In the United States Bankruptcy Court

for the Northern District of Iowa

MIDWEST COUNTRY KITCHENS INC. Bankruptcy No. 93-11231KC
Debtor(s). Chapter 11

ORDER

On July 8, 1994, the above-captioned matter came on for hearing for consideration of the Disclosure Statement filed by Country Kitchen International, Inc. On July 12, 1994, hearing was held on Confirmation of Debtor's Plan, Valuation Hearing, a Motion to Appoint Trustee or Examiner by Robert Jakobitz, and a Motion for Relief from Stay also filed by Robert Jakobitz.

Appearing at these hearings were:

Frances Henkels for Debtor

Timothy Moratzka for CKI

Gary Hassel for Robert Jakobitz

Martin McLaughlin for the Internal Revenue Service

Mike Vestle for Herbert Loops

Dan Childers for Carl Fobian

All matters were discussed and pursuant to the record made, the Court took the matters under advisement.

DISCLOSURE STATEMENT OF CKI

The hearing on July 8, 1994 related to the Disclosure Statement filed by CKI on June 9, 1994. Objections were filed to the Disclosure Statement by Robert Jakobitz, Carl Fobian, Herbert Loops, and Debtor. The objections are numerous, however, they relate to ten primary areas which the Court will address. The first of these relate to the objection that CKI is not a party in interest nor a creditor and is, therefore, not entitled to submit a proposed plan for consideration. The record establishes that CKI is a franchisor and is the holder of a franchise agreement with Debtor which constitutes an executory contract under § 365.

Under § 1121(c), a "party in interest" may file a plan of reorganization after the expiration of a Debtor's exclusivity period. A party in interest is defined by the Code as including Debtor, Trustee, and Creditors among others. However, it is not an exclusive list. 11 U.S.C. § 102(3). Courts have consistently held that the concept of party in interest is elastic and is intentionally designed to give the Court great latitude to ensure fair representation of all constituencies impacted in any significant way

by a Chapter 11 case. In re First Humanics Corp., 124 B.R. 87, 90 (Bankr. W.D. Mo. 1991); In re River Bend-Oxford Assoc., 114 B.R. 111, 113 (Bankr. D. Md. 1990). Because of the latitude given to Courts in evaluating party in interest standing, its application must be determined on a case by case basis. In re Rook Broadcasting, 154 B.R. 970, 972 (Bankr. D. Idaho 1993). This analysis requires a finding that the party seeking involvement have a sufficient stake in the proceedings so as to require representation. In re Kaiser Steel Corp., 998 F.2d 783, 788 (10th Cir. 1993).

The parties objecting to CKI's standing in this case assert that CKI cannot propose a Plan because it is not a Creditor. Nevertheless, CKI does have an interest in Debtor's Chapter 11 proceeding based upon its franchise agreement with Debtor which is an executory contract under § 365. Some courts have held that vendors under executory contracts are creditors as defined in § 101(10). In re Iberis Int'l., Inc., 72 B.R. 624, 626 (Bankr. W.D. Wis. 1986) (party to licensing agreement is creditor and party in interest under § 1109(b)); In re Beavers, 26 B.R. 502, 504 (Bankr. N.D. Ala. 1983) (vendor under contract for sale of real estate is creditor boundy by confirmed plan).

It is not necessary that CKI be determined to be a Creditor as defined in the Bankruptcy Code to establish standing. It is the Court's determination that CKI's franchise agreement with the Debtor provides it with a sufficient stake in the proceeding to otherwise give it standing as a party in interest under § 1121(c). CKI is a constituency which could be significantly impacted by Debtor's Chapter 11 proceedings and Debtor's franchise agreement with CKI is a substantial asset of the Bankruptcy estate. As CKI has a significant interest in receiving adequate assurance of future performance of its agreement with Debtor under § 365, it is the conclusion of this Court that CKI has sufficient interest to establish standing. Therefore, the various objections to CKI standing under § 1121(c) are OVERRULED.

Secondly, various objections have been filed asserting that the Disclosure Statement, as filed, is inconsistent. Disclosure Statement language identifies certain of the Classes as impaired. At the time of the Disclosure hearing, CKI presented to the Court language changes in both the Disclosure Statement and the proposed Plan which are apparently intended to address what are categorized as "internal inconsistencies" by CKI. CKI advised the Court that it is the intent of these changes, as well as the intent of the Plan, to treat all Classes as unimpaired. Various Creditors, including Robert Jakobitz, assert that regardless of any changes made, there are Classes including that of Robert Jakobitz which remain impaired despite assertions to the contrary by CKI.

