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Order Up! The Krystal Company Bankruptcy

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Order Up! The Krystal Company Bankruptcy

By:
W. Preston White
&
Jonathan E. Williams



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Interested Parties

Debtors

The Krystal Company – Primary debtor and operating company of this case. Wholly owned subsidiary of Krystal Holdings, Inc. Second oldest fast-food chain in America and headquartered in Dunwoody, Georgia.

Krystal Holdings, Inc. - Wholly owned subsidiary of K-Square Acquisition Co., LLC.

K-Square Acquisition Co., LLC - Wholly owned subsidiary of Krystal Holdings, LP.

Krystal Parent Holdings, L.P. - Main holding company.

Rody Davenport Jr. and Glenn Sherrill – Founders of Krystal.

Jonathan Tibus – Managing director Alvarez & Marsal in Atlanta, GA. Brought in by Krystal to take the position of Chief Restructuring Officer. Tibus assisted in decision making and planning of the restructuring and ultimate sale of The Krystal Company.

Bankruptcy Players

Wells Fargo – Multinational financial services company with corporate headquarters in San Francisco, California. Wells Fargo was the primary loan provider and secured creditor in this proceeding.

King and Spalding, LLP – Corporate law firm that is headquartered in Atlanta, Georgia and was the Debtor’s primary counsel in this proceeding.

Judge Paul W. Bonapfel – Federal bankruptcy judge for the United States Bankruptcy Court, Northern District of Georgia.

Fortress Investment Group – Purchaser of Krystal through DB KRST Investors, LLC. Founded in 1998, Fortress manages \$53.3 billion of assets under management as of December 31, 2021, on behalf of approximately 1,800 institutional clients and private investors worldwide across a range of credit and real estate, private equity and permanent capital investment strategies. Fortress is an affiliate of Wells Fargo Bank.

U.S. Trustee – Thomas Wayne Dworschak - Appointed by The Office of the U.S. Trustee, this individual protected the interest of, most notably, the unsecured creditors in this case.

U.S. Foods – One of America’s leading food distributors servicing restaurants and a Super Priority Vendor.

Committee of Unsecured Creditors

- NCR Corporation – Cleveland, OH
- Charles Tombras Advertising, Inc. – Atlanta, GA
- The Coca-Cola Company – Atlanta, GA
- Realty Income Corporation – San Diego, CA
- Flowers Foods, Inc. – Atlanta, GA
- Pension Benefit Guaranty Corporation – Washington, D.C.
- SLM Waste Recycling Services, Inc. – Carrollton, GA

Piper Sandler & Co - is a leading investment bank and institutional securities firm offering M&A advisory. In this case, they served as the financial advisors for the 363 sale of The Krystal Company and directed the course of action for the company.

Nashville Capital Group – A smaller private equity investment group that attempted to purchase Krystal prior to Fortress offering a substantially higher bid.

Introduction

On January 19, 2020, on the eve of the COVID-19 pandemic, The Krystal Company, along with affiliates Krystal Holdings, Inc. and K-Square Acquisition Co., LLC, filed a voluntary petition in the United States Bankruptcy Court for the Northern District of Georgia declaring Chapter 11 Bankruptcy.¹ The company sought reorganization but the case concluded with a sale of substantially of its assets to senior lender Fortress Investment Group for a \$27 million dollar credit bid and a \$21 million assumption of liabilities.² This marked the second time in 25 years that Krystal declared bankruptcy, with the prior Chapter 11 case occurring in 1995.³

This research paper serves as a case synopsis of Krystal's Chapter 11 proceedings and is an educational tool for cases that result in a sale of the debtor when reorganization is not practical. Further, the paper summarizes and explains in simple terms the actions taken to relieve the company of underperforming locations, unattractive leases, and debt obligations. Along with large amounts of secured debt, the nation's second-oldest fast-food chain found itself on the wrong end of industry trends towards healthier options and innovative delivery methods. In 2018, equity holders attempted a "Hail Mary" in the form of a \$59.8 million equity infusion to repay \$42 million of the term loan facility and fund other capital expenditures.⁴ In the fourth quarter of 2018, the efforts proved to be all for not as it violated debt covenants of its Prepetition Credit Agreement, and the game was all but over.⁵

In the months before the petition date, the company closed unproductive locations, streamlining their management structure, and hired two veteran executives with considerable industry-specific experience.⁶ While the scene was rather grim in mid-January 2020, the

¹ Chapter 11 Voluntary Petition for Non-Individuals Filing for Bankruptcy, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) 1.pdf [hereinafter Krystal Voluntary Petition]. Jurisdiction was proper under 28 U.S.C. §§ 157 and 1334 because the company's corporate headquarters was located in the Northern District of Georgia at 1455 Lincoln Parkway, Suite 600, Dunwoody, Georgia 30346. *Id.* at 1.

² Notice of No Auction and Filing of Asset Purchase Agreement, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) 425.pdf at Ex.A p. 19; Jonathan Maze, *Bankrupt Krystal Is Being Sold to One of Its Lenders*, RESTAURANT BUS. (May 14, 2020), <https://www.restaurantbusinessonline.com/financing/bankrupt-krystal-being-sold-one-its-lenders> [<https://perma.cc/E4YX-4UQV>].

³ The Krystal Company History, FUNDING UNIVERSE, <http://www.fundinguniverse.com/company-histories/the-krystal-company-history/> [<https://perma.cc/J98T-TSM4>] (last visited May 15, 2022). Krystal filed due to financial issues related to the fast expansion of locations and a class action lawsuit with employees. In re The Krystal Company, No. 96-15306 (NWW) (Bankr. E.D. Tenn. Dec. 15, 1995).

⁴ Declaration of Jonathan M. Tibus in Support of Chapter 11 Petitions and First Day Pleadings, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) 17.pdf at 6 [hereinafter Declaration of Jonathan Tibus].

⁵ *Id.* at 8.

⁶ *Id.* at 9.

company persevered through COVID-related challenges and exited the Chapter 11 proceedings following a section 363 sale.⁷

Firing Up the Grill: Background

In 1932, amidst the Great Depression, Rody Davenport Jr. and Glenn Sherrill partnered to found Krystal in Chattanooga, Tennessee.⁸ Davenport was a businessman in the textile industry and was inspired by White Castle, the only quick-service food chain older than Krystal. The founders prided themselves on cleanliness and adopted the Krystal name after Mary Davenport, Rody's wife, compared the clean appearance of the restaurant to a crystal ball lawn ornament. The initial 25-by-10 foot building cost the founders roughly \$5,000.⁹ The chain's five cent hamburger was an instant success and the founders aggressively expanded throughout the southeast region in 1930s and 1940s, focusing on Tennessee, Alabama, and Georgia.¹⁰ Subject to an agreement with White Castle, the company never expanded into northern regions because of the similarity of the businesses.¹¹ A Krystal spokesperson once told the *Atlanta Journal-Constitution* that the Mason-Dixon line separated the two quick service juggernauts.¹²

After World War II, fast food companies began offering drive-through options, motivated by the success of drive-in movie theaters.¹³ Krystal pounced on this trend and stopped building restaurants with indoor seating; instead, the company opted for only drive-throughs in new locations.¹⁴ However, these drive-throughs were not like the ones that dominate today's fast-food market. The customer would walk up to the window and the worker would bring the food out. The customer would typically simply eat the food in their car.¹⁵

Through the 1960s and 1970s, Krystal's position in the market changed. Consumers were increasingly eating fast food in their everyday lives and low prices, consistency, and convenience became more important. This changed fast food companies' operations as they could trim staff and streamline operations and menus. During this period, Krystal also tied itself to Elvis Presley and Dolly Parton as a way to further ingratiate itself to the southern market and compete with

⁷ 11 U.S.C. § 363. See [Section 363 Sale](#).

⁸ *Krystal History*, Krystal, <https://www.krystal.com/about-us/krystal-history/> [<https://perma.cc/9T8X-M9F6>] (last visited May 15, 2020); *The Krystal Company History*, FUNDING UNIVERSE, <http://www.fundinguniverse.com/company-histories/the-krystal-company-history/> [<https://perma.cc/J98T-TSM4>] (last visited May 15, 2022).

⁹ *Krystal History*, KRYSTAL, <https://www.krystal.com/about-us/krystal-history/> [<https://perma.cc/9T8X-M9F6>] (last visited May 15, 2020)

¹⁰ *The Krystal Company History*, FUNDING UNIVERSE, <http://www.fundinguniverse.com/company-histories/the-krystal-company-history/> [<https://perma.cc/J98T-TSM4>] (last visited May 15, 2022).

¹¹ *Id.*

¹² *Id.*

¹³ *Id.*

¹⁴ *Id.*

¹⁵ *Id.*

larger fast-food companies. Elvis' love of Krystal was well documented as it was reported that Presley would commonly order bags full of the famous hamburgers.¹⁶

Another way Krystal differentiated itself was the conscious choice to avoid franchising restaurants due to the cap on revenue the company could receive per store.¹⁷ Instead, in 1969, the company started DavCo Foods as a subsidiary of Krystal, to acquire and operate Wendys' franchises in the north.¹⁸ Because of this, Krystal was able to have exposure to other fast-food chains and markets while not directly competing with Krystal locations. Most notably, DavCo became "the exclusive operator of Wendy's franchises in Baltimore and Washington, D.C."¹⁹

Krystal eventually doubted DavCo's viability due to its operating costs.²⁰ After DavCo acquired Po Folks, another restaurant chain, Krystal decided to spin off Po Folks through an initial public offering.²¹ Po Folks then acquired DavCo and Krystal decided to focus solely on its own brand.²²

Krystal also diversified using other unique methods. In 1977, Krystal acquired an airplane hangar and fueling station in Chattanooga, Tennessee.²³ In 1989, Krystal also started managing the leasing of airplanes.²⁴ These operations were done through Krystal Aviation

¹⁶ Holly Riddle, *The Untold Truth of Krystal*, MASHED, <https://www.mashed.com/466492/the-untold-truth-of-krystal/> [<https://perma.cc/MF2Q-76RN>] (Feb. 8, 2022, 11:38 AM).

¹⁷ The Krystal Company History, FUNDING UNIVERSE, <http://www.fundinguniverse.com/company-histories/the-krystal-company-history/> [<https://perma.cc/J98T-TSM4>] (last visited May 15, 2022). Typically, franchising a restaurant—as opposed to operating it—results in lower revenue per store for the franchisor because the income comes from franchise, marketing, and royalty fees paid by the franchisee. A Franchise fee is typically a fixed upfront payment while marketing and royalty fees are a percentage of the location's revenue. Thus, the upside is lower than if the franchisor operated the location. See Joe Libava, *Franchise Fees: Why Do You Pay Them and How Much Are They?*, U.S. Small Business Administration (Apr. 18, 2017), <https://www.sba.gov/blog/franchise-fees-why-do-you-pay-them-how-much-are-they> [<https://perma.cc/Q7VK-NQ9T>].

¹⁸ *Clyde Culp Named President of New Po Folks Operation*, The Krystal Gazer, Jan. 1983, at 1, 11. "A franchise relationship is a contract agreement between a franchisor and a franchisee that allows the franchisee the right to utilize the franchisor's business model, brand, and/or resources to start a new business. . . . There are two primary parties in a franchising relationship: the franchisor and the franchisee. While the franchisor maintains the overall direction of the business—including managing other franchises—the franchisee has a direct connection with the customers and the business." Franchise Information, *What Is a Franchising Relationship?*, FRANCHISE.COM (July 22, 2021), <https://www.franchise.com/blog/what-is-a-franchising-relationship/> [<https://perma.cc/6EQ7-U58J>].

¹⁹ The Krystal Company History, FUNDING UNIVERSE, <http://www.fundinguniverse.com/company-histories/the-krystal-company-history/> [<https://perma.cc/J98T-TSM4>] (last visited May 15, 2022).

²⁰ *Id.*

²¹ *Id.* "An initial public offering (IPO) refers to the process of offering shares of a private corporation to the public in a new stock issuance." Jason Fernando, *Initial Public Offering (IPO) Definition*, INVESTOPEdia, <https://www.investopedia.com/terms/i/ipo.asp> [<https://perma.cc/2P3T-G9DM>] (Nov. 30, 2021).

²² The Krystal Company History, FUNDING UNIVERSE, <http://www.fundinguniverse.com/company-histories/the-krystal-company-history/> [<https://perma.cc/J98T-TSM4>] (last visited May 15, 2022).

²³ The Krystal Company, Annual Report (Form 10-K) (Mar. 25, 1997), <https://www.sec.gov/Archives/edgar/data/885640/0000885640-97-000006.txt> [<https://perma.cc/XNZ5-AXK5>].

²⁴ *Id.*

Company.²⁵ It is unclear when Krystal spun off the operation, but it was still a subsidiary of Krystal as recently as 1997.²⁶

In the early 1980s, Krystal emphasized its products in a large nationwide ad campaign to reinvigorate the brand.²⁷ The campaign succeeded in improving Krystal's image, but the company still struggled to add new locations.²⁸ Additionally, the existing stores had outdated equipment that led to slower service times. As a result, in 1985, R.B. Davenport III orchestrated a leveraged buyout of the company and invested in technology for the locations to improve service.²⁹ Later in 1990, Davenport focused on expanding the chain through franchising. Worried about lack of control and costs, Davenport limited franchise locations to only drive-throughs called Krystal Kwik.³⁰ These changes increased gains and to further expand, Krystal went public in 1992.³¹ Bringing in \$24 million through the initial public offering, the company's new strategy was to operate store-owned locations in larger cities leaving smaller markets to franchisees. The expansion was fairly rapid and the company's footprint spread to North Carolina, Missouri, South Carolina, Kentucky, and Arkansas after being consolidated mainly in Georgia, Tennessee, and Alabama for years.³²

There is something to be said for the old adage "slow and steady wins the race." From 1993 to 1994, Krystal increased sales from \$236 million to \$248 million, however profits dropped from \$7.5 million to \$6.9 million partially due to the capital outlays associated with the new locations.³³ 1995 was even worse as sales remained at \$248 million but the company posted a \$5.3 million dollar loss. The company also was forced to significantly cut prices to keep up with its competitors.³⁴ Additionally, the company settled a class action lawsuit brought by employees for \$800,000 and racked up \$2 million in legal fees associated with the case.³⁵ The employees alleged that Krystal violated the Fair Standards Labor Act and did not adequately compensate them for overtime hours. Employees in other states hopped on the bandwagon and initiated more lawsuits.³⁶ As a result, Krystal filed for Chapter 11 bankruptcy protection in the Eastern District of Tennessee in December 1995.³⁷

²⁵ *Id.*

²⁶ *Id.*

²⁷ The Krystal Company History, FUNDING UNIVERSE, <http://www.fundinguniverse.com/company-histories/the-krystal-company-history/> [<https://perma.cc/J98T-TSM4>] (last visited May 15, 2022).

²⁸ *Id.*

²⁹ *Id.*

³⁰ *Id.*

³¹ *Id.*

³² *Id.*

³³ *Id.*

³⁴ *Id.*

³⁵ *Id.*

³⁶ *Id.*

³⁷ In re The Krystal Company, No. 96-15306 (NWW) (Bankr. E.D. Tenn. Dec. 15, 1995).

The company exited bankruptcy proceedings in the second quarter of 1997.³⁸ In September of 1997, Port Royal Holdings acquired the company for \$135 million.³⁹ Phillip Sanford, owner of Port Royal, claimed he purchased the company due to his fond memories of eating the famous burgers in his adolescence.⁴⁰ He planned to focus on the nostalgic aspect of the brand and revitalize its image after bankruptcy and the lawsuit settlements. His goal was to increase Krystal's presence in the southeast and avoid other regions where the company had less market penetration.⁴¹

In the 2000s, Krystal began updating its drive-through experience.⁴² The company installed television monitors that had audio features through customer car stereos. Additionally, they improved the indoor area of stores by installing televisions and jukeboxes for a more comfortable dining-in experience.⁴³ The move was done to harken back to the drive-in popular in the 1950s and 1960s.⁴⁴ Krystal experienced marginal success during the 2000s.

Prepetition Debt

In 2012, the company was acquired by K-Square Restaurant Partners LP.⁴⁵ On March 21, 2012, Krystal entered into "a senior secured credit facility with Wells Fargo Bank, National Association ("Wells Fargo") and certain other lenders."⁴⁶ The parties amended the agreement on August 4, 2015 and entered into a Second Amended and Restated Credit Agreement ("Second A&R Credit Agreement").⁴⁷ "The Second A&R Credit Agreement provided the Debtors with a Term Loan facility in the amount of \$95,000,000 and a revolving credit facility in the amount of \$20,000,000."⁴⁸

In April 2018, the company modified the agreement yet again. Additionally, the owners of Krystal contributed a \$59,800,000 equity infusion. The company's Chief Restructuring Officer's declaration states:

³⁸ *Id.*

³⁹ The Krystal Company History, FUNDING UNIVERSE, <http://www.fundinguniverse.com/company-histories/the-krystal-company-history/> [<https://perma.cc/J98T-TSM4>] (last visited May 15, 2022).

⁴⁰ *Id.*

⁴¹ *Id.*

⁴² Jason M. Reynolds, *Krystal Dishes Up Nostalgia*, CHATTANOOGA TIMES FREE PRESS (May 15, 2007), <https://web.archive.org/web/20070829150515/http://www.timesfreepress.com/absolutenm/templates/business-toplocal.aspx?articleid=15249&zoneid=169>.

⁴³ *Id.*

⁴⁴ *Id.*

⁴⁵ Declaration of Jonathan Tibus, [17.pdf](#) at 4.

⁴⁶ *Id.* at 6.

