Honorable Mike K. Nakagawa
United States Bankruptcy Judge

Entered on Docket
March 29, 2018

UNITED STATES BANKRUPTCY COURT

DISTRICT OF NEVADA

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In re:	)	Case No. 16-16656-MKN
	)	Chapter 11
DRAFT BARS LLC,	)	
	)	
Debtor.	)	Date: March 21, 2018
	)	Time: 9:30 a.m.
	)	

ORDER ON MOTION OF ANHEUSER-BUSCH, LLC FOR ORDER CONVERTING BANKRUPTCY CASE TO CHAPTER 7, OR ALTERNATIVELY, APPOINTING A CHAPTER 11 TRUSTEE [1]

On March 21, 2018, the court heard the Motion of Anheuser-Busch, LLC for Order Converting Bankruptcy Case to Chapter 7, or Alternatively, Appointing a Chapter 11 Trustee ("Motion"). The appearances of counsel were noted on the record. After arguments were presented, the matter was taken under submission.

BACKGROUND

On December 15, 2016, Draft Bars LLC ("Debtor") filed a voluntary Chapter 11 petition for reorganization. (ECF No. 1). The petition is signed by Michael Manion as managing member.

On December 29, 2016, Debtor filed its schedules of assets and liabilities ("Schedules") along with its Statement of Financial Affairs ("SOFA") and List of Equity Security Holders ("Equity Holders List"). (ECF Nos. 9 and 10). All are signed under penalty of perjury by the

[1] In this Order, all references to "ECF No." are to the numbers assigned to the documents filed in the case as they appear on the docket maintained by the clerk of the court. All references to "Section" are to the provisions of the Bankruptcy Code, 11 U.S.C. §§ 101-1532. All references to "FRBP" are to the Federal Rules of Bankruptcy Procedure.

managing member. On its property Schedule "A/B," Debtor lists no real property as well as miscellaneous personal property having a total value of $124,000. The most valuable property interests listed are a 2014 Porsche 911 Turbo automobile valued at $63,000, a lease security deposit with Gibson Road Trust Resources Group LLC in the amount of $23,000, and accounts receivable ("AR") of $20,000. The property schedule also lists a breach of contract action against Anheuser-Busch, Inc. ("Anheuser-Busch") as having an unknown value. On its secured creditor Schedule "D," Debtor lists two entities: Santander having a claim in the amount of $73,243.29 secured by the Porsche, and Strategic Funding with a claim in the amount of $422,205 secured by various equipment having a value of $15,000. On its unsecured creditor Schedule "E/F," Debtor lists priority and nonpriority unsecured claims totaling $2,391,132.08, the largest of which is owed to Austin General Contracting in the amount of $1,397,350.24. On its co-debtor Schedule "H," Debtor lists its managing member, Michael Manion, as a co-obligor on the secured debt owed to Strategic Funding.

Item 1 of the SOFA states that the Debtor had gross revenues from business operations in the amount of $2,700,000 in 2015, and $5,600,000 from January 1, 2016, through the bankruptcy petition date. Item 7 of the SOFA lists no lawsuits involving the Debtor within 1 year prior to the petition date, but Item 22, regarding environmental law proceedings, lists four breach of contract and other lawsuits against the Debtor.

The Equity Holders List is signed by Michael Manion as managing member of the Debtor and lists the equity holders of the limited liability company as "None."

On January 13, 2017, Debtor filed a motion seeking to reject the lease of its existing space in favor of moving into other leased premises at a lower monthly rate. (ECF No. 23). On the same date, Debtor filed a motion seeking authorization to employ special counsel to pursue its claims against Anheuser-Busch. (ECF No. 26).

On January 17, 2017, the Debtor's existing landlord filed a motion for relief from stay so that it could evict the Debtor from the premises. (ECF No. 30).

On January 27, 2017, the Debtor filed amendments to its Schedules, including an increase in the value of its personal property to $165,610. (ECF No. 40). The value of the

personal property securing the claim of Strategic Funding increased from $15,000 to $31,200. The value of the AR increased from $20,000 to $21,680.

On February 9, 2017, the Debtor filed a stipulation to assume the lease of the Porsche vehicle. (ECF No. 47).

On February 21, 2017, an order was entered authorizing the employment of bankruptcy counsel. (ECF No. 52). On the same date, an order was entered approving a stipulation to reject the prior leased premises. (ECF No. 54).

On March 3, 2017, an order was entered authorizing the employment of Charles W. Bennion, Ltd., as special litigation counsel for the Debtor. (ECF No. 57).