The initial issue raised is whether this is a proper subject for the Disclosure Statement hearing or whether this is a Confirmation issue. A creditor clearly has the authority to object that it is improperly treated as unimpaired. However, this is ordinarily a matter for determination at the Confirmation hearing. In re Forest Hills Assoc. Ltd., 18 B.R. 104 (Bankr. D. Del. 1982). However, impairment may be determined prior to the Confirmation hearing if appropriate under Rule 3013 as well as the logic of the Bankruptcy Code. While determination of impairment is ordinarily to be determined at the Confirmation hearing, the Court does have discretion to resolve these issues at an earlier time. For present purposes, the Court is determining the adequacy of the Disclosure Statement only. It is the determination of this Court that, for Disclosure Statement purposes, the information contained in the Disclosure Statement and the assertion of no impaired classes, is sufficient to satisfy § 1125.

Third, objection has been made that CKI's Plan and Disclosure Statement do not make sufficient reference to Debtor's Plan which has already been balloted and set for Confirmation hearing. This objection is OVERRULED for two reasons. First, while CKI's Disclosure Statement does not discuss Debtor's Plan in great length, reference is made in at least two places in the Disclosure Statement to the proposed Plan of Debtor. Secondly, case law, as well as the Bankruptcy Code, specifically provide

that a Disclosure Statement need not include information regarding any other possible or proposed Plan of Reorganization. The Code, at § 1125(a)(1), specifically states that "adequate information need not include such information about any other possible or proposed Plan". As such, any objection to CKI's Disclosure Statement on this ground is OVERRULED.

Several objectors have stated that the Plan filed by CKI is nonconfirmable and the Disclosure Statement accompanying this Plan should not be approved. There exists a substantial body of case law which holds that a Disclosure Statement may be disapproved if it is apparent that the proposed Plan cannot comply with the provisions of the Bankruptcy Code. In re Pecht, 57 B.R. 137, 139 (Bankr. E.D. Va. 1986). However, the case law also clearly holds that this provision should not be used to turn a Disclosure Statement hearing into a Confirmation hearing. Ordinarily courts held that a Disclosure Statement will be rejected on this basis only where it is obvious that the Disclosure Statement on its face relates to a Plan that cannot be confirmed. In re Monroe Well Service, Inc., 80 B.R. 324, 333 (Bankr. E.D. Pa. 1987). In the present case, Herbert Loops, as objector, states that the Plan is not confirmable and therefore, the Disclosure Statement should be denied.

Three specific areas are raised by Mr. Loops asserting that the Plan is not confirmable on its face. He states that two Classes of Creditors are impaired and neither Class will accept the Plan. There is not at least one Class of claims that is impaired and accepts the Plan. Also, he asserts that the proposed sale under this Plan will generate cash collateral in which Robert Jakobitz has a security interest. He states that there is no provision for segregating this cash collateral and the Plan is, therefore, violative of § 363(b)(2) and § 363(b)(4). Finally, he asserts that State and Federal income tax returns are required to be filed on behalf of a debtor by a liquidating agent. He asserts that the proposed Plan does not provide adequate means for compliance with tax requirements and is, therefore, nonconfirmable. While an examination of these objections raises the potential of confirmation problems for CKI's Plan, this Court cannot conclude that the matters raised are so compelling on their face that the Plan cannot be confirmed. These are more appropriately issues for confirmation and therefore, Mr. Loops' objection on this ground is DENIED.

Several objectors assert that the litigation analysis contained in CKI's Disclosure Statement is inadequate. The Disclosure Statement and summary state that the estate may hold claims against certain parties including officers, directors and shareholders in Classes D and E. These causes of action may include actions relating to accounts receivable as well as actions to avoid and recover preferential and fraudulent transfers, actions to equitably subordinate certain claims and interest, and actions to recover damages for breach of fiduciary duty. The case law is clear that a professional evaluation of potential litigation is unnecessary in a Disclosure Statement. It appears clear that a general statement relating to the existence of potential lawsuits, as well as a general description, is adequate. In re Texas Excursion Corp., 844 F.2d 1142, 1157 (5th Cir. 1988). While the litigation analysis here is admittedly cursory, it is the conclusion of this Court that, for purpose of this Disclosure Statement, the information provided is adequate.

