

**UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF LOUISIANA
LAFAYETTE DIVISION**

IN RE:

PROGRESSIVE ACUTE CARE, LLC, *et al.*,

Debtors.

CASE NO. 16-50740

CHAPTER 11

JOINTLY ADMINISTERED

OBJECTION TO MOTION TO APPOINT TRUSTEE

The Official Committee of Unsecured Creditors of Progressive Acute Care, LLC, *et al.* (the “Committee”) submits this objection to the Motion to Appoint Trustee (the “Trustee Motion”) [ECF 314] filed by DeAnna W. Jensen Living Trust Dated Jan 26, 2012 (Dr. Wade Jensen, Trustee), Dan Kensinger, Ray Sherman, Steve Stokesbary, Steve Meyer, Grant Shumaker, and Tom Jacobson (collectively, the “Movants”) and respectfully represents as follows:

PRELIMINARY STATEMENT¹

1. The Trustee Motion seeks the appointment of a trustee to investigate and pursue potential claims against the Debtors’ management and board members. The Trustee Motion is premature and, if granted, would burden these estates with additional expenses and no corresponding benefit. The Committee, having first worked with the Debtors to implement a sale of the Debtors’ assets to preserve their value, is now investigating and, where necessary, pursuing potential claims of the Debtors and their estates, including the potential claims identified in the Trustee Motion, to recover additional value for the estates. To that end, the Committee has obtained the Debtors’ consent to a grant of leave, standing, and authority to

¹ Any capitalized terms otherwise undefined in the preliminary statement shall have the meanings ascribed to them elsewhere in this objection.

commence, prosecute, and settle any and all claims of the Debtors and their estates against current and former insiders of the Debtors and any and all claims under chapter 5 of the Bankruptcy Code and filed a complaint challenging the claims and liens of the Debtors' prepetition lender Business First Bank.

2. The services performed by a trustee with respect to the issues raised in the Trustee Motion would therefore be entirely duplicative of the services already being undertaken by the Committee. The Committee takes the allegations set forth in the Trustee Motion seriously and should be afforded the opportunity to investigate any potential claims of the estates raised thereby before the estates are saddled with additional expense which would be detrimental to the estates.

3. The movants' concern that the Debtor's insiders, who are subject to a conflict of interest, are unlikely to investigate or pursue claims against themselves, is adequately addressed through the Committee undertaking such responsibility, as a party free of conflict of interest and statutorily charged with maximizing value for the benefit of all creditors.

4. In light of the foregoing, and because, as set forth more fully below, the Movants have not demonstrated by clear and convincing evidence that there is "cause" to appoint a trustee under section 1104(a)(1) of the Bankruptcy Code or that appointment of a trustee under section 1104(a)(2) of the Bankruptcy Code would be in the best interests of the estates, the Committee respectfully requests that the Trustee Motion and the extraordinary relief of appointment of a trustee be denied.

BACKGROUND

5. Progressive Acute Care, LLC ("PAC"), Progressive Acute Care Avoyelles, LLC ("PAC Avoyelles"), Progressive Acute Care Oakdale, LLC ("PAC Oakdale"), and Progressive

Acute Care Winn, LLC (“PAC Winn,” and collectively with PAC, PAC Avoyelles, and PAC Oakdale, the “Debtors”) filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code (the “Bankruptcy Code”) on May 31, 2016 (“Petition Date”).

6. Since the Petition Date, the Debtors have continued in possession of their respective property and the operation of their respective businesses as debtors-in-possession pursuant to 11 U.S.C. §§ 1107(a) and 1108.

7. The Committee was appointed on June 21, 2016, weeks after the Debtors’ jointly administered chapter 11 cases (the “Chapter 11 Cases”) had been commenced. The Committee retained counsel that same day.

8. Upon its appointment, the Committee undertook an analysis of the Debtors and the issues in these Chapter 11 Cases, including but not limited to issues relating to the preservation and disposition of the Debtors’ assets, liens asserted against the estates, and potential causes of action against insiders and secured creditors, for the benefit of the estates.

