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**UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF WASHINGTON**

IN RE:

ASTRIA HEALTH, et al.,

Debtors.<sup>1</sup>

Lead Case No. 19-01189-11

Jointly Administered

**OFFICIAL COMMITTEE OF  
UNSECURED CREDITORS' REPLY  
TO LAPIS SECURED PARTIES'**

<sup>1</sup> The Debtors, along with their case numbers, are as follows: Astria Health (19-01189-11), Glacier Canyon, LLC (19-01193-11), Kitchen and Bath Furnishings, LLC (19-01194-11), Oxbow Summit, LLC (19-01195-11), SHC Holdco, LLC (19-01196-11), SHC Medical Center-Toppenish (19-01190-11), SHC Medical Center-Yakima (19-01192-11), Sunnyside Community Hospital Association (19-01191-

DIP/Cash Collateral Reply



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**OBJECTION TO DEBTORS'  
MOTION FOR FINAL ORDER  
AUTHORIZING POST-PETITION  
FINANCING, USE OF CASH  
COLLATERAL AND RELATED  
RELIEF**

The Official Committee of Unsecured Creditors (the "Committee") in the chapter 11 cases of Astria Health (together with its affiliated debtors in possession, the "Debtors"), by and through its proposed undersigned counsel, hereby files this reply (the "Reply") to the Lapis Secured Parties' *Objection to Debtors' Motion for Final Order Authorizing Post-Petition Financing, Use of Cash Collateral and Related Relief* [Docket No. 226] (the "Lapis Objection").<sup>2</sup> In support of the Reply, the Committee respectfully represents as follows:

**REPLY**

As noted in the Committee's limited objection to the Debtors' DIP Financing Motion [as amended, Docket No. 233] (the "Committee Limited Objection"), the Committee objects to any adequate protection provisions or other requests by the Lapis Secured Parties beyond the adequate protection package provided in the

11), Sunnyside Community Hospital Home Medical Supply, LLC (19-01197-11), Sunnyside Home Health (19-01198-11), Sunnyside Professional Services, LLC (19-01199-11), Yakima Home Care Holdings, LLC (19-01201-11), and Yakima HMA Home Health, LLC (19-19-01200-11).

<sup>2</sup> Capitalized terms used but not defined herein shall have the meanings ascribed to them in the DIP Financing Motion, the DIP Loan Documents, or the Committee Limited Objection, as applicable.

1 Proposed Final Order. Any additional protections for the Lapis Secured Parties,  
2 which would strip all unsecured creditors of statutory rights (potentially exposing  
3 the Debtors' estates to administrative insolvency) and negativity impact the  
4 Debtors' ability to deliver the highest degree of patient care, are unnecessary in  
5 these chapter 11 cases. The risks to these estates inherent in granting the requests  
6 by the Lapis Secured Parties far exceed any potential benefits.

7 **I. The Lapis Secured Parties Are Adequately Protected Under the**  
8 **Proposed Final Order**

9 As set forth in greater detail in the Committee Limited Objection, the Lapis  
10 Secured Parties are already adequately protected in these cases pursuant to the  
11 terms of the Proposed Final Order. First, an equity cushion in the range of 80% to  
12 100% exists in the Lapis Prepetition Collateral, which percentage could be  
13 increased when taking into account that (i) the Debtors, at this time, may not need  
14 to make an additional draw from the DIP Facility, eliminating up to \$8 million in  
15 priming liens, (ii) the Lapis Senior Holdco Liens are not being primed and remain  
16 senior to the DIP Liens, and (iii) the Committee understands that the Debtors'  
17 financial performance appears to be better than projected. Lane Declaration, ¶ 55;  
18 Proposed Final Order, ¶ 12.

