UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

In re:	)	
	)	Chapter 11
SCHWAB INDUSTRIES, INC., *et al.*[1]	)	
	)	Case No. 10-60702-rk
Debtors.	)	(Jointly Administered)
	)	
	)	Judge Russ Kendig

OBJECTION OF THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS TO DEBTORS' MOTION FOR ENTRY OF A FINAL ORDER (I) AUTHORIZING POST-PETITION SECURED SUPERPRIORITY FINANCING PURSUANT TO BANKRUPTCY CODE SECTIONS 105, 361, 362, 363(C), 363(E), 364(C)(1), 364(C)(2), 364(C)(3), 364(D) AND 364(E), (II) GRANTING ADEQUATE PROTECTION PURSUANT TO SECTIONS 361, 363 AND 364 OF THE BANKRUPTCY CODE, (III) MODIFYING THE AUTOMATIC STAY, AND (IV) SETTING A FINAL HEARING PURSUANT TO BANKRUPTCY RULE 4001

The Official Committee of Unsecured Creditors (the "*Committee*") appointed in the above-captioned bankruptcy cases, by and through its proposed counsel, hereby objects (the "*Objection*") to the entry of a final order (the "*Final Order*") on the *Debtors' Motion for Entry of a Final Order (I) Authorizing Post-Petition Secured Superpriority Financing Pursuant to Bankruptcy Code Sections 105, 361, 362, 363(c), 363(e), 364(c)(1), 364(c)(2), 364(c)(3), 364(d) and 364(e), (II) Granting Adequate Protection Pursuant to Sections 361, 363 and 364 of the Bankruptcy Code, (III) Modifying the Automatic Stay, and (IV) Setting a Final Hearing Pursuant to Bankruptcy Rule 4001* (the "*Motion*"). In support of this Objection, the Committee states:

PRELIMINARY STATEMENT

1. The proposed debtor-in-possession financing (the "*DIP Facility*") demands a critical and thorough evaluation at this important juncture in these chapter 11 cases. While the

[1] The Debtors are Schwab Industries, Inc. ("*SII*"), Medina Cartage Co. ("*MCC*"), Medina Supply Company ("*MSC*"), Quality Block & Supply, Inc. ("*QBS*"), O.I.S. Tire, Inc. ("*OIS*"), Twin Cities Concrete Company ("*TCC*"), Schwab Ready-Mix, Inc. ("*SRM*"), Schwab Materials, Inc. ("*SMI*") and Eastern Cement Corp. ("*ECC*").

Committee recognizes that the Debtors' liquidation, and the complete disenfranchisement of unsecured creditors, may result if the estates are denied immediate access to post-petition liquidity, the Debtors similarly risk their own survival by jumping blindly into a commercially unreasonable financing transaction that also fails to comply with the Bankruptcy Code and related processes. Even in the very best case scenario, these estates and unsecured creditors will be seriously prejudiced without intervention from this Court and significant modification of the proposed DIP Facility.

2. As an initial matter, the Committee seeks additional evidence that the Debtors engaged in a reasonable effort to secure an alternative financing arrangement under more advantageous terms than those offered by the proposed DIP Facility lender, and that a sufficient equity cushion exists to justify the imposition of priming liens on the Debtors' assets. This evidentiary showing is necessary to provide comfort to the Committee that more favorable financing could not have been found elsewhere, and that the potentially significant risk to the estates from the proposed DIP Facility is justifiable under the circumstances.

3. Additionally, the Committee has identified numerous terms in the proposed DIP Facility that are above-market, commercially unreasonable or potentially hazardous to unsecured creditors and the Debtors themselves. These terms include a series of commitment, exit and break-up fees, insufficient protections for estates and their professionals, and conditions to lending that will be costly, time-consuming and unnecessary in light of the priming liens and other protections proposed to be granted to the DIP Facility lender. Yet the absence of any meaningful check on the DIP Facility lenders' virtual absolute discretion under the loan is perhaps its most objectionable feature.

4. The 13-week DIP Facility budget also relies on projections that are (perhaps wildly) inconsistent with estimates prepared by the Debtors' financial advisor and ignores several potentially significant expenses that will have a noticeable impact on cash flow during the initial weeks of these cases. For all of these reasons, the Committee requests that each of its concerns detailed in the following twenty-two pages of objections be addressed and rectified before the Committee will be satisfied that the proposed DIP Facility is commercially reasonable, in the best interests of unsecured creditors and should be finally approved by this Court.

BACKGROUND

A. The Chapter 11 Cases

5. On February 28, 2010 (the "*Petition Date*"), Schwab Industries, Inc. and its affiliated debtors and debtors-in-possession (collectively, the "*Debtors*") filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code (the "*Bankruptcy Code*") in the United States Bankruptcy Court for the Northern District of Ohio (the "*Court*").

6. The Debtors are currently operating and managing their businesses as debtors-in-possession pursuant to sections 1107 and 1108 of the Bankruptcy Code.