9. The Committee discovered or was apprised of many of the issues raised in the Trustee Motion, filed September 27, 2106, shortly after its appointment, including through discussions between the Committee’s attorneys and relevant parties, including Mr. Richard (Dick) Hylland, who previously acted as a consultant to the Debtors and filed proof of claim number 18 in this case. However, because (i) the timeline in these Chapter 11 Cases was compressed due to, *inter alia*, a scarcity of funding, and (ii) the Debtors could not operate indefinitely without further dissipating their assets, the most pressing issue at the outset of these Chapter 11 Cases was to preserve the value of those assets. To that end, the Committee, through their counsel, took an active role in both the establishment of an open sale process designed to maximize the value of the Debtors’ assets for the benefit of the estates and the ultimate sale of

the Debtors' assets to Central Louisiana Hospital Group, LLC (the "Purchaser") for approximately \$10,550,000.

10. To ensure the sale did not compromise any rights to contest liens and preserve value for the estates, the Committee negotiated the inclusion of the following provision on page six of the order approving the sale:

IT IS FURTHER ORDERED that nothing in this Order shall be deemed an admission, acknowledgment, or allowance of the validity, extent, rank, or priority of any liens, claims or interests that may attach to the proceeds of the Sale, and any and all rights, claims, defenses, and other challenges of the Debtors, the Official Committee of Unsecured Creditors, or any other parties-in-interest with respect to the validity, extent, rank, or priority of such liens, claims, or interests are hereby expressly preserved[.]

[ECF 322, ¶ 6.]

11. Having obtained approval of the sale and related transactions, the Committee has turned its attention more fully to other avenues of recovery for the estates, including through the investigation and, if necessary, prosecution of claims against insiders of the Debtors and the Debtors' prepetition lenders.

12. The Committee's attorneys accordingly sent the Debtors' attorneys the letter attached as Exhibit A hereto outlining areas of inquiry and potential causes of action against the Debtors' insiders. The Committee further obtained the Debtors' consent to a grant of leave, standing, and authority to the Committee to commence, prosecute, and if necessary, settle any and all claims of the Debtors and their estates against current and former insiders of the Debtors and any and all claims under chapter 5 of the Bankruptcy Code. On October 6, 2016, the Debtors and the Committee filed a joint motion and stipulation in support of entry of a consent order granting the Committee such leave, standing, and authority.

13. Pursuant to the sale order and the pending joint motion, in light of the Debtors' consent, the Committee is also filing contemporaneously with this objection a complaint for, among other things, annulment and/or avoidance of obligations and liens, avoidance of preferential transfers, declaratory judgment, determination of secured claim, disallowance of claim, and surcharge of collateral against Business First Bank.

14. The Committee intends to fully investigate and pursue all available avenues of recovery, including the foregoing. The Committee further requests that the Court expressly find that none of the estates' claims or causes of action shall be impaired in any manner as a result of the statements and arguments set forth herein in light of the early stages of the Committee's investigation.

OBJECTION

15. The Committee objects to the Trustee Motion on the grounds that the Trustee Motion is premature and the Movants have not demonstrated by clear and convincing evidence that there is cause to appoint a trustee under section 1104(a)(1) of the Bankruptcy Code or appointment of a trustee pursuant to section 1104(a)(2) of the Bankruptcy Code would be in the interests of the estates.

I. The Trustee Motion Is Premature

16. As an initial matter, the Trustee Motion is premature. The Committee takes the issues raised in the Trustee Motion seriously and intends to investigate them and, if necessary, prosecute claims against current and former insiders of the Debtors based on the results of that investigation. While the Committee is sympathetic to the Movants' desire to pursue the issues raised in the Trustee Motion, the Committee should be afforded the opportunity to undertake its investigation and pursue claims as appropriate, which it is now possible to do since the more

urgent issues presented at the outset of these Chapter 11 Cases have been addressed, before the extraordinary relief of appointment of a trustee is considered.

II. Standard for Appointment of a Trustee Under Section 1104(a) of the Bankruptcy Code

17. Section 1104(a) of the Bankruptcy Code provides 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 –

(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

(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.