⁴⁷ *Id.*

⁴⁸ *Id.*

The equity infusion was primarily used to: (a) repay approximately \$42,000,000 of the existing term loan facility; and (b) fund substantial remodeling capital expenditures, marketing expenditures, and general working capital needs. In connection with the modification, the Debtors entered into that certain Third Amended and Restated Credit Agreement (the “Prepetition Credit Agreement,” and the facilities thereunder, the “Prepetition Credit Facility”), with Wells Fargo, as administrative agent, and the lenders party thereto (together with Wells Fargo, the “Prepetition Lenders”). Under the Prepetition Credit Agreement, the outstanding term loans were reduced to \$53,100,000 and the revolving credit facility was reduced to \$10,000,000. The Prepetition Credit Facility [was to] mature[] on April 26, 2023, and [was] secured by assets of the Debtors.⁴⁹

Even with the high amounts of debt relative to the company’s size, Krystal acquired further financing in the form of a Second Lien Promissory Note (“Prepetition Second Lien Note”) from KRY, LLC.⁵⁰ The note was for \$1,500,000 and was to mature on October 23, 2023.⁵¹ This Second Lien Promissory note was guaranteed by Krystal and some of its subsidiaries and was secured by a second priority blanket lien on Krystal’s assets.⁵²

Events Leading Up to Filing

Despite Krystal’s aggressive financing measures, the company faced challenges due to changes in the fast-food market. CRO Jonathan Tibus’s declaration in support of the Debtor’s first day motions stated:

In the past few years, the Debtors have experienced strong industry-specific headwinds due to a combination of shifting consumer tastes and preferences, growth in labor and commodity costs, increased competition, and unfavorable lease terms. The proliferation of fast casual restaurants as well as online delivery platforms has created new competition for traditional quick-service chains. Moreover, quick-service restaurants have faced increasing difficulty finding and retaining qualified employees in the current labor market. It is not uncommon for quick-service restaurants to face store-level turnover in excess of 200%. These challenges (together with

⁴⁹ Id.

⁵⁰ Id. at 7.

⁵¹ Id.

⁵² Id.

company-specific business challenges) have resulted in deteriorating financial performance.⁵³

The company fought the negative trends by engaging Boston Consulting Group in Fall 2107.⁵⁴ In an attempt to revamp key stores, the company completely rebuilt nine stores.⁵⁵ The investments were significant but did lead to higher sales for the stores; five were completed in 2018 and the remaining four were finished in 2019.⁵⁶ “On average, these rebuilds required an investment of approximately \$950,000 per location.”⁵⁷

Because of these challenges, Krystal “failed to comply with certain of the financial covenants in the Prepetition Credit Agreement for the fourth quarter of 2018.” This prompted the previously mentioned equity infusion to cure the covenant defaults. Later, the company defaulted again under Prepetition Credit Agreement “due to the Debtors’ failure to deliver audited financial statements without a ‘going concern’ qualification for the fiscal year ending December 31, 2018.” This was serious:

The going concern principle is that you assume a business will continue in the future, unless there is evidence to the contrary. When an auditor conducts an examination of the accounting records of a company, he or she has an obligation to review its ability to continue as a going concern; if the assessment is that there is a substantial doubt regarding the company's ability to continue in the future (which is defined as the following year), a going concern qualification must be included in his or her opinion of the company's financial statements. This statement is typically presented in a separate explanatory paragraph that follows the auditor's opinion paragraph.

The going concern qualification is of great concern to lenders, since it is a major indicator of the inability of a company to pay back its debts. . . . A lender is typically only interested in lending to a business that has received an unqualified opinion from its auditors regarding its financial statements.⁵⁸

⁵³ *Id.* at 7–8.

⁵⁴ *Id.* at 8.

⁵⁵ *Id.*

⁵⁶ *Id.*

⁵⁷ *Id.*

⁵⁸ *Going Concern Qualification Definition*, Accounting Tools (Jan. 9, 2022), <https://www.accountingtools.com/articles/what-is-a-going-concern-qualification.html> [<https://perma.cc/C7K6-UJAG>].

Essentially, Krystal’s auditor was not able to certify that the company was a going concern which was a condition of the Prepetition Credit Agreement. As a result, the company was in default under the covenants of the Prepetition Credit Facility in the second quarter of 2019 and was forced to seek and enter into a forbearance agreement with its lenders (“Prepetition Forbearance Agreement”).⁵⁹ Under the Prepetition Forbearance Agreement, the lenders agreed to defer exercising their rights under the loan agreement for a period of time.⁶⁰ This took some pressure off of Krystal. Krystal’s Prepetition Forbearance Agreement would expire on the day after the company filed for Chapter 11 bankruptcy protection.⁶¹

In addition to the Prepetition Forbearance Agreement, the company took other measures to address liquidity issues. These consisted of laying off of certain senior executives, shrinking regional management teams, and closing underperforming locations.⁶² Krystal was so aggressive in closing certain locations that if the company “[was] unable to sell, convert, or sublease the restaurant, the [company] turned the store ‘dark’ by entirely ceasing business at the location.”⁶³ In total, the company closed 44 locations in 2019 to improve its financial situation.⁶⁴

Krystal replaced the executives by hiring Tim Ward as President and Chief Operating Officer, and Bruce Vermilyea as Chief Financial Officer.⁶⁵ The new officers had extensive experience in the industry. Ward had served as Chief Operating Officer of Captain D’s and Vermilyea spent 18 years with Qdoba, last serving as Chief Financial Officer for three years.⁶⁶

Security Breach

At the time of its bankruptcy filing, Krystal faced an odd predicament. From July 2019 to September 2019, its payment systems at some locations were breached by computer hackers.⁶⁷ The hackers obtained customer information from payment cards.⁶⁸ Two-thirds of the restaurants were affected but because the company used a variety of different payment systems, one-third of their locations were not compromised.⁶⁹

⁵⁹ Declaration of Jonathan Tibus, [17.pdf](#) at 8.

⁶⁰ *Id.*; Stephen M. Kindsmith, *Commercial Loan Forbearance Agreements: Striking a Fair Balance from the Borrower’s Perspective*, ZEISLER & ZEISLER, P.C. (Nov. 30, 2020), <https://www.zeislaw.com/Commercial-Loan-Forbearance-Agreements-Striking-a-Fair-Balance-from-the-Borrower-s-Perspective> [<https://perma.cc/88V7-MH4X>].

⁶¹ Declaration of Jonathan Tibus, [17.pdf](#) at 8.

⁶² *Id.* at 9.

⁶³ *Id.*

⁶⁴ *Id.*

⁶⁵ *Id.*

⁶⁶ *Id.*

⁶⁷ *Id.* at 10.

⁶⁸ *Id.*

⁶⁹ *Id.*

While not an event that contributed to filing Chapter 11, the CRO Jonathan Tibus later explained:

The Debtors have already taken steps to contain and remediate the incident and are working hard to determine the specific locations and dates for each restaurant involved in the attack. To date, the investigation has determined that about a third of the Debtors' restaurants are not impacted. The Debtors are committed to protecting the privacy and security of their customers and will continue to take quick action as the investigation continues.⁷⁰

Organizational Structure, Directors, and Key Employees

When Krystal eventually filed for Chapter 11 protection in January 2020, their organizational structure was relatively streamlined and straightforward. In descending order, it went: (1) Krystal Parent Holdings, LP, (2) K-Square Acquisition Co., LLC, (3) Krystal Holdings, Inc, and (4) The Krystal Company.⁷¹ Krystal Parent Holdings, LP owned 100% of K-Square Acquisition Co., LLC which was a Delaware limited liability company and had no significant assets or operations other than its investment in Krystal Holdings, Inc.⁷² Krystal Holdings, Inc. was a Georgia corporation and had no significant assets or operations other than its 100% ownership of the Krystal Company.⁷³ And finally, The Krystal Company was a Tennessee corporation that owned all of the operating assets.⁷⁴ Krystal's board of directors were Michael Klump, Karl Jaeger, and Mike Elliott.⁷⁵ Michael Klump was the founder and President of Argonne Capital Group, LLC and Karl Jaeger was a managing director at the time.⁷⁶ Klump and Jaeger joined the board after Argonne Capital Group, LLC purchased Krystal in 2012.⁷⁷ Mike Elliott was an independent director who joined the board of directors on December 12, 2019.⁷⁸

⁷⁰ [Id.](#)

⁷¹ [Id.](#) at 5.

⁷² [Id.](#)

⁷³ [Id.](#)

⁷⁴ [Id.](#)

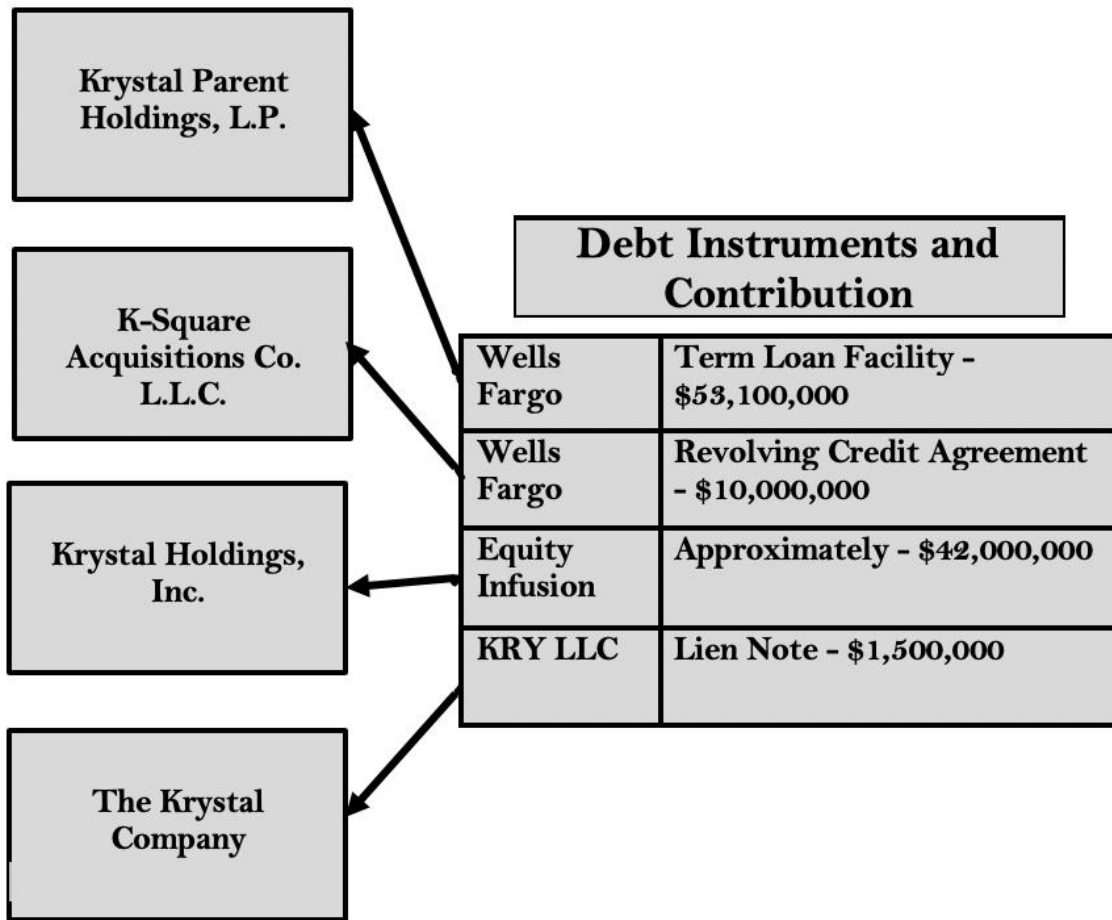
⁷⁵ [Id.](#)

⁷⁶ Krystal Purchased by Argonne Capital Group, LLC, Argonne Capital Group (Mar. 21, 2012), <https://argonnecapital.com/krystal-purchased-by-argonne-capital-group-llc-the-80-year-old-burger-company-held-by-private-equity-investors/> [<https://perma.cc/Y6UF-6746>].

⁷⁷ [Id.](#)

⁷⁸ Declaration of Jonathan Tibus, [17.pdf](#) at 6.

Corporate Structure Diagram



First Day Motions

Initial motions and orders filed with the Bankruptcy court are unique to each case, however, commonalities exist in almost every proceeding. Iterations of case dockets vary yet the filings often depend on “the facts of the case, the needs of the debtor, and the willingness of the court to enter such orders.”⁷⁹ The name “First Day Motions” is somewhat misleading as these filings often span over the course of a week or so and are instrumental in setting the foundation for which the entirety of the case will be built. The Federal Rules of Bankruptcy Procedure governs these motions under Federal Rules of Bankruptcy Procedure §4001 and §6001.⁸⁰ Generally speaking, the most significant requirement of these rules resides in §4001 which mandates a minimum 14-day gap between the service of the motion and a final hearing.⁸¹ The following analysis seeks to cut through the legal jargon and present the objectives of material filings in understandable language.

⁷⁹ Michael L. Bernstein & George W. Kuney, *Bankruptcy In Practice* 290 (forthcoming 2022).

⁸⁰ Fed. R. Bankr. P. 4001; Fed. R. Bankr. P. 6001.

⁸¹ Fed. R. Bankr. P. 4001.

Orders Facilitating Administration of the Estate

The Krystal Company and its affiliates filed voluntarily on January 19, 2020.⁸² All three levels of Krystal's corporate structure had generated a growing list of unsatisfied vendors, rent, and operational costs. In the scheduled list of creditors, Krystal listed their thirty largest unsecured debts totaling over \$11 million dollars in unpaid expenses and characterized the last seven of those debts as "undetermined."⁸³

The debtors moved to be designated as a complex Chapter 11 case on January 19, 2020.⁸⁴ In justifying this, they emphasized that the total debt exceeded \$25 million with over 400 interested parties.⁸⁵ The line of creditors, as opposed to customers, was out the door. Filing for complex case treatment is common in Chapter 11 cases. The benefit to Krystal is that complex cases receive expedited consideration for certain first day matters.⁸⁶ On January 20, 2020, the court granted Krystal complex Chapter 11 case treatment.⁸⁷

On January 19, 2020, Krystal Holdings, Inc., The Krystal Company, and K-Square Acquisition Co., LLC, moved for an order directing joint administration of their related cases.⁸⁸ Federal Rule of Bankruptcy Procedure § 1015(b) provides, "If a joint petition or two or more petitions are pending in the same court by or against . . . a debtor and an affiliate, the court may order a joint administration of the estates."⁸⁹ This simply means that the separate Chapter 11 cases would be heard as a single case. Realistically, it would have been impractical to hear the cases separately because a significant portion of the debts were tied to more than one debtor. The court entered an order approving the motion for joint administration on January 22, 2020.⁹⁰

To minimize the impact of filing for Chapter 11 on their internal operations, the Debtors made efforts to allow for their businesses to maintain a steady income to avoid the growth of debt.⁹¹ After being designated as a complex case and obtaining an order of joint administration,

⁸² Krystal Voluntary Petition, [1.pdf](#).

⁸³ *Id.* at 10.

⁸⁴ Notice of Designation of Complex Chapter 11 Case, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [3.pdf](#).

⁸⁵ *Id.*

⁸⁶ *Id.*; Request for Expedited Consideration of Certain First Day Matters, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [19.pdf](#) at 1–2; Order Granting Complex Chapter 11 Bankruptcy Case Treatment and Scheduling First Day Matters, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [20.pdf](#).

⁸⁷ Order Granting Complex Chapter 11 Bankruptcy Case Treatment and Scheduling First Day Matters, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [20.pdf](#).

⁸⁸ Debtors' Emergency Motion for Entry of an Order (I) Directing Joint Administration of Related Chapter 11 Cases and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [4.pdf](#).

⁸⁹ Fed. R. Bankr. P. § 1015(b).

⁹⁰ Order (I) Directing Joint Administration of Related Chapter 11 Cases and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [33.pdf](#).

⁹¹ See Debtors' Emergency Motion For Entry Of Interim And Final Orders (I) Authorizing Debtors to Pay Certain Prepetition Taxes and Related Obligations and (I) Granting Related Relief, In re The Krystal Company, No. 20-

The Krystal Company and their affiliates requested that a consolidated list of creditors or “Creditor Matrix” be utilized as opposed to the typical mailing matrix for each debtor.⁹² The Krystal Company alleged to have in excess of 5,000 potential creditors and other parties in interest which raised a concern that additional creditors would emerge, claiming that they had not received notice.⁹³

61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [9.pdf](#); Debtors’ Emergency Motion for Entry of an Order (I) Authorizing Debtors to Continue Prepetition Insurance and Workers’ Compensation Policies and to Pay Prepetition Premiums and Related Obligations and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [10.pdf](#); Debtors’ Emergency Motion for Entry of an Order (I) Authorizing The Debtors to Honor Prepetition Obligations to Customers and Otherwise Continue Customer Programs in the Ordinary Course of Business and (I) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [11.pdf](#); Debtors’ Emergency Motion for Entry of an Order (I) Authorizing Payment of Prepetition Wages, Payroll Taxes, Certain Employee Benefits, and Related Expenses; (II) Directing Banks to Honor Related Prepetition Transfers; and (III) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [12.pdf](#).

⁹² Debtors’ Emergency Motion for Entry of an Order (I) Authorizing the Debtors to Prepare a Consolidated List Of Creditors in Lieu of Submitting a Formatted Mailing Matrix, File a Consolidated List of the 30 Largest Unsecured Creditors, and Redact Certain Personal Identification Information for Individual Creditors; (II) Approving the Form and Manner of Notifying Creditors of the Commencement of These Chapter 11 Cases and Other Information; and (III) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [5.pdf](#).