Objection is made to the fact that CKI does not provide a valuation of the Debtor's assets in the Disclosure Statement. However, § 1125(b) provides that a Disclosure Statement may be approved without a valuation. In this case, a valuation hearing was scheduled and then continued upon application of the parties. This valuation hearing can still be held in the future if needed. As the Code specifically excepts asset valuation from the requirements of a Disclosure Statement, the Court finds that objection on this ground is without merit.

In addition to the foregoing, additional objections have been made. Objection has been made that the background and qualifications of the liquidating agent are inadequate. Objection is made concerning

the adequacy of the tax consequences analysis. Finally, objection is made to an alleged failure by the Plan proponent, CKI, to disclose certain information relating to its business relationship with the Debtor. More specifically, it is objected that it is misleading that this Plan is designated as a liquidation Plan when, in fact, it is the intention of CKI to buy back the franchise which constitutes Debtor's major asset. They also object that CKI allegedly fails to mention that they are the franchisor of the general system of Country Kitchens. They object that CKI has substantial financial information and valuation information but has failed to provide a fair market value analysis of the franchise. They object that CKI has provided inadequate information regarding its ability to maintain projected payments to Robert Jakobitz. They also object that CKI has failed to explain adequately its involvement with certain Kentucky franchises which objectors apparently feel cause financial losses which may have precipitated the present financial crisis of the Debtor.

The Court does not feel that it is necessary to discuss each of these matters specifically. The Disclosure Statement and the Plan do discuss the liquidating agent, it discusses in general terms the anticipated tax consequences, and it does discuss in fairly specific terms CKI's business arrangement with the Debtor. Ultimately, an evaluation of the Disclosure Statement is subjective and is done on a case by case basis. Less detailed information is necessary where the creditor body is limited in number and the creditor's relationship with the debtor is such that knowledge of the individuals involved is more complete than would be the case with a typical investor or creditor. Even though a creditor is not expected to be clairvoyant, a more modest Disclosure Statement is adequate where the individuals involved are very knowledgeable about their business relationship. In re Adana Mortgage Bankers, Inc., 14 B.R. 29, 31 (Bankr. N.D. Ga. 1981). Here, the primary individuals and creditors involved in this process have had a closely intertwined business relationship for an extended period of time. In general terms, they are quite knowledgeable about the nature of the business and their relationship. As such, the level of disclosure necessary to comply with 11 U.S.C. § 1125 is less than would be required under other circumstances. The Court has evaluated all of the objections made to CKI's Disclosure Statement. In so doing, the Court has evaluated the Disclosure Statement in light of the parties' long-standing business relationship, their level of sophistication, and the limited creditor body. The Court has discussed certain of the objections specifically and certain of the objections in general terms. However, in the final analysis, it is the conclusion of this Court that the Disclosure Statement now presented is sufficient to satisfy the statutory mandate of 11 U.S.C. § 1125 which is to provide adequate information such that it will enable a reasonable investor typical of holders of claims or interests of the relevant class to make an informed judgment about the Plan.

CKI filed with the Court certain technical amendments to eliminate internal inconsistencies. Additionally, at the Disclosure Statement hearing, objection was made to the fact that certain Exhibits, which were previously marked and attached to the prior Disclosure Statement, were not attached to the present Disclosure Statement. It is the conclusion of this Court, to the extent that it is material, all interested parties did have an opportunity to examine these Exhibits. They are presented to the Court by way of professional statement that they are identical and the reason they were not attached is it was assumed that the Disclosure Statement was substituted and that it was unnecessary to attach these identical Exhibits to the new Disclosure Statement. However, it is the finding of this Court that, to remove any ambiguity, the Exhibits should be attached also to this Disclosure Statement.

As such, the Court finds that if the technical amendments proposed are placed in the Disclosure Statement to eliminate any internal inconsistencies and the Exhibits which were deleted are attached to the Disclosure Statement, the same is adequate to meet the requirements of § 1125 and will be approved.

However, both Debtor and Objector Carl Fobian ask the Court to prohibit CKI from submitting and balloting its Plan until Debtor's Confirmation Plan hearing has been held. The Debtor's Plan has been balloted, preliminary hearing has been held, and the matter is ready to be set for Final Confirmation hearing. The reasons propounded to delay balloting of CKI's Plan of Reorganization is to avoid confusion with the Debtor's Plan prior to its Final Confirmation hearing and to avoid unnecessary expense based on a reasonable probability of confirmation of Debtor's Plan. The record does establish that Debtor's Plan will go to final hearing with no objections having been filed except that of CKI. The final confirmation hearing will involve the requirements of 11 U.S.C. § 1129 as well as evidence of adequate assurance to CKI of future performance of its executory contract under § 365.