18. Appointing a trustee is an “extraordinary remedy” that should not be undertaken lightly. *Cajun Elec. Power Coop. v. Central La. Elec. Co. (In re Cajun Elec. Power coop.)*, 69 F.3d 746, 749 (5th Cir. La. 1995), *different result on rehearing on different grounds*, 74 F.3d 599 (5th Cir. 1996) (“The appointment of a trustee . . . is an extraordinary remedy, and there is a strong presumption that the debtor should be permitted to remain in possession absent a showing of need for the appointment of a trustee.”); *Altman v. Rafael Galleries, Inc. (In re Altman)*, 2000 U.S. Dist. LEXIS 16235, *8 (D. Conn. July 27, 2000) (“The order appointing the trustee in the Chapter 11 context is an exceptional remedy in light of the strong presumption that the debtor should remain in possession of the Chapter 11 estate[.]”) (citing *In re U.S. Communications of Westchester*, 123 B.R. 491, 495 (Bankr. S.D.N.Y. 1991) (noting that appointment of trustee in Chapter 11 case is an extraordinary remedy, inasmuch as the Bankruptcy Code favors allowing a

debtor to remain in possession and operate its business)). *See also, e.g., In re Sharon Steel Corp.*, 871 F.2d 1217, 1226 (3d Cir. 1989) (“It is settled that appointment of a trustee should be the exception, rather than the rule.”).

19. The party seeking appointment of a trustee must therefore demonstrate by clear and convincing evidence the need for a trustee under either section 1104(a)(1) or section 1104(a)(2) of the Bankruptcy Code. *In re Amerejuve, Inc.*, 2015 Bankr. LEXIS 1496, *16 (Bankr. S.D. Tex. Apr. 29, 2015) (quoting *Cajun Elec. Power Coop.*, 69 F.3d at 749) (“The parties moving to appoint a trustee bear the burden, by clear and convincing evidence, of demonstrating that cause exists for the appointment of a trustee.”); *Official Comm. of Asbestos Claimants v. G-I Holdings, Inc. (In re G-I Holdings, Inc.)*, 385 F.3d 313, 317-318 (3d Cir. 2004) (“The party moving for appointment of a trustee must prove the need for a trustee under either subsection by clear and convincing evidence.”); *In re Ashley River Consulting, LLC*, 2015 Bankr. LEXIS 1008, *28 (Bankr. S.D.N.Y. Mar. 31, 2015) (“The party seeking appointment of a chapter 11 trustee bears the burden of showing, by clear and convincing evidence, ‘cause’ under section 1104(a)(1) or the need for a trustee under section 1104(a)(2).”).

20. The grounds for the appointment of a trustee identified in the Trustee Motion are: “the misrepresentation and overly optimistic projections of the financial condition of the Debtors by PAC management, duress and/or undue pressure used by PAC management and the board to force the equity unit owners to vote in favor of this bankruptcy proceeding, the failure of the board or management to pursue causes of action and collection of the guaranties against PAC management, and the conflicts of interest PAC management has as a result of the guaranties.”

(Trustee Motion, p.9.) For the reasons set forth below, the foregoing is not sufficient to support the appointment of a trustee under section 1104(a)(1) or section 1104(a)(2).²

III. The Movants Have Not Demonstrated “Cause” Under 11 U.S.C. § 1104(a)(1) by Clear and Convincing Evidence

21. Section 1104(a)(1) requires a demonstration of “cause” by fraud, dishonesty, incompetence, gross mismanagement, or a similar ground, none of which are supported by the Trustee Motion. The Movants make no allegation of fraud by current management, and the allegations regarding misrepresentation, incompetence, and/or gross mismanagement are unsupported by clear and convincing evidence at this time.

22. For example, the Movants provide no evidence that the alleged misrepresentations were inaccurate or intentionally misleading at the time they were made.³ Further, it is not clear based on the information presented that any errors in judgment identified by the Movants rise to the level of incompetence or gross mismanagement to justify the appointment of a trustee.⁴ *See, e.g., In re Bergeron*, 2013 Bankr. LEXIS 4556, *24-*25 (Bankr. E.D.N.C. Oct. 31, 2013) (“Isolated instances of prepetition mismanagement, fraud, dishonesty or other misconduct by the debtor or its management are not sufficient to support a finding of cause under § 1104(a)(1). . . . [Reluctance to appoint a trustee in such instances] is attributable to the fact that some degree of mismanagement or misconduct exists in virtually every insolvency case.”) (citations and

² The allegations made in the Trustee Motion may give rise to claims and causes of action, and all rights and remedies to address any such claims and causes of action are preserved and reserved.

³ As the Committee’s investigation is in the early stages, nothing contained herein should limit or impair the Committee’s investigation, and the Committee reserves the right to supplement, amend, and/or alter its conclusions and determinations as the facts are confirmed or discovered. Nothing contained herein shall be an admission (or deemed an admission) as to any facts or circumstances to the contrary.

