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UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF NEVADA

In re: Front Sight Management, LLC, Debtor.	Case No.: 22-11824-abl Chapter 11 **OPPOSITION TO EMERGENCY MOTION FOR ENTRY OF INTERIM AND FINAL ORDERS: (I) AUTHORIZING DEBTOR TO OBTAIN POST-PETITION FINANCING, (II) GRANTING PRIMING LIENS AND ADMINISTRATIVE EXPENSE CLAIMS, (III) AUTHORIZING THE DEBTOR'S USE OF CASH COLLATERAL, (IV) MODIFYING THE AUTOMATIC STAY, AND (V) GRANTING RELATED RELIEF** HEARING DATE: June 24, 2022 HEARING TIME: 9:30 a.m.

Michael Meacher, dba Bankgroup Financial Services ("Meacher/BFS"), a secured creditor in the above-captioned Chapter 11 proceeding, hereby opposes the Debtor's *Emergency Motion for Entry of Interim and Final Orders: (I) Authorizing Debtor to Obtain Post-Petition Financing, (II) Granting Priming Liens and Administrative Expense Claims, (III) Authorizing the Debtor's Use of Cash Collateral, (IV) Modifying the Automatic Stay, and (V) Granting Related Relief* (the "DIP Financing Motion") [ECF No. 4]. In support of this opposition, Meacher/BFS submits the attached points and authorities, the Declaration of Michael Meacher ("Meacher Declaration"), and the exhibits attached thereto. For the reasons set forth below, Front Sight Management, LLC (the "Debtor") has not met its required burden of proof to obtain any post-petition loan, let alone one on a priming basis. Accordingly, the Court should deny the DIP Financing Motion on a final basis.

I.

INTRODUCTION

Pursuant to the DIP Financing Motion, the Debtor seeks authority, without any substantive evidence, under Bankruptcy Code Sections 364(b), (c), (d) and 503(b)(1) to obtain a $5 million DIP financing loan, with a 9.5% non-default interest rate, 16% default interest rate, $100,000 in fees (the "Proposed DIP Loan") that, among other things, primes Meacher/BFS's pre-petition secured claim (DIP Financing Motion, pages 13-16; DIP Financing Motion Ex. 4, page 2).[1] The DIP Financing Motion does not provide, for example, any evidence of:

- The specific efforts that were made by the Debtor to try to obtain a loan;
- The specific parties with whom the Debtor spoke in efforts to obtain the loan:
- The Debtor being unable to obtain a loan on less onerous terms;
- The market value and reasonableness of the terms of the loan;
- The existence of a substantial equity cushion to justify a priming lien; and
- An increase in the value of the collateral.

[1] Moreover, the DIP Financing Motion prematurely seeks authority to designate FS DIP, LLC (the "Lender") as the stalking horse bidder in the event of a sale, with approval of a break-up fee comprising 3% of the purchase price, plus expense reimbursement of up to $235,000 (DIP Financing Motion, page 16).

In fact, to the contrary, the only conclusory statements made (in the way of an inadmissible budget that is attached with no foundation) reflect unequivocally a significant decrease in value. During the 13-week period, the Debtor's budget shows an erosion of more than $2 million. In addition, there is no disclosure about the identity of the lender and its relationship, if any, to the Debtor and its principals.

While Meacher/BFS fully supports a successful business, based on the Debtor's own projections and admissions, Meacher/BFS is very concerned about and questions the viability of the Debtor.

The Debtor's budget and own statements in support of the DIP Financing Motion suggest that the Debtor cannot sustain its operations. Accordingly, based on the record before the Court, Meacher/BFS requests that the DIP Financing Motion not be approved on a final basis.

II.