It appears to this Court that no significant purpose is served at this time by balloting CKI's Plan. To avoid confusion and to minimize costs, without prejudice to CKI, the Court finds that the Motion to Withhold Balloting of CKI's Plan is compelling. If Debtor's Plan is denied confirmation, the Court will then allow CKI's balloting to proceed and the Court will consider all options at that juncture. Therefore, the Court sustains the Motion of Creditor Fobian and Debtor that CKI not be allowed to submit and ballot its Plan until subsequent to the Court's Order after the confirmation hearing on Debtor's Plan.

PRELIMINARY HEARING ON DEBTOR'S PLAN CONFIRMATION

On July 12, 1994, a preliminary hearing was held on confirmation of Debtor's Plan. Also scheduled for that date was a valuation hearing requested by Debtor, a Motion to Appoint Trustee or Examiner filed by Robert Jakobitz and a Motion for Relief from Stay also filed by Robert Jakobitz. At the time of hearing, Debtor requested that the valuation hearing previously set be continued for cause. As no party objected to continuation of this valuation hearing, the same was granted. The valuation hearing was continued by separate order.

Regarding the Motion for Appointment of Trustee and a Motion for Relief from Stay both filed by Robert Jakobitz, the Court was advised that an agreement had been reached between Mr. Jakobitz and Debtor which was being placed in final form and would be submitted to the Court. In part, this agreement involved withdrawal of the Motion for Appointment of Trustee and also withdrawal of the Motion for Relief from Stay. Upon Motion of Robert Jakobitz, without objection, the Motion to Appoint Trustee or Examiner previously filed is considered withdrawn. Also, the Motion for Relief from Stay, also filed by Robert Jakobitz, is considered withdrawn.

The Court was advised of the essence of an agreement between Debtor and Robert Jakobitz which would satisfy Mr. Jakobitz's objection to Debtor's Plan. This agreement had not been executed at the time of hearing. This agreement has now been presented to the Court in a pleading designated Modification of Plan Per 1127.

At the July 12, 1994 hearing, CKI stated that this agreement between Debtor and Robert Jakobitz changed the essence of the Debtor's Plan to such an extent that it is mandatory that the Debtor go back to the Disclosure Statement stage of these proceedings and renotice the Disclosure Statement for hearing. Debtor, however, asserted that these changes were such that they could be incorporated into the Plan without the necessity of requiring a new Disclosure Statement and Notice. Debtor asserts that the changes are such that a minimal amount of notice under 11 U.S.C. § 1127 is mandated. The Court advised the parties, at the time of hearing, that it would await the proposed Plan modifications after which it would examine the same and determine whether a new Disclosure Statement was necessary and, if not, the amount of notice necessary. The Court having examined the file and the Modification of Plan finds that adequate notice can be provided and the interests of involved creditors can be

protected adequately under 11 U.S.C. § 1127(d). As such, any holder of a claim or interest that has accepted or rejected the Plan of Debtor will be deemed to have accepted or rejected, as the case may be, such Plan as modified, unless, within 10 days notice of the Plan Modification, such holder changes its previous acceptance or rejection.

WHEREFORE, the Disclosure Statement of CKI considered on July 8, 1994, is approved subject to those matters noted in the body of this opinion.

FURTHER, for the reasons set forth in this opinion, it is ordered that CKI is prohibited from submitting and balloting its Plan until further Order of Court.

FURTHER, the Motion to Appoint Trustee or Examiner is withdrawn by proponent Robert Jakobitz.

FURTHER, the Motion for Relief from Stay is withdrawn by proponent Robert Jakobitz.

FURTHER, the Valuation Hearing requested by Debtor is continued by separate Order.

FURTHER, the Court finds that adequate notice can be provided and the interests of involved creditors can be protected adequately under 11 U.S.C. § 1127(d) as it relates to the Modification of Plan propounded by Debtor.

FURTHER, as it relates to the Modification of Plan, any holder of a claim or interest that has accepted or rejected the Plan of Debtor, will be deemed to have accepted or rejected such Plan as modified unless within ten days of notice of the Plan Modification such holder changes its previously acceptance or rejection.

FURTHER, Debtor is authorized to proceed with noticing the Modification of Plan as provided in the Bankruptcy Code and Rules.

SO ORDERED this 19th day of July, 1994.

Paul J. Kilburg
U.S. Bankruptcy Judge