19 In fact, in the Lapis Objection the Lapis Secured Parties rely on the equity  
20 cushion to argue they are entitled to monthly adequate protection payments under  
21 section 506(b) of the Bankruptcy Code. Lapis Objection, page 24. However, as

1 explained below, this is a mischaracterization of section 506(b), which does not  
2 entitle alleged secured creditors to payment of interest during the pendency of a  
3 case in the form of adequate protection. Instead, the Lapis Secured Parties will  
4 receive any distribution (including interest, if appropriate), pursuant to a plan after  
5 the Committee has had the opportunity to investigate the liens and claims of the  
6 Lapis Secured Parties. *See e.g., Countrywide Home Loans, Inc. v. Hoopai (In re*  
7 *Hoopai)*, 581 F.3d 1090, 1100 (9th Cir. 2009) (“[N]oting that ‘[a]n oversecured  
8 creditor . . . is entitled to receive postpetition interest as part of its claim at the time  
9 of confirmation of a plan.’”) (emphasis added) (*citing Key Bank Nat’l Ass’n v.*  
10 *Milham (In re Milham)*, 141 F.3d 420, 423 (2d Cir. 1999).

11       Next, even if no equity cushion exists, the replacement liens provided in the  
12 Proposed Final Order provide adequate protection to the Lapis Secured Parties.  
13 Here, despite the Lapis Secured Parties’ claim that the replacement liens are  
14 illusory, the replacement liens provide significant value in the form of liens on,  
15 among other things, post-petition accounts receivable of the Debtors’ operating  
16 hospitals, and the proceeds thereof—assets on which the Lapis Secured Parties did  
17 not previously have a lien. *See* 11 U.S.C. § 552(a) and (b); *In re Skagit Pac. Corp.*  
18 316 B.R. 330, 336 (B.A.P. 9th Cir. 2004) (“Proceeds of post-petition accounts  
19 receivable do not fall within the § 552(b) proceeds exception. Therefore, a  
20 creditor’s security interest only encompasses the cash collected on existing pre-  
21 petition accounts.”).

1 Third, the Lapis Secured Parties are adequately protected by the 507(b)  
2 administrative expense superpriority claims in an amount equal to the diminution in  
3 value of the Lapis Prepetition Collateral from and after the Petition Date, if any, for  
4 any reasons provided under the Bankruptcy Code, subject and subordinate only to  
5 the Carve-Out and DIP Superpriority Claims, with recourse to the DIP Collateral  
6 (excluding the Commercial Tort Claims and Excluded Avoidance Actions). In  
7 addition to pre-petition collateral, and excluding the Commercial Tort Claims and  
8 Excluded Avoidance Actions, the DIP Collateral includes post-petition real and  
9 personal property of the Debtors. As such, this is another significant source of  
10 adequate protection and, together with the equity cushion and replacement liens, is  
11 more than sufficient to protect the interests of the Lapis Secured Parties with respect  
12 to the diminution in value, if any, of their interests in the Lapis Prepetition  
13 Collateral.

14 **II. Any Additional Adequate Protection Requests by the Lapis Secured**  
15 **Parties Are Unnecessary and Potentially Detrimental to the Debtors'**  
16 **Unsecured Creditors and Patients of the Hospitals**

17 As set forth in the Committee Limited Objection, the additional adequate  
18 protection terms requested by the Lapis Secured Parties will harm the Debtors'  
19 estates at the expense of the unsecured creditors and patients of the hospitals.  
20 Further, many of the requested forms of adequate protection are the result of the  
21 Lapis Secured Parties seeking to augment their rights by conflating their position as

1 a pre-petition creditor with that of a post-petition lender and otherwise ignoring  
2 certain provisions in the DIP Loan Agreement.

3 First, in the Lapis Objection, the Lapis Secured Parties state that an “all  
4 options’ strategy is necessary to adequately protect the [Lapis Secured Parties] and  
5 relief on the Financing Motion should be conditioned on an obligation to proceed in  
6 that manner.” Lapis Objection, pages 19-20. However, the DIP Loan Agreement  
7 does not set the Debtors down an exclusive path to proceed as a standalone hospital  
8 without allowing for the pursuit of an alternative transaction. For example, section  
9 8.1 of the DIP Loan Agreement provides that the following events, among others,  
10 shall constitute an Event of Default:

11 (p) Following one hundred and twenty (120) days from the Petition  
12 Date, the failure of the Borrowers to have (i) filed an Acceptable Plan  
13 or (ii) presented an alternative going forward strategy for resolving the  
Chapter 11 Cases that is acceptable to the Lender, in its sole  
discretion; or

14 (q) Following one hundred and eighty (180) days from the Petition  
15 Date, the failure of the Borrowers to have (i) effectuated an  
16 Acceptable Plan or (ii) obtained final court approval of an alternative  
transaction acceptable to the Lender, in its sole discretion.