⁹³ [Id.](#)

Chapter 11 or Chapter 9 Cases: Consolidated List of Creditors Who Have the 30 Largest Unsecured Claims and Are Not Insiders

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A list of creditors holding the 30 largest unsecured claims must be filed in a Chapter 11 or Chapter 9 case. Include claims which the debtor disputes. Do not include claims by any person or entity who is an insider, as defined in 11 U.S.C. § 101(31). Also, do not include claims by secured creditors, unless the unsecured claim resulting from inadequate collateral value places the creditor among the holders of the 30 largest unsecured claims.

| Name of creditor and complete mailing address, including zip code | Name, telephone number, and email address of creditor contact | Nature of the claim (for example, trade debts, bank loans, professional services, and government contracts) | Indicate if claim is contingent, unliquidated, or disputed | Amount of unsecured claim if the claim is fully unsecured, fill in only unsecured claim amount. If claim is partially secured, fill in total claim amount and deduction for value of collateral or setoff to calculate unsecured claim. | | |
|---|---|---|--|---|---|-----------------|
| | | | | Total claim, if partially secured | Deduction for value of collateral or setoff | Unsecured claim |
| 1 THE TOMBRAS GROUP 620 S. GAY STREET KNOXVILLE, TN 37902 | ATTN: DOOLEY TOMBRAS TITLE: PRESIDENT PHONE: 865-524-5376 EMAIL: DTOMBRAS@TOMBRAS.COM FAX: 865-524-5667 | Trade Payable | | | | \$ 4,223,982.29 |
| 2 US FOODS, INC 9399 WEST HIGGINS ROAD SUITE 500 ROSEMONT, IL 60018 | ATTN: DIRK LOCASCIO TITLE: CHIEF FINANCIAL OFFICER PHONE: 847-232-5800 EMAIL: DIRK.LOCASCIO@USFOODS.COM FAX: 847-729-2345 | Trade Payable | | | | \$ 2,871,146.70 |
| 3 RADIANT SYSTEMS 864 SPRING ST NW ATLANTA, GA 30308 | ATTN: SCOTT SYKES TITLE: HEAD OF CORPORATE COMMUNICATIONS PHONE: 212-589-8428 EMAIL: SCOTT.SYKES@NCR.COM | Trade Payable | | | | \$ 560,053.14 |
| 4 SLM WASTE & RECYCLING SERVICES, INC 5000 COMMERCE DRIVE GREEN LANE, PA 18054 | ATTN: SUSAN DAYWITT TITLE: CHIEF EXECUTIVE OFFICER PHONE: 215-258-7401 EMAIL: SUSAN.DAYWITT@SLMFACILITIES.COM FAX: 215-258-3823 | Trade Payable | | | | \$ 535,021.39 |
| 5 VEREIT 2325 E. CAMELBACK ROAD, 9TH FLOOR PHOENIX, AZ 85016 | ATTN: LAUREN GOLDBERG TITLE: GENERAL COUNSEL PHONE: 602-778-8700 EMAIL: LGOLDBERG@VEREIT.COM | Rent | | | | \$ 366,215.60 |
| 6 UNITED HEALTH CARE 9800 HEALTH CARE LN MINNEAPOLIS, MN 55436 | ATTN: DAVID S. WICHMANN TITLE: CHIEF EXECUTIVE OFFICER PHONE: 866-204-0911 EMAIL: DAVID_S_WICHMANN@UHG.COM | Trade Payable | | | | \$ 300,693.17 |
| 7 ALETHEIA MARKETING & MEDIA LLC 15770 NORTH DALLAS PARKWAY, SUITE 200 DALLAS, TX 75248 | ATTN: CHRIS SCHEMBRI TITLE: CHIEF EXECUTIVE OFFICER PHONE: 972-776-4070 EMAIL: CSICHEMBR1@ALETHEIA-NA.COM FAX: 972-829-9100 | Trade Payable | | | | \$ 278,658.69 |
| 8 MARRIOTT INTERNATIONAL 10400 FERNWOOD ROAD BETHESDA, MD 208170 - AND - SAWGRASS MARRIOTT GOLF RESORT & SPA 1000 PGA TOUR BLVD PONTE VEDRA BEACH, FL 32082 | ATTN: ARNE SORENSON TITLE: CHIEF EXECUTIVE OFFICER PHONE: 214-905-0050 EMAIL: ARNE.SORENSON@MARRIOTT.COM FAX: 301-644-7624 | Trade Payable | | | | \$ 264,422.74 |
| 9 FIREEYE INC 601 MCCARTHY BLVD. MILPITAS, CA 95035 | ATTN: KEVIN MANDIA TITLE: CHIEF EXECUTIVE OFFICER PHONE: 408-324-9046 EMAIL: KEVIN.MANDIA@FIREEYE.COM FAX: 408-321-9818 | Trade Payable | | | | \$ 216,000.00 |
| 10 FLOWERS BAKING COMPANY OF OPELIKA 1919 FLOWERS CIRCLE THOMASVILLE, GA 31757 | ATTN: BRAD ALEXANDER TITLE: CHIEF OPERATING OFFICER PHONE: 229-227-2353 EMAIL: BRAD_ALEXANDER@FLOCORP.COM FAX: 229-225-2646 | Trade Payable | | | | \$ 185,952.44 |
| 11 INTERGRATED GRAPHICS LLC 8800 EAST PLEASANT VALLEY ROAD INDEPENDENCE, OH 44131 | ATTN: BILL BYRNE TITLE: PRESIDENT PHONE: 216-520-480 ext. 3126 EMAIL: BILL.BYRNE@PROFORMA.COM | Trade Payable | | | | \$ 179,130.85 |
| 12 QUATRO FPO SOLUTIONS, LLC 1850 PARKWAY PLACE SE # 1100 MARIETTA, GA 60018 | ATTN: CHARLES HARMORNICK TITLE: PRESIDENT PHONE: 866-622-7011 EMAIL: CHUCK.H@QUATRO.COM | Trade Payable | | | | \$ 152,912.35 |
| 13 MCGUIREWOODS LLP 1230 PEACHTREE STREET, N.E. SUITE 2100 ATLANTA, GA 30309-3534 | ATTN: CHRISTOPHER K GREENE TITLE: PARTNER PHONE: 404-443-5721 EMAIL: CGREENE@MCGUIREWOODS.COM FAX: 404-443-5092 | Trade Payable | | | | \$ 137,232.12 |
| 14 YEXT, INC 1 MADISON AVE 5TH FLOOR NEW YORK, NY 10010 | ATTN: STEVE CAKEBREAD TITLE: CHIEF FINANCIAL OFFICER PHONE: 415-507-8101 EMAIL: SCAKEBREAD@YEXT.COM | Trade Payable | | | | \$ 114,660.00 |
| 15 SNAP TECH IT LLC 1414 W. BROADWAY RD. STE 105 TEMPE, AZ 85285 | ATTN: KARI BICKMORE TITLE: CHIEF EXECUTIVE OFFICER PHONE: 480-553-9967 EMAIL: KBICKMORE@SNAPTECHIT.COM | Trade Payable | | | | \$ 112,694.20 |
| 16 JOHNSON CONTROLS 5757 N. GREEN BAY AVE. P.O. BOX 591 MILWAUKEE, WI 53201 | ATTN: BRIAN STIEF TITLE: CHIEF FINANCIAL OFFICER PHONE: 229-529-9365 EMAIL: BRIAN.STIEF@JCI.COM | Trade Payable | | | | \$ 110,339.60 |

| | Name of creditor and complete mailing address, including zip code | Name, telephone number, and email address of creditor contact | Nature of the claim (for example, trade debts, bank loans, professional services, and government contracts) | Indicate if claim is contingent, unliquidated, or disputed | Amount of unsecured claim if the claim is fully unsecured, fill in only unsecured claim amount. If claim is partially secured, fill in total claim amount and deduction for value of collateral or setoff to calculate unsecured claim. | | |
|----|---|---|---|--|---|---|-----------------|
| | | | | | Total claim, if partially secured | Deduction for value of collateral or setoff | Unsecured claim |
| 17 | CSI OF THE SOUTHEAST INC 110 SKYLINE DRIVE MAYNARDVILLE, TN 37807 | ATTN: JUSTIN SAWYER TITLE: VICE PRESIDENT OF SALES PHONE: 865-805-0344 EMAIL: JSAWYER@CSISE.COM FAX: 865.992.7169 | Trade Payable | | | | \$ 109,529.04 |
| 18 | STRATEGIC EQUIPMENT AND SUPPLY 2801 SOUTH VALLEY PARKWAY, STE. 200 LEWISVILLE, TX 75067 | ATTN: MARTY MONNAT TITLE: CHIEF EXECUTIVE OFFICER PHONE: 972-401-5300 EMAIL: MMONNAT@STRATEGICEQUIPMENT.COM FAX: 469-240-7202 | Trade Payable | | | | \$ 105,177.97 |
| 19 | REPUBLIC SERVICES NATIONAL ACCOUNTS, LLC 18500 N ALLEED WAY PHOENIX, AZ 85054 | ATTN: JON VANDER ARK TITLE: PRESIDENT EMAIL: JON.ARK@REPUBLICSERVICES.COM | Trade Payable | | | | \$ 101,633.01 |
| 20 | HALO BRANDED SOLUTIONS, INC 1500 HALO WAY STERLING, IL 61081 | ATTN: MARC SIMON TITLE: CHIEF EXECUTIVE OFFICER PHONE: 212-695-9800 EMAIL: MARC.SIMON@HALO.COM FAX: 815-632-6900 | Trade Payable | | | | \$ 101,374.70 |
| 21 | RAGONA ARCHITECTURE & DESIGN PLLC 145 SCALEYBARK RD A CHARLOTTE, NC 28209 | ATTN: MATT RAGONA TITLE: PRINCIPAL PHONE: 704-943-9091 EMAIL: MRAGONA@RAD-ARCH.COM | Trade Payable | | | | \$ 87,812.61 |
| 22 | DTT SURVEILLANCE 111 SPEEN STREET #550 FRAMINGHAM, MA 01701 | ATTN: MIKE COFFEY TITLE: CHIEF EXECUTIVE OFFICER PHONE: 617-949-8900 EMAIL: MIKE@DTTQ.COM | Trade Payable | | | | \$ 86,169.01 |
| 23 | HORIZON RIVER TECHNOLOGIES, LLC 3340 PEACHTREE ROAD NE SUITE 2600 ATLANTA, GA 30326 | ATTN: JEF WALLACE TITLE: CHIEF EXECUTIVE OFFICER PHONE: 404-662-2216 EMAIL: JEF.WALLACE@HORIZONRIVER.COM | Trade Payable | | | | \$ 83,430.50 |
| 24 | AR GLOBAL 650 FIFTH AVENUE NEW YORK, NY 10019 | ATTN: KATIE KURTZ TITLE: CHIEF FINANCIAL OFFICER PHONE: 212-415-6500 EMAIL: KATIE.KURTZ@AR-GLOBAL.COM | Rent | Contingent & Unliquidated | | | \$ 57,602.45 |
| 25 | PREFERRED PREMIUM PROPERTIES, LLC 125 BRAZILIAN AVENUE PALM BEACH, FL 33480 | ATTN: BAGBY MEREDITH TITLE: VICE PRESIDENT PHONE: 561-655-9510 EMAIL: MEREDITHBAGBY@GMAIL.COM FAX: 561-655-6495 | Rent | Contingent & Unliquidated | | | \$ 56,916.82 |
| 26 | WANDA COLLINS ADDRESS ON FILE | PHONE: ON FILE | General Liability Claim | Contingent, Unliquidated & Disputed | | | Undetermined |
| 27 | ROBIN HOBBS ADDRESS ON FILE | PHONE: ON FILE | General Liability Claim | Contingent, Unliquidated & Disputed | | | Undetermined |
| 28 | REALTY INCOME, LP 11995 EL CAMINO REAL SAN DIEGO, CA 92139 | ATTN: SUMIT ROY TITLE: CHIEF EXECUTIVE OFFICER PHONE: 877-219-2434 EMAIL: SROY@REALTYINCOME.COM | Rent | Contingent & Unliquidated | | | Undetermined |
| 29 | STORE CAPITAL CORP/STORE MASTER FUNDING I, LLC 8377 E. HARTFORD DR. SUITE 100 SCOTTSDALE, AZ 85255 | ATTN: CHRISTOPHER H. VOLK TITLE: CHIEF EXECUTIVE OFFICER PHONE: 480-256-1100 EMAIL: CHRIS@STORECAPITAL.COM FAX: 480-256-1101 | Rent | Contingent & Unliquidated | | | Undetermined |
| 30 | PENSION BENEFIT GUARANTY CORPORATION 1200 K STREET, N.W. SUITE 540 WASHINGTON, DC 20005-4026 | ATTN: PATRICIA KELLY TITLE: CHIEF FINANCIAL OFFICER PHONE: 703-449-0461 EMAIL: KELLY.PATRICIA@PBGC.GOV FAX: 202-326-4112 | Pension | Contingent, Unliquidated & Disputed | | | Undetermined |

Note: Unsecured amounts contain projected estimates of pre-petition liability as of the Petition Date and are subject to change as accrued liabilities become invoiced.

Day to Day Operations

Motion Authorizing use of Pre-Petition Bank Accounts

To kick off the substantive filings outside of schedules and applications to retain professionals, Krystal's first move was to secure funds in an effort to keep their brick-and-mortar business open. In a motion to continue use of prepetition bank accounts, The Krystal Company described its cash management structure.⁹⁴ According to the motion, store level depository accounts were used by each restaurant primarily through Wells Fargo or Regions Bank to take in payments through the franchises via sales.⁹⁵ These accounts paid into a funding account twice a week that was used for operating costs to satisfy debts incurred on the franchise level.⁹⁶ The funding account was described as having a disbursement account within it, which paid out of the

⁹⁴ Debtors' Emergency Motion for Entry of an Order (I) Authorizing Continued Use of Prepetition Bank Accounts, Cash Management System, Forms, and Books and Records and (Ii) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [8.pdf](#) [hereinafter Bank Accounts Motion].

⁹⁵ *Id.* at 3.

⁹⁶ *Id.* 3-4.

profits to the company.⁹⁷ This account dynamic was used by every store and overseen by the Krystal Parent Holdings.

Additionally, Krystal Holdings utilized this same account structure.⁹⁸ Through Regions Bank and Wells Fargo, Krystal Holdings operated depository accounts that received transfers from a funding account that their subsidiaries and franchisees paid into.⁹⁹ In practice, these depository accounts were aimed at keeping a zero balance. These deposits tracked who was paying their obligations to Krystal Holdings and assisted in itemizing where the funds were coming and who payments were being made to. The company also reported an estimated \$55,000 in unpaid bank fees that were accrued in day-to-day operations including negative balances.¹⁰⁰ These miscellaneous accounts were also used to fund and receive payments on customer programs such as gift cards that are paid directly to the parent company.¹⁰¹

Utilities Motion

On January 20, 2020, Krystal filed an Emergency Motion for Interim and Final Orders Prohibiting Utilities from Altering, Refusing, or Discontinuing Service on Account of Prepetition Invoices.¹⁰² Utilities are addressed in the Bankruptcy Code under §366(a).¹⁰³ This rule states in part:

[A] utility may not alter, refuse, or discontinue service to, or discriminate against, the trustee or the debtor solely on the basis of the commencement of a case under this title or that a debt owed by the debtor to such utility for service rendered before the order for relief was not paid when due.¹⁰⁴

The provision goes on to state that the debtor must provide adequate assurance of payment to secure the non-cancellation of these utility services.¹⁰⁵ Without this filing, the Debtors would be forced to close their locations if they were unable to prove they had sufficient maintenance funds.

⁹⁷ [*Id.*](#)

⁹⁸ [*Id.*](#)

⁹⁹ [*Id.*](#)

¹⁰⁰ [*Id.*](#)

¹⁰¹ See [*id.*](#) at 4 (“[A] corporate gift card account in which the Debtors receive the proceeds from all gift card sales.”).

¹⁰² Debtors’ Emergency Motion for Entry of Interim and Final Orders (I) Prohibiting Utilities from Altering, Refusing, or Discontinuing Service on Account of Prepetition Invoices; (II) Deeming Utilities Adequately Assured of Future Performance; (III) Establishing Procedures for Determining Adequate Assurance of Payment; and (IV) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [14.pdf](#) [hereinafter Utilities Motion].

¹⁰³ 11 U.S.C. § 366(a).

¹⁰⁴ [*Id.*](#)

¹⁰⁵ [*Id.*](#)

In this motion, Krystal identified the open utilities accounts listed below; however, the company failed to mention the substantiality of the debts incurred by monthly operations. The debtor identified that over 230 utility servicers provide natural gas, electricity, water, sewage, waste management, and phone services to their locations.¹⁰⁶ The motion noted in general that Krystal had established satisfactory payment history with these servicers listing no material defaults as represented in their three most substantial utilities accounts listed below.¹⁰⁷ Krystal provided adequate assurances to these servicers amounting to \$299,000 currently residing in a checking account that would be sufficient to pay these monthly charges.¹⁰⁸

| <u>Utility</u> | <u>No. of Accts.</u> | <u>Estimated Prepet. Debt</u> | <u>Deposit Request</u> |
|-----------------------|-----------------------------|--------------------------------------|-------------------------------|
| FPL | 7 | \$7,365.11 | \$21,247 (2-month) |
| Georgia Power | 99 | \$not yet available | \$303,231 (2-month) |
| OUC | 1 | \$not yet available | \$20,600 (2-month) |

Florida and Georgia disagreed. Out of fear that the court would authorize Krystal to continue their services with them, the utility companies sought to cut ties with the debtor.¹⁰⁹ In their Objection to the Utilities Motion, the companies noted that Krystal had an average utility cost of \$987,000 monthly and that the open bank account was insufficient to cover this amount.¹¹⁰ Section 366(c) of the Federal Bankruptcy Code addresses utilities when a company files for bankruptcy.¹¹¹ Accordingly, a debtor must provide adequate assurances that the utility obligations will be paid in order to maintain their use.¹¹² Here, the utility companies identified that the \$299,000 bank account was not sufficient in providing adequate assurances of payment.¹¹³ Specifically:

366(c)(1)(A) defines the forms that assurance of payment may take as follows:

- (i) a cash deposit;
- (ii) a letter of credit;
- (iii) a certificate of deposit;

¹⁰⁶ Utilities Motion, [14.pdf](#) at 3.