STATEMENT OF FACTS

A. Factual Background

The Debtor and Meacher/BFS are parties to a Consulting Agreement dated July 1, 2010 (the "Consulting Agreement"), pursuant to which Meacher/BFS agreed to serve as a consultant to Debtor. A true and correct copy of the Consulting Agreement is attached as **Exhibit 1** to the Meacher Declaration. In consideration of the deferment of certain fees due under the Consulting Agreement, and to secure Debtor's obligations under the Consulting Agreement, the Debtor granted Meacher/BFS a security interest in, among other things, "all handguns, shotguns, rifles and machine guns owned by [Debtor] and accounted for on the [Debtor's] books under Federal Firearm Licenses No. 9-88-023-01-4M-01495 and No. 9-88-023-01-00199" (the "Collateral"). To perfect its security interest in the Collateral, on March 22, 2021, Meacher/BFS filed a UCC-1 financing statement with the Nevada Secretary of State, filing number 2021162123-4 (the "Financing Statement"). A true and correct copy of the Financing Statement is attached as **Exhibit 2** to the Meacher Declaration. The Financing Statement covers the following collateral: "1. All of the collateral listed on Exhibit A attached hereto, which consists of 37 pages of itemized firearms and firearm equipment; plus 2. All of the collateral listed on Exhibit B

attached hereto, which consists of 23 pages of itemized firearms and firearm equipment."

B. Correction of Debtor's Misstatements

Michael Meacher is incorrectly referred to as the Debtor's former CFO and as the owner of an entity Bankgroup Financial Services. Michael Meacher was never the Debtor's CFO, but rather the Debtor's COO, the Chief of Operations. Bankgroup Financial Services is not an entity, but a dba of Mr. Meacher.[2] (Meacher Declaration ¶¶ 1, 3.)

III.

A PRIMING DIP LOAN UNDER BANKRUPTCY CODE SECTION 364(d) IS NOT WARRANTED

The Bankruptcy Code recognizes the primacy of pre-petition contractual liens and seeks to preserve the financial interests created thereby. *In re Mosello*, 195 B.R. 277, 287 (Bankr. S.D.N.Y. 1996). The ability to prime an existing lien under Bankruptcy Code Section 364(d) is extraordinary, as it displaces bargained-for lien rights, and should not be approved except as a last resort. *See In re Den-Mark Construction, Inc.*, 406 B.R. 683, 688 (E.D.N.C. 2009); *In re Planned Systems, Inc.*, 78 B.R. 852, 861 (Bankr. S.D. Ohio 1987) (secured creditor to be primed "is entitled to constitutional protection for its bargained-for property interest"). As set forth herein, the Debtor cannot satisfy the necessary elements of Bankruptcy Code Section 364(d), and the Court should deny the DIP Financing Motion.

A. The Debtor Cannot Satisfy the Requirements of Bankruptcy Code Sections 364(d)(1)(B) and 364(d)(2).

The Debtor has failed to meet its burden of proof that Meacher/BFS' interest is adequately protected. Pursuant to Bankruptcy Code Section 364(d)(1)(B), to grant an equal or priming lien, the Debtor must establish that there is adequate protection of Meacher/BFS's lien against the Collateral. *In re Swedeland Development Group, Inc.*, 16 F.3d 552, 564 (3rd Cir. 1994); *In re Mosello*, 195 B.R. 277, 287-288 (Bankr. S.D.N.Y. 1996). Section 364(d) provides,

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[2] In addition, the List of 20 Largest Unsecured Creditors appears to be incorrect because it includes Mr. Meacher, with the amount listed as "TBD," when Meacher/BFS holds a secured claim pursuant to the Consulting Agreement and Financing Statement. (*See* Meacher Declaration ¶¶4-7.)

in relevant part:

> (d)(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--
> …
> (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).

The trustee or debtor in possession bears the burden of proof to establish adequate protection under Section 364(d). 11 U.S.C. § 364(d)(2) ("In any hearing under this subsection, the trustee has the burden of proof on the issue of adequate protection."). *See also In re Thurston Highland Associates, LLC*, 2010 WL 148683 (Bankr. W.D. Wash. Jan. 13, 2010) ("The burden of proof in establishing adequate protection lies with the Debtor.").