On April 6, 2017, the Debtor commenced Adversary Proceeding No. 17-01176 against Anheuser-Busch, LLC, and Anheuser-Busch Companies, LLC, asserting among other claims, a claim for breach of contract ("Anheuser-Busch Adversary"). (ECF No. 72).[2]

On May 31, 2017, the Debtor batch-filed monthly operating reports ("MOR(s)") ending December 2016, as well as January 2017 through April 2017. (ECF Nos. 103, 104, 105, 106, 107).

On August 4, 2017, the Debtor filed its MOR for June 2017. (ECF No. 124).

On August 29, 2017, the Debtor filed an amended MOR for May 2017. (ECF No. 125).

On October 4, 2017, the Debtor filed its MORs for July and August 2017. (ECF Nos. 126, 127).

On November 21, 2017, the Debtor filed its MORs for September and October 2017. (ECF Nos. 128, 129).

On February 1, 2018, an order was entered approving a stipulation between the Debtor and Strategic Funding for use of cash collateral ("Cash Collateral Order"). (ECF No. 133).

On February 5, 2018, the Debtor filed its MORs for November and December 2017. (ECF Nos. 136, 137).

On February 9, 2018, Anheuser-Busch filed the instant Motion (ECF No. 138), along

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[2] In this Order, all references to "AECF No." are to the numbers assigned to the documents filed in the Anheuser-Busch Adversary.

with a separate motion seeking reconsideration of the Cash Collateral Order ("Reconsideration Motion"). (ECF No. 139). Both matters were noticed to be heard on March 21, 2018. (ECF Nos. 142, 143).

On March 2, 2018, the Debtor filed an objection to the proof of claim filed by Anheuser-Busch in the unsecured amount of $646,461.27. (ECF No. 147). That objection was noticed to be heard on April 4, 2018. (ECF No. 148).[3]

On March 7, 2018, the Debtor filed oppositions to the instant Motion as well as the Reconsideration Motion, accompanied by declarations from its managing member ("Manion Declaration"). (ECF Nos. 152, 153, 154, 155).

On March 7, 2018, Anheuser-Busch filed a statement under FRBP 7032(b) in support of the instant Motion ("Supporting Statement") as well as a declaration of its counsel in support of both motions. (ECF Nos. 151, 156).

On March 7, 2018, Strategic Funding filed an opposition to the Reconsideration Motion. (ECF No. 158). On March 8, 2018, Strategic Funding filed a declaration in support of that opposition. (ECF No. 159).

On March 14, 2018, Anheuser-Busch filed its reply in support of this instant Motion. (ECF No. 164). On the same date, creditor Gary Thorne ("Thorne") filed a joinder in the instant Motion. (ECF No. 165).

On March 16, 2018, Anheuser-Busch filed an objection to certain exhibits accompanying the oppositions filed by the Debtor. (ECF No. 166).[4]

On March 21, 2018, the noticed hearings were conducted on both matters. Apparently during the court's hearing calendar, the Debtor filed MORs for January and February 2018. (ECF Nos. 167, 168).

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[3] On March 14, 2018, Anheuser-Busch filed a response to the claim objection. (ECF No. 163).

[4] Because the Manion Declaration in opposition to the instant Motion includes as a proposed exhibit only an excerpt of the complete transcript otherwise submitted by Anheuser-Busch with its Supporting Statement, the objection is overruled.

APPLICABLE STANDARDS

Conversion or dismissal of a Chapter 11 proceeding is governed by Section 1112. A Chapter 11 debtor in possession may seek such relief voluntarily under Section 1112(a). Such relief also may be sought by a creditor or other party in interest under Section 1112(b). The latter provision states as follows:

> (1) Except as provided in paragraph (2) and subsection (c), on request of a party in interest, and after notice and a hearing, the court shall convert a case under this chapter to a case under chapter 7 or dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, for cause unless the court determines that the appointment under section 1104(a) of a trustee or an examiner is in the best interests of creditors and the estate.
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> (2) The court may not convert a case under this chapter to a case under chapter 7 or dismiss a case under this chapter if the court finds and specifically identifies unusual circumstances establishing that converting or dismissing the case is not in the best interests of creditors and the estate, and the debtor or any other party in interest establishes that – (A) there is a reasonable likelihood that a plan will be confirmed within the timeframes established in sections 1121(e) and 1129(e) of this title, or if such sections do not apply, within a reasonable period of time; and (B) the grounds for converting or dismissing the case include an act or omission of the debtor other than under paragraph (4)(A) – (i) for which there exists a reasonable justification for the act or omission; and (ii) that will be cured within a reasonable period of time fixed by the court.