7. The Committee was appointed on March 9, 2010, and retained Freeborn & Peters LLP and Frost Brown Todd LLC as its lead and local counsel, respectively, on March 11, 2010. The Debtors subsequently granted the Committee until 5:00 p.m. (ET) on Monday, March 15, 2010 to submit any objections to the Motion.

B. Pre-Petition Indebtedness

8. The Debtors' pre-petition secured lenders are KeyBank National Association (as lender and agent, "*KeyBank*"), The Huntington National Bank and Bank of America, N.A.

(collectively, the "*Pre-Petition Lenders*"). According to the Motion, the Pre-Petition Lenders and the Debtors entered into an Amended and Restated Credit Agreement on October 18, 2007 (the "*Pre-Petition Loan Agreement*"), which provided for a revolving line of credit and two term loan facilities, called "Term A" and "Term B." As of December 31, 2009, the Debtors owed the Pre-Petition Lenders $8,582,950 with respect to the revolving line of credit, $19,125,245 with respect to the "Term A" loan and $31,995,586 with respect to the "Term B" loan, resulting in aggregate outstanding indebtedness of not less than $59,703,781. To secure these loans, the Pre-Petition Lenders were granted a first-priority security interest in substantially all of the personal property assets of the Debtors and a first-priority mortgage interest in substantially all of the Debtors' real property (collectively, the "*Pre-Petition Collateral*").[2]

9. In its objection to the Motion (Docket No. 36) (the "*KeyBank Objection*"), KeyBank asserts that prior to the Petition Date, the Debtors defaulted on the Pre-Petition Loan Agreement and, on January 13, 2010, KeyBank provided formal notice to the Debtors of their various defaults and exercised its right to cease further advances under the Pre-Petition Loan Agreement. KeyBank Objection, at ¶ 4.

10. The Debtors and KeyBank apparently discussed the terms of a post-petition financing facility prior to the Petition Date. KeyBank indicated that it provided the Debtors with a proposed term sheet for post-petition financing that would allow the Debtors to operate through the closing of the sale of substantially all of the Debtors' assets under section 363 of the Bankruptcy Code. The Debtors apparently never formally accepted or rejected the term sheet.

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[2] Nothing herein shall prejudice the Committee's rights to investigate the Pre-Petition Lenders' collateral, and to challenge the validity, priority and amount of the Pre-Petition Lenders' claims and liens. Accordingly, the Committee hereby reserves all of its rights to investigate these matters as necessary and appropriate during these cases.

Id. at ¶ 5. Rather, on the eve of the Petition Date, the Debtors declared their intention to file for chapter 11 protection and that DIP financing would be obtained from a third party.

C. The Proposed DIP Facility

11. On the Petition Date, the Debtors filed the Motion seeking authority to obtain post-petition financing from EFO Financial Group, LLC (succeeded in interest by Naples Lending Group, L.C., the "*DIP Lender*").[3] In brief, the proposed DIP Facility provides the Debtors with a maximum commitment of $18,308,655 to be advanced in three stages. Proceeds of the DIP Facility must be used in accordance with a 13-week cash-flow budget (the "*Budget*") attached to the Motion. The DIP Facility has a twelve-month maturity. Interest is charged in the amount of twelve percent (12%) per annum on a monthly basis, with default interest established at twenty percent (20%). The DIP Facility provides for a series of lucrative fees for the DIP Lender, including, among others: (a) a commitment fee of two percent (2%) of each advance; (b) an exit fee of two percent (2%); (c) a loan servicing fee of 1.1% of the maximum amount of each advance; and (d) an unused line fee of 35 basis points per month of the principal amount of loan proceeds yet to be advanced.

12. The proposed DIP Facility is to be secured by a first-priority lien on the Debtors' unencumbered assets pursuant to section 364(c)(2) of the Bankruptcy Code, and a first-priority priming lien on all other assets of the Debtors pursuant to section 364(d)(1) of the Bankruptcy Code (the "*Priming Liens*"). All obligations under the DIP Facility are granted superpriority administrative expense status pursuant to section 364(c)(1) of the Bankruptcy Code, senior to all other administrative expenses, subject only to a professional fee carveout (the "*Carveout*"). The terms of the DIP Facility also provide that the DIP Lender's collateral will not include

[3] Terms not otherwise defined herein shall have the meaning ascribed to them in the Motion.

segregated proceeds or property recovered in respect of avoidance actions. *See* Interim DIP Order, at ¶ 8.

13. The Debtors also propose to adequately protect the Pre-Petition Lenders from any diminution in the value of their collateral with the following: (a) replacement liens, subject to both the Priming Liens and the Carveout; and (b) superpriority administrative claims that are junior to the DIP Lender's superpriority claims and the Carveout.

