UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK

In re

ONE CANANDAIGUA PROPERTIES, INC. Case No. 90-22631 K

Debtor

OPINION

This is a Chapter 11 case, filed on December 5, 1990. Its sole significant asset is a hotel. It is stipulated that the hotel is vastly overencumbered if all secured claims of record are sustained. One mortgagee, Chase-Lincoln First Bank, N.A., has moved under 11 USC § 362(d) to lift the automatic stay to permit it to foreclose its mortgage. Other mortgagees, including one that is at least partly undersecured based on stipulated estimates of value, support the motion. The debtor and the creditors' committee oppose.

It is the conclusion of the Court that the stay must be lifted.

BACKGROUND

On December 16, 1991 (which was approximately one year after the filing date and after various other motions to lift stay had been denied, continued or settled), this Court (by Hon. Edward

D. Hayes, now-retired) entered an Order that would lift the automatic stay in favor of mortgagee Chase Lincoln unless the debtor were to bring a Plan of Reorganization on for a confirmation hearing within 90 days from the date of that Order.

Thus on March 12, 1992 there came on for confirmation a Plan of Reorganization. On the eve of that hearing (March 10, 1992) the debtor sought to modify the Plan. At hearing the Court denied confirmation of the original Plan and ruled that the Modified Plan could not be considered at that time because of lack of proper notice. Confirmation of the original Plan was denied because its separate classification (but identical treatment) of trade debt, on the one hand, and of the unsecured portion of certain undersecured mortgages, on the other hand, was viewed by the Court as having impermissibly gerrymandered the unsecured class in order to artificially acquire the acceptance of one impaired class. ("Trade" had narrowly voted to accept. The very large dollar amount of undersecured mortgage claims that had been split off artificially into a separate class had rejected. Combining the two left the Plan unconfirmable for lack of one accepting impaired class.)

The attempted modification on the eve of that hearing was an effort to justify the separate classification by providing different treatment for that class -- i.e. letting that class

retain their liens (which were stipulated to currently be without any section 506(a) value).

That modification had not been addressed in a Disclosure Statement, had not been voted upon, etc., and thus was not considered by the Court at that hearing. The parties then invited the Court to rule upon the propriety of the new classification treatment proposed by the debtor in its modification. They briefed the matter in late March and early April. On April 10 the debtor proposed a further modification, this time offering a cash infusion from an outside source in addition to its earlier proposals. On May 1, 1992, the debtor reported that that infusion had fallen through but that the existing ownership would now offer a cash infusion, but much smaller. On May 6 the current motion by Chase Lincoln was filed. By a Decision and Order entered on May 14 the Court declined to rule on the classification issue submitted to it: the Court determined that it had been asked to rule on an issue that it might otherwise not have to reach in this case, and that to rule on it would be to permit the Court to be impermissibly drawn into the process of negotiating a Plan.

At hearing on Chase Lincoln First's motion, on May 29, the debtor proposed yet a further modification, this time suggesting a larger infusion.

Neither the original Plan nor the subsequent proposals are within the "mainstream" of reorganization plans; rather, they have been on the frontiers.[1] The debtor has highly skilled and experienced reorganization counsel who has candidly acknowledged the respects in which these efforts have been on such frontiers, and the reasons why the debtor has had to maneuver in that region -- the mortgagees have repeatedly vowed rejection of any Plan that leaves certain members of current management and ownership in affiliation with this hotel, and every effort of the debtor (at least since this Court gave it 90 days beginning last December) has been an effort to "get around" the mortgagees' unwillingness to work with current ownership.

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[1] As indicated above, the original plan unsuccessfully attempted to establish that the Bankruptcy Code does not prohibit placing like claims in different classes to affect the vote; even before I ruled against it, this notion had largely been rejected in the Courts that have considered it. That Plan also called for ownership to remain in place without paying creditors in full and without infusing new capital, thus flying in the face of the Supreme Court's rejection of the idea that "sweat equity" constitutes "new value." Indeed, this Court has yet to rule on whether there even is a "new value" exception to the absolute priority rule in this District or this Circuit. But each of the proposals depend or could depend upon the Court finding either (1) that there is a "new value" exception, so that current ownership may retain ownership, or (2) that there is merit to the debtor's suggestion that letting the mortgagees keep their liens (which currently have no value but which could expected to gain value in the future if the reorganization succeeds in paying down senior encumbrances) renders that class a "secured" class, which cannot invoke the absolute priority rule so long as it is receiving the "value" that 11 USC § 1129(b) commands for secured classes. In addition to these issues of law, all parties agree that at any confirmation hearing there will be an expensive and protracted battle on "feasibility" and other fact issues, such as the "value" of the promised stream of payments.

