

1 Citizens filed a motion to substantively consolidate Citizens,
2 LSM Hotel, LLC, and other affiliated entities.

3 On October 21, Citizens filed a motion to stay all non-
4 bankruptcy litigation against Mr. DiNofia for a limited time
5 period, through March 31, to permit Mr. DiNofia to focus on
6 developing the reorganization of the entities. The motion
7 listed a suit by German American Credit Corporation (GACC),
8 filed July 2, 2010, and a suit filed by El Toreador Properties on
9 April 22, 2010. Both are directly against Mr. DiNofia on various
10 counts, including on personal guarantees of the underlying
11 obligations. As of the date of Citizens' motion, the Superior
12 Court in the Toreador litigation had entered a scheduling order
13 setting deadlines: 1) first expert exchange December 2, 2010;
14 2) second expert exchange December 22; 3) motion and discovery
15 cutoff February 25, 2011; 4) deadline for filing jury fees
16 February 25; 5) trial readiness conference March 4; and
17 6) trial March 25, 2011.

18 On November 18, the motion to extend the stay was denied on
19 procedural grounds, for the central reason that it should be
20 brought in the context of an adversary proceeding seeking relief
21 against a third party. Then, on January 27, 2011 the Court
22 granted Citizens' motion for substantive consolidation after
23 multiple days of evidentiary hearing.

24 In the meantime, LSM Hotel filed an adversary proceeding in
25 its Chapter 11 against Toreador and Mr. Serhan, asserting that
26 the defendants' lien against the hotel should be avoided because

1 it was the result of a fraudulent conveyance. That suit was
2 filed on or about December 23, and amended December 29. Then, on
3 January 13, 2011 LSM Hotel filed an "Emergency Motion to Stay
4 State Court Proceedings Pursuant to Bankruptcy Code Section
5 105(A) and 362". Following a briefing schedule, this matter was
6 set for hearing before this Court.

7 As noted, debtor has styled the motion as an "Emergency
8 Motion to Stay". As such, the movant seeks injunctive relief.
9 Because of the full briefing this matter has received, as well as
10 the elapsed time between its filing on January 13 and the hearing
11 on February 4, the Court has proceeded to treat the motion as
12 requesting preliminary injunctive relief, not a temporary
13 restraining order.

14 In its moving papers seeking to stay only the Toreador state
15 court proceedings against Mr. DiNofia, LSM Hotel argued there was
16 a risk of inconsistent verdicts between the state court action on
17 Mr. DiNofia's guarantee and a bankruptcy court decision avoiding
18 LSM's liability on the same obligation because of the fraudulent
19 conveyance claim. They also argued Mr. DiNofia might have a
20 right of indemnification against LSM Hotel if he was found liable
21 in the state court action. LSM Hotel's third argument was that
22 allowing the state court litigation to go forward against
23 Mr. DiNofia would draw his time and attention away from focusing
24 on the reorganization of the debtor. In support of that
25 argument, they asked the Court to take judicial notice of the
26 declaration Mr. DiNofia filed in the Citizens case in support of

1 the motion there to extend the stay. That declaration was filed
2 on October 21.

3 In his declaration filed in the Citizens case, Mr. DiNofia
4 stated with the then-pending litigation over substantive
5 consolidation and two significant stay relief matters, he needed
6 "a reprieve from pending litigation." He mentioned the German
7 American lawsuit and the Toreador litigation, and added two
8 others brought by Bank of the West and Telesis, both of which had
9 been settled by him prepetition. He anticipated, however, that
10 those creditors of his might claim a breach of the settlement by
11 the filing of the Chapter 11 petitions. He claimed then that
12 having to allocate time to those litigations would deprive the
13 bankruptcy estates of his availability to assist in defense of
14 the relief from stay matters, prosecution of the substantive
15 consolidation motion, and working on reorganization. He stated:
16 "I expect that the following approximately two months will be
17 spent litigating these Motions, performing discovery, and
18 preparing for trial."

19 Since that declaration was filed, the German American relief
20 from stay and the substantive consolidation matters have been
21 concluded, in the most part. As already noted, substantive
22 consolidation was granted, and the stay was modified and
23 continued consistent with the deadlines for filing a plan and
24 disclosure statement, and showing evidence of the likelihood of
25 sufficient financial commitments to support a reorganization.
26 As an aside, it appears that on January 6, 2011 Mr. DiNofia filed

1 a cross-complaint in the Toreador litigation.

2 Curiously, Mr. DiNofia supplied a declaration in support of
3 LSM Hotel's emergency motion to stay the Toreador state court
4 proceedings focusing only on whether LSM Hotel might prevail on
5 its fraudulent conveyance claim against Toreador and Mr. Serhan.
6 His declaration is silent on the need for "a reprieve" from the
7 Toreador litigation, or any other litigation, except by adoption
8 of his October declaration filed in support of the Citizens
9 motion. Most of the grounds asserted in the Citizens motion have
10 since abated, except the argument concerning the need of the
11 debtor for Mr. DiNofia's attention to the now-consolidated
12 debtor's reorganization against the deadlines set by the court in
13 conjunction with the German American stay relief motion. (The
14 Court is aware that Symphony Asset Pool is the successor to
15 German American's interest as of November 19, 2010, but has
16 continued to refer to the movant as German American for
17 continuity.)