D. KeyBank's Objection and Entry of the Interim Order

14. KeyBank, on behalf of the Pre-Petition Lenders, filed the KeyBank Objection, asserting that, among other things: (a) the adequate protection proposed by the Debtors is inadequate given the absence of an equity cushion in the Pre-Petition Collateral; (b) the DIP Lender is not entitled to priming liens and superpriority administrative claims in an interim financing order; and (c) the DIP Lender's lending commitment is illusory because it permits the DIP Lender to effectively terminate that commitment in its sole and absolute discretion.

15. On March 10, 2010, the Court overruled the KeyBank Objection and entered an interim order (Docket No. 44) (the "*Interim Order*"), which granted all of the relief requested in the Motion on an interim basis, and scheduled a final hearing on the Motion for March 17, 2010.

ARGUMENT

16. Section 364(d) of the Bankruptcy Code governs the circumstances under which a debtor may incur debt secured by a priming lien:

> (1) The court, after notice and a hearing, may authorize the obtaining of credit or the incurring of debt secured by a senior or equal lien on property of the estate that is subject to a lien only if –
>
> (A) the trustee is unable to obtain such credit otherwise; and
>
> (B) there is adequate protection of the interest of the holder of the lien on the property of the estate on which such senior or equal lien is proposed to be granted.

> (2) In any hearing under this subsection, the trustee has the burden of proof on the issue of adequate protection.

11 U.S.C. § 364(d).

17. While the Committee recognizes the Debtors need financing to cover operating expenses, including payroll obligations, the Committee objects to the burdensome and unnecessary protections being required by the proposed DIP Lender for its money. The Committee further submits that the Debtors have failed to satisfy the requirements of section 364(d) of the Bankruptcy Code in certain critical respects. At the very least, the DIP Facility should not be approved by this Court without compelling proof from the Debtors (1) as to the absence of any meaningful financing alternatives, and (2) that the proposed financing ultimately will not obliterate these estates given its many onerous terms, a significant risk in the Committee's opinion. This Court simply cannot risk the redistribution of the estates' unencumbered assets to the DIP Lender or the Pre-Petition Lenders as adequate protection.

A. The Debtors Have Neither Demonstrated the Absence of Alternative Financing Arrangements on Less Onerous Terms, Nor Adequately Proven the DIP Facility's Necessity.

18. The Committee acknowledges that the Debtors are entitled to obtain debtor-in-possession financing, but this entitlement is not without limits. Particularly in this case, where the Debtors seek approval of a "priming" DIP Facility, including onerous terms and substantial fees, the Debtors must make a showing that it diligently sought alternative financing arrangements on more favorable terms before accepting the DIP Facility. The Motion, however, makes no such showing, and the Debtors rely instead on mere conclusory statements to convince parties-in-interest that their marketing efforts were sufficient.

19. The Motion alleges only that:

> Debtors have sought financing (both in and out of bankruptcy) from numerous possible lending services, including key customers,

> such as National Lime and Stone Company, and both conventional and asset based lenders, among others. Debtors have pursued such lending opportunities seeking lending both (i) on an unsecured, administrative priority basis; and also (ii) secured by a junior lien on some or all of Debtors' assets. Unfortunately, these efforts have been unsuccessful. The DIP Facility is the only opportunity Debtors are aware of for the financing required to complete an effective reorganization of Debtors' operations and businesses.

Motion, at ¶¶ 27-29. The Debtors, however, do not disclose specific information regarding their efforts to obtain financing on better terms. The Debtors do not provide any evidence regarding under what terms they sought post-petition financing, the number of potential lenders they approached, how many potential lenders provided proposals and why such proposals were deemed unsatisfactory. The Debtors even fail to mention in their Motion that the Pre-Petition Lenders presented a term sheet to lend additional funds to the Debtors, and do not explain why the Pre-Petition Lenders' proposal was inadequate and, apparently, not even worth negotiating.

20. In the absence of a showing that the Debtors have made reasonable efforts to obtain financing on better terms than those of the DIP Facility, this Court should not approve it on a final basis. Such a finding is consistent with the views of other courts on this issue:

> Although a debtor is not required to seek credit from every possible source, *see In re Snowshoe Co., Inc.*, 789 F.2d 1085, 1088 (4th Cir. 1986), a debtor must show that it made a "reasonable effort" to obtain post-petition financing from other potential lenders on less onerous terms and that such financing was unavailable. *See In re Ames Dept. Stores*, 115 B.R. 34, 40 (Bankr. S.D.N.Y. 1990) (citations omitted). A court must make its decision as to "[h]ow extensive the debtor's efforts to obtain credit must be" on a case-by-case basis. *In re Reading Tube Industries*, 72 B.R. 329, 332 (Bankr. E.D. Pa. 1987).