⁴ To the extent that the Committee confirms or discovers evidence of gross mismanagement, misrepresentation, fraud, or any other action or omission by the Debtor’s directors and/or officers, the Committee reserves the right to take all appropriate action based upon those facts and circumstances. Nothing contained herein shall be deemed to operate as estoppel, admission, waiver, or limitation of any kind or nature as to the Committee’s or the estates’ rights and remedies in connection with any future litigations that may be commenced on behalf of the estates against any of the Debtors’ directors, officers, or any other third parties.

quotations omitted); *In re Sundale, Ltd.*, 400 B.R. 890, 907 (Bankr. S.D. Fla. 2009) (“Gross mismanagement suggests some extreme ineptitude on the part of management to the detriment of the organization. . . . But it must rise above simple mismanagement to achieve the level envisioned by the Code. . . . Poor management alone does not warrant appointment of a trustee. After all, it is reasonable to assume that the majority of businesses that arrive in chapter 11 have exercised a certain degree of incompetence or mismanagement.”) (citations and quotations omitted); *In re Evans*, 48 B.R. 46, 47 (Bankr. W.D. Tex. 1985) (“In every bankruptcy there exists a certain level of incompetence or mismanagement. As a result, the courts have required a finding of more than simple mismanagement or incompetence.”).

23. Conflicts of interest might be cause for the appointment of a trustee under other circumstances, but the conflicts of interest identified by the Movants in these Chapter 11 Cases have been resolved by the Debtors’ consent to the grant of leave, standing, and authority to the Committee to commence, prosecute, and if necessary, settle any and all claims of the Debtors and their estates against current and former insiders of the Debtors, including the Debtors’ current and former management and board members, and any and all claims under chapter 5 of the Bankruptcy Code.

24. Accordingly, while the allegations set forth in the Trustee Motion might, with further investigation, form the basis of claims against the Debtors’ management and board – claims which the Committee intends to investigate, and if necessary, pursue – they do not demonstrate cause for the appointment of a trustee under section 1104(a)(1) by clear and convincing evidence at this point in time.⁵

⁵ All rights to pursue all such claims are hereby reserved and preserved.

IV. The Movants Have Not Demonstrated That Appointment of a Trustee Pursuant to 11 U.S.C. § 1104(a)(2) Would Be in the Interests of the Estates by Clear and Convincing Evidence

25. Section 1104(a)(2) of the Bankruptcy Code requires that appointment of a trustee be “in the interests of creditors, any equity security holders, and other interests of the estate.”

For the reasons set forth below, there is no clear and convincing evidence that appointment of the trustee would be in the estates’ interests, and it is clear that appointment of a trustee would actually be to the estates’ detriment.

26. Section 1104(a)(2) is a more flexible standard than section 1104(a)(1) that “entails the exercise of a spectrum of discretionary powers and equitable considerations.” *In re New Orleans Paddlewheels, Inc.*, 350 B.R. 667, 692 (Bankr. E.D. La. 2006). “It must therefore be determined on a case by case basis and will rely heavily on the facts.” *Id.* (citing *Petit v. New England Mortg. Services, Inc.*, 182 B.R. 64 (Bankr. D. Me. 1995)). “In making this determination the court may consider the trustworthiness of the debtor balanced against the costs of the appointment.” *Id.* (citing *Cajun Elec. Power Coop.*, 69 F.3d 599; *In re Ionosphere Clubs, Inc.* 113 B.R. 164 (Bankr. S.D.N.Y. 1990).

27. The facts of these Chapter 11 Cases weigh heavily against the appointment of a trustee under this standard. First, the Movants do not highlight, and the Committee is not aware of, any action taken by the Debtors since the filing of these Chapter 11 Cases that would call into question their trustworthiness or adherence to the requirements imposed upon them by the Bankruptcy Code as debtors-in-possession. As set forth above, the Debtors have resolved the apparent conflicts of interest raised by the Trustee Motion through their consent to the grant of leave, standing, and authority to the Committee to commence, prosecute, and if necessary, settle any and all claims of the Debtors and their estates against current and former insiders of the Debtors and any and all claims under chapter 5 of the Bankruptcy Code.