11 U.S.C. § 1112(b) (Emphasis added). Section 1112(b)(1) expressly permits the court to appoint a Chapter 11 trustee under Section 1104(a), as an alternative to conversion or dismissal. The latter provision states as follows:

> (a) At any time after the commencement of the case but before confirmation of a plan, on request of a party in interest or the United States trustee, and after notice and a hearing, the court shall order the appointment of a trustee -
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> (1) for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management, either before or after the commencement of the case, or similar cause, but not including the number of holders of securities of the debtor or the amount of assets or liabilities of the debtor; or
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> (2) if such appointment is in the interests of creditors, any equity security holders, and other interests of the estate, without regard to the number of holders of securities of the debtor or the amount of assets or liabilities of the debtor.

11 U.S.C. § 1104(a) (Emphasis added).

The party seeking relief under Section 1112(b) or Section 1104(a) bears the burden of proof under a preponderance of the evidence standard. See generally 7 COLLIER ON BANKRUPTCY, 1112.04[4] (16th ed. 2018). See also Sullivan v. Harnisch (In re Sullivan), 522 B.R. 604, 614 (B.A.P. 9th Cir. 2014)(applying a preponderance standard under § 1112(b)).

DISCUSSION

The instant Motion seeks to convert this Chapter 11 proceeding to a Chapter 7 liquidation under Section 1112, or, to have a Chapter 11 trustee appointed under Section 1104. The court has considered the written and oral arguments of the parties, as well as the evidence submitted in support of the request. Additionally, the court has reviewed the entire record and history of this proceeding. On that basis, the court concludes that appointment of a Chapter 11 trustee is in the best interest of creditors and the estate. Several considerations support this conclusion.

First, there is no dispute that this Chapter 11 proceeding has been pending for more than 15 months without a plan of reorganization and accompanying disclosure statement being filed. No committee of unsecured creditors has been formed, and the 120-day plan exclusivity period under Section 1121(b) elapsed on April 17, 2017. In spite of a lengthy "breathing spell" afforded by the automatic stay, the Debtor has offered no plan of reorganization to emerge from bankruptcy.

Second, MORs have been filed sporadically by the Debtor through February 2018, all signed under penalty of perjury by the Debtor's principal. According to the latest report, the Debtor's operations during the Chapter 11 proceeding have resulted in a loss of $54,826. The same report discloses that during the Chapter 11 proceeding, the Debtor's cash receipts total $166,511, with the largest portion consisting of $67,472 constituting an "Advance from Unrelated Company," and the second largest portion consisting of $50,741 from "Rent/Leases Collected." There is nothing on the docket for this Chapter 11 proceeding, however, indicating that the Debtor ever sought court authorization to obtain postpetition credit under Section 364, nor any disclosure of the identity of the so-called "unrelated company" that advanced funds to the Debtor. Additionally, there is nothing on the docket indicating that the Debtor ever sought court authorization under Section 363 to rent or lease any of its assets outside the ordinary

course of business.

Third, the SOFA filed on December 29, 2016, stated under penalty of perjury that the Debtor had gross revenues in 2015 totaling $2.7 million that increased to $5.6 million in 2016. As of the date the Chapter 11 was filed, the Debtor had no more than $21,680 in AR according to the amended personal property schedule filed under penalty of perjury. Debtor's MOR for the period ending December 31, 2017, filed under penalty of perjury, states that the AR balance was $3,459. The same operating report states that as of December 31, 2017, the Debtor's total gross revenues received during the case were $54,049, even though the AR decreased significantly. In other words, the Debtor's annual gross revenues apparently went from $5.6 million in 2016 to less than $100,000 in 2017.[5] Both revenue figures are offered under penalty of perjury, but nothing in the record provides a cogent explanation for this difference.

Fourth, the Debtor's business relationship with Anheuser-Busch allegedly commenced some time in late 2014, see Manion Declaration at ¶ 5, accelerated some time in mid or late 2015, see id. at ¶ 6, 8 and 12, and fell apart in 2016. See id. at ¶¶ 14, 15, 16, 17, 18. Debtor alleges that it furnished work, services and goods for which Anheuser-Busch has not paid. See id. at ¶ 20. At the end of December 2016, however, Debtor's AR was no more than $21,680. In spite of the rise and fall of its relationship with Anheuser-Busch, Debtor apparently had gross revenues of $2.7 million in 2015 and $5.6 million in 2016. If the Debtor was able to generate $5.6 million in gross revenues in 2016 despite allegedly being stiffed by Anheuser-Busch for a maximum of $21,680,[6] there is no readily apparent explanation for why the Debtor's gross revenues in 2017 were only $54,049.