¹⁰⁷ *Id.* at 4.

¹⁰⁸ Utilities Motion, [14.pdf](#) at 6.

¹⁰⁹ Objection Of Florida Power & Light Company, Georgia Power Company, and Orlando Utilities Commission to the Debtors' Emergency Motion for Entry of Interim and Final Orders (I) Prohibiting Utilities from Altering, Refusing, or Discontinuing Service on Account Of Prepetition Invoices; (II) Deeming Utilities Adequately Assured Of Future Performance; (III) Establishing Procedures For Determining Adequate Assurance Of Payment; And (IV) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [91.pdf](#) [hereinafter Withdrawn Objection to Utilities Motion].

¹¹⁰ *Id.* at 5.

¹¹¹ 28 U.S.C. § 366(c)(1)(A).

¹¹² *Id.*

¹¹³ Withdrawn Objection to Utilities Motion, [91.pdf](#) at 2–3.

- (iv) a surety bond;
- (v) a prepayment of utility consumption.¹¹⁴

Notably, a bank account is excluded from this list of possible assurances of payment. Additionally, the power companies were not informed of the bank account prior to the filing of this motion. Instead, Krystal went over these creditors' heads and sought to secure their utilities by court order without consulting the power companies. After this objection was filed, there seemed to be a lapse in time with no response from Krystal. Ultimately, the court docket indicates that the parties reached an agreement that addressed the adequate assurance concerns because the objection was later withdrawn.¹¹⁵

On February 5, 2020, the court entered an interim order that prohibited the utility companies from discontinuing their services. The interim order included more agreeable language that was not present in the original motion. Under this order, if Krystal failed to pay beyond the applicable grace period, these providers could request a disbursement from the adequate assurances account by giving notice to all interested parties.¹¹⁶ Until the court entered a final order, the utility companies were not to discontinue services for any unpaid amounts prior to January 19, 2020. However, if the Debtors failed to bring their account current or resolve any dispute arising from a payment default for periods after January 19, 2020, the power company was to be entitled to discontinue services.¹¹⁷ The additional terms remedied the power companies' adequate assurance concerns and the objection was withdrawn on February 10, 2020.¹¹⁸ On February 13, 2020, the court entered a final order that continued the terms of the interim order.¹¹⁹

¹¹⁴ 28 U.S.C. § 366(c)(1)(A).

¹¹⁵ *Withdrawal of Document Objection of Florida Power & Light Company, Georgia Power Company, and Orlando Utilities Commission to the Debtors' Emergency Motion for Entry of Interim and Final Orders (I) Prohibiting Utilities from Altering, Refusing, or Discontinuing Service on Account of Prepetition Invoices; (II) Deeming Utilities Adequately Assured of Future Performance; (III) Establishing Procedures for Determining Adequate Assurance of Payment; and (IV) Granting Related Relief*, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [140.pdf](#); see *Withdrawn Objection to Utilities Motion*, [91.pdf](#).

¹¹⁶ *Interim Order (I) Prohibiting Utilities from Altering, Refusing, or Discontinuing Service on Account of Prepetition Invoices; (II) Deeming Utilities Adequately Assured of Future Performance; (III) Establishing Procedures for Determining Adequate Assurance of Payment; and (IV) Granting Related Relief*, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [120.pdf](#).

¹¹⁷ *Id.* at 5.

¹¹⁸ *Withdrawal of Document Objection of Florida Power & Light Company, Georgia Power Company, and Orlando Utilities Commission to the Debtors' Emergency Motion for Entry of Interim and Final Orders (I) Prohibiting Utilities from Altering, Refusing, or Discontinuing Service on Account of Prepetition Invoices; (II) Deeming Utilities Adequately Assured of Future Performance; (III) Establishing Procedures for Determining Adequate Assurance of Payment; and (IV) Granting Related Relief*, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [140.pdf](#); see *Withdrawn Objection to Utilities Motion*, [91.pdf](#).

¹¹⁹ *Final Order Prohibiting Utilities from Altering, Refusing or Discontinuing Service on Account of Prepetition Invoices and Establishing Procedures for Determining Adequate Assurance of Payment*, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [159.pdf](#).

Waiver of US Trustee's Guidelines

In a bankruptcy proceeding of a company, The Office of the U.S. Trustee has established operating guidelines that require a company to close all of its bank accounts and accounting books.¹²⁰ Following this, the company would open new books with the funding accrued in previous accounts with the account holder listed as a debtor in possession.¹²¹ This guideline was apparently burdensome to the company, as they requested that the trustee's office waive these guidelines and allow for their continued operations as is.¹²² To justify this, the company claimed to have advanced computerized record keeping systems that would allow the court to ensure that all prepetition and post-petition transactions to be accounted for properly and easily distinguishable.¹²³ Citing sections 1107(a) and 1108 of the Federal Bankruptcy Code, a debtor in possession, operating its business pursuant to the above cited statutes, may use property of the estate in the ordinary course of business without notice or a hearing.¹²⁴

Despite Krystal's rocky track record in banking, the court agreed. In an order allowing for the continued ordinary course of business for the company, the court allowed for the above requested relief.¹²⁵ The court recognized that the law would allow for Krystal to maintain ownership and operations of their day-to-day business accounts.¹²⁶ However, there was a twist; Krystal Holdings and their subsidiaries were no longer to operate with bank accounts "in the red."¹²⁷ If a payment was necessary to come out of one of the above-described accounts it could not be on the bank's dime. Any post-petition payments would have to be made with readily available funds and negative balances were not permitted.¹²⁸

During the court hearing, the US Trustee's office raised only one issue in connection to the waiver of their guidelines. In the original motion, there was language included that these bank accounts would be used to pay prepetition debts in its own discretion. The Trustee's Office moved to have this language stricken from the order as there was a fear that this supported the contention that Krystal would be under no obligation to use this money management system to pay back the claims they had just represented would be paid. The judge amended the order and removed this language.

¹²⁰ 28 U.S.C. § 581.

¹²¹ Bank Accounts Motion, [8.pdf](#) at 6–8.

¹²² *Id.*

¹²³ See *id.*

¹²⁴ 11 U.S.C. §§ 1107(a) and 1108

¹²⁵ Interim Order (I) Authorizing Continued Use of Prepetition Bank Accounts, Cash Management System, Forms, and Books and Records And (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [48.pdf](#).

¹²⁶ *Id.* at 2–4.

¹²⁷ *Id.* at 3 (stating that all manual and automatic debits from the Debtors' account are subject to court approval in the cash collateral motion, which in effect disallows a negative balance).

¹²⁸ *Id.*

Cash Collateral Motion

Under its prepetition Forbearance Agreement, Krystal was to work in good faith with the secured creditors to finalize debtor-in-possession financing (“DIP Financing”) under section 364.¹²⁹ However, 48 hours before filing the Chapter 11 case, Krystal notified Wells Fargo that they would be rejecting the DIP Financing offer and would instead seek to self-fund the Chapter 11 case through use of cash collateral.¹³⁰ Section 363(c)(2) provides that a debtor may use, sell, or lease cash collateral if the secured creditors consent or if, after notice and a hearing, the court authorizes the use of cash collateral.¹³¹ Further, section 363(e) provides that a court may prohibit or condition the use of cash collateral “as is necessary to provide adequate protection” of the secured creditor’s interest.¹³²

On January 20, 2020, Krystal filed a motion requesting authorization to use cash collateral, granting adequate protection to lenders, and modifying the automatic stay.¹³³ Krystal requested to use the full amount of cash collateral and stated it was necessary to “stabilize their operations, and pay for ordinary, postpetition operating expenses approved in the first-day orders, to minimize the damage occasioned by their cash flow problems.”¹³⁴ Krystal stated that without the use of cash collateral, they would be unable to pay operating expenses which would harm all parties.¹³⁵

Krystal also requested an interim hearing to consider the Cash Collateral Motion.¹³⁶ They relied on the exceptions to Federal Rules of Bankruptcy Procedure 4001 and 6001 which permit a court to grant motions before the 14- and 21-day periods “as is necessary to avoid immediate and irreparable harm to the estate pending a final hearing.”¹³⁷

¹²⁹ Wells Fargo Bank, National Associations (I) Objection to Debtors Emergency Motion for Entry of Interim and Final Orders (1) Authorizing the Debtors to Use Cash Collateral; (2) Granting Adequate Protection to Lenders; (3) Modifying the Automatic Stay; (4) Scheduling a Final Hearing; and (5) Granting Related Relief; (II) Limited Objection to Certain First Day Relief; And (III) Request for Adequate Protection, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [28.pdf](#) at 2 [hereinafter Wells Fargo Cash Collateral Objection].

¹³⁰ *Id.*

¹³¹ 11 U.S.C. § 362(c)(2).

¹³² 11 U.S.C. § 362(e).

¹³³ Debtor’s Emergency Motion for Entry of Interim and Final Orders (1) Authorizing the Debtors to Use Cash Collateral; (2) Granting Adequate Protection to Lenders; (3) Modifying the Automatic Stay; (4) Scheduling a Final Hearing; and (5) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [18.pdf](#) [hereinafter Cash Collateral Motion].

¹³⁴ *Id.* at 8.

¹³⁵ *Id.* at 8–9.

¹³⁶ *Id.* at 9.

¹³⁷ Fed. R. Bankr. P. 4001 and 6001.

Krystal filed a Proposed Budget for the use of cash collateral.¹³⁸ The Proposed Budget was for the weeks of January 26, February 2, and February 9 of 2020.¹³⁹ The total projected net cash flow for the three weeks after accounting for Chapter 11 expenses was \$862,000.¹⁴⁰ The Proposed Budget is provided below.

¹³⁸ Notice of Filing Proposed Budget in Connection with Debtors Emergency Motion for Entry of Order Authorizing the Debtors to Use Cash Collateral, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [29.pdf](#).

¹³⁹ *Id.* at Ex. A.

¹⁴⁰ *Id.*

The Krystal Company
Weekly Cash Flow Forecast
Cash Collateral Budget

| Projected Week Week Ending | 1 1/26/2020 | 2 2/2/2020 | 3 2/9/2020 | Total |
|---|----------------|----------------|----------------|----------------|
| Operating Receipts | | | | |
| Restaurant Receipts | \$ 3,909 | \$ 4,305 | \$ 4,305 | \$ 12,519 |
| Franchisee and Royalty Receipts | 114 | 40 | 126 | 280 |
| Other Receipts | - | - | - | - |
| Total Operating Receipts | 4,024 | 4,345 | 4,431 | 12,799 |
| Operating Disbursements | | | | |
| Payroll & Benefits | 2,036 | 1,232 | 1,985 | 5,252 |
| G&A (Non-Payroll) | 113 | 111 | 111 | 335 |
| Food & Paper Costs | 85 | 85 | 85 | 255 |
| Marketing Costs | 202 | 202 | 202 | 606 |
| Sales Taxes | 1,500 | - | - | 1,500 |
| Restaurant Operating Expenses | 638 | 608 | 608 | 1,854 |
| Occupancy | - | - | 1,701 | 1,701 |
| Total Operating Disbursements | 4,574 | 2,238 | 4,692 | 11,504 |
| Operating Cash Flow | (550) | 2,107 | (262) | 1,295 |
| Non-Operating Disbursements/(Receipts) | | | | |
| Independent Director Fees | - | - | 8 | 8 |
| Total Non-Operating Disbursements/(Receipts) | - | - | 8 | 8 |
| Net Cash Flow | (550) | 2,107 | (269) | 1,287 |
| Chapter 11 Related Cash Flows | | | | |
| Utility Deposits into Escrow | - | - | 325 | 325 |
| Vendor Support Fees | 100 | - | - | 100 |
| Debtor Professional Fees | - | - | - | - |
| Other Professional Fees | - | - | - | - |
| US Trustee Fees | - | - | - | - |
| Total Chapter 11 Related Cash Flows | 100 | - | 325 | 425 |
| Net Cash Flow | (650) | 2,107 | (594) | 862 |
| Beginning Book Cash | 2,000 | 1,350 | 3,457 | 2,000 |
| Change in Cash | (650) | 2,107 | (594) | 862 |
| Ending Book Cash | \$1,350 | \$3,457 | \$2,862 | \$2,862 |

Wells Fargo filed an objection to the Cash Collateral Motion, certain other first day relief, and the Motion for Adequate Protection.¹⁴¹ Wells Fargo stated that Krystal and the prepetition secured creditors were in agreement that the goal of the Chapter 11 case would be a section 363 sale to maximize value for all parties.¹⁴² However, Wells Fargo was still upset about Krystal foregoing DIP financing under section 364 of the Federal Bankruptcy Code as had been argued upon in the prepetition Forbearance Agreement.¹⁴³

Wells Fargo's primary reason for objecting was because the self-funding through cash collateral was achieved by delaying payments to US Foods, Krystal's largest vendor, and withholding adequate protection payments from the prepetition secured creditors.¹⁴⁴ Wells Fargo was concerned that using cash collateral would not provide adequate financing to sustain operations until the company could achieve a section 363 sale nor provide the secured creditors adequate protection.¹⁴⁵ Wells Fargo was not satisfied with Krystal's assertion that the secured creditors would have adequate protection.¹⁴⁶ Specifically, Wells Fargo contended that the Proposed Budget showed that prepetition cash would be depleted without a dollar-for-dollar replacement.¹⁴⁷ Thus, Wells Fargo argued that tangible adequate protection should be provided, otherwise, junior creditors would be paid with cash in which it had a security interest.¹⁴⁸

Ultimately, the court granted an interim order, authorizing Krystal to use cash collateral on January 22, 2020.¹⁴⁹ The court provided adequate protection to the secured creditors by granting perfected replacement liens and adequate protection claims.¹⁵⁰ The replacement liens were to be second only to security interests and liens in existence on the petition date and the adequate protection claims were to be superpriority administrative expenses provided for by Section 507(b).¹⁵¹

On February 27, 2020, Krystal's Official Committee of Unsecured Creditors objected to the Cash Collateral Motion.¹⁵² The objection pointed out Krystal's deficiencies in its filings. The

¹⁴¹ Wells Fargo Cash Collateral Objection, [28.pdf](#).

¹⁴² *Id.* at 2.

¹⁴³ *Id.*

¹⁴⁴ *Id.*

¹⁴⁵ *Id.* at 3.

¹⁴⁶ *Id.*

¹⁴⁷ *Id.* at 11.

¹⁴⁸ *Id.*

¹⁴⁹ Interim Order (1) Authorizing the Debtors to Use Cash Collateral, (2) Granting Adequate Protection to Lenders, (3) Modifying the Automatic Stay, and (4) Providing Notice of Second Interim Hearing, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [39.pdf](#).

¹⁵⁰ *Id.* at 4–5.

¹⁵¹ *Id.*; 11 U.S.C. § 507(b).

¹⁵² Link to part of paper that introduces creditors' committee. Limited Objection of the Official Committee of Unsecured Creditors to Debtors Emergency Motion for Entry of Interim and Final Orders (1) Authorizing the Debtors to Use Cash Collateral; (2) Granting Adequate Protection to Lenders; (3) Modifying The Automatic Stay; (4) Scheduling a Final Hearing; and (5) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [197.pdf](#) [hereinafter Creditors' Committee Cash Collateral Objection].

motion stated that the Debtors' professionals were slated to receive \$2.9 million while the committee's professionals were only allocated \$675,000.¹⁵³ The Official Committee of Unsecured Creditors expressed concerns that a 363 sale would not result in sufficient proceeds to pay all administrative expenses.¹⁵⁴ They noted that Krystal had not marketed the assets or identified prospective bidders.¹⁵⁵ Additionally, the committee argued that the adequate protection for the secured creditors enhanced their position and should be limited.¹⁵⁶ On March 3, 2020, the court entered another interim order authorizing the use of cash collateral which did not comport to the committee's requests.¹⁵⁷

On March 31, 2020, the committee filed a reservation of rights regarding the cash collateral motion.¹⁵⁸ The thrust of the motion was that the committee believed that the budget did not allocate a fair amount for their professional fees.¹⁵⁹ The motion stated that the Debtors' professionals were allocated \$1,891,608 and the committee's professionals were only allocated \$494,000 until for the periods February 1 to May 17, 2020.¹⁶⁰ They also stated that from the petition date to May 17, 2020, Krystal's professionals would have received \$2,424,539 which equaled 83.1% of the total budget for professional fees.¹⁶¹ A residual 20% of the fees for February 1 to May 17, 2020 were reserved for the facilitation and payment of representation for this creditors committee who pointed out the disparate treatment.¹⁶² In response the committee sought to make their allocation closer to the customary 40% frequently used in other cases.¹⁶³ For relief there they ultimately request 35% of the budget be allocated to sufficiently represent the interests of the unsecured creditors.¹⁶⁴ The motion included a reservation of rights but it appears they never exercised it.

¹⁵³ *Id.* at 9.

¹⁵⁴ *Id.* at 10.