28. Moreover, in light of such grant, the services provided by a trustee with respect to the issues raised in the Trustee Motion would duplicate those of the Committee, adding an additional estate expense with no additional benefit. This is particularly important in these Chapter 11 Cases, as the total consideration for the sale of the Debtors' assets to the Purchaser (approximately \$10,550,000) only narrowly exceeds the face amount of the secured claim asserted by Business First Bank (approximately \$10,314,125.10). Appointment of a trustee would only further exacerbate this issue.

29. Based on the foregoing, appointment of a trustee under section 1104(a)(2) of the Bankruptcy Code would not be in the interests of the estates.

WHEREFORE, the Committee respectfully requests that the Court (i) deny the Trustee Motion; (ii) order that nothing contained herein shall be deemed to operate as estoppel, admission, waiver or limitation of any kind or nature as to the Committee's or the estate's rights and remedies in connection with any future litigations that may be commenced on behalf of the estates against any of the Debtor's directors, officers or any other third parties; and (iii) grant such other and further relief that the Court deems just and appropriate.

Respectfully submitted,

Date: October 11, 2016

/s/ J. Eric Lockridge

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Certificate of Service

I hereby certify that a copy of the foregoing *Objection to the Motion to Appoint Trustee* was served on the Office of the U.S. Trustee, the Debtor through its counsel, and all parties requesting and receiving notice through the Court's CM/ECF System on October 11, 2016.

/s/ J. Eric Lockridge

EXHIBIT A

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October 6, 2016

Via Email

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Re: Progressive Acute Care LLC, et al.

Dear Mr. Steffes:

As you know, this Firm represents the Official Committee of Unsecured Creditors (the "Committee") of Progressive Acute Care, LLC, Progressive Acute Care Avoyelles, LLC, Progressive Acute Care Oakdale, LLC, Progressive Acute Care Winn, LLC (collectively, the "Debtors") in their chapter 11 bankruptcy cases pending in the United States Bankruptcy Court for the Western District of Louisiana under Case No. 16-50740 (Jointly Administered). We write on behalf of the Committee regarding the Motion to Appoint a Trustee (the "Motion") filed by certain equity holders of the Debtors on September 27, 2016 [Docket No. 314].

The Motion sets forth extensive allegations regarding various actions and omissions of the Debtors' directors and officers that are of deep concern to the Committee. Those allegations, combined with other information that has become available to the Committee since the Committee's appointment in these cases, lead the Committee to believe that the Debtors' estates may have substantial claims and causes of action against the Debtors' directors and officers for numerous breaches of fiduciary duties arising from the actions and omissions of such directors and/or officers relating to, among other things:

(i) acquisition of Dauterive Hospital of New Iberia ("Dauterive") from Hospital Corporation of America in April 2013;

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(ii) causing the Debtors to become jointly and severally liable for the repayment of debt in excess of \$20 million used by the Debtors' directors and officers largely to finance the acquisition of Dauterive and pledging substantially all of the Debtors' assets to secure Dauterive's repayment of such debt without a concomitant reasonably equivalent benefit to the Debtors in exchange for assuming such obligations;

(iii) causing the Debtors' insolvency and/or failing to prevent the deepening of such insolvency;

(iv) failing to operate the Debtors in the best interests of the Debtors' creditors while the Debtors were insolvent;

(v) failing to maintain corporate separateness of each of the Debtors and causing the commingling of the assets and liabilities of the Debtors; and

(vi) wasting of the Debtors' assets.

The foregoing list is non-exclusive, as the Committee's investigation is in its nascent stages, but if proven, these breaches of fiduciary duties have caused the Debtors' estates and their creditors damages ranging in multiples of millions of dollars.

In light of the Motion and the Committee's independent concerns, the Committee will continue to vigorously investigate any and all potential causes of action against the Debtors' directors and/or officers and intends to seek the entry of an order by the Bankruptcy Court granting the Committee standing to commence, prosecute and, if appropriate, settle any and all claims and causes of action that the Debtors' estates may have against the Debtors' directors and/or officers. The grant of standing to the Committee is necessary and appropriate under these circumstances in which the persons who control the Debtors are unlikely to investigate or prosecute claims against themselves. Accordingly, to obviate the need for motion practice, which will only increase the administrative expense burden on the estates, the Committee hereby requests that the Debtors enter into a consent order granting the Committee requisite standing as set forth herein.

Very truly yours,

/s/ Andrew H. Sherman
Andrew H. Sherman