Tex. 2015), this Court held that even where the non-debtor guarantors held managerial positions, managed accounting functions that were important to the debtor's operations, and were stockholders of the debtor, those connections to the debtor were not sufficient to meet the shared identify of interest for the first factor of the *Zale* test. *Couture Hotel*, 536 at 751-52. Here, Denishkumar Patel and Mehul Patel clearly do not meet the identify of interest factor from *Zale* because they are not equity owners, have no managerial roles, and are not even employees of the Debtor. Accordingly, the temporary injunction as to Denishkumar Patel and Mehul Patel renders the proposed plan unconfirmable on its face.

C. The Disclosure Statement should be denied because it fails to provide adequate information due to significant false, misleading, and incomplete information.

6. *Art. II.1, p. 4.* The Disclosure Statement fails to disclose a prepetition ownership transfer in the Debtor in violation of First Western's loan documents. This section of the Disclosure Statement says Jagdishbhai Patel and Binal Patel are the sole members of the Debtor. However, at the time First Western made the mortgage loan to the Debtor, Pooja Patel was also a member, and First Western's loan documents prohibit any transfer of equity interests in the Debtor without First Western's prior consent, which was never requested or obtained.² The

² Deed of Trust, Security Agreement and Assignment of Rents at ¶ 1.20. That document is attached as part of the proof of claim that First Western filed in this case (Claim No. 4-1).

Debtor should be required to disclose the date and terms of the transaction(s) by which Pooja Patel transferred her membership interest in the Debtor to Jagdishbhai Patel and/or Binal Patel.

7. *Art. II.2, p. 5.* The statement that “For the two months the Binals operated...” is wrong and should refer to “the Patels” instead of “the Binals.”

8. *Art. II.3.B, p. 6.* The Disclosure Statement fails to disclose that First Western’s payment of the Debtor’s delinquent 2015 property taxes payment avoided penalties that would have been assessed on July 1, 2016 and reduced the interest accrual from 1% per month to 6.25% per year.

9. *Art. II.3.B, p. 6.* The Debtor erroneously states that Claim No. 1 filed by Harris County and Houston Sports Authority asserts \$15,984.49 as an unsecured claim. In fact, Harris County and Houston Sports Authority assert that amount as a *secured* claim in Claim No. 1. [Art. II.9, pp. 13-14]

10. *Art. II.3.C, p. 7.* The Disclosure Statement falsely implies that the reason the Debtor had insufficient funds to pay for taxes and make the repairs required by Red Roof Inn was that First Western impermissibly stopped funding the loan. In fact, the only remaining loan funds totaled \$47,250.15 [Art. II.3.A, p. 5], which was far less than the property taxes alone of \$99,590 [Art. II.3.B, p. 6], and FW refused to advance any of those funds because the Debtor did not comply with the terms required to release those funds.

11. *Art. II.4, p. 7.* The Disclosure Statement falsely states that the Debtor was beginning to make a profit before bankruptcy. In fact, the Debtor lost money in 2013 [Art. II.2, p. 5], 2014 [*Id.*], 2015 when the unpaid 2015 property taxes are considered [*Id.*; Art. II.3.B, p. 6; Art. II.4, p. 8.], and the first six months of 2016 when unpaid 2016 property taxes and unpaid prepetition wages are considered [*Id.*; Art. II.9.Class 3, p. 14; Dkt. No. 6, ¶ 11].

12. *Art. II.5, p. 8.* The Debtor falsely states “there are no more Schedule E priority wages owing.” The Court’s order authorizing payment of prepetition wages expressly excluded payment of prepetition wages to Binal Patel, Angie Patel, Pooja Patel, Tapan Patel, and Gunvantiben Patel (Dkt. No. 24, ¶ 2.) The Debtor’s Amended Bankruptcy Schedule E (Dkt. No. 39) shows prepetition wages owed to Binal Patel (\$800), Angie Patel (\$400), Pooja Patel (\$400), and Gunvantiben Patel (\$400). In another section of the Disclosure Statement, the Debtor states that it still owes approximately \$1,600 in prepetition priority wage claims but fails to explain the apparent discrepancy between that amount and the amounts listed in its Amended Bankruptcy Schedule E. [Art. II.9, Class 6, p. 14] That section is inconsistent with yet another section of the Disclosure Statement, where the Debtor states that Binal Patel will release her claims against the Debtor. [Art. II.10, p. 16]

13. *Art. II.6, p. 9.* The statement that “the Monthly Operating Report for September, 2016 shows a positive cash flow of \$20,865.89 is misleading because it fails to explain that the Debtor paid only \$6,000.00 toward its mortgage for that month (Dkt. 66, p. 2), which was less than half the regular monthly mortgage payment [Art. II.7, p. 12].