18 Boiling the motion down to essentially what is left, LSM
19 Hotel asks this court to stay the Toreador litigation presently
20 pending in the Superior Court for a finite period of time. At
21 argument, it was not clear whether debtor was asking for relief
22 only until the plan and disclosure statement is filed on or
23 before March 31, or whether the relief sought would extend
24 through May 25 when the continued hearing is set. LSM Hotel LLC
25 is not a party to the Superior Court proceedings. The remaining
26 argument in support of the motion is the need for Mr. DiNofia's

1 time and attention to reorganization of the now-consolidated
2 debtor, rather than having his attention consumed with defending
3 himself in the state litigation.

4 The controlling authority in the Ninth Circuit on the issue
5 of granting injunctions/stays of third party proceedings is In re
6 Excel Innovations, Inc., 502 F.3d 1086 (2007). There, the court
7 held: 1) "the usual preliminary injunction standard applies to
8 stays of proceedings against non-debtors under § 105(a)" (the
9 court commented: 'The usual standard helps to ensure that stays
10 would not be granted lightly'), 502 F.3d at 1094-95; 2) "a debtor
11 seeking to stay an action against a non-debtor must show a
12 reasonable likelihood of a successful reorganization", id., at
13 1095; 3) "the relative hardship of the parties"; and 4) "any
14 public interest concerns if relevant", id., at 1096.

15 In this proceeding, the focus of LSM Hotel seems to have
16 been on the likelihood of success on its fraudulent conveyance
17 adversary, not on the likelihood of a successful reorganization.
18 In Excel, the Bankruptcy Appellate Panel had found a reasonable
19 likelihood of a successful reorganization, but the Court of
20 Appeals held such a finding was an abuse of discretion because
21 the record did not provide evidentiary support for it. The
22 instant proceeding finds the debtor in a similar position, with
23 scant, if any, evidence provided in this motion on the likelihood
24 of a successful reorganization. In years past, this Court has
25 followed the Fourth Circuit decision in A.H. Robins Co. V.
26 Piccinin, 788 F.2d 994 (1986), and this Court would likely have

1 concluded that the request of debtor here was reasonable for a
2 finite period of time because of the effort required to
3 reorganize a financially troubled business, especially in times
4 of tight financing. If the business can be reorganized in a
5 reasonable period of time, that benefits most of the parties in
6 interest. (Here, that might not be as clear since LSM Hotel is
7 looking to avoid its liability of over \$3 million through its
8 fraudulent conveyance adversary). But Excel has raised the bar
9 for movants seeking to enjoin non-debtor third party litigation
10 even for a finite period of time. Here, the record is virtually
11 silent on the reasonable likelihood of a successful
12 reorganization.

13 The Excel decision reminds us:

14 The moving party must show:

15 (1) a strong likelihood of success on the
16 merits, (2) the possibility of irreparable
17 injury to plaintiff if preliminary relief is
18 not granted, (3) a balance of hardships
19 favoring the plaintiff, and (4) advancement
20 of the public interest (in certain cases).
21 Alternatively, a court may grant the
22 injunction if the plaintiff demonstrates
23 either a combination of probable success on
24 the merits and the possibility of irreparable
25 injury or that serious questions are raised
26 and the balance of hardships tips sharply in
his favor.

22 As we have said many times regarding the
23 two alternative formulations of the
24 preliminary injunction test: these two
25 formulations represent two points on a
26 sliding scale in which the required degree of
irreparable harm increases as the probability
of success decreases. They are not separate
tests but rather outer reaches of a single
continuum.

1 502 V.3d at 1093.

2 With respect to hardships, Excel instructs: "A bankruptcy
3 court must 'identify the harms which a preliminary injunction
4 might cause to defendants and . . . weigh these against
5 plaintiff's threatened injury.'" 502 F.3d at 1097. In Excel,
6 the court found that the fact the individual defendant might
7 raise a defense of indemnification, that denying the stay might
8 lead to inconsistent results, and that the individual defendant
9 might disclose privileged communications were "insufficient to
10 support the conclusion that Excel stands to suffer irreparable
11 harm if arbitration proceeds." 502 F.3d at 1097. The Excel
12 court also found that the bankruptcy court had ignored the harm
13 to the party to be enjoined. That party "had argued that it
14 would suffer harm from losing its bargained-for right to bring an
15 arbitration claim against Hoffman at a time of its choosing." Id.
16 The court reiterated: "'A plaintiff must do more than merely
17 allege imminent harm sufficient to establish standing; a
18 plaintiff must demonstrate immediate threatened injury as a
19 prerequisite to preliminary injunctive relief.'" 502 F.2d at
20 1099.

21 With the Excel standard in sharp focus, the Court concludes
22 that movant LSM Hotel has failed to demonstrate either a
23 reasonable possibility of reorganization, or that it would suffer
24 relative hardship, much less irreparable injury sufficient to

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1 warrant issuance of an injunction to stay state court proceedings
2 involving non-debtor third parties.

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Conclusion

For the foregoing reasons, LSM Hotel's motion for a stay of the so-called Toreador state court litigation shall be, and hereby is denied.

IT IS SO ORDERED.

DATED: ~~FEB~~ - 9 2011


PETER W. BOWIE, Chief Judge
United States Bankruptcy Court