Suntrust Bank v. Den-Mark Const., Inc., 406 B.R. 683, 691 (E.D.N.C. 2009); *see also In re 495 Cent. Park Ave. Corp.*, 136 B.R. 626, 630-31 (Bankr. S.D.N.Y. 1992) ("Section 364(d)(1) does not require the debtor to seek alternate financing from every possible lender. However, the debtor must make an effort to obtain credit without priming a senior lien."); *In re Stacy Farms*,

78 B.R. 494, 498 (Bankr. S.D. Ohio 1987) (holding that debtor failed to carry its burden under section 364(d) where there was no evidence that the debtor had applied for loans from institutions other than its pre-petition senior lender and the proposed priming lender).

21. While the courts do not appear to have established a bright-line test for evaluating the sufficiency of a debtor's efforts to obtain alternative debtor-in-possession financing, the Committee submits that under no interpretation of applicable case law can the Debtors' disclosures be considered adequate. The Debtors have not provided the Committee or other parties-in-interest with *meaningful* information concerning the number of alternative lenders approached, the terms of competing financing proposals received (if any), or evidence that in the absence of the DIP Facility, the Debtors would be unable to operate as a going concern in chapter 11. In other words, no proof has been provided that unsecured creditors are better off with the DIP Facility than without it. While it may indeed be the case that the Debtors have engaged in reasonable efforts to obtain alternative financing on less onerous terms, a full disclosure of those efforts must be made before the Committee can support the DIP Facility.

B. The Debtors Have Not Established That Their Proposed Adequate Protection Is Sufficient.

22. Section 364(d)(1)(B) of the Bankruptcy Code provides that a court may authorize a credit facility secured by priming liens only if the debtor provides adequate protection to the creditor being primed. The DIP Facility purports to adequately protect the Pre-Petition Lenders in only a superficial manner.

23. According to section 361 of the Bankruptcy Code, adequate protection may be provided by:

> (1) requiring the trustee to make a cash payment or periodic cash payments to such entity, to the extent that the stay under section 362 of this title, use, sale, or lease under

> section 363 of this title, or any grant of a lien under section 364 of this title results in a decrease in the value of such entity's interest in such property;
>
> (2) providing to such entity an additional or replacement lien to the extent that such stay, use, sale, lease, or grant results in a decrease in the value of such entity's interest in such property; or
>
> (3) granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense, as will result in the realization by such entity of the indubitable equivalent of such entity's interest in such property.

11 U.S.C. § 361. Here, the Debtors propose to adequately protect the Pre-Petition Lenders by granting replacement liens and superpriority administrative claims, to the extent of diminution of value in the Pre-Petition Collateral, subject to the Priming Liens and the Carveout.

24. In order to adequately protect secured lenders that are being primed pursuant to section 364(d)(1)(B) of the Bankruptcy Code, the debtor has the burden of demonstrating that (1) sufficient equity will remain in the collateral after the senior lien is granted to cover the indebtedness of the primed lender or (2) the proceeds of the loan to be secured by the senior lien will result in an increase in the value of the collateral. *See, e.g.*, *Swedeland Dev. Group, Inc. v. Resolution Trust Corp. (In re Swedeland Dev. Group, Inc.)*, 16 F.3d 552, 567 (3d Cir. 1994) ("The law does not support the proposition that a creditor . . . undersecured by many millions of dollars, may be adequately protected when a superpriority lien is created without the provision of additional collateral by the debtor."); *In re Phoenix Steel Corp.*, 39 B.R. 218, 224 (D. Del. 1984) ("The concept of adequate protection does not envision a court stripping a secured creditor of the benefit of its bargain."); *Shaw Indus., Inc. v. First Nat'l Bank of PA (In re Shaw Indus., Inc.)*, 300 B.R. 861, 865 (Bankr. W.D. Pa. 2003) ("The purpose of providing 'adequate protection' is to insure that a secured creditor receives in value essentially what he bargained for."); *In re*

Windsor Hotel, L.L.C., 295 B.R. 307, 314 (Bankr. C.D. Ill. 2003) ("The authorization to prime an existing lien should not be read as authorization to increase substantially the risk of the existing lender in order to provide security for a new, post-petition lender. When the effect of the new borrowing with a senior lien is merely to pass the risk of loss to the holder of the existing lien, the request for authorization should be denied. The burden is on the movant to prove that existing lienholders are adequately protected.").