14. *Art. II.6, p. 9.* The Debtor makes a misleading representation that its monthly operating expenses have “decreas[ed] monthly from \$122,255 in June to \$85,041 in July, \$83,827 in August to \$61,685 in September.” Although the Debtor refers to its October monthly operating report (Dkt. No. 66) in the very next sentence, it conveniently leaves out the fact that its monthly operating expenses for October soared to \$111,277.63. (Dkt. No. 66, p. 2) Monthly operating expenses climbed even higher in November to \$136,877.65, the highest of any month during the whole case. (Dkt. No. 83, p. 2)

15. *Art. II.6, p. 10.* The Debtor falsely states that it paid \$15,279 in adequate protection payments to First Western during October 2016. The Debtor did not pay anything to First Western during October, and its monthly operating report for October (Dkt. No. 66, pp. 2 and 8) does not show any payment to First Western. That false statement makes all of the ensuing calculations in that paragraph wrong.

16. *Art. II.7, p. 10.* The Debtor falsely states “The Debtor has shown that it can fund its operating costs and debt service with the current revenues” In the immediately preceding paragraph, the Debtor states that it had net cash losses in June, July, and August 2016 and acknowledges that it “cannot fund its obligations with a 35-40% occupancy rate as it has been experiencing [Art. II.6, p. 10].

17. *Art. II.7, pp. 10-12.* The lynchpin of the Debtor’s proposed plan is to reinstate the Red Roof Inn franchise. From the inception of this case, the Debtor has acknowledged that it must get a national motel franchise to survive. In the Disclosure Statement, the Debtor reiterates that regaining the Red Roof Inn franchise is “the key to restoring the business to sustained profitability.” [Art. II.7, p. 10] The Disclosure statement is incomplete and misleading on several points concerning the Red Roof Inn franchise:

a. According to the Disclosure Statement, the Debtor does not have a commitment from Red Roof Inn to reinstate the franchise. [Art. II.7, p. 11] The Debtor fails to explain whether, when, and the terms upon which Red Roof Inn will actually reinstate the franchise agreement. The Debtor also fails disclose the steps, terms, timing, and expense needed to transform Red Roof Inn’s tentative agreement into a binding contract. This Court recently entered an order (Dkt. No. 77) authorizing the Debtor to

enter into a franchise agreement with Red Roof Inn, but the Disclosure Statement has not been supplemented to disclose the status of that proposed franchise agreement.

b. A key term of Red Roof Inn's tentative agreement is to complete the repairs and improvements described in the Property Improvement Plan attached as Exhibit 2 to the Disclosure Statement. [Art. II.7, pp. 10-11] However, the Property Improvement Plan attached as Exhibit 2 is not signed by either party.

c. The Disclosure Statement falsely states that the proposal from 4th Dimension Builders attached as Exhibit 3 to the Disclosure Statement shows that all of the items required by the Property Improvement Plan can be completed for \$350,000. The proposal does not cover all of the items required by the Property Improvement Plan such as swimming pool work and bed linens and does not include any costs for shipping, storage, or taxes. Nothing in the proposal provides assurance that the furniture and other materials will meet the Red Roof Inn standards required by the Property Improvement Plan. The prices stated in the proposal do not support the Debtor's allocation of \$150,000 for repairs and improvements and \$200,000 for new furniture. [Art. II.7, pp. 10-11] Another part of the Disclosure Statement acknowledges that the Debtor has a history of underestimating the costs to make the renovations required to comply with Red Roof Inn's standards. [Art. II.3.C, p. 7]

d. Another key term of Red Roof Inn's tentative agreement is that the Debtor install \$200,000 worth of new guest room furniture. [Art. II.7, pp. 10-11] The Disclosure Statement says that Binal Patel and Jagdisbhai Patel will pay for the new furniture with a personal loan that the Debtor will reimburse through substantially higher salary payments to them. [Art. II.7, p. 12] However, the Disclosure Statement fails to

disclose who will own that new furniture, *i.e.*, the Debtor or the Patels, and whether the lender will be granted a security interest in the new furniture. The Disclosure Statement also fails to provide any information that would enable creditors to evaluate the likelihood that the Patels actually will be able to obtain the personal loan, such as a binding loan commitment or even the identity of the prospective lender.