¹⁵⁵ *Id.*

¹⁵⁶ *Id.* at 12.

¹⁵⁷ See generally Third Interim Order Authorizing the debtors to use Cash Collateral, Granting Adequate Protection to Prepetition Secured Parties, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [218.pdf](#).

¹⁵⁸ Reservation of Rights of the Official Committee of Unsecured Creditors to Debtors' *Emergency Motion for Entry of Interim and Final Orders (1) Authorizing the Debtors to Use Cash Collateral; (2) Granting Adequate Protection to Lenders; (3) Modifying the Automatic Stay; (4) Scheduling a Final Hearing; and (5) Granting Related Relief*, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [299.pdf](#).

¹⁵⁹ See *id.*

¹⁶⁰ *Id.* at 2.

¹⁶¹ *Id.* at 3.

¹⁶² *Id.* at 2–3.

¹⁶³ *Id.* at 3–4.

¹⁶⁴ *Id.* at 4.

Substantive Motions

Motion Authorizing Payment of Prepetition Wages, Payroll Taxes, Certain Employee Benefits and Related Expenses

From a risk management standpoint, it is a purely “business move” to avoid obligations to pay when the money is simply not there. In a bankruptcy proceeding, section 503 of the Federal Bankruptcy Code governs this issue and provides that an entity may request to make a payment for an administrative expense after a filing with the court was made.¹⁶⁵ This section takes the option out of the debtor's hand and leaves it up to the judge to determine if these debts were to be paid.¹⁶⁶ These debts include: wages, salaries, employee benefits, taxes, etc. and is common practice for restructuring companies.¹⁶⁷ However, based on their filing history, requesting authority but not direction does not make them a sympathetic debtor.¹⁶⁸

Although the court allowed the Debtors to continue operations without an obligation to reduce their existing debt, this permission was not open ended.¹⁶⁹ This order authorizing the continuance of business operations is subject to the order granting cash collateral.¹⁷⁰ Specifically, the subsequent order stated in part:

The Debtors are authorized to use Cash Collateral until the conclusion of the second interim hearing on the Motion, solely in accordance with and pursuant to the terms and provisions of this Order and only to the extent required to pay the expenses necessary to avoid immediate and irreparable harm to the estate and contained in the Budget.¹⁷¹

Operatively, any order discussed below is subject to the cash collateral order. If the court learned that the Debtors were engaged in harmful or deceptive payment practices, it would have modified the terms of the cash collateral order at a later hearing.¹⁷²

¹⁶⁵ 11 U.S.C. § 503.

¹⁶⁶ *Id.*

¹⁶⁷ *Id.*

¹⁶⁸ Order (I) Authorizing Debtors to Continue Prepetition Insurance and Workers Compensation Policies and to Pay Prepetition Premiums and Related Obligations and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [37.pdf](#) (discussing Krystal’s request to receive operation of their bank accounts with no obligation to use them in good faith of the employees in accordance with their justifications in filing the motion).

¹⁶⁹ See Interim Order (I) Authorizing Continued Use of Prepetition Bank Accounts, Cash Management System, Forms, And Books And Records And (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [48.pdf](#) (stating that all manual and automatic debits from the Debtors’ account are subject to court approval in the cash collateral motion which In effect disallows a negative balance).

¹⁷⁰ See Interim Order (1) Authorizing the Debtors to Use Cash Collateral, (2) Granting Adequate Protection To Lenders, (3) Modifying the Automatic Stay, and (4) Providing Notice of Second Interim Hearing, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [39.pdf](#).

¹⁷¹ *Id.* at 6.

¹⁷² See *id.* at 2–3.

Employee Obligations

At the time of filing The Krystal Company reported to have approximately 4,890 employees, 55 of whom work within a corporate office in Dunwoody, Georgia.¹⁷³ 291 of those employees were full-time salary, 743 were full-time hourly, and 3,856 were part-time hourly.¹⁷⁴ Additionally, the Debtor claims to contract with six independent contractors.¹⁷⁵ The Debtors claim that through the ordinary course of business they have incurred prepetition operational debts.¹⁷⁶ These debts are listed as: wages, salaries and other compensation, payroll taxes, sick and vacation programs, 401(k) plans, and health and welfare benefits.¹⁷⁷ Krystal's debt matrix shows that there was only \$1,482,000 debt tied to payroll obligations.¹⁷⁸ Although that is a large number, it is small relative to debts owed to the secured creditors.

401k Obligations

In more detail, Krystal made a first day motion to allow use of cash collateral to uphold their 401k contributions to their employees. Specifically, Krystal's employees contracted to have a 100% match of up to 100% of their paycheck contributed to their 401k.¹⁷⁹ Krystal wanted to protect these employees and incentivize them not to give up during its restructuring.¹⁸⁰

Of the 4,890 employees currently working for Krystal Holdings, 261 were part of the payment plan.¹⁸¹ Of those employees the company withheld and remitted \$28,320 every two weeks for 401(k) contributions and \$14,069 in payments matching those contributions.¹⁸² At the time of filing, Krystal claimed to owe approximately \$3,400 in unpaid 401(k) Loan Withholdings to Fidelity Bank.¹⁸³ Krystal requested authority, not the obligation, to make these payments.¹⁸⁴

While the 401(k) analysis is not as material as other filings in terms of the overarching narrative of this bankruptcy proceeding, it demonstrates Krystal's intention for their first day motions. As an actively operating company, Krystal sought to maintain current operations

¹⁷³ Debtors' Emergency Motion for Entry of an Order (I) Authorizing Payment of Prepetition Wages, Payroll Taxes, Certain Employee Benefits, and Related Expenses; (II) Directing Banks to Honor Related Prepetition Transfers; and (III) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [12.pdf](#) at 2 [hereinafter Employee Wages and Benefits Motion].

¹⁷⁴ [Id.](#)

¹⁷⁵ [Id.](#)

¹⁷⁶ [Id.](#) at 3.

¹⁷⁷ [Id.](#) at 3–8.

¹⁷⁸ [Id.](#) at 5.

¹⁷⁹ [Id.](#)

¹⁸⁰ See generally Cash Collateral Motion, [18.pdf](#).

¹⁸¹ Employee Wages and Benefits Motion, [12.pdf](#) at 5.

¹⁸² [Id.](#)

¹⁸³ [Id.](#)

¹⁸⁴ [Id.](#) at 6.

without interruption. Additionally, their attempts at avoiding judicial directive over every aspect of their payment obligations is worthy of remark.¹⁸⁵

Tax Obligations

In Krystal's declaration, the company reported to have approximately \$2,786,000 in sales and use tax, \$10,000 in franchise tax, \$290,273 in administrative payroll taxes, and \$1,342,505 in operating payroll taxes; all amounts were accrued over the six months prior to filing the Chapter 11 case.¹⁸⁶ At the time of filing, these debts were unpaid. Failure to pay these taxes would result in heavy penalties and assessments against the company should these claims be determined non-dischargeable.¹⁸⁷ Had the debtor not requested authority to make these payments, facing an aggregate tax bill of over \$4 million could drain the operating accounts and result in substantial harm to the company.

Gift Card Obligations

As part of the motion to honor prepetition customer obligations, the Debtors requested authorization to honor their gift card program.¹⁸⁸ Even though a debtor would not want to irritate their creditors, it was also understandable that Krystal had a heightened interest in not upsetting their customers. Specifically, there was a concern that failing to secure authorized use of their bank accounts would potentially freeze their gift card program.¹⁸⁹ As mentioned above, gift card payments are made directly to the parent company's funding account and flow through to their disbursement account.¹⁹⁰

Effectively, this was a ticking time bomb of debt. However, freezing access to pay for the lost funds to the franchisees from gift card transactions would raise concern about the intent of Krystal.¹⁹¹ At the time of filing, Krystal reported to have \$435,000 of outstanding gift card obligations.¹⁹² Here, Krystal had a choice; suffer the consequences of turning away customers with validly purchased gift cards as they had no access to the funds tied to them, or they could seek court authority to honor these gift card obligations post-petition. The Debtor chose the latter

¹⁸⁵ Order (I) Authorizing Debtors to Continue Prepetition Insurance and Workers Compensation Policies and to Pay Prepetition Premiums and Related Obligations and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [37.pdf](#) at 2 (“The Debtors are authorized, but not required, to maintain the Insurance Policies, and to pay any prepetition or post-petition obligations related to the Insurance Policies, including Brokerage fees, insurance deductibles, and any other amounts related thereto.”).

¹⁸⁶ Declaration of Jonathan Tibus, [17.pdf](#) at 17, 33–34.

¹⁸⁷ See 11 U.S.C. § 522 (listing exemptions to dischargeable debt including federal liens resulting from unpaid tax debt).

¹⁸⁸ Debtors' Emergency Motion for Entry of an Order (I) Authorizing the Debtors to Honor Prepetition Obligations to Customers and Otherwise Continue Customer Programs in the Ordinary Course of Business and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [11.pdf](#) at 3–4 [hereinafter Customer Obligations Motion].

¹⁸⁹ *Id.*

¹⁹⁰ Bank Accounts Motion, [8.pdf](#) at 6–8.

¹⁹¹ See generally Customer Obligations Motion, [11.pdf](#).

¹⁹² *Id.*

course, moving the court for authorization to honor outstanding gift cards. Notably, there were no objections to this section of the motion. In the following order granting this relief, the court upheld Krystal's authority to honor these transactions as Krystal noted it was in the best interest of the company.¹⁹³

Vendor Credit Support Arrangement: Superiority Administrative Expenses

On January 20, 2020 the Debtors filed an Emergency Motion for entry of Interim and Final Orders Authorizing and Confirming Vendor Credit Support Arrangements.¹⁹⁴ Under the Bankruptcy Code §1107(a), a debtor in possession is afforded all rights subject to limitation by the US Trustee to perform their functions and duties as a business.¹⁹⁵ Accordingly, a Vendor Credit Support Agreement is a contract between parties that define the relationship, scope of work, payment schedules, and other provisions specific to a working partnership.¹⁹⁶ This filing allows a debtor to engage in ongoing business with a priority vendor by contractually securing their interests during the stay of a proceeding. In this case, Krystal assured repayment of borrowed funds through this line of credit which enticed US Foods to maintain their current lines of business.¹⁹⁷

Notably, no objections to this agreement were filed. Through their pleadings, Krystal made it clear that they would be incapable of continuing their operations without securing their relationship with US Foods. Krystal continued to use their income and bank procedures to pay their employees, banking fees, and customer programs. In absence of negative relationships with customers and employees, it was important that Krystal avoid disrupting their relationship with their food vendors. The Krystal Company and US Foods, Inc. ("US Foods") were engaged in a Master Distribution Agreement ("MDA") as of May 2018. In total, US Foods was estimated to provide \$1,400,000 in goods to Krystal per week.¹⁹⁸ As of the date of filing, Krystal owed US Foods a total amount of \$5,852,630.¹⁹⁹

¹⁹³ Order (I) Authorizing Payment of Prepetition Wages, Payroll Taxes, Certain Employee Benefits, and Related Expenses; (II) Directing Banks to Honor Related Prepetition Transfers; and (III) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [34.pdf](#) at 3.

¹⁹⁴ See, Debtors' Emergency Motion for Entry of Interim and Final Orders (I) Authorizing and Confirming Vendor Credit Support Arrangement; (II) Granting Superpriority Administrative Expense Claims; and (III) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [16.pdf](#) at 1.

¹⁹⁵ 11 U.S.C. §1107(a), ("[A] debtor in possession shall have all the rights, other than the right to compensation under section 330 of this title, and powers, and shall perform all the functions and duties. . . of a trustee serving in a case under this chapter.").

¹⁹⁶ Andrew Bloomenthal Vendor Financing, INVESTOPEDIA, <https://www.investopedia.com/terms/v/vendorfinancing.asp> [<https://perma.cc/HXN2-3XMV>] (August 31, 2021).

¹⁹⁷ Debtors' Emergency Motion for Entry of Interim and Final Orders (I) Authorizing and Confirming Vendor Credit Support Arrangement; (II) Granting Superpriority Administrative Expense Claims; and (III) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [16.pdf](#) at 2.

¹⁹⁸ *Id.*

¹⁹⁹ *Id.*

In their first day motions, Krystal conceded that this would be categorized as a priority claim under §503(b)(9).²⁰⁰ Additionally, for added protection, the MDA included provisions to allow them full repayment of their debts resulting from its ordinary course of business.²⁰¹ Specifically, US Foods agreed to give Krystal a 21-day payment plan for post-petition goods delivered under the agreement and defer those payments on their §503(b)(9) claim.²⁰²

Within this distribution claim, Krystal was granted post-petition trade credits to allow for a 21-day extension of payment after the delivery date of the goods.²⁰³ This credit system was allowed so long as the debts did not exceed \$4,500,000.²⁰⁴ Additionally, Krystal agreed to pay the outstanding balance claim to US Foods at the time of closing pursuant to §503(b)(9).²⁰⁵ The debtor argues that this payment was justified not only pursuant to this agreement, but under §364(c)(1) of the Bankruptcy Code.²⁰⁶ This would classify these expenses as superpriority administrative expenses that would take precedence over any other secured or unsecured creditor at the execution of a sale and repayment.²⁰⁷

Rejection of Leases

In hindsight, the purpose of this filing was Krystal was to shed lease obligations. Specifically, there were more leases than there were Krystal locations.²⁰⁸ With Krystal aggressively closing stores, the lease obligations were of utmost importance for improving the company's financial position.²⁰⁹

At the time of filing, Krystal reported 182 outstanding lease obligations.²¹⁰ This accounted for all open Krystal locations at that time that were tied to existing contracts. In their motion to reject certain unexpired leases, Krystal detailed their strategy in identifying and closing certain brick and mortar locations that were underperforming.²¹¹ They termed these designations "Dark Store Leases."²¹² The company reported to have closed the doors on 78

²⁰⁰ *Id.* at 2.

²⁰¹ *Id.* at 6.

²⁰² *Id.* at 4 (detailing the credit plan extended to Krystal by U.S. Foods).

²⁰³ *Id.*

²⁰⁴ *Id.*

²⁰⁵ *Id.*

²⁰⁶ *Id.*; 11 U.S.C. § 364(c)(1) (stating that the court, after notice and a hearing, may authorize the obtaining of credit or the incurring of debt with priority over any or all administrative expenses of the kind specified in section 503(b) or 507(b) of this title).

²⁰⁷ *Id.*

²⁰⁸ *See generally id.*

²⁰⁹ *Id.*

²¹⁰ Debtors' First Omnibus Motion for Entry of an Order (I) Authorizing and Approving the Rejection of Certain Unexpired Leases as of the Petition Date and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020). [13.pdf](#) at 2. [hereinafter First Motion Rejecting Unexpired Leases].

²¹¹ *Id.* at 3.

²¹² *Id.*

locations and listed them as unexpired Dark Store Leases.²¹³ While these locations were no longer in operation, the obligation to pay under contract constituted a substantial burden to the company.²¹⁴

Unfortunately, Krystal never quantified the exact burden that the Dark Store Leases imposed on their finances. In their motion, the only justification for the request to reject the leases was pursuant to Federal Rule of Bankruptcy Procedure 6006(f), which requires in relevant part, that a motion to reject multiple executory contracts or unexpired leases:

- a. state in a conspicuous place that parties receiving the motion should locate their names and their contracts or leases in the motion;
- b. list parties alphabetically and identify the corresponding contract or lease;
- c. be numbered consecutively with other omnibus motions to assume, assign, or reject executory contracts or unexpired leases; and
- d. be limited to no more than 100 executory contracts or unexpired leases.²¹⁵

Outside of procedural requirements, Krystal relied on the business judgment rule to justify their decision to reject these leases.²¹⁶ Under this rule, any decision, such as a request to reject these leases, would be completely justified and in the best interest of the company absent bad faith, whim, or caprice.²¹⁷ The tone of this motion was almost authoritative as opposed to a debtor requesting an action.

Analysis of the tone used in these motions paints a picture that was foreshadowed by the company filing. Krystal was transparent in their intentions to downsize as a result of this filing. As noted above, the majority of these first day pleadings were fairly similar to other organizational restructurings, reducing their risk and trimming the fat of the company to exit the bankruptcy proceedings a more streamlined and efficient business.

Even though the debtor was fully justified in seeking rejection of the leases under the business judgment rule, lingering creditors raised objections to the motion. Of the 70 identified leases that were attached to the motion, three notable creditors stepped forward in an attempt to recover debts prior to its approval. Tindell Properties, Hachman LLC, and Lakepoint presented themselves in opposition to their leases being outright rejected. Although these three objections were in no way connected, they shared similar claims.

²¹³ *Id.*

²¹⁴ Krystal Voluntary Petition, [4.pdf](#). (recognizing the aggregate liability in their Schedule C filing).

²¹⁵ First Motion Rejecting Unexpired Leases, [13.pdf](#) at 6.

²¹⁶ Adam Hayes, *Business Judgment Rule*, INVESTOPEDIA, <https://www.investopedia.com/terms/b/businessjudgmentrule.asp#:~:text=The%20business%20judgment%20rule%20protects,optimal%20decisions%20all%20the%20time> [<https://perma.cc/AH9N-4PUD>] (April 27, 2022).

²¹⁷ *Id.*

The issue they presented was not with the overall rejection, these creditors had no issue with reclaiming their properties considering the stay prevented them from enforcing their preexisting contractual rights.²¹⁸ The common argument in all three claims arose from Krystal's occupation of the properties in dispute.²¹⁹ Krystal was operating their fast-food chains on these properties with a lapse in their rent all the while attempting to cancel their lease. Even still, the property owners in these situations did not take issue with the rejection of their leases. Their main contention was in conflict with the language within the motion: "The Rejected Leases identified on Schedule 1, Schedule 2, and Schedule 3 to this Order are hereby rejected nunc pro tunc to the Petition Date."²²⁰ The consequences of this language meant that Krystal was under no obligation to pay the unpaid post-petition rent.