17 DIP Loan Agreement, section 8.1(p) and (q) (emphasis added).

18 The Proposed Final Order further accommodates the Debtors’ ability to  
19 pursue an alternative transaction, delaying payment of the Stated Maturity Date Fee  
20 in the event that, among other things, the Debtors have obtained final court approval  
21 of an alternative transaction that has not closed due to the process of obtaining

1 requisite governmental approvals. Proposed Final Order, ¶ 1. As such, the Debtors  
2 are not being forced down a path to continue as a standalone hospital without the  
3 opportunity to simultaneously explore an alternative transaction. Further, to the  
4 extent any deadlines or termination provisions are ultimately tied to dates for an  
5 alternative transaction, the Lapis Secured Parties should not have exclusive control  
6 over the alternative transaction process—the Committee should receive the same  
7 rights as the Lapis Secured Parties with respect thereto.

8       Next, the Lapis Secured Parties argue they are entitled to “adequate  
9 protection that is customary in hospital chapter 11 cases,” and provide a list of such  
10 types of adequate protection. Lapis Objection, pages 23-24. However, this request  
11 suggests that the facts of all hospital chapter 11 cases are similar and ignores the  
12 replacement liens and superpriority claims they are already receiving as adequate  
13 protection, as well as the equity cushion that exists in these cases.

14       First, the Lapis Secured Parties request superpriority claims on the Excluded  
15 Avoidance Actions and Commercial Tort Claims. As set forth in the Committee  
16 Limited Objection, this is not a “customary” form of adequate protection, as these  
17 unencumbered assets and the proceeds thereof should remain available for  
18 distribution to unsecured creditors whose only recourse may be against such assets.  
19 *See e.g., Buncher Co. v. Official Comm. of Unsecured Creditors of GenFarm Ltd.*  
20 *Pshp. IV*, 229 F.3d 245, 250 (3d Cir. 2000); *In re Sweetwater*, 884 F.2d 1323, 1328  
21 (10th Cir. 1989).

1 Second, the Lapis Secured Parties request rights with respect to the Budget,  
2 but such rights are “customarily” reserved for the DIP lender who is providing the  
3 post-petition financing—the Lapis Secured Parties are not the DIP lender in these  
4 cases.

5 Third, as set forth in the Committee Limited Objection, the Committee does  
6 not dispute that it may be appropriate to establish an investigation and challenge  
7 period and related budget with respect solely to the validity, extent, perfection,  
8 priority and/or amount of the liens and claims of the Lapis Secured Parties under  
9 the Lapis 2017 Loan Documents and the Lapis 2019 Loan Documents (the “Lapis  
10 Lien Challenge”). However, any such investigation, challenge period and budget  
11 for the Lapis Lien Challenge must be reasonable to allow the Committee to fulfill  
12 its investigatory duties in these complex cases for the benefit of the Debtors’  
13 unsecured creditors. *See* 11 U.S.C. § 1103(c)(2) (empowering the committee to  
14 “investigate the acts, conduct, assets, liabilities, and financial condition of the  
15 debtor . . . and any other matter relevant to the formulation of the plan”). Further,  
16 any claims or causes of action that the Debtors’ estates may have against the Lapis  
17 Secured Parties not related to Lapis Lien Challenge should not be subject to any  
18 challenge deadlines or budget. All such claims and causes of action should be  
19 pursued consistent with the deadlines imposed by Congress or applicable state law  
20 rather than an arbitrary deadline imposed by an alleged junior secured creditor.  
21