e. Still another key term of Red Roof Inn's tentative agreement is that Red Roof Inn must receive \$25,000 as a deposit to secure future franchise fee payments. [Art. II.7, p. 11] The Disclosure Statement says that Jagdisbhai Patel will pay that amount prior to confirmation, but no information is given about his financial ability to fund that amount.

18. *Art. II.7, p. 12.* The Disclosure Statement falsely states that "First Western has agreed that it will accept the normal principal and interest payment of \$15,729.37 monthly until one year after confirmation (at expected renovation completion) and then the Note will be re-amortized at the end of the following first quarter." First Western has engaged in discussions with the Debtor about possibly agreeing to delay re-amortization until a year after confirmation, but no agreement has been reached and First Western absolutely would not agree to delay re-amortization until the end of the "following first quarter" after one year following confirmation.

19. *Art. II.7, p. 13.* The Debtor's reference to projections attached as Exhibit "5" is misleading and confusing because the Profit and Loss Statement and Balance Sheet contained in Exhibit "5" are dated for the year 2014. [Ex. 5, pp. 55-56]

20. *Art. II.9, p. 15.* The Debtor fails to explain when it proposes to pay the administrative expenses of Regan Stewart, the Debtor's financial consultant, over and above his

retainer. Unlike the Debtors' bankruptcy counsel, there is no indication that Mr. Stewart will agree to be paid over time after confirmation.

21. *Art. II.11, p. 16.* The Debtor's description of the post-confirmation injunction is misleading, because it refers only to claims against Jagdishbhai and Binal Patel. In fact, the proposed injunction would apply to all "Guarantors" [Plan § 7.7], which is defined in the plan to mean Binal Patel, Jagdishbhai Patel, Pooja Patel, Gunvantiben Patel, Denishkumar Patel, and Mehul Patel [Plan § 1.53]. The Disclosure Statement says that Jagdishbhai Patel and Binal Patel are the sole members and managers of the Debtor [Art. II.1, p.4], Binal Patel alone will be responsible for day to day management after confirmation [Art. II.11, p. 16], and Pooja Patel and Gunvantiben Patel are employees [Art. II.1, p. 4]. Denishkumar Patel and Mehul Patel are not mentioned anywhere in the Disclosure Statement or Plan except for being included in the plan's definition of "Guarantors." The Disclosure Statement fails to explain why an injunction prohibiting creditors from pursuing claims against Binal Patel is necessary, let alone any of the other individuals.

22. *Ex. 5, pp. 55 and 58.* The Debtor's projections in Exhibit "5" are false and misleading for several reasons, including but not necessarily limited to the following:

a. The projections for **Commissions** of zero every year on pp. 55 and 58 are unreasonable in light of the facts that (i) online travel agencies like Expedia, Travelocity, Hotels.com, etc. charge significant commissions (over ten percent) for reservations made through them and (ii) the Debtor's proposed franchise agreement with Red Roof Inn will require the Debtor to reimburse Red Roof Inn for all of those commissions. (Franchise Agreement at § 4.5 [Dkt. No. 77, p. 9])

b. The projections for **Computer and Internet Expenses** of zero every year on pp. 55 and 58 are unreasonable in light of the facts that (i) the Debtor's 2015 federal income tax return showed actual computer and internet expenses totaling \$22,677 and (ii) the Debtor's proposed franchise agreement with Red Roof Inn and related documents will require the Debtor to pay unspecified computer support and maintenance fees. (Franchise Agreement at § 5.17 [Dkt. No. 77, p. 14]; Redistay Property Management Software Sublicense Agreement at § 2.2 [Dkt. No. 77, p. 62])