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[5] Debtor's monthly operating report for the period ending February 28, 2018, filed under penalty of perjury, states that the AR balance is now $3,459. The same operating report states that during the Chapter 11 proceeding, the Debtor's total revenues have been $59,712, while its total expenses have been $114,537, resulting in the $54,826 operating loss.

[6] According to its MOR ending January 31, 2017, the Debtor's AR balance went from $21,680 on the bankruptcy petition date to $4,000, as a result of the collection of a prepetition receivable in the amount of $17,680 from "T-Mobile." It therefore appears that very little of the AR listed by the Debtor as of the petition date reflected amounts that allegedly were owed by Anheuser-Busch for unpaid work, services and goods.

Fifth, the Debtor has moved to a smaller factory, but has discharged all of its employees. See Manion Declaration at ¶ 31. Presumably, the Debtor's operations no longer include the manufacture of any products or goods, resulting in the premises being used solely as a storage facility. Presumably, only the Debtor's principal remains in the factory and his business judgment on behalf of the estate, *inter alia*, was to assume a prepetition lease on a Porsche 911 (ECF No. 47), resulting in a significant postpetition administrative expense liability.[7] There was no apparent reason to assume an unexpired lease of personal property prior to confirmation of a Chapter 11 plan, see 11 U.S.C. § 365(d)(2), and no plan of reorganization has ever been proposed in this case. Retaining a "sweet ride" in the midst of a Chapter 11 proceeding may be desirable to the principal of a debtor in possession, compare Orange County's Credit Union v. Garcia (In re Garcia), 709 F.3d 861, 862 (9th Cir. 2013) (affirming remand to bankruptcy court for determination of whether "a 2001 Mercedes 320E sedan, was in fact a tool of the [chapter 7] debtors' trade as a real estate agent, or just a sweet ride."), but is hardly in the best interest of creditors.[8]

Sixth, the Debtor last amended its Schedules on January 27, 2017. On August 29, 2017, however, an examination under FRBP 2004 ("2004 Examination") was taken of the Debtor's principal by counsel for Anheuser-Busch.[9] Throughout the course of that examination, the testimony of the Debtor's principal revealed that there are numerous omissions and misstatements appearing in the Schedules even after the prior amendment. For example, the

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[7] Debtor entered into a 60 month lease on August 3, 2016, with monthly payments of $775.44, commencing October 10, 2016. When the Debtor entered into the stipulation to assume the lease in February 2017, there would have been approximately 55 payments owing to the end of the lease term, totaling $42,469.20.

[8] In a 2004 Examination, see discussion at 8, supra, the Debtor's principal testified in his that prior to the bankruptcy filing, he paid down the lease initially by giving the lessor a 2013 Porsche vehicle that he owned personally. Unfortunately, the vehicle lease was still under the Debtor's name and assumption of the unexpired lease postpetition still incurred an administrative liability of the bankruptcy estate.

[9] A copy of the transcript of that examination was submitted as Exhibit "A" to the Supporting Statement filed by Anheuser-Busch. No objection to the admission of the transcript was filed or raised by the Debtor.

Schedules do not disclose that the Debtor is the parent company of an entity known as Bar Pods, that the Debtor was once the parent company of an entity or product known as Turbo Tap, that the Debtor transferred its interest in Turbo Tap to the principal some time prior to the bankruptcy,[10] and that the Debtor apparently has over $300,000 worth of raw materials in its premises.[11] Although the principal represented at the examination that the Schedules would be amended, more than six months have elapsed and no correction of the many significant inaccuracies in the Schedules has ever occurred.[12] Additionally, the same testimony reveals that the Debtor's principal has refused to explore recapitalization, refinancing, or sale options that typically are explored by distressed businesses, in favor of trying to bring in new business gradually over time.

Finally, the Anheuser-Busch Adversary commenced by the Debtor on April 6, 2017, survived a motion to dismiss brought under FRBP 7012(b)(6), and a discovery plan was

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[10] The examination testimony indicated that both Bar Pods and Turbo Tap operate out of the same factory premises, but it is unclear whether any revenues or profits from those entities are received by the Debtor rather than the Debtor's principal. The Debtor's principal also testified that individuals identified as Kiel Murray and Frank Han each hold 8 percent membership interests in the Debtor even though neither of them are disclosed on the Equity Holders List.