"Given the fact that super priority financing *displaces liens* on which creditors have relied in extending credit, a court that is asked to authorize such financing must be particularly cautious when assessing whether the creditors so displaced are adequately protected." *In re Fontainebleau Las Vegas Holdings, LLC*, 434 B.R. 716, 754 (S.D. Fla. 2010) (emphasis in original). Moreover, pursuant to Bankruptcy Code Section 364(d)(2), the burden is not on Meacher/BFS to establish a lack of adequate protection. Rather, the Debtor has the burden of proof of the existence of adequate protection. *Swedeland*, 16 F.3d at 564; *Mosello*, 195 B.R. at 287.

A debtor or trustee seeking to prime an existing secured creditor bears a particularly high burden of proof.

> Priming is extraordinary relief requiring a strong showing that the loan to be subordinated is adequately protected. *In re Swedeland Development Group, Inc.*, 16 F.3d 552 (3d Cir.1994). Bankruptcy judges are required to grant Section 364(d) financing only upon a tangible demonstration of adequate protection. *Id.* at 567. The Court must be cautious in assuring that Wells Fargo has received genuine adequate protection, and the facts simply do not provide the Court with confidence that the DIP financing protects Wells Fargo's security interest. For instance, the proposal to pay $10 million to reduce Wells Fargo's loan does not negate Wells Fargo's undersecured position. The additional $40 million priming the DIP Motion proposes only makes matters

> worse. Providing Wells Fargo with a replacement lien on assets against which it already has a lien is illusory. Debtor must provide Wells Fargo with additional collateral, and there is none.

In re LTAP US, LLLP, 2011 WL 671761 (Bankr. D. Del. Feb. 18, 2011).

"The § 364(d) process, which allows a debtor in possession to 'prime' an existing lien is 'considered **rare and extraordinary**.'" *In re Thurston Highland Associates, LLC*, 2010 WL 148683 (Bankr. W.D. Wash. Jan. 13, 2010) (emphasis added). See also *Bland v. Farmworker Creditors*, 308 B.R. 109, 115 (S.D. Ga. 2003) ("§ 364(d) process is considered **rare and extraordinary**") (emphasis added); *In re Dunckle Associates, Inc.*, 19 B.R. 481, 485 (Bankr. E.D. Pa. 1982) ("Section 364(d) is actually a provision to be invoked only in the **most compelling and extraordinary circumstances**.") (emphasis added); *In re DB Capital Holdings, LLC*, 454 B.R. 804, 822 (Bankr. D. Colo. 2011) ("granting post-petition financing on a priming basis is extraordinary and is allowed only as a last resort."); *In re Seth Co., Inc.*, 281 B.R. 150, 153 (Bankr. D. Conn. 2002) ("The ability to prime an existing lien is extraordinary").

Accordingly, a debtor seeking a priming lien under Section 364(d) is subject to a very heavy burden of proof. *See In re Reading Tube Indus.*, 72 B.R. 329, 332 (Bankr. E.D. Pa. 1987) ("we note that Section 364(d) carries a much heavier burden than 364(b) since subsection (d) contemplates the priming of liens").

Adequate protection must be in a tangible form such as replacement liens on additional collateral. As stated by the Third Circuit:

> Congress did not contemplate that a creditor could find its priority position eroded and, as compensation for the erosion, be offered an opportunity to recoup dependent upon the success of a business with inherently risky prospects. We trust that in the future bankruptcy judges in this circuit will require that adequate protection be demonstrated more tangibly than was done in this case.

In re Swedeland Dev. Grp., Inc., 16 F.3d 552, 567 (3d Cir. 1994).

In order to establish adequate protection, the debtor must provide a side-by-side analysis of the value of the secured creditor's interest, both before and after the priming lien, and thereby account for the decrease in value caused by the priming lien:

> When formulating adequate protection in connection with post-petition financing on a priming basis, preserving or enhancing the value of collateral must be viewed side-by-side with the decrease in value of a creditor's interest in the property caused by the priming lien. *See In re Swedeland Dev. Grp.*, 16 F.3d at 566 ("[C]ontinued construction based on projections and improvements to the property does not alone constitute adequate protection. Those cases which have considered improvements to be adequate protection have done so only when the improvements were made *in conjunction with the debtor's providing additional collateral beyond contemplated improvements.*" (emphasis added)); COLLIER, *supra*, ¶ 361.03[5][b], at 361–21. Here, the Debtors and the bankruptcy court focused on preserving the value of the Project for the benefit of all creditors. That goal was worthy and important, and the Court does not question it. **But the Debtors did not try to establish, and the bankruptcy court did not find, that the decrease in the value of the Statutory Lienholders' *interests therein* caused by the priming lien was compensated, replaced, or substituted in any way: to be blunt, the Statutory Lienholders were not adequately protected**. The proceedings below failed to account for what a priming lien does. *See In re First S. Sav. Ass'n*, 820 F.2d 700, 710 (5th Cir.1987) ("Given the fact that super priority financing *displaces liens* on which creditors have relied in extending credit, a court that is asked to authorize such financing must be particularly cautious when assessing whether the creditors so displaced are adequately protected." (emphasis added)); COLLIER, *supra*, ¶ 364.05, at 364–21 ("The ability to prime an existing lien is extraordinary, and in addition to the requirement that the trustee be unable to otherwise obtain the credit, the trustee must provide adequate protection for *the interest* of the holder of the existing lien." (emphasis added)). **Not accounting for the decrease caused by the priming lien was fundamentally at odds with the principle of adequate protection**, which must "as nearly as possible under the circumstances of the case provide the creditor with the value of his bargained for rights." *In re Swedeland Dev. Grp.*, 16 F.3d at 564 (internal quotation marks omitted).

In re Fontainebleau Las Vegas Holdings, LLC, 434 B.R. 716, 754-55 (S.D.Fla. 2010) (emphasis added).

In order to establish that an existing lienholder is adequately protected, a debtor will often attempt to establish that the proposed financing will increase the value of the collateral by more than amount of the priming lien. *See, e.g.*, *In re First South Savings Ass'n*, 820 F.2d 700, 710–15 (5th Cir. 1987) (loan of $2 million would enhance value of property by only $1 million; denial of motion for a stay pending an appeal of an order granting a § 364(d) motion reversed). Here, Meacher/BFS's Collateral consists of firearms and firearm equipment. The proposed financing will not enhance or increase the value of Meacher/BFS's Collateral. However, Meacher/BFS's interest will be diminished by the $5 million amount of the priming lien. Thus, Meacher/BFS's interest is clearly not adequately protected.

Despite having the burden of proof under Bankruptcy Code Section 364(d)(2) to establish there is adequate protection of the Meacher/BFS's lien on the Collateral pursuant to Section 364(d)(1)(B), the DIP Financing Motion contains no evidence whatsoever. Not only has the Debtor proffered no evidence on the value of the Collateral, it has not even asserted whether Meacher/BFS is oversecured or undersecured, and whether or not there is a sufficient equity cushion in the Collateral. The Debtor has made no attempt whatsoever to provide adequate protection of Meacher/BFS's security interest. The Declaration of Ignatius Piazza (the "Piazza Declaration") in support of the DIP Financing Motion offers no evidence of adequate protection. For example, the Piazza Declaration does not establish that Meacher/BFS's interest will be protected by an equity cushion of 20% or more, after the granting of the priming lien. See *In re Mellor*, 734 F.2d 1396, 1401 (9th Cir. 1984) (holding an equity cushion of 20% or more constitutes adequate protection). The Debtor's Motion does not offer additional collateral as an alternative form of adequate protection. Thus, as a matter of law, Meacher/BFS is not adequately protected.