c. The projections for **Franchise Fee** of \$78,075 to \$89,282 on pp. 55 and 58 are unreasonable in light of the facts that (i) the Franchise Fee amounts in the projections are calculated as a flat 7.0% of projected "Room Revenue" for all five post-confirmation years, (ii) the Debtor's proposed franchise agreement with Red Roof Inn will require royalty, marketing and reservation fees totaling 7.5% of room revenue for years 1-3 and 8.5% of room revenues for years 4-5 (Franchise Agreement at §§ 4.2.1 and 4.3 and Special Stipulations Addendum [Dkt. No. 77 at pp. 8-9 and 53]), and (iii) the franchise agreement will require an additional fee of 4% of room revenue generated from guests who are part of a preferred member program. (Franchise Agreement at § 4.4 [Dkt. No. 77, p. 9])

d. The projections for **Insurance Expense** of \$18,000 per year on pp. 55 and 58 are grossly understated in light of the facts that (i) the Debtor's 2015 federal income tax return showed actual insurance expenses totaling \$96,259, (ii) the Disclosure Statement says the Debtor just recently paid \$25,000 for insurance [Art. II.6, p. 10], which was only half of the total annual premium (for casualty, liability, and flood

insurance only),³ (iii) the projections do not include anything for workers compensation insurance, and (iv) the Debtor's most recent monthly operating report [Dkt. No. 83, p. 9] shows workers' compensation insurance expenses of \$316.00 per month.

e. The projections for **Payroll Expenses** of \$243,187 to \$286,978 per year on pp. 55 and 58 are grossly understated in light of the facts that (i) the Debtor's 2015 federal income tax return showed actual payroll expenses and management fees totaling \$344,193, (ii) the Debtor's most recent monthly operating report [Dkt. No. 83] shows payroll expenses (including payroll taxes) totaling \$115,284.30 for August through November 2016, which would come out to more than \$345,000 for a full year, with a lower occupancy rate than the occupancy rates projected after confirmation [Art. II.6, p.10; Art. II.7, p. 13], and (iii) the Debtor's plan proposes to increase Binal and Jagdishbhai Patel's salaries by \$48,000 per year for the first five years after confirmation. [Art. II.7, p. 12]

f. The projections for **Payroll Taxes** of \$18,329 to \$21,523 per year are unreasonable in light of the facts that (i) the Payroll Tax amounts in the projections are calculated as a flat 7.5% of projected "Payroll Expenses" for all five post-confirmation years and (ii) the Debtor's most recent monthly operating report [Dkt. No. 83] shows that the Debtor's payroll taxes for August through November 2016 were 21.8 % of net payroll.

g. The projections for **Taxes** of \$85,380 per year for post-confirmation years 2 through 5 on pp. 55 and 58 are unreasonable in light of the fact that the value of the property will increase after the Debtor makes \$350,000 worth of repairs and

³ Attached hereto as Exhibit "A" is an email from the Debtor's attorney confirming that the total annual insurance premium is \$50,641.51.

improvements to comply with Red Roof Inn's property improvement plan [Art. II.7, pp. 10-11] (the \$85,380 projection appears to be for *ad valorem* property taxes based on the Debtor's estimate of 2016 property taxes totaling \$85,374. [Art. II.9, Class 3, p. 14])

h. The projections for **Utilities** of \$92,400 per year for post-confirmation years 2 through 5 on pp. 55 and 58 are unreasonable in light of the facts that (i) the Debtor projects increased occupancy rates after year 1 [Ex. 5, p. 58, "Revenue Assumptions"] and (ii) utility rates ordinarily increase over time.

i. The projections on pp. 55 and 58 fail to deduct any **Bad Debt Expense** from uncollectible accounts receivable caused by disputed credit card charges and disputed charges on corporate accounts (charges the Debtor bills directly to a guest's employer or a third-party agent rather than having the guest personally pay the charges at check-in or check-out).

D. Approval of the Disclosure Statement should be denied.

23. For all of the foregoing reasons, approval of the Disclosure Statement should be denied.

WHEREFORE, PREMISES CONSIDERED, First Western requests that the Court enter an order denying approval of the Disclosure Statement and granting First Western such other and further relief, at law or in equity, to which First Western may be justly entitled.

Respectfully submitted,

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By: /s/ Kenneth A. Hill
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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing document was served concurrently with filing by ECF upon all persons who have filed ECF appearances in this case, including counsel of record for the Debtor.

/s/ Kenneth A. Hill
Kenneth A. Hill

4820-1888-3389, v. 11