25. Courts have refused to grant priming liens on collateral where the existing creditor is undersecured, or where an inadequate equity cushion exists to adequately protect the existing secured creditor. While the courts differ on the amount of equity cushion that is considered sufficient to adequately protect an existing secured creditor, case law generally has established that this equity cushion should be at least 20% – if not substantially greater. *See, e.g.*, *Pistole v. Mellor (In re Mellor)*, 734 F.2d 1396, 1401 (9th Cir. 1984) ("A 20% cushion has been held to be an adequate protection for a secured creditor."); *Kost v. First Interstate Bank of Greybull (In re Kost)*, 102 B.R. 829, 831 (D. Wyo. 1989) ("Case law has almost uniformly held that an equity cushion of 20% or more constitutes adequate protection."); *Travelers Ins. Co. v. Plaza Family P'ship (In re Plaza Family P'Ship)*, 95 B.R. 166, 171-72 (E.D. Cal. 1989) ("Generally, if the value of a debtor's property in which the creditor has an interest is at least fifty percent greater than the value of the creditor's lien, most courts will conclude that the value of the property sufficiently satisfies the creditor's claim, and provides adequate protection."); *In re Las Torres Dev., L.L.C.*, 2009 Bankr. LEXIS 2983, at *27 (Bankr. S.D. Tex. Sept. 17, 2009) ("[C]ase law is clear that an equity cushion of 20% or more constitutes adequate protection."); *In re Snead*, 2008 Bankr. LEXIS 1160, at *3 (Bankr E.D.N.C. Apr. 1, 2008) ("Therefore, a 27% equity cushion exists in the property, and the court finds that this provides sufficient protection

of Bayview's interest without the necessity of adequate protection payments."); *In re WRB v. Assocs. Joint Venture*, 106 B.R. 215, 220 (Bankr. D. Mont. 1989) ("MAILP is adequately protected by a substantial equity cushion of 40%.").

26. Unfortunately in this case, the Debtors have done nothing but allege – albeit in a conclusory manner – that the Pre-Petition Lenders will be adequately protected. Motion, at ¶ 40 ("The Debtors submit that the Pre-Petition Lenders' interests in the Collateral are adequately protected[.]"). These types of statements are not enough. The Debtors are required to put forth strong evidence (including credible financial projections) to establish that the creditors being primed are adequately protected. *See, e.g.*, *In re Windsor Hotel, L.L.C.*, 295 B.R. at 314 ("A finding of adequate protection should be premised on facts, or on projections grounded on a firm evidentiary basis."); *In re Mosello*, 195 B.R. 277, 292 (Bankr. S.D.N.Y. 1996) (same). The Debtor has provided no evidence that *any* equity cushion – let alone a sufficient equity cushion – exists, or that the value of the Pre-Petition Collateral will be improved by the proceeds of the DIP Facility. Without such evidence, the Committee cannot consent to the Debtors' adequate protection proposal.

27. Indeed, the evidence provided by KeyBank in the KeyBank Objection suggests that *no* equity cushion will remain after the granting of the Priming Liens, and therefore, the adequate protection being offered by the Debtors is illusory. KeyBank Objection, at ¶12 (implying that a collateral shortfall of $4.5 million will result from the granting of the Priming Liens). These figures cause the Committee serious concern, in that the granting of the Priming Liens, and the subordination of the Pre-Petition Lenders' liens, may result in the Pre-Petition Lenders holding a substantial deficiency claim, and will dilute whatever value exists in these estates for unsecured creditors. In light of these concerns, it is imperative that the Debtors

present compelling evidence that KeyBank's calculations are incorrect, and that a sufficient equity cushion will in fact exist upon the approval of the DIP Facility.

28. The Committee also notes that the Interim Order purports to grant the Pre-Petition Lenders replacement liens in *all* "Collateral," which is defined as both the Pre-Petition Collateral *and* the unencumbered assets that will become subject to the DIP Lender's first-priority liens. Interim DIP Order, at ¶ 12. To the extent that these adequate protection liens do grant the Pre-Petition Lenders additional post-petition liens, such liens may serve to cure any pre-petition defects in the Pre-Petition Collateral. As the Committee has not been afforded a reasonable amount of time to investigate the validity, priority and extent of the Pre-Petition Lenders' liens, the Committee requests that the granting of replacement liens to the Pre-Petition Lenders be subject in all respects to the Committee's right to perform a collateral analysis and to initiate proceedings in this Court to challenge the validity, priority or extent of the Pre-Petition Lenders' liens, to the extent that defects are uncovered.

C. The Debtors Should Not Be Permitted To Grant Liens on Unencumbered Assets, and Must Preserve Both Reclamation Rights and the Property Rights of Non-Debtors.

29. In the Motion, the Debtors propose to grant the DIP Lender liens in all unencumbered assets of the estates, and to grant the Pre-Petition Lenders replacement liens in such assets. The effect of granting these liens, to the extent that unencumbered assets even exist, will be to deprive unsecured creditors of a potentially significant source from which their claims may be satisfied. Moreover, the Debtors fail to establish the nature or amount of their unencumbered assets, leaving the Committee with no method by which to gauge the reasonableness of this request, or the impact of the granting of such liens on the estates. Without a detailed accounting by the Debtors of their unencumbered assets, and the value of the granting

of liens on those assets, the Debtors' request should be denied. Based upon preliminary discussions with the Debtors' financial advisors, there may be considerable value in unencumbered assets.