Moreover, the Budget projects that Debtor's cash position will decline over the next 13 weeks. The Proposed DIP Loan imposes additional significant risk on Meacher/BFS. The consequences of Debtors' failure to comply with the Budget are dire—the Lender can terminate the Proposed DIP Loan and exercise remedies. Moreover, Debtor has not indicated what its exit strategy from bankruptcy is. Remarkably, the Debtor is presenting the DIP Financing Motion without the context of an exit strategy (or even a preview thereof) of any kind for this case. The proposed DIP Loan is a bridge to nowhere: the Debtor seeks to prime Meacher/BFS with $5 million of financing, then proposes to operate for 13 weeks at a loss of more than $2 million, without providing any context in which such financing and unprofitable operations make any sense. Further, the Debtor offers no evidence or explanation of how this case will be funded beyond the 13-week Budget. There is no explanation or evidence that the Debtor can survive beyond week 13 without additional funding. Approval of the proposed DIP Loan will likely result in the Debtor becoming illiquid after 13 weeks with the substantial additional burden on Meacher/BFS of having $5 million of senior debt in front of it.

The Debtor has not offered any consideration whatsoever, let alone adequate protection, for the undisputed diminution in Meacher/BFS's interest that would result from Debtor's proposed priming lien. The Bankruptcy Code requires adequate protection to be provided in one of three ways: (a) periodic cash payments; (b) additional or replacement liens, or (c) other relief constituting the "indubitable equivalent" of the primed creditor's interests in the collateral. *See* 11 U.S.C. § 361; *Swedeland*, 16 F.3d at 564.

Irrespective of the value of the Collateral (as to which Debtor has offered no evidence in satisfaction of its burden) and whether there is an equity cushion in the Collateral, granting the Lender a priming lien for $5 million would result in a diminution of Meacher/BFS's interest in the amount of $5 million. In *Swedeland*, the Third Circuit Court of Appeals concluded that:

> The district court ruled that the bankruptcy court's findings were clearly erroneous because Swedeland offered no new consideration to Carteret to offset its diminution of interest as a result of the superpriority lien given to First Fidelity. Accordingly, none of the factors the bankruptcy court enumerated showed Carteret had adequate protection. We agree with the district court.

Swedeland, 16 F.3d at 564-565.

Especially in the absence of any evidence of the value of the Collateral, the only way to measure adequate protection is by using the amount of the priming loan. The Debtor does not offer any cash payments, any additional unencumbered collateral, or any other value of any kind to offset a $5 million diminution in Meacher/BFS's interests. Under *Swedeland*, Meacher/BFS is not adequately protected.

Next, even if an equity cushion alone could constitute adequate protection, irrespective of what equity cushion is sufficient, Debtor has not proffered any evidence whatsoever, and the burden is on Debtor. As noted above, there is no evidence whatsoever as to whether Meacher/BFS is oversecured or undersecured. The only evidence is that based on the Budget, Meacher/BFS will suffer an almost $5 million decline in its position as a result of the DIP Loan over the next 13 weeks.

Thus, the Debtor has failed to make any attempt to provide Meacher/BFS with adequate protection, and, in fact, the Debtor lacks the ability to provide adequate protection. As a result, the DIP Financing Motion must be denied.

B. The Debtor Can *Not* Use Post-Petition Financing to Pay Pre-Petition Claims.

The Debtor has filed a critical vendor motion in this case [ECF No. 12]. The Debtor presumably would use the loan proceeds to pay certain creditors' pre-petition unsecured claim.

Meacher/BFS objects to any use of post-petition loan proceeds to pay pre-petition unsecured claims. A debtor cannot use Section 364(d) to circumvent the confirmation requirements of Section 1129. *See In re Chevy Devco*, 78 B.R. 585, 589 (Bankr. C.D. Cal. 1987). The Debtor cannot use Section 364 or 363 to circumvent the confirmation requirements of Section 1129, and thereby pay pre-petition claims. See *In re Metro. Cosmetic & Reconstructive Surgical Clinic, P.A.*, 115 B.R. 185, 189 (Bankr. D. Minn. 1990) ("Post-petition payment of prepetition debt is not authorized by § 363(c)(1).")

It would violate Meacher/BFS's rights as a secured creditor, to use a priming loan to pay general unsecured creditors. Among other things, the Debtor should not be allowed to circumvent the absolute priority rule through the use of a priming lien. Accordingly, the Debtor should be required to explicitly disclose the proposed disposition of any loan proceeds and disclose whether any of the funds are proposed to be paid to unsecured creditors.