1 Consistent therewith, the Lapis Secured Parties should not be entitled to a broad  
2 release from the Debtors.

3 Fourth, the Lapis Secured Parties request waivers of the Debtors' and  
4 Committee's rights under sections 506(c) and 552(b) of the Bankruptcy Code. In  
5 support of such requests, the Lapis Secured Parties claim they have already been  
6 "surcharged" by the DIP Loan and the Carve-Out. This is incorrect. Certain of  
7 their liens have been primed pursuant to section 364(d) of the Bankruptcy Code.  
8 Section 364(d) does not entitle a prepetition secured lender to a waiver of the  
9 Debtors' and/or Committee's rights under sections 506(c) or 552(b)—it only  
10 requires the prepetition secured lender receive adequate protection to the extent the  
11 collateral is declining in value, nothing more. Here the Lapis Secured Parties are  
12 receiving adequate protection. Similarly, the Carve-Out is for professional fees and  
13 expenses—not any trailing expenses in these chapter 11 cases—and thus is not in  
14 exchange for any rights under sections 506(c) or 552(b) of the Bankruptcy Code,  
15 which rights are designed to protect the Debtors' estates in the event of  
16 administrative insolvency. If the Lapis Secured Parties agree to fund all trailing  
17 expenses, the Committee will support a section 506(c) surcharge waiver as to the  
18 Lapis Secured Parties.

19 In further support of the requested waivers, the Lapis Secured Parties state  
20 that they "should not be subjected to still further raids on their collateral." Lapis  
21 Objection, page 24. This too mischaracterizes sections 506(c) and 552(b) of the

1 Bankruptcy Code. To surcharge a lender's collateral under 506(c) or avoid pre-  
2 petition liens from attaching to post-petition proceeds under section 552(b), the  
3 Debtors or Committee, as appropriate, must establish that circumstances warrant  
4 such relief pursuant to the requirements in the Bankruptcy Code. With respect to  
5 section 506(c), a debtor can recover the "reasonable, necessary costs and expenses  
6 of preserving, or disposing of, [secured property] to the extent of any benefit to the  
7 holder of such claim[.]" 11 U.S.C. § 506(c). With respect to section 552(b), courts  
8 can disregard a post-petition lien on "proceeds, products, offspring, or profits" of  
9 collateral based on the "equities of the case." 11 U.S.C. § 552(b). Thus, neither  
10 provision allows a debtor or committee to "raid" collateral.

11 Further, such waivers are inappropriate in these cases. Section 506(c) was  
12 carefully designed to protect against the risk of a debtor's administrative insolvency  
13 and to ensure secured creditors do not use the chapter 11 process to fund their own  
14 foreclosure proceedings. *See Comerica Bank-California v. GTI Capital Holdings,*  
15 *L.L.C. (In re GTI Capital Holdings, L.L.C.)*, 2007 Bankr. LEXIS 4853, at \*43  
16 (B.A.P. 9th Cir. Mar. 29, 2007) (*citing Silver State Sav. & Loan Ass'n v. Young*,  
17 252 F.2d 236, 238-39 (9th Cir. 1958)). The concern of administrative insolvency is  
18 particularly acute in hospital bankruptcy cases, such as these, where patients' lives  
19 are at stake. Thus, here, the Debtors should not be left without a vehicle to  
20 surcharge the Lapis Prepetition Collateral. With respect to section 552(b)—which  
21 is "relevant in chapter 11 to prevent a secured creditor from reaping benefits from

1 collateral that has appreciated in value as a result of the trustee's/debtor-in-  
2 possession's use of other assets of the estate"—it is not appropriate at the outset of  
3 these cases “to waive prospectively an argument that other parties in interest may  
4 make.” *In re Sine*, 2018 Bankr. LEXIS 2553, at \*25 (Bankr. W.D. Wash. Aug. 24,  
5 2018); *In re Metaldyne Corp.*, 2009 Bankr. LEXIS 1533, at \*20 (Bankr. S.D.N.Y.  
6 June 23, 2009). As such, any waiver of rights under sections 506(c) and 552(b) is  
7 not appropriate at this stage of these cases and could be detrimental to the Debtors’  
8 estates and the communities served by the Debtors.