30. Any final order approving the DIP Facility also must provide that the rights of creditors to assert reclamation claims under section 546 of the Bankruptcy Code are not affected by the DIP Facility or the Priming Liens being granted to the DIP Lender. In addition, the order should explicitly state that the Priming Liens do not extend to any property owned by third parties – such as raw materials – that were in the Debtors' possession as of the Petition Date, or come into the possession of the Debtors after approval of the DIP Facility.

D. The DIP Lenders' Commitment To Loan Is Illusory at Best.

31. As set forth in the DIP Lender's commitment to lend, attached as Exhibit B to the Motion (the "*Commitment*"), the DIP Lender may terminate its commitments under the DIP Facility at any time and for any reason:

> In addition, within twenty one (21) business days following the later of (a) the Closing of the Interim Advance, or (b) following the Lender's receipt of the last item of due diligence materials required by it to have been furnished by the Borrower, the Lender, in its sole discretion, may choose to terminate this Commitment with respect to the Final Advance following the Full Due Diligence Review, *for any reason whatsoever*, and shall deliver to Borrower in writing notice of its election to withdraw and terminate the Commitment with respect to the Final Advance.

Commitment, at p. 13.

32. That the DIP Lender's so-called "Commitment" is anything but an obligation to loan is troubling. Yet the DIP Lender effectively seeks to be entitled to hundreds of thousands of dollars in commitment fees, as well as valuable Priming Liens, without the burden of actually having to provide a loan to these estates! The very likely scenario that the DIP Facility could be approved, only to have the DIP Lender back out without consequence, will result in irreparable

harm to these estates, and in particular, the unsecured creditors, whose position will further deterioriate without a corresponding benefit. If this Court is inclined to grant the Motion and approve the DIP Facility, it should, at a minimum, require that the above termination provision be stricken, or that realistic conditions be imposed on the DIP Lender's right to terminate the Commitment.

E. Certain Terms of the DIP Facility Are Onerous and Commercially Unreasonable.

33. Certain of the terms of the DIP Facility appear to be onerous and commercially unreasonable, and may result in a significant diminution of value of these estates to the detriment of unsecured creditors. Without a showing by the Debtors that such terms are reasonable under the circumstances, the DIP Facility should not be approved in its current form.

34. *Commitment, servicing and other fees*. As an initial matter, the DIP Facility proposes to levy a series of fees against the estates, in amounts that appear to be well in excess of those imposed by other debtor-in-possession lenders against similarly-situated debtors. These fees, which are paid automatically pursuant to draws on the DIP Facility, include the following:

- Loan application fee of $30,000 (Commitment, at p. 15);
- Commitment Fee: 2% of each Advance (for Final Advance, this fee is due at the time of the initial disbursement, but shall be equal to 2% of entire commitment) (Commitment, at p. 14);
- Loan Servicing Fee: 1.1% of the maximum principal amount of each Advance, due at closing of each Advance (Commitment, at p. 5);
- Unused Line Fee: .35% of the principal amount of the undisbursed DIP Facility, payable monthly (Commitment, at p. 5);
- Legal fee deposit of $30,000 (Commitment, at p. 17);
- Stand-by Fee: 2% of each Advance (if portions of the DIP Facility are not consummated for the listed reasons) (Commitment, at pp. 15-17); and
- Exit Fee: 2% of the maximum loan amount (Commitment, at p. 14).

35. The budget attached to the Commitment itself assumes that as part of the $3.5 million "Emergency Advance" made under the Interim DIP Order, $191,000 is being allocated to certain of the above fees, and an additional $420,000 is being allocated to a reserve account for interest. In fact, approximately only $2.5 million of each of the Emergency and Interim Advances will be available to the Debtors for working capital purposes. Further, with respect to the Final Advance of $18,308,655, various fees will total, at a minimum, $750,655, and only about $7.7 million (less than half of the Final Advance amount) will be available to the Debtors for working capital. Given this reality, the Debtors should be required to provide a justification for these seemingly excessive fees before the DIP Facility is approved.

36. Moreover, the Debtors are required to pay "loan servicing" and "commitment" fees on the full amount of the Final Advance, despite the fact that $7,000,000 of the Final Advance is being used to pay the Emergency and Interim Advances (for which those same fees were already paid). If the DIP Facility is approved as-is, the Debtors will effectively pay those fees twice, despite receiving no incremental benefit. To avoid this result, the Commitment should be modified to provide that the loan servicing and commitment fees are chargeable only on the $11.3 million of "new money" from the Final Advance.

37. The Commitment also provides for a "break up fee" (or as the DIP Lender terms it, a "Stand-by Fee") equal to 2% of each advance under the DIP Facility if the Debtors elect not to enter into the DIP Facility, fail to comply with any of the conditions to the Commitment or if the Bankruptcy Court approves debtor-in-possession financing with another lender. Commitment, at pp. 15-17. This provision is highly unusual in debtor-in-possession facilities, is excessive under the circumstances, and is far too easily triggered in light of the onerous

conditions placed upon the Debtors under the Commitment. The Committee submits that this provision is commercially unreasonable and should be stricken.