C. The Debtor Has Failed to Establish that It Is Unable to Obtain Credit on Less Onerous Terms

Section 364(d)(1)(A) also requires the Debtor to establish that it "is unable to obtain such credit otherwise." Specifically, "section 364(d) specifically sets forth the additional standards requiring that the debtor must demonstrate that it is unable to make less burdensome credit arrangements." *In re Defender Drug Stores, Inc.*, 145 B.R. 312, 317 (B.A.P. 9th Cir. 1992).

This requirement necessitates evidence of the Debtor's attempts to obtain financing from other sources. Conclusory statements that the Debtor cannot obtain alternative financing is insufficient. See *In re TBH19 LLC*, 2021 WL 275490, at *8 (C.D.Cal., 2021) ("In this case, Debtor argues in conclusory fashion that it "sought alternative financing without success" but fails to provide any evidence regarding those attempts. However, such conclusory statements are insufficient to satisfy Section 364(c)."). For example, in *In re Plabell Rubber Products, Inc.*, 137 B.R. 897 (Bankr. N.D. Ohio 1992), the Court denied the debtor's motion where the debtor's

chief executive officer referred only to one contact with a manager of a bank, other than the one from which it was proposed to obtain credit. *Plabell Rubber*, 137 B.R. at 900 ("Debtor's one contact is insufficient.")

The Debtor's mere opinion that financing is otherwise unavailable is insufficient to meet the Debtor's burden of proof under Section 364(d):

> The debtor, in the case at hand, has failed to demonstrate that they have approached even one institution[4] to request financing. N.T. at 8 (2/5/87) The debtor chose, for whatever reason, to rely solely upon the *opinion* of its Chairman of the Board, James Lash, to demonstrate the unavailability of other financing. While we recognize the extensive financing experience and business acumen of the Chairman, we do not find that his opinion alone, without some demonstrated effort to approach other potential lenders, meets the requirements contemplated in Section 364(d)(1)(A). The debtor also argues that the objectors have not shown that financing could be secured on less onerous terms. However, no provision of the Code, and specifically of Section 364(d), requires the bank to prove availability of credit. The burden is clearly upon the debtor. The debtor has been given every opportunity to show even minimal effort in seeking credit. It has chosen not to do so and its failure compels this court to deny the debtor's motion pursuant to Section 364(d)(1)(A).

In re Reading Tube Indus., 72 B.R. 329, 332 (Bankr. E.D. Pa. 1987). *See also In re Phase–I Molecular Toxicology, Inc.*, 285 B.R. 494, 496 (Bankr.D.N.M.2002) (finding that although debtor reasonably may have believed it would be unable to obtain alternative financing, it made an insufficient showing that it attempted to do so but was unsuccessful); *In re Stacy Farms*, 78 B.R. 494, 498 (Bankr.S.D.Ohio 1987) (noting debtor failed to carry its burden under § 364(d) where there was no evidence that debtor had applied for loans from institutions other than pre-petition senior lender and priming lender).

In contrast, in *In re Beker Industries Corp.*, 58 B.R. 725, 729 (Bankr.S.D.N.Y.1986), the Court held that the debtor's efforts were sufficient to carry its burden under § 364(d) where the debtor's voluminous testimony indicated that it had approached 35 to 40 lenders to obtain replacement financing prior to filing its Chapter 11 petition, and approximately 20 lenders after it filed its Chapter 11 petition.

Here, the Piazza Declaration provides absolutely no evidence of the Debtor's attempts to obtain "less burdensome credit arrangements." Therefore, Debtor cannot satisfy the

requirements of Bankruptcy Code Section 364(d)(1)(A). Accordingly, the DIP Financing Motion must be denied.

IV.

CONCLUSION

For the reasons set forth above, a priming lien is not warranted because Debtor cannot meet its burden of proof and satisfy all (or even any) of the requirements of Bankruptcy Code Sections 364(d)(1)(A), (d)(1)(B), and (d)(2). Therefore, Meacher/BFS respectfully requests that the Court deny the DIP Financing Motion.

DATED this 10th day of June 2022.

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