The rejection date requested was the petition date, at that point two months of unpaid rent was due to the objecting lessors.²²¹ The three parties all identified that the subleases that Krystal assigned to the restaurant operators were in good standing, meaning that the franchises were paying their rent in a timely fashion but Krystal retained the payments without making payments to the landlords.²²² As a result, the three creditors sought relief from the stay to enforce their contractual obligations and be granted a set-off to allow them to utilize the debtors' security deposits from their leases. In the alternative, they sought that the date of rejection be the time of filing for the motion.²²³

Unfortunately, their alternative claims were unsuccessful. The judge signed the order granting the rejection of leases as of the petition date effectively eliminating over 70 leases with attached liabilities. For these three creditors, the court called for a setoff to allow them to utilize their security deposit payments toward their claims. Finally, Krystal was ordered to relinquish active control of the properties tied to these rejected leases.

²¹⁸ See generally Limited Objection to Debtors First Omnibus Motion for Order Approving Rejection of Certain Nonresidential Leases, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [142.pdf](#); Limited Objection to Debtors First Omnibus Motion for Entry of an Order (I) Authorizing and Approving the Rejection of Certain Unexpired Leases as of the Petition Date and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [145.pdf](#) [hereinafter Motion Rejecting Unexpired Leases]; Objection to Debtor's First Omnibus Motion for Order Approving Rejection of Certain Nonresidential Leases, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [147.pdf](#).

²¹⁹ *Id.*

²²⁰ Debtors' First Omnibus Motion for Entry of an Order (I) Authorizing and Approving the Rejection of Certain Unexpired Leases as of the Petition Date and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [13.pdf](#) at 2.

²²¹ See First Motion Rejecting Unexpired Leases, [13.pdf](#).

²²² Limited Objection to Debtors First Omnibus Motion for Order Approving Rejection of Certain Nonresidential Leases, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [142.pdf](#) at 2.

²²³ Motion Rejecting Unexpired Leases, [145.pdf](#) at 6.

Unsecured Committee of Creditors

Pursuant to 11 U.S.C. § 1102(a), the United States Trustee is entitled to appoint a committee of creditors to represent the interests of unsecured creditors. According to the statute, the trustee can make whatever appointments necessary to represent the equitable interest of the unsecured creditors.²²⁴ This statute promotes efficiency in the bankruptcy proceeding as in this case, the list of unsecured creditors is substantial. It is important to note that this appointment is not required in all cases.²²⁵

The Official Committee of Unsecured Creditors (“OCC”) was composed of seven different creditors located across the country.²²⁶ A list with their information is provided below.

NCR Corporation

Mark Rogers
(470) 415-8614 Mark.rogers@ncr.com
Todd Atkinson
Ulmer & Berne LLP
1660 West 2nd Street, Suite 1100 Cleveland, OH 44113
(216) 583-7162 tatkinson@ulmer.com

Charles Tombras Advertising, Inc.

Alice Matthews
(865) 524-5376 amathews@tombras.com
Mark Duedall
Bryan Cave Leighton Paisner LLP One Atlantic Center
14th Floor, 1201 West Peachtree Street Atlanta, GA 30309
(404) 572-6611 mark.duedall@bclplaw.com

The Coca-Cola Company

Curtis Marshall
R. Kenny Werner
The Coca-Cola Company One Coca-Cola Plaza NW NAT 11
Atlanta, GA 30313
(404) 304-1550 cumarshall@coca-cola.com rwenner@coca-cola.com

Realty Income Corporation

Kirk Carson
Senior Legal Counsel, AVP Realty Income Corporation
11995 El Camino Real

²²⁴ 11 U.S.C. § 1102(a)2 (“On request of a party in interest, the court may order the appointment of additional committees of creditors or of equity security holders if necessary to assure adequate representation of creditors or of equity security holders. The United States trustee shall appoint any such committee.”).

²²⁵ 11 U.S.C. § 1102(a)3 (“Unless the court for cause orders otherwise, a committee of creditors may not be appointed in a small business case or a case under subchapter V of this chapter.”).

²²⁶ Notice Appointing Creditors' Committee, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [143.pdf](#) at 2–3.

San Diego, CA 92130 (858) 284-5260 kcarson@realtynincome.com

Flowers Foods, Inc.

Paul Rosenblatt
Kilpatrick Townsend & Stockton LLP Suite 2800
1100 Peachtree Street NE
Atlanta, GA 30309-4528
(404) 815-6321 PRosenblatt@kilpatricktownsend.com

Pension Benefit Guaranty Corporation

Hannah Uricchio
Stephanie Thomas
Kartar Khalsa
Office of the General Counsel
1200 K Street, N.W. Washington, D.C. 20005
(202) 229-6252 uricchio.hannah@pbgc.gov

SLM Waste Recycling Services, Inc.

Jim Stauffer
(267) 429-7413 Jim.Stauffer@slmfacilities.com
Raymond Lemisch
(215) 569-4298 Rlemisch@KLEHR.com

Of all the objections made in this case, few were brought by the OCC. For the duration of the case, the committee clearly had one concern; whether the sale would yield sufficient cash to allow for distributions to unsecured creditors.

Pursuant to 11 U.S.C. § 506 (b) the OCC had a right to object to the claims of secured creditors in an effort to make the pool of funds more readily available after a sale or restructuring of the company.²²⁷ Accordingly, the creditors committee identified ten secured claims at issue with arguments challenging their validity represented below.²²⁸ Ultimately, the secured creditors waived their right to receive a settlement of their claims causing this motion to be ineffective.²²⁹

²²⁷ 11 U.S.C. § 506 (b) (“An allowed claim of a creditor secured by a lien on property in which the estate has an interest, or that is subject to setoff under section 553 of this title, is a secured claim to the extent of the value of such creditor’s interest in the estate’s interest in such property, or to the extent of the amount subject to setoff, as the case may be, and is an unsecured claim to the extent that the value of such creditor’s interest or the amount so subject to setoff is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor’s interest.”)

²²⁸ Creditors’ Committee Cash Collateral Objection, [197.pdf](#). at 13.

²²⁹ *Id.* at 10.

| Item | Description of Challenge in Item |
|------|---|
| 1 | Funds held by the Debtors that were necessary to pay trust fund taxes, such as sales taxes, are not property of the estate. |
| 2 | The Lenders do not have a perfected security interest in commercial tort claims. |
| 3 | The Lenders do not have a perfected security interest in certain of the Debtors' real property leases and franchise agreements. |
| 4 | The Lenders do not have a perfected security interest in the funds that were in certain of the Debtors' deposit accounts. |
| 5 | Any valuation of the Debtors' assets as of the filing date should not attribute any value to the Lenders' pre-petition security interest in general intangibles. |
| 6 | The Lenders do not have a security interest in the Debtors' post-petition inventory by virtue of 11 U.S.C. § 552(a), and the appropriate method for determining the value of the Lenders' pre-petition security interest in the Debtors' inventory and equipment is a liquidation valuation method. |
| 7 | The Lenders do not have a perfected security interest in certain insurance claims where the Lenders were not identified as loss payees. |
| 8 | The Lenders do not have a perfected security interest in the Debtors' intellectual property rights that are not identified on Schedule 2 of the Statement. |
| 9 | The Lenders do not have a perfected lien or security interest in the Debtors' real property located on Alabama Highway located in Catoosa County, Georgia. |
| 10 | <p>The Lenders do not have a security interest in any property that the Debtors acquired after the Petition Date by virtue of 11 U.S.C. § 552(a) unless such property constitutes proceeds of the Lenders' collateral under 11 U.S.C. § 552(b).</p> <p>To the extent that the Debtors have a security interest in proceeds such interest should be invalidated based on the "equities of these bankruptcy cases."</p> |

Outside of this initial objection, the committee objected to the Stalking Horse Agreement and the Cash Collateral motion. The thrust of these arguments was that there was either not a going concern regarding the purchase of this company or that residual funds would not be left over for unsecured claims after a 363 sale.

Notice to Contract Parties to Potentially Assumed Executory Contracts and Unexpired Leases

In early April, the debtor issued a notice to the contracting parties of Krystal detailing all indebtedness subject to their existing contracts.²³⁰ In an attached exhibit, this notice provided for over 700 contracts that Krystal was engaged in that had an existing liability.²³¹ The language within the notice made it clear that if the listed contract holders failed to object to their designated cure price, it would account for resolution of any claims they would have against Krystal moving forward from the sale.²³² Additionally, the language of the contract provided that payment for the debts listed would not inherently mean that Krystal would assume the obligations tied to the agreements alluding that some would inevitably be rejected.²³³

This notice also included a clause stating that if any of the listed creditors provided notice of this sale and cure cost objected to the sale, qualified bidder, or bidding procedure, they would need to step forward with the claim.²³⁴ Further, any potential claim that may arise in response to this notice would need to be heard by the bankruptcy court at a later date and time.²³⁵ Prior administrative expenses and claims previously heard were listed as having a \$0 balance in this chart.²³⁶ This required that creditors who previously secured a judgment or resolution through Krystal would need to step forward and claim their monetary damages through this process all contained within a now relinquished website, “<http://www.kccllc.net/krystal>.”²³⁷

Of these contracts, only a few opponents stepped forward in disagreement with their cure price. In a chart listed below, few creditors of the approximately 700 listed disagreed with their proposed cure.²³⁸ The majority of these objections consisted of discrepancies in rent amounts that had been left unpaid.²³⁹ However, a few of these objections were from service providers including the previously discussed power companies. Most notably, Media and Marketing companies stepped forward with claims in excess of \$600,000 that were left unpaid prior to filing.²⁴⁰ These claimants mainly had issues with executory contracts and interest accrued on unpaid amounts.

Aside from the dissolution and payment of existing contracts. There was a going concern that several of the creditors would be left vulnerable after the sale of the company. A few of the rejections to expired leases had issues with the lack of insurance in their business relationship.²⁴¹

²³⁰ Notice to Contract Parties to Potentially Assumed Executory Contracts and Unexpired Leases, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020). [310.pdf](#) at 1.

²³¹ See *id.* at Ex. A.

²³² *Id.* at 2.

²³³ *Id.*

²³⁴ *Id.*

²³⁵ See *id.* at Ex. A, pg. 1.

²³⁶ See *id.* at Ex. A, pg. 12.

²³⁷ *Id.* at 1.

²³⁸ See Notice to Contract Parties to Potentially Assumed Executory Contracts and Unexpired Leases, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020). [310.pdf](#) at Ex. A.

²³⁹ See *id.* (representing the objections to cure based on similar claims).

²⁴⁰ Limited Objection to the Debtors' Proposed Cure, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020). [378.pdf](#) at 2.

²⁴¹ Several of these objections contained provisions addressing this court enforcing the occupancy of their premises without an active insurance policy due to Krystal's non-payment of premiums. See *id.*

As the price of the contract was left unpaid, the creditor in turn did not pay whatever insurance policies were tied to the agreement and were at issue with reentering business operations with Krystal without active insurance coverage.²⁴²

Relative to the total amount of liabilities listed in this notice, Krystal was fairly successful in identifying and paying off their existing contractual liabilities. Many of the objections made were done in good faith and contained unexpected fees accounted for in their agreements.

²⁴² *Id.*

| Doc ID | Creditor | Contract Type | Proposed Cure | Requested Relief |
|---------------|-----------------------------------|---------------------------|----------------------|-------------------------|
| 322 | Desai Holdings | Lease | \$20,912.70 | \$25,432.70 |
| 338 | Rachel Pruette | Lease | \$5,856.40 | \$21,156.36 |
| 339 | PPB & D, Inc. | Rent (Interest) Arrearage | \$37,840.89 | \$37,840.89 |
| 345 | Gloria D. McCall | Lease | \$16,083.33 | \$18,450.00 |
| 349 | Alan B. Watts | Lease | \$18,694.26 | \$23,118.62 |
| 350 | Calluro Family Partners | Lease | \$37,517.38 | \$53,662.55 |
| 360 | DSS Krystal Stockbridge | Lease | \$7,916.67 | \$14,666.65 |
| 365 | Leon S. Jones | Lease | \$33,040.32 | \$42,262.84 |
| 369 | Eden Star Properties LLC. | Lease | \$21,791.00 | \$26,523.49 |
| 377 | 1045 Ellis Ave. | Lease | \$15,234.01 | \$24,768.20 |
| 378 | Aletha Marketing & Media | Service Agreement | \$26,878.50 | \$634,961.03 |
| 381 | Cirignano L.P. | Lease | \$12,994.02 | \$20,418.60 |
| 383 | D.J. Rash Realty Co. | Lease | (Aggregate Below) | \$26,358.65 |
| | M.J. Holdings | Lease 2 | \$31,299.50 | \$17,412.04 |
| 384 | 182 Emerson LLC | Lease | \$27,624.99 | \$34,564.46 |
| 385 | SLM Waste Recycling Services | Services | \$617,304.86 | \$661,005.54 |
| 387 | Carnello Family Trust | Lease | \$ | \$56,769.67 |
| 388 | Buckhead 14TH KB, LLC | Lease | \$20,115.82 | \$ 26,079.56 |
| | Buckhead 14 TH KB, LLC | Lease | \$23,566.68 | \$27,644.99 |
| | Fairburn KB Freestanding, LLC | Lease | \$18,338.56 | \$25,257.52 |
| | KB Ringgold GA, LLC | Lease | \$14,364.48 | \$17,982.70 |
| | Krystal Columbus DT, LLC | Lease | \$17,602.69 | \$21,474.77 |
| 389 | AR Global | Lease | \$60,687.26 | \$98,819.99 |
| 390 | Ladus Development | Lease | \$10,473.76 | \$12,480.07 |
| 391 | KRY Warner Robins | Lease | \$38,593.80 | \$47,076.45 |
| 392 | Mississippi Power Co. | Services | \$0 | \$13,443.51 |
| 393 | Alabama Power Co. | Services | \$0 | \$63,261.70 |
| 394 | C&L Properties | Lease | \$30,014.98 | \$41,552.05 |
| 395 | Georgia Power | Services | \$0 | \$141,987.05 |
| 396 | Faith Sumerson | Lease | \$36,780.92 | \$58,457.38 |
| 397 | Store Master Funding | Lease | \$14,890.17 | \$86,657.71 |
| 398 | Pier Point Ltd. | Lease | \$7,986.00 | \$8,784.60 |

Section 363 Sale

Sale Challenges

As Krystal prepared for the Chapter 11 case, they contemplated a reorganization. However, on the eve of the Chapter 11 filing, Krystal's management pivoted towards a section 363 sale. Under section 363(f) of the Federal Bankruptcy Code, a Debtor-in-Possession may sell estate assets free and clear of any claims or liens.²⁴³ This is known as a section 363 sale and is common practice in Chapter 11 cases where the debtor does not reorganize.

Around the time of filing for Chapter 11 protection, Krystal had 10 potential buyers.²⁴⁴ However, after closing stores and being forced to only serve customers by delivery and drive-through due to COVID-19 restrictions, the company's revenue fell sharply, and some potential buyers lost interest.²⁴⁵ This threatened the viability of the company. Krystal's bankruptcy lawyer, Sarah R. Borders of King & Spalding LLP stated the company faced "a very real prospect of a broken sale process and a complete liquidation."²⁴⁶ These challenges were an obstacle for the company, but they still pushed forward as they searched for potential buyers.

Bidding Procedures

Krystal filed a motion to approve bidding procedures, scheduling hearing and objection deadlines, bid deadlines and an auction, and related relief to obtain a section 363 sale.²⁴⁷ Prior to the motion, Piper Sandler & Co. advised Krystal in determining which option provided the most value for the company.²⁴⁸ Relying on Piper Sandler & Co.'s advice, Krystal believed in their business judgment that a section 363 sale would provide the most value for the company and stakeholders.²⁴⁹

Further, Piper Sandler & Co. marketed the company's assets and compiled a list of potential buyers with enough capital to complete the sale.²⁵⁰ As part of the motion, Krystal sought authority to select one or more stalking horse purchasers.²⁵¹ Stalking horse purchasers are

²⁴³ 11 U.S.C. § 363(f).

²⁴⁴ Aisha Al-Muslim, *Bankrupt Burger Chain Krystal Strikes Takeover Deal With Senior Lender*, WALL ST. J. (May 13, 2020), <https://www.wsj.com/articles/bankrupt-burger-chain-krystal-strikes-takeover-deal-with-senior-lender-11589404398> [<https://perma.cc/PJC4-CHM8>].

²⁴⁵ *Id.*

²⁴⁶ *Id.*

²⁴⁷ Motion for Entry of an Order (I) Approving Bidding Procedures for the Sale of the Debtors Assets, (II) Scheduling Hearings and Objection Deadlines with Respect to the Sale, (III) Scheduling Bid Deadlines and an Auction, (IV) Approving the Form and Manner of Notice Thereof, (V) Approving Contract Assumption and Assignment Procedures, and (VI) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [148.pdf](#) at 1.

²⁴⁸ *Id.* at 3.

²⁴⁹ *Id.*

²⁵⁰ *Id.* at 4.

²⁵¹ *Id.*

commonly used in bankruptcy 363 sales to set a minimum price for the assets and prevent potential buyers from “low-balling” with their bids.