38. In addition to these fees, the Debtors are required to pay all of the DIP Lender's reasonable costs and expenses (including travel and lodging and all out-of-pocket expenses and legal fees) related to closing and the Debtors' bankruptcy cases. These fees also automatically become part of the DIP Facility. *See* Commitment, at p. 14. The Court, the Committee and other parties-in-interest have no ability to review the amount or reasonableness of these fees before they become obligations of the Debtors, to be paid as a superpriority administrative expense claim and secured by the Priming Liens. The Committee submits that these fees and costs should be capped in an amount commensurate with the size and complexity of the DIP Facility, and that any fees and expenses sought by the DIP Lender should be subject to reasonable scrutiny by the Debtors, the Committee and the Court.

39. *Above-market interest rates*. The Committee believes that the proposed interest rates under the DIP Facility (12% non-default rate, 20% default rate and almost 25% effective rate after fees and other charges) are excessive for a debtor-in-possession loan of this size. In fact, the proposed DIP Facility interest rate exceeds the effective rates charged by lenders for loans of similar amounts in other recent chapter 11 cases:

Filing Date	**Debtor**	**Lender**	**Final DIP Amount (millions)**	**Effective Interest Rate**
11/25/2009	Arch Aluminum & Glass Company, Inc.	PNC, Agent	4	8.75%
11/18/2009	Taylor-Wharton International LLC	GE	20	9.25%
11/15/2009	Champion Enterprises	Credit Suisse	38	10.50%

11/5/2009	Lazy Days RV Center Inc.	Key Bank, Bank of America	65	5.50%
10/8/2009	Accuride Corp.	Deutsche Bank	50	10.00%
10/8/2009	True Temper Sports Inc.	GE	10	11.00%
7/1/2009	Genmar Holdings Inc.	Fifth Third Bank, Wells Fargo	50	11.25%
6/30/2009	Grede Foundries Inc.	Wayzata Opp. Fund II (Revolver)	35	7.35%
6/30/2009	Grede Foundries Inc.	Wayzata Opp. Fund II (Term Loan A)	10	9.50%
6/9/2009	Fontainebleau Las Vegas Holdings	Icahn Nevada Acquisitions LLC	51	10.00%
5/6/2009	Crucible Materials Corp.	Wachovia Bank	9	9.05%

40. The default interest rate, equal to 8% above the non-default rate, also is in excess of that which is similarly charged to chapter 11 debtors. At a hearing on the Motion, the Committee will be prepared to offer evidence suggesting that a commercially reasonable default interest rate should be less than 5% above the non-default rate.

41. That the interest rate proposed by the DIP Lender exceeds the rates charged by other debtor-in-possession lenders suggests that this rate may be commercially unreasonable, and that the Debtors could have secured alternative debtor-in-possession financing at a more attractive interest rate. At a minimum, the Debtors and the DIP Lender should be prepared to explain to the Committee and to the Court why an above-market interest rate is appropriate in these cases.

42. *Other terms*. Unfortunately for these estates, several of the other Commitment terms are commercially unreasonable, or deviate from the terms customarily offered by debtor-in-possession lenders to similarly-situated debtors:

- The Commitment provides for a $250,000 carveout to secure payment of U.S. Trustee fees and retained professionals fees following the occurrence of a Termination Event. Given the size and complexity of these cases (including sheer number of professional firms already involved), as well as the significant discretion afforded the DIP Lender to terminate the Commitment, the Committee submits that this carveout is unreasonably small, and puts retained professionals at significant risk.
- The Commitment requires that the Debtors secure title insurance, a survey of the collateral securing the DIP Facility, and legal opinions regarding ownership of the Debtors' real estate as conditions to making the DIP Facility advances. Each of these requirements will consume substantial resources of the estates, and are both unnecessary and excessive in light of the Priming Liens and superpriority administrative expense claims that will be granted to the DIP Lender.
- The existence of several material adverse change clauses ("*MAC*") in the Commitment is peculiar. The very fact that the Debtors are in chapter 11 suggests that a number of events will occur in the future that may qualify as material adverse changes that could unnecessarily trigger a costly default under the DIP Facility. The Committee therefore requests that any MAC clauses be stricken from the Commitment.
- Section J of the Conditions to the Commitment requires the Debtors to prove that there are no environmental, land use or zoning issues that will adversely impact the collateral. In order to meet this condition, the Debtors may be required to provide environmental assessments (including Phase I and Phase II) – a costly, time-consuming exercise that will seriously impact the Debtors' ability to access the DIP

Facility. The necessity of this condition should be clarified, and if the condition is not needed, it should be eliminated.

- Section K of the Conditions to the Commitment provides that the maximum loan amount shall not exceed 50% of the "as completed" value of the collateral. The Committee is unclear as to the meaning of "as completed," and is concerned that this limitation will limit the Debtors' access to the full amount of the Final Advance. Without sufficient clarification, this provision is unacceptable to the Committee.