9 Fifth, the Lapis Secured Parties request other rights provided to the DIP  
10 Lender, who, unlike the Lapis Secured Parties, is providing the Debtors’ estates  
11 with new money under the DIP Loan Agreement. For example, the Lapis Secured  
12 Parties request the right to credit bid all of their alleged claims (of which most are  
13 junior to the claims of the DIP Lender) in any sale of the Debtors’ assets. However,  
14 it is not “customary” or appropriate to provide an alleged junior creditor the right to  
15 credit bid, especially when, in these cases, the Committee intends to conduct an  
16 investigation of the liens and claims of the Lapis Secured Parties. *See* 11 U.S.C. §  
17 363(k) (“At a sale under subsection (b) of this section of property that is subject to a  
18 lien that secures an allowed claim, unless the court for cause orders otherwise the  
19 holder of such claim may bid at such sale . . . .”) (emphasis added); *In re Fisker*  
20 *Auto. Holdings, Inc.*, 510 B.R. 55, 61 (Bankr. D. Del. 2014) (“The law leaves no  
21

1 doubt that the holder of a lien the validity of which has not been determined, as  
2 here, may not bid its lien.”).

3 Finally, the Lapis Secured Parties request adequate protection payments in  
4 the amount of monthly interest accrued on the principal amount of the Bonds and  
5 Working Capital Loan at non-default rates. Lapis Objection, page 24. As  
6 explained above, they rely on the equity cushion in their collateral in making the  
7 argument they are entitled to post-petition interest. However, this too is a  
8 misinterpretation of the Bankruptcy Code. Even if the court ultimately determines  
9 that the Lapis Secured Parties are oversecured and thus entitled to post-petition  
10 interest, such post-petition interest will be paid pursuant to a plan, not in the form of  
11 immediate adequate protection payments during the pendency of the chapter 11  
12 cases. *See e.g., In re Hoopai*, 581 F.3d at 1100 (9th Cir. 2009) (“[N]oting that ‘[a]n  
13 oversecured creditor . . . is entitled to receive postpetition interest as part of its  
14 claim at the time of confirmation of a plan.’”) (emphasis added) (*citing Key Bank  
15 Nat'l Ass'n v. Milham (In re Milham)*, 141 F.3d 420, 423 (2d Cir. 1999)); *Telfair v.  
16 First Union Mortg. Corp.*, 216 F.3d 1333, 1339 (11th Cir. 2000) (“[T]he purpose of  
17 section 506(b) [is to] allow[] oversecured creditors to include post-petition interest  
18 and certain fees as part of the secured claim they will receive upon confirmation of  
19 the plan”) (emphasis added); *In re Milham*, 141 F.3d at 423 (“On the date of  
20 confirmation, the allowed claim of an oversecured creditor is augmented by the  
21 inclusion of section 506(b) pendency interest.”) (emphasis added).

1 It would be illogical to establish the existence of an equity cushion in  
2 collateral, which precludes the need for further adequate protection, while  
3 simultaneously requiring adequate protection interest payments as a result of that  
4 equity cushion. Further, the Committee intends to investigate the liens and claims  
5 of the Lapis Secured Parties and thus it is premature to make payments based on the  
6 status of the Lapis Secured Parties' asserted liens and claims.

7 Additionally, requiring the Debtors to make adequate protection interest  
8 payments in these cases could be the sole reason the Debtors would need to draw  
9 additional funds from the DIP Facility or could impair the Debtors' ability to utilize  
10 such funds for the provision of patient care. A second draw on the DIP Facility will  
11 be extremely costly to the Debtors' estates, as such additional draw carries with it  
12 high fees and expenses, including, among others, (i) non-default interest at a rate of  
13 12% per annum on the Daily Balance; (ii) default interest at a rate of 17% per  
14 annum on the Daily Balance; and (iii) a funding fee at a rate of 1.5% of each  
15 Advance payable upon funding such Advance. Thus, making adequate protection  
16 interest payments would be costly to the Debtors' estates without providing any  
17 necessary protection to the already adequately protected Lapis Secured Parties.  
18 Further, the Committee submits that the Debtors' capital in these cases should be  
19 used to provide patient care rather than diverting such funds to creditors asserting  
20 security interests in the Debtors' property.

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**WHEREFORE**, for the foregoing reasons, the Committee respectfully requests that this Court deny any adequate protection requests by the Lapis Secured Parties in the Lapis Objection beyond what it is included in the Proposed Final Order, and grant such other and further relief as this Court deems just and proper.

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## DIP/Cash Collateral Reply