Krystal requested that the final bid deadline and auction be set for May 4, 2020 and May 7, 2020.²⁵² They requested the objection deadline and sale hearing be scheduled for May 12, 2020 and May 14, 2020.²⁵³ Krystal also proposed that they submit to the court and provide notice for the unexpired leases and executory contracts to be assumed and assigned with the sale, the amount necessary to cure monetary defaults, and the deadline to file connected objections.²⁵⁴ If a party were to file an objection that was not resolved with the potential buyer by the sale hearing, the dispute would be resolved at the sale hearing or later if the court allowed.²⁵⁵ If the objection was not resolved, it would be up to the potential buyer to determine if unexpired lease or executory contract be rejected.²⁵⁶ In that scenario, the potential buyer would not be responsible for the cost to cure.²⁵⁷

Material provisions of the proposed bid requirements included: setting forth the purchase price; making the bid formal, binding, and irrevocable until two business days after the closing; disclosing enough financial information for Krystal to determine if the potential buyer could compete the sale; providing that the payment be only in cash but allowing Krystal or Wells Fargo be allowed to credit bid to the extent of their outstanding secured obligations; committing to close by May 29, 2020; exceeding the sum of the bid of any stalking horse purchaser, approved break-up fees and expense reimbursement, and \$250,000; and providing a cash deposit that equaled the greater of \$1,000,000 or 10 percent of the bid to be held in escrow.²⁵⁸

If there was more than one bid that met the requirements (“Qualifying Bids” and “Qualified Bidders”), the court would hold an auction for the Qualified Bidders and stalking horse purchaser.²⁵⁹ The bids would be required to be in at least \$250,000 increments and subject to the Bidding Procedures.²⁶⁰ The court would then approve the sale for the highest Qualifying Bidder (“Successful Bidder”).²⁶¹ If the Successful Bidder were to not close the sale by May 29, 2020, the second highest bidder would be deemed the Successful Bidder.²⁶² Thus, all bids were binding and irrevocable offers.²⁶³

²⁵² *Id.* at 7.

²⁵³ *Id.* at 8.

²⁵⁴ *Id.* at 9.

²⁵⁵ *Id.* at 10.

²⁵⁶ *Id.*

²⁵⁷ *Id.* at 11.

²⁵⁸ *Id.* at 43.

²⁵⁹ *Id.*

²⁶⁰ *Id.* at 9.

²⁶¹ *Id.*

²⁶² *Id.*

²⁶³ *Id.*

Krystal subsequently amended the proposed Bidding Procedures on March 2, 2020.²⁶⁴ Material modifications included: (1) changing the bid deadline from May 4, 2020 to May 5, 2020, (2) changing the sale hearing from May 14, 2020 to May 13, 2020, (3) changing assumption and assignment objection filing date from April 20, 2020 to April 27, 2020, and (4) requiring that Qualified Bids include adequate assurance information within one day following an auction.²⁶⁵ The modifications were completed after negotiations “with the creditors’ committee, with a number of the landlords, with the PBGC, with executory-contract counterparties, and with the second-lien lender to the debtors.”²⁶⁶ There were no objections filed with the court and all parties were content with the modified bidding procedures.²⁶⁷ After a hearing on March 3, 2020, the court issued an order for the Bidding Procedures on March 4, 2020, adopting the terms of the modified motion.²⁶⁸

Bidding Schedule

| | |
|---|--|
| Selection of Stalking Horse Bidder, if applicable | April 1, 2020 |
| Potential Assumption and Assignment Notice Deadline and Deadline to Provide Adequate Assurance Information for Stalking Horse Bidder, if applicable | April 7, 2020 |
| Hearing to Approve Stalking Horse Bidder | April 7, 2020 |
| Cure Cost/Assignment Objection Deadline | April 27, <u>2020</u> at 4:00 p.m. EST |
| Bid Deadline | May 5, <u>2020</u> at 5:00 p.m. EST |
| Auction | May 7, <u>2020</u> at 10:00 a.m. EST |
| Deadline to Service Notice of Successful Bidder and Successful Bidder’s Adequate Assurance Information | May 8, 2020 |
| Sale Objection Deadline | May 12, 2020 |
| Sale Hearing | May 13, 2020 |
| Closing Date | No later than May 29, 2020 |

²⁶⁴ Notice of Filing of Modified Proposed Order (I) Approving Bidding Procedures for the Sale of the Debtors’ Assets, (II) Scheduling Hearings and Objection Deadlines with Respect to the Sale, (III) Scheduling Bid Deadlines and an Auction, (IV) Approving the Form and Manner of Notice Thereof, (V) Approving Contract Assumption and Assignment Procedures, and (VI) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [211.pdf](#) at 1.

²⁶⁵ *Id.* at 11.

²⁶⁶ Transcript regarding Hearing Held 03/03/20, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [230.pdf](#) at 9-10.

²⁶⁷ *Id.*

²⁶⁸ Order Approving Bidding Procedures, Scheduling Hearings and Objection Deadlines, Scheduling Bidding Deadlines and an Auction, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [227.pdf](#).

Stalking Horse Bid

Krystal moved the court for approval to enter into a Stalking Horse Agreement on April 21, 2020.²⁶⁹ Krystal negotiated with Krystal Acquisition, LLC and entered into an stalking horse purchase agreement (“Stalking Horse Agreement”), subject to court approval, to buy substantially all of their assets.²⁷⁰ Krystal Acquisition, LLC was an affiliate company of Nashville Capital Group, a Nashville based private equity firm.²⁷¹

The material terms of the Stalking Horse Agreement included Krystal Acquisition, LLC: (1) assuming of all claims and liabilities associated with the purchased assets, (2) wire transferring a \$1,000,000 as a good faith deposit, (3) assuming sole responsibility of cure costs, (4) receiving a \$500,000 break-up fee if the Stalking Horse Agreement was terminated, (5) having rights to designate which assets would be acquired or excluded for 60 days after closing, (6) having a management agreement where Krystal would manage certain restaurants until Krystal Acquisition, LLC acquired necessary permits or designated the asset as excluded or purchased, and (7) having a right to terminate the agreement if closing did not occur by May 18, 2020.²⁷²

In simpler terms, Krystal Acquisition, LLC agreed to purchase the company for \$1,000,000 plus an assumption of approximately \$20 million in liabilities.²⁷³ Krystal believed the Stalking Horse Agreement would provide them with a solid base to solicit competing bids.²⁷⁴ Krystal argued the \$500,000 breakup fee to be paid to Krystal Acquisition, LLC was fair and reasonable in light of the due diligence and other work required of a stalking horse purchaser.²⁷⁵ Krystal subsequently filed a motion for an entry shortening notice and scheduling an expedited hearing on the motion that was approved by the court.²⁷⁶

The extended 60-day designation period proved to be a point of contention for creditors as a group of Landlords objected to the motion because of this period.²⁷⁷ The Landlords argued while having additional time to make decisions of which assets to include or exclude was understandable, the 60-day period would lead to a delay of post-petition rent payments from

²⁶⁹ Debtors' Emergency Motion for Entry of an Order (I) Approving Entry into Stalking Horse Agreement and Authorizing Break-Up Fee and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [340.pdf](#) at 1. [hereinafter Stalking Horse Agreement].

²⁷⁰ *Id.* at 3.

²⁷¹ Ben Coley, *Bankrupt Krystal Agrees to \$48 Million Deal with Fortress Investment Group*, QSR (May 2020), <https://www.qsr magazine.com/fast-food/bankrupt-krystal-agrees-48-million-deal-fortress-investment-group> [<https://perma.cc/QTG7-AVKW>].

²⁷² Stalking Horse Agreement, [340.pdf](#) at 4.

²⁷³ Al-Muslim, *supra* note 249; Coley, *supra* note 276.

²⁷⁴ Stalking Horse Agreement, [340.pdf](#) at 5.

²⁷⁵ *Id.* at 8–9. It is important to note that the break-up fee was half of the Purchase Price and twice the amount of the minimum bid increment. This evidences the company's desperation to find a purchaser.

²⁷⁶ Emergency Motion for Entry of an Order Shortening Notice and Scheduling Expedited Hearing on Debtors' Emergency Motion for Entry of an Order (I) Approving Entry into Stalking Horse Agreement and Authorizing Break-Up Fee and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [342.pdf](#) at 1, 2; Order Shortening Notice and Scheduling Hearing on Debtors' Emergency Motion for Entry of an Order (I) Approving Entry into Stalking Horse Agreement and Authorizing Break-Up Fee and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [344.pdf](#) at 1.

²⁷⁷ Limited Objection of Certain Landlords to Debtors' Motion for Approval of Stalking Horse Agreement, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [368.pdf](#) at 1.

April to July.²⁷⁸ At that time, Krystal had not paid rent for April and the landlords feared this period would allow Krystal to further skirt their post-petition rent obligations. The Landlords asked the court to require Krystal to bring their post-petition rent payments to the motioning Landlords current at the time of closing and pay any post-petition rent payments for leases that Krystal Acquisition, LLC may have chosen to exclude.²⁷⁹

The OCC also objected to the Stalking Horse Agreement.²⁸⁰ The committee's concern was that in the event of a "Fiduciary Out Action," the Debtors would have to pay the \$500,000 break-up.²⁸¹ The term "Fiduciary Out Action" was defined broadly. The OCC stated that bidding procedures are typically designed to foster a competitive bidding process.²⁸² However, in this case, Fiduciary Out Actions included Krystal soliciting bids.²⁸³ This would require Krystal to pay the Stalking Horse Bidder \$500,000 for merely soliciting a higher bid. Thus, the OCC argued that the \$500,000 fee should only be payable in the event of a higher bidder and successful sale because the break-up fee disincentivized the Debtors from maximizing the value for all parties by soliciting bids.²⁸⁴ Additionally, the OCC argued the bankruptcy estate did not have enough capital to offer such a friendly break-up fee payout.²⁸⁵ While it was compelling, the OCC's objection proved to be a moot point after the Stalking Horse Agreement fell through for reasons detailed in the next section.

Settlement Agreement: Changing Bidders

After negotiations with Fortress Investment Group ("Fortress"), Krystal filed a motion to withdraw the Stalking Horse Motion without prejudice.²⁸⁶ Fortress offered roughly \$20 million over Nashville Capital Group's, in the form of a \$27 million credit bid and an assumption of liabilities in excess of \$20 million.²⁸⁷ As a result, Krystal decided to abandon the Stalking Horse Agreement altogether and accepted Fortress's offer. On May 1, 2020, Krystal filed a motion for an order authorizing and approving a settlement agreement.²⁸⁸ In the settlement agreement, an affiliate of Fortress and Wells Fargo, DB KRST Investors LLC, offered a credit bid for substantially all of the assets of Krystal and an assumption of certain liabilities.²⁸⁹ Fortress did this as a subagent of Krystal's creditors and thus could rely on the creditor's claim to the assets as their bid.²⁹⁰ The Settlement Agreement stipulated and agreed that under the Prepetition

²⁷⁸ *Id.* at 2.

²⁷⁹ *Id.* at 3.

²⁸⁰ Limited Objection to Debtors' Emergency Motion for Entry of an Order Approving Entry into Stalking Horse Agreement and Authorizing Break-up Fee, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020). [364.pdf](#) at 3. See [Unsecured Committee of Creditors](#).

²⁸¹ *Id.* at 1–3.

²⁸² *Id.* at 2.

²⁸³ *Id.* at 2.

²⁸⁴ *Id.* at 2–3.

²⁸⁵ *Id.* at 3.

²⁸⁶ Notice of Withdrawal of Debtors Emergency Motion for Entry of an Order (I) Approving Entry Into Stalking Horse Agreement and Authorizing Break-Up Fee and (II) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [407.pdf](#).

²⁸⁷ Coley, *supra* note 276.

²⁸⁸ Emergency Motion to Approve Settlement Agreement, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [415.pdf](#) [hereinafter Settlement Agreement Motion].

²⁸⁹ *Id.* at 3.

²⁹⁰ *Id.* at 3.

Agreement, Krystal owed their creditors \$51,076,402.17.²⁹¹ As part of the Settlement Agreement, Krystal agreed that this amount was secured by the assets of the bankruptcy estate and would not be subject to “any avoidance, disallowance, disgorgement, reductions, setoff, offset, recharacterization, subordination (whether equitable, contractual, or otherwise), counterclaims, cross-claims, defenses, or any other challenges of any kind or nature under the Bankruptcy Code or any other applicable law or regulation,” and that they would waive any challenges to the amount and liens.²⁹²

The Settlement agreement provided Fortress would provide funds to cover all costs and expenses associated with winding down the Chapter 11 case.²⁹³ The total winddown costs to be provided to Krystal totaled \$4,696,300.²⁹⁴ Any amount not used in the winding down of the Chapter 11 case was to be returned to Fortress.²⁹⁵ Further, after completion of the winddown or confirmation of a plan, 100% of the equity of Krystal Holdings and all rights and interests in Krystal would be transferred to DB KRST Investors LLC.²⁹⁶

The Settlement Agreement also provided for mutual releases of claims after the transfer of equity. Fortress, in their capacity as subagent for Krystal’s creditors, would release Krystal (with some exceptions) and the OCC from all claims.²⁹⁷ The OCC would release DB KRST Investors LLC and Krystal from all claims.²⁹⁸ Krystal would release claims against DB KRST Investors LLC and the OCC from all claims.²⁹⁹ However, unsecured general and administrative claims would not be released.³⁰⁰

On May 13, 2020, the court approved the Settlement Agreement without modification stating:

The Court has considered the Motion and the matters reflected in the record of the hearing held on the Motion on May 13, 2020. It appears that the Court has jurisdiction over this proceeding; that this is a core proceeding; that proper and adequate notice of the Motion has been given and that no other or further notice is necessary; that the relief sought in the Motion is in the best interests of the Debtors, their estates, and their creditors; and that good and sufficient cause exists for such relief.³⁰¹

²⁹¹ *Id.* at 4.

²⁹² *Id.*

²⁹³ *Id.* at 5–6.

²⁹⁴ *Id.* at Ex. B.

²⁹⁵ *Id.* at 6.

²⁹⁶ *Id.* at 4.

²⁹⁷ *Id.* at 6–7.

²⁹⁸ *Id.*

²⁹⁹ *Id.*

³⁰⁰ *Id.*

³⁰¹ Order Granting Motion for Entry of an Order Authorizing and Approving Settlement Agreement, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [467.pdf](#) at 2.

Proposed Budget for Wind Down Costs

| Item | Amount |
|---|--------------|
| Transaction Fees | \$1,645,000 |
| Debtor Professional Fee Budget - May '20 | \$840,000 |
| UCC Professional Fees Budget - May '20 | \$160,000 |
| US Trustee Fees - Q2 & Q3 2020 | \$301,300 |
| Funds to cover outstanding checks as of close | \$1,000,000 |
| Estate Wind Down Budget | \$250,000 |
| Other / Contingency | \$500,000 |
| Total Wind Down Budget | \$ 4,696,300 |

Asset Purchase Agreement

On May 6, 2020, Krystal filed a notice of no auction and filing of the Asset Purchase Agreement with DB KRST Investors, LLC.³⁰² The total purchase price of the assets included a \$27 million credit bid of the Prepetition First Lien Obligations,³⁰³ and an assumption of liabilities up to \$21.5 million.³⁰⁴ The assumed liabilities included: (1) “all Claims, liabilities and obligations arising in connection with the Business or the Purchased Assets after the Closing;” (2) all liabilities and obligations from assigned contracts and permits; (3) “all Cure Costs, and any and all costs and expenses necessary in connection with providing “adequate assurance of future performance” with respect to the Assigned Contracts,” and Krystal’s unpaid rental obligations for April and May 2020 for purchased locations; (4) all gift card obligations required by law; (5) all obligations and liabilities for accrued salaries, benefits, wages and applicable payroll taxes in each case solely with respect to the most current and active pay period as of the Closing Date;” (6) all priority status trade payable and accrued liabilities arising in the ordinary course of business both before and after filing the Chapter 11 case except for professional fees; (7) all accrued and unpaid sales tax obligations; and (8) all property taxes for purchased assets.³⁰⁵

The Asset Purchase Agreement provided that the Credit Agreement Lenders could exercise an option for DB KRST Investors LLC to pay them their pro rata share of the purchase price at closing.³⁰⁶ The purchased assets included essentially all assets and contract rights of the company except for the \$4,696,300 used for wind down, security deposits with landlords, certain

³⁰² Notice of No Auction and Filing of Asset Purchase Agreement, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [425.pdf](#).

³⁰³ *Id.* at Ex. A p. 5.

³⁰⁴ *Id.* at Ex. A p. 19.

³⁰⁵ *Id.* at Ex. A p. 18.

³⁰⁶ *Id.* at Ex. A p. 4.

tangible personal property, and excluded contracts.³⁰⁷ DB KRST Investors LLC also had the right to designate whether to include or exclude certain assets for a period of 45 days after closing.³⁰⁸ These assets were referred to as Designation Rights Assets.³⁰⁹ Before three days after closing, DB KRST Investors LLC could specify certain assets and contracts that would be excluded from the purchased assets.³¹⁰ They would then have the 45 day period to determine whether to include or exclude the assets, provided that for the period they would be required to cover all costs and obligations associated with the Designation Rights Assets.³¹¹ If DB KRST Investors LLC decided to assume and assign a Designation Rights Asset, they would not be required to provide additional consideration.