[11] At the examination, a balance sheet provided by the Debtor as of December 31, 2016, was presented to the Debtor's principal as an exhibit. The assets shown on that balance sheet, as well as the liabilities, are significantly different from those set forth in the Schedules as of the December 15, 2016, bankruptcy petition date. That balance sheet includes a liability to Thorne in the amount of $409,000 representing one of six "Loans Per Court Case." One of the lawsuits erroneously listed in Item 22 of the SOFA, see discussion at 2, supra, was a proceeding brought in a Nevada state court styled as Gary Thorne, et al. v. Michael Manion, Draft Bars LLC, Turbo Tap LLC, Bar Pods LLC, and Lots of Cabbage LLC, denominated Case No. A701235-B. If that judgment was obtained against all of the named defendants, then the Debtor's principal individually, along with the Debtor and all related entities, are co-obligors. This obligation, however, is not disclosed on the co-debtor Schedule "H" that was filed under penalty of perjury.

[12] Nor did the Debtor disclose that it has subleased portions of the factory to other parties, which may explain the postpetition rents that appear in its MORs. Inasmuch as the Debtor apparently never previously subleased any of its space, these subleases would constitute the use of property outside the ordinary course of business requiring court approval. It also is unclear whether any necessary consents from the lessor of the current factory premises was ever sought or obtained.

approved at a scheduling conference held on August 24, 2017. (AECF No. 25). A November 10, 2017, initial disclosure deadline was set as well as a February 5, 2018, discovery bar date. A further scheduling conference was set for April 12, 2018. When the Debtor's principal was examined on August 29, 2017, he testified that the outcome of the Anheuser-Busch Adversary is not necessary to the reorganization prospects of the Debtor. He also testified repeatedly that the Debtor is ready to proceed to trial immediately on its complaint. In opposition to the instant Motion, he now attests that the Debtor is prepared to go to trial as soon as the court is available and that success in the lawsuit is "essential to reorganization." See Manion Declaration at ¶¶ 28, 29. In spite of the views of the Debtor's principal, however, there is no declaration, affidavit, or other information from the Debtor's bankruptcy counsel or special litigation counsel, indicating that the Anheuser-Busch Adversary is anywhere close to being ready for trial. To the contrary, on March 14, 2018, Anheuser-Busch filed a motion to exclude the Debtor's initial disclosures or to continue the discovery bar date. (AECF No. 26). That motion is scheduled to be heard on April 12, 2018. (AECF No. 30).

A Chapter 11 trustee can fully address the foregoing concerns. In addition to certain duties under Section 704, see 11 U.S.C. § 1106(a)(1), a Chapter 11 trustee is required to "investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and the desirability of the continuance of such business." Id. at § 1106(a)(3). Additionally, "as soon as practicable," a Chapter 11 trustee must: (a) file a statement of any investigation, including "any fact ascertained pertaining to fraud, dishonesty, incompetence, misconduct, mismanagement, or irregularity in the management of the affairs of the debtor, or to a cause of action available to the estate," and (b) "file a plan," file a report of "why the trustee will not file a plan," or "recommend conversion of the case . . . or dismissal of the case." Id. at §1106(a)(4)(A) and §1106(a)(5).

Of course, Debtor's existing management as well as all counsel employed on behalf of the bankruptcy estate, are required to cooperate with the appointed trustee.

IT IS THEREFORE ORDERED that the Motion of Anheuser-Busch, LLC for Order Converting Bankruptcy Case to Chapter 7, or Alternatively, Appointing a Chapter 11

Trustee, Docket No. 138, be, and the same hereby is, **GRANTED AS PROVIDED HEREIN**.

IT IS FURTHER ORDERED that a Chapter 11 trustee shall be appointed to administer this proceeding. The Office of the United States Trustee shall immediately undertake steps to determine a trustee appropriate for this proceeding and to obtain court approval.

IT IS FURTHER ORDERED that a status conference in this Chapter 11 proceeding will be held on May 9, 2018, at 9:30 a.m. No later than May 2, 2018, the trustee appointed in this matter shall file an initial status report addressing his or her preliminary efforts in the case.

IT IS FURTHER ORDERED that the hearings on all other contested matters, claim objections, or other motions and conferences currently calendared in this Chapter 11 proceeding, as well as any adversary proceeding, are **VACATED**. Those matters shall be renoticed for hearing, if appropriate, after the conclusion of the May 9, 2018, status conference.

Copies sent to all parties via CM/ECF ELECTRONIC FILING

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