43. The Committee respectfully requests that the DIP Lender modify or strike these offending provisions to conform the DIP Facility to principles of commercial reasonableness and to reflect current market conditions.

F. The DIP Budget Requires Certain Modifications and Clarifications.

44. The Committee and its professionals have identified a number of issues with the Budget attached to the Motion and Interim DIP Order that could impact the Debtors' reorganization efforts and materially impact unsecured creditors. The Committee requests that Budget issues to be addressed by the Debtors and the DIP Lender include, but are not limited to, the following:

- *Unbudgeted administrative and priority claims*. The Budget, in its current form, fails to account for approximately $2.3 million in administrative and priority claims that may come due during the Budget period, including past due taxes, section 503(b)(9) claims, unpaid pension obligations, PBGC insurance and real estate license fees. The Debtors should be required to explain why these significant liabilities are missing from the Budget.

- *Disparity in budgeted professional fees*. The Debtors budget only $350,000 to Committee professional fees during the Budget period, while the Debtors' professional fees are budgeted at $1.7 million. This gross disparity is unjustified, and simply does not provide the Committee with the resources necessary to carry out its duties during the Budget period. The Committee requests that the amounts budgeted be adjusted so that the Debtors' and Committee's professionals are being treated fairly and equitably.
- *Clarification regarding sales estimates for Budget period*. Significant disconnect exists between the sales estimates set forth in Parkland's Viability Analysis and the sales assumed in the Budget; compared to the Parkland analysis, the Budget understates sales for the 13-week period by $6.7 million. The Committee requests that the Debtors provide a justification for this disparity, and that the Debtors adjust the sales projections in the Budget accordingly or otherwise confirm what sales figure represents the best estimate during the Budget period.
- *Sale of non-core assets*. The Budget estimates that proceeds from the sale of non-core assets will total $4.2 million during the Budget period. In light of the significance of these sales during the Budget period, the Committee requests further clarification and back-up from the Debtors so that it may evaluate the accuracy of this estimate and the nature of the assets being sold.

45. To the extent that the above issues cannot be resolved in advance of the hearing on the Motion, the Committee submits that the Budget cannot be approved in its current form.

G. Chapter 5 Causes of Action Should Be Protected From the DIP Lender's Liens.

46. While the Committee acknowledges that chapter 5 causes of action and the recoveries therefrom are excepted from the DIP Lender's collateral package, a serious concern exists that the DIP Lender still could obtain control of these assets by indirect means. Indeed, the Commitment provides that avoidance claim recoveries may become collateral of the DIP Lenders if the Debtors commingle the recoveries with other collateral of the DIP Lender:

> [P]roceeds from all Litigation Recoveries shall be segregated from Borrower's other cash accounts which non-segregated cash accounts shall be part of the Collateral for the Loan. In the event that the Borrower elects to commingle Litigation Recoveries with Borrower's other cash resources, all such funds shall be deemed Collateral as security for the Loan.

Commitment, at p. 6.

47. Because the Committee has no control over how the Debtors manage or segregate their funds, the Committee is concerned with the approval of any mechanism that would subject chapter 5 recoveries to the DIP Lender's liens. In this case, where avoidance recoveries may be the unsecured creditors' only source of distributions on their claims, the Court should not permit the DIP Lender to include them as part of its collateral – whether as a result of commingling or otherwise. *See In re Tex. Gen. Petroleum Corp. v. Evans (In re Tex. Gen. Petroleum Corp.)*, 58 B.R. 357, 358 (Bankr. S.D. Tex. 1986) (refusing to grant a lien on avoidance actions on grounds that "neither a trustee in bankruptcy, nor a debtor-in-possession, can assign, sell or otherwise transfer the right to maintain a suit to avoid a preference."); *United Capital Corp. v. Sapolin Paints Inc. (In re Sapolin Paints Inc.)*, 11 B.R. 930, 937 (Bankr. E.D.N.Y. 1981) (refusing to give effect to assignment of avoidance actions, even where contracts negotiated at arm's-length explicitly provide for assignment in exchange for consideration). If

the DIP Facility is approved, the Committee therefore requests that chapter 5 avoidance actions, and the proceeds thereof, must remain unencumbered under every possible circumstance.

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WHEREFORE, the Committee respectfully requests that the Court (a) deny the Motion unless the Debtors and the DIP Lender satisfy each of the requests, and agree to each of the modifications, set forth in this Objection; and (b) grant such other and further relief as is just and proper.

Dated: March 15, 2010

OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF SCHWAB INDUSTRIES, INC., *et al.*

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CERTIFICATE OF SERVICE

I hereby certify that on March 15, 2010, a copy of this Objection was served by Electronic Mail or by ECF Noticing on the parties listed below, as indicated.

/s/ Douglas L. Lutz
Douglas L. Lutz

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