With the changes wrought by the 1978 Reform Act itself and expansion of the U.S. Trustee system in 1986, Congress has sufficiently isolated the Court from what is going on "behind the scenes" that the whole story behind the postures taken in the case is not known to the Court. What is on the record is that this ownership caused the assets of this debtor hotel, and of another corporate debtor's hotel this ownership controls, to be encumbered and diverted for the benefit of a third which they own. (See the Disclosure Statement.) All three are now in Chapter 11. In this case alone, many hundreds of thousands of dollars of mortgage liens appear to be without value and more than $500,000 in prepetition trade debt can receive nothing outside a dramatic reorganization, a miraculous sale, or a major recovery on certain lawsuits which the Creditors' Committee wishes to assert against insiders and certain mortgagees. There being neither any miraculous sale in the offing nor any fund of money to finance the lawsuit if the estate is not generating unencumbered revenues, the Creditors' Committee ardently supports the debtor's creative Plans and opposes the section 362(d) motion. Further, the Committee has moved for leave to commence the actions (on behalf of the debtor) by which certain mortgages might be voided or subordinated.

The undersecured mortgagees, however, ardently support Chase's section 362(d) motion. One of those mortgagees is "on the bubble": an arms-length sale will determine the extent to

which there is value supporting that mortgage. Even the mortgagees junior to that one apparently want nothing more to do with current ownership and believe said ownership to be an impediment to getting this property sold at fair value. It is not disputed that this (being late spring) begins the proper season for a sale of this asset. The hotel is principally a summer resort. The maximum price will be obtained by negotiating a firm sale agreement soon.

In certain regards it may be said that this hotel remains in Chapter 11 strictly on the off-chance that something can be salvaged for trade creditors.

None of the Plans since the first have come on for a hearing on disclosure partly because the parties had expected (until my May 14 decision) a ruling on the propriety of the separate classification. The debtor and Creditors' Committee stand ready to bring on for hearing the latest creative Plan, while the mortgagees (even those who are "underwater" based on generally-agreed valuations for this debtor's assets) ask that Chase-Lincoln be permitted to move its foreclosure action along and move this property to a sale that is free of current management (and, obviously, free of trade debt).

While it may be said that confirmation is not impossible in this case, it appears safe to say that a final order of

confirmation is not likely to be obtained soon, if at all.

ANALYSIS

Those who support lift of stay rely upon the Supreme Court's decision in the case of *In re Timbers of Inwood Forest Associates, Ltd.*, 484 U.S. 365, 98 L Ed 2d 740 , 108 S Ct 626 (1988), wherein the Court said that for purposes of § 362(d)(2)(B), "effective reorganization" means one that is "in prospect". The Court added that "there must be 'a reasonable possibility of a successful reorganization within a reasonable time'" , and "lack of any realistic prospect of reorganization will require § 362(d) relief."

Six months ago the Court gave the debtor (and the Committee) 3 months in which to bring on a plan of reorganization, or the stay would lift. The Plan filed in January, and each of the four modifications proposed since then, test the boundaries of Chapter 11 in an effort to neutralize the vote of the mortgagees. With "adequate protection" payments being made (as they are) we can test these boundaries all summer, with no "expectation" that the mortgagees will not be left looking for a buyer in the off-season.

The current ability of the debtor to make adequate protection payments, together with the desire of the committee to

still have an operating debtor while it seeks to pursue claims against mortgagees, makes this a close case. But I believe that *Timbers* commands lift of stay. It is my reading of Timbers that if an "effective reorganization" connotes one that is a reasonable "prospect" in a reasonable period of time, then once a reasonable period of time has already passed (over the objection of the mortgagees) and an inventive effort at reorganization has failed, the debtor and Committee must show more than a mere "possibility" of obtaining a final order of confirmation within a reasonable period of time. The debtor and Committee had more than a year prior to the March, 1992 denial of the confirmation of a plan to experiment with cram down theories. They chose to do so during the small window offered by this Court's order of December 16, 1991, unsuccessfully. They now oppose the lift of stay on the grounds that they think that they now have their section 1129(b) theories "down pat." This experimentation is speculation at the expense of mortgagees on or near the "bubble". After seventeen months it is also pressing the limits of the Court's authority to prevent senior liens from realizing upon the positions they bargained for.

I find that "cause" exists for the stay to lift.

ORDER TO BE SUBMITTED

This constitutes the finding and conclusions of the Court. Chase Lincoln First Bank, NA may submit a suitable Order after consultation with all appearing parties. If an Order which will suitably protect and preserve the assets during transition to receivership or sale cannot be agreed upon, then the Bank may file a Motion to Resolve the Terms of the Order.

Dated: Buffalo, New York
June 8, 1992

U.S.B.J.