The Asset Purchase Agreement also included provisions covering the Data Breach.³¹² DB KRST Investors LLC was to work with Krystal to publish notices reasonably calculated to reach the affected customers, government authorities, and other affected parties.³¹³ In an amendment to the Asset Purchase Agreement, the parties stated that after closing DB KRST Investors LLC would be deemed to have waived all actions and release all claims related to the Data Breach.³¹⁴ Additionally, the amendment provided that DB KRST Investors LLC would waive any claims against Argonne Capital Group that were purchased.³¹⁵

Prevailing Bid and Objections

Krystal stated that the only Qualifying Bid the company received by the Bid Deadline of May 5, 2020 was from DB KRST Investors LLC.³¹⁶ Thus, that was the prevailing bid, and no auction would take place. However, objections could still be filed by the May 12, 2020 deadline.³¹⁷ On May 11, 2020 certain landlords filed a limited objection to the sale of the assets.³¹⁸ The thrust of the objection was the same as the objection to the Stalking Horse Motion. The landlords stated that Krystal was not current on their postpetition rent payments and were concerned about the Asset Purchase Agreement's terms relating to the Designation Rights Assets.³¹⁹

The landlords expressed concerns that the Asset Purchase Agreement did not provide any adequate assurance. Under the Asset Purchase Agreement, DB KRST Investors LLC had the

³⁰⁷ *Id.* at Ex. A p. 14–16.

³⁰⁸ *Id.* at Ex. A p. 5, 19.

³⁰⁹ *Id.*

³¹⁰ *Id.*

³¹¹ *Id.*

³¹² *Id.* at Ex. A p. 36.

³¹³ *Id.*

³¹⁴ Notice of Filing of First Amendment to Asset Purchase Agreement, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [461.pdf](#).

³¹⁵ *Id.*

³¹⁶ Notice of No Auction and Filing of Asset Purchase Agreement, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [425.pdf](#) at 1–2.

³¹⁷ *Id.*

³¹⁸ Limited Objection of Certain Landlords to Debtors' Proposed Sale of Assets, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [444.pdf](#).

³¹⁹ *Id.* at 1–3.

right to assign leases to subsidiaries and affiliates.³²⁰ The landlords stated they were worried that DB KRST Investors LLC would assign undesirable leases to undercapitalized entities and declare bankruptcy for each entity individually.³²¹ This would leave the landlords with virtually no recourse against shell companies. The landlords requested that the court order: (1) Krystal to catch up on all postpetition rent payments and remain current through the time when DB KRST Investors LLC designated whether the assets were to be included or excluded and (2) that “may not re-assign any of the Landlords’ leases to a subsidiary or any other party without the Landlords’ consent.”³²²

On May 13, 2020, the court granted an order approving the asset sale.³²³ In the order, the court stated that Krystal and their professionals complied with the Bidding Procedures and thus, Krystal would be allowed to sell its assets free and clear of all claims and liens.³²⁴ The court also stated that DB KRST Investors LLC was not an insider or an affiliate of Krystal and would be “entitled to the protections of Section 363(m) and (n) of the Bankruptcy Code” regarding the sale and purchased assets.³²⁵

Closing of Sale

Krystal and DB KRST Investors LLC closed the section 363 sale of substantially all of Krystal’s assets pursuant to the Asset Purchase Agreement on May 18, 2020.³²⁶ DB KRST Investors LLC designated “certain contracts, agreements and leases as Designation Right Assets.” DB KRST Investors LLC had until July 2, 2020 to determine which assets would be assumed or excluded. Additionally, DB KRST Investors LLC designated which assets they would assume and assign as of closing. In total, DB KRST Investors LLC designated 613 assets, comprised mostly of franchise and lease agreements.³²⁷ DB KRST Investors LLC assumed a total of 55 assets.³²⁸ Krystal published the notice of sale and deadline for filing proof of claims in The Charlotte Observer, The Wall Street Journal, The Birmingham News, The Atlanta Journal-

³²⁰ Notice of No Auction and Filing of Asset Purchase Agreement, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [425.pdf](#) at Ex. p. 48; Limited Objection of Certain Landlords to Debtors’ Proposed Sale of Assets, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [444.pdf](#) at 3.

³²¹ Limited Objection of Certain Landlords to Debtors’ Proposed Sale of Assets, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [444.pdf](#) at 4.

³²² *Id.*

³²³ Order (A) Approving Sale Motion and Asset Purchase Agreement, (B) Authorizing the Sale of Assets Outside the Ordinary Course of Business and Free and Clear of All Liens, Claims, Encumbrances, and Interests, (C) Authorizing the Assumption and Sale and Assignment of Certain Executory Contracts and Unexpired Leases, and (D) Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [468.pdf](#) at 1.

³²⁴ *Id.* at 7.

³²⁵ *Id.* at 9; 11 U.S.C. § 363(m)–(n).

³²⁶ Notice of (I) Closing of Sale of Substantially All of the Assets of the Debtors and (II) Filing of Designation Right Assets and Assigned Contracts, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [493.pdf](#) at 1.

³²⁷ *Id.* at 2.

³²⁸ *Id.* at 5.

Constitution, The Florida Times-Union, The State, and The Tennessean between May 8 and May 11 of 2020.³²⁹

Assumption and Rejection of Leases

After the notice was filed providing the cure amounts and terms, Krystal made it evident that it had planned on rejecting at least a portion of the leases and contractual agreements mentioned in their previous filings. The exact detail of which assignments and rejections was not provided until the debtor began filing notices containing lengthy charts of creditors names, property addresses, and a simple status of “Accepted/Rejected.”³³⁰ These charts were sent to all interested parties both listed on the chart and listed on the creditors matrix in the overall proceeding.³³¹

Operatively, the Sale Order and Agreement allowed the debts to assume and assign the Assigned Contracts to the Purchaser, and the purchaser had the right to designate these contracts as assumed and assigned until July 2, 2020. It further provided:

Pursuant to the Amended Order Establishing Procedures for the Assumption or Rejection of Certain Executory Contracts and Unexpired Leases [Docket No. 535] and the Notice of Rejection of Remaining Executory Contracts and Unexpired Leases [Docket No. 581], all executory contracts or unexpired leases that (i) were not Rejected Contracts or Assigned Contracts or (ii) had not been rejected or assumed pursuant to a prior order of the Court or a prior notice were rejected effective as of July 2, 2020.³³²

Ultimately Krystal rejected over 100 leases from their register which opened a fresh wound with their franchisees.³³³ Following July 2, 2020, leaseholders and restaurant owners began stepping forward voicing grievances of this Babylonian style decision. Mainly, restaurant owners sought Krystal to pay the past due balances of their rent for which they received payment, and accordingly, the landlords sought those payments that were never received during the stay of this proceeding.

³²⁹ Affidavit Regarding Publication of Notice of Sale and Deadline for Filing of Proofs of Claim in The Charlotte Observer, The Wall Street Journal, The Birmingham News, The Atlanta Journal-Constitution, The Florida Times-Union, The State, and The Tennessean, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [519.pdf](#), at 4.

³³⁰ See generally Notice of (I) Closing of Sale of Substantially All of the Assets of the Debtors and (II) Filing of Designation Right Assets and Assigned Contracts Lists, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [493.pdf](#).

³³¹ Notice to Contract Parties to Potentially Assumed Executory Contracts and Unexpired Leases, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [310.pdf](#), at 1.

³³² Notice of Rejection of Remaining Executory Contracts and Unexpired Leases, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [581.pdf](#), at 1.

³³³ See generally, Motions to Reject Executory Contracts.

Dismissal of the Chapter 11 Case: A Light at the End of the Tunnel

After closing the sale, Krystal was nearing the finish line for their Chapter 11 case. After several intense months, they had identified a buyer, achieved court approval, and closed the sale. Additionally, through the Settlement Agreement, they had cleansed themselves of most of their debt and other obligations. On August 17, 2020, Krystal filed a motion for entry of an order for dismissal of their Chapter 11 case.³³⁴ In the motion, Krystal stated that after the sale of substantially all of their assets, “no meaningful assets remain in the Debtors’ estates for the Debtors to monetize or distribute to creditors.”³³⁵ Accordingly, the Debtors have determined that dismissal is the most effective way to conclude these Chapter 11 cases.”³³⁶ Krystal argued dismissal was warranted because it would avoid accrual of administrative expenses, “provide for a limited winddown framework,” and “otherwise be in the best interest of the Debtors, their estates, and their creditors.”³³⁷

The motion further stated that a portion of the \$4,696,300 amount for winddown costs would be allocated to pay any unpaid U.S. Trustee fees, Krystal’s professional fees of \$840,000 and \$160,000 of the OCC’s professional fees as laid out in the Settlement Agreement.³³⁸ The Debtors requested that after a final fee application, the court enter an order to dismiss and close the jointly administered Chapter 11 cases.³³⁹

Krystal argued that under section 1112(b)(1) of the Bankruptcy Code, they had demonstrated there was cause to dismiss and that it would be in the best interest of the creditors and the estate.³⁴⁰ They argued that was because there was essentially nothing left in the estates to liquidate and distribute to creditors, that the accrual of administrative fees was damaging the estate, and there was no feasible plan for rehabilitation.³⁴¹ Alternatively, Krystal argued that cause existed under section 305(a) at the court’s discretion because of the same reasons.³⁴²

After the motion, several parties filed objections to the final order motion. These creditors included Southeast Gas, Live Oak Restaurant Services and T.B. Starke, Inc., Black Horse Studio, and two individuals, Cecelia Jenks and Jerry Van Hoose. Southeast Gas objected because a “Krystal location in Greenville[,] Alabama ” had not paid the natural gas utility company \$725.51 for the period January 2 to January 23 of 2020.³⁴³ Krystal initially owed

³³⁴ Debtors' Motion for Entry of an Order Regarding Dismissal of the Debtors' Chapter 11 Cases and Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [596.pdf](#) at 1.

³³⁵ *Id.* at 2.

³³⁶ *Id.*

³³⁷ *Id.*

³³⁸ *Id.* at 6.

³³⁹ *Id.*

³⁴⁰ *Id.* at 7; 11 U.S.C. § 1112(b)(1) (2010).

³⁴¹ *Id.* at 9.

³⁴² *Id.* at 13.

³⁴³ Objection to Debtors' Motion for Entry of an Order Regarding Dismissal of the Debtors' Chapter 11 Cases and Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [617.pdf](#) at 2.

\$836.73 but made a payment of \$111.22 on March 30, 2020 leaving the outstanding balance.³⁴⁴ Black Horse and Ceceilia Jenks both objected individually for unpaid services related to advertising photo shoots in December 2019. Black Horse invoiced the photoshoots for a total of \$18,715.36.³⁴⁵ Ceceila Jenks stated in her objection that she did an advertising photoshoot and was expecting full payment but failed to include the amount she was owed.³⁴⁶

Live Oak Restaurant Services and T.B. Starke, Inc. objected because they sold “the operations, assets, and contractual rights of Krystal-branded restaurants” in Lake City and Live Oak, Florida.³⁴⁷ The total purchase price was \$200,000 and Krystal took possession after closing. Although Krystal acknowledged the secured claims in their filings, they listed the cure amount as \$0.³⁴⁸ The objection states the entities filed adversary proceedings seeking a declaratory judgment and payment of the \$200,000.³⁴⁹ They objected to the extent the dismissal would create a dismissal of their adversary proceedings.

If there were an award for the most comical bankruptcy objection, Jerry Van Hoose would surely receive it. Mr. Van Hoose’s objection is best presented in his own words:

That on or about the 3rd day of December 2018, the Plaintiff was a customer and business invitee of the Defendants, The Krystal Company, at the restaurant located in London, Kentucky. As the Plaintiff approached the Krystal Company restaurant entrance, which displayed an "OPEN" sign, the Plaintiff attempted to open the door, however The Krystal Company had failed to unlock the door. As a result, the Plaintiff received a right arm shoulder fracture, a sprain to his right arm and a rotator cuff injury.³⁵⁰

Mr. Van Hoose claimed Krystal had breached their duty of care and as a result, he “suffered permanent injuries[,] . . . medical bills, . . . severe mental pain and anguish past and future and physical pain and suffering.”³⁵¹ In the wise words of Michael Scott and Wayne Gretzy, “You miss 100% of the shots you don’t take.” Sadly, it appears that he missed this shot and his window of opportunity, like the Krystal door, was also closed and locked. Additionally, four

³⁴⁴ *Id.* at 3.

³⁴⁵ Appeal to Bankruptcy Dismissal Motion (Objection) filed by Black Horse Studio, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [603.pdf](#) at 1.

³⁴⁶ Objection to Dismissal Motion Regarding Dismissal of Debtor's Chapter 11 Cases and Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [601.pdf](#) at 2.

³⁴⁷ Adversary case 20-06176. Complaint against The Krystal Company, Krystal Restaurant, LLC, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [609.pdf](#) at 3.

³⁴⁸ Supplemental Notice to Contract Parties to Potentially Assumed Executory Contracts and Unexpired Leases, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [441.pdf](#) at 3.

³⁴⁹ Adversary case 20-06176. Complaint against The Krystal Company, Krystal Restaurant, LLC, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [609.pdf](#) at 95.

³⁵⁰ Objection to Debtors' Motion For Entry of an Order Regarding Dismissal of the Debtors' Chapter 11 Cases Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [611.pdf](#) at 2.

³⁵¹ *Id.*

individuals filed handwritten letters in response to the motion for dismissal. The handwriting is difficult to read, but it appears the letters all dealt with the issues the individual's faced with unemployment from certain Krystal locations closing.³⁵²

The court responded to these objections in a memorandum filed on November 12, 2020. The memorandum explains the harsh realities of being an unsecured creditor in a bankruptcy proceeding.³⁵³ The memorandum explains that because Wells Fargo's secured claim was in excess of the total value of Krystal's assets, there was no way for unsecured creditors to be paid. Additionally, the memorandum states that Wells Fargo did not receive around \$24 million of their claims.³⁵⁴ The final section of the memorandum justifies the result of the claim stating that while "many employees lost jobs arising out of lay-offs during the pandemic or because some locations closed, many others continued to have employment."³⁵⁵ What this chapter 11 case accomplished was the preservation of jobs, the payment of rent in full under most leases, and a reduction in the amount of the Wells Fargo debt.

The memorandum further states that the process worked for some parties, such as employees and landlords.³⁵⁶ The result for others, like the objectors, was a disaster. The point is that the disaster resulted from financial circumstances, not the operation of the bankruptcy laws." The memorandum defends the circumstances stating that it is not corporate welfare as suggested in one of the handwritten letters. The memorandum concludes on a somber note:

It has been said that, in many bankruptcy cases, there are no good alternatives, only less bad ones. As financial realities in this case took hold, it became clear that, for most creditors, including the objectors, there were not even "less bad" alternatives. The Court is saddened that it can offer only an explanation for what happened and why. For the reasons stated above, the Court must overrule the objections, and will enter a separate order dismissing this case.

It is important to see the effects of bad corporate stewardship on unsecured creditors like the objectors. There are certainly consequences that trickle down to employees and independent contractors that are not felt by certain "higher up" individuals. However, as the court noted, this

³⁵² Letter filed by Khaaliyah Berry (rfs), Krystal Restaurant, LLC, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [617.pdf](#) at 1.

³⁵³ Memorandum Regarding Objections To Dismissal of The Debtor's Chapter 11 Cases, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [625.pdf](#) at 1.

³⁵⁴ *Id.* at 5.

³⁵⁵ *Id.* at 9.

³⁵⁶ *Id.* at 7.

was because of bad financial decisions, not the operation of bankruptcy law.³⁵⁷ Had Krystal not been afforded the opportunity to file Chapter 11, the business would likely have liquidated, harming even more individuals.

Fee Application

On September 21, 2020, the first and final fee application was filed.³⁵⁸ Material fees included: (1) \$1,533,613.50 to King and Spalding, LLP; (2) \$258,800 to Scroggins & Williamson, P.C.; (3) \$2,248,270 to Alvarez & Marsal; (4) \$1,732,500 to Piper Sandler & Co.; (5) \$545,266.35 to Kelley Drye & Warren LLP; (6) \$171,381 to Arnall Golden Gregory LLP; and (7) \$182,857.95 to FTI Consulting for a total of \$6,672,688.80.³⁵⁹ On October 16, 2020, the court granted the fee application noting that there were no objections and “that the legal and factual bases set forth in the Application establish just cause for the relief granted.”³⁶⁰

The Grand Finale: Dismissal

Ultimately, on November 12, 2020, the court entered an order dismissing Krystal’s Chapter 11 cases.³⁶¹ The order stated that Krystal’s board of directors were entitled to seek dissolution and would not be required to pay any related taxes or fees.³⁶² Additionally, the OCC was to be dissolved and discharged from any rights or duties.³⁶³

Conclusion

In the face of financial pressure, bankruptcy can quickly become the only option for a company such as Krystal. As this brief glimpse into the mechanics of Chapter 11 has shown, handing the reins over to a court can quickly achieve the relief a debtor seeks. Within 9 months Krystal exited bankruptcy under new ownership, in much better financial condition, and equipped to re-enter the market. As for the unsecured creditors, they were left appeased by either a cure cost or returned control of property that had been tied up with unoccupied, unpaying lessees. Unfortunately for employees and independent contractors, the court made it clear that there was nothing left. This Chapter 11 case serves as an example of how companies exit bankruptcy proceedings through a 363 sale when it is not practical to reorganize.

³⁵⁷ See generally Memorandum Regarding Objections to Dismissal of The Debtor's Chapter 11 Cases, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [625.pdf](#).

³⁵⁸ Consolidated First and Final Application for Allowance of Fees and Reimbursement of Expenses, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [610.pdf](#) at 1.

³⁵⁹ *Id.* at 16.

³⁶⁰ Order Granting Consolidated First and Final Application for Allowance of Fees and Reimbursement of Expenses, Subject to Objection, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [619.pdf](#) at 2.

³⁶¹ Order Dismissing The Debtor's Chapter 11 Cases and Granting Related Relief, In re The Krystal Company, No. 20-61065 (PWB) (Bankr. N.D. Ga. Jan. 19, 2020) [626.pdf](#) at 1.

³⁶² *Id.*

³⁶³ *Id.*