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**PROPOSED COUNSEL FOR THE
COMMITTEE OF UNSECURED CREDITORS**

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION**

In re:

Northwest Senior Housing Corporation, *et*
al.,¹

Debtors.

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Chapter 11

Case No. 22-30659 (MLV)

(Jointly Administered)

**OBJECTION BY THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS TO
THE DEBTORS' CASH MANAGEMENT MOTION**

[Relates to Docket Nos. 19 and 93]

The Official Committee of Unsecured Creditors (the “**Committee**”) of the above-captioned debtors and debtors in possession (the “**Debtors**”), hereby files this *Limited Objection* (the “**Objection**”) to Debtors’ Motion for Entry of Interim and Final Orders (I) Authorizing (A) Continued Use of Debtors’ Existing Cash Management System, (B) Maintenance of Debtors’ Existing Bank Accounts, and (C) Continued Use of Debtors’ Existing Business Forms and (II)

¹ The Debtors in these chapter 11 cases (the “**Chapter 11 Cases**”), along with the last four digits of each Debtor’s federal tax identification number, are Northwest Senior Housing Corporation (1278) and Senior Quality Lifestyles Corporation (2669). The Debtors’ mailing address is 8523 Thackery Street, Dallas, Texas 75225.



Granting Related Relief [Docket No. 19] (the “**Cash Management Motion**”).² In support of the Objection, the Committee respectfully represents as follows:

I.
EXECUTIVE SUMMARY

1. It appears from the Cash Management Motion that:

- Lifespace owns numerous subsidiaries which operate fourteen (14) continuing care retirement communities (“**CCRCs**”) like Edgemere (the “**Lifespace Group**”);
- Lifespace serves as the management company for all or most of its subsidiaries CCRCs;
- According to the Cash Management Motion, Lifespace provides substantial “back office” or administrative services to these CCRCs, like accounting, legal, billings, and insurance procurement. This is the “Corporate Overhead” which is allocated to each subsidiary CRCC based on respective gross revenues (the “**Corporate Overhead Fee**”). In addition to the Corporate Overhead Fee, Lifespace allocates the cost of goods or services provided to the CCRCs pursuant to an “Intercompany Accounting Protocol” (as defined in the Cash Management Motion), with the method of allocation different for each service or product. For example, property insurance might be allocated based on the estimated value of property insured, but workers compensation insurance coverage might be allocated by number of employees. The Committee has not reviewed the costs nor the allocation methods for relative fairness, but has no reason to question them at this time;

² Capitalized terms used but not defined herein shall have the meanings ascribed to them in the Cash Management Motion.

- At the beginning of each year, Lifespace estimates the aggregate costs it will incur on behalf of all of its facilities, and then allocates those estimated costs to each facility, and collects that allocated estimated cost in monthly installments paid to Lifespace. At the end of the year, Lifespace reconciles the actual costs versus the estimated costs, and if Edgemere overpaid Lifespace, Edgemere is reimbursed by Lifespace or, alternatively, records an intercompany account receivable on its books and records from Lifespace. The Committee is unsure which actually occurs. If Edgemere underpaid its actual costs, Edgemere owes Lifespace money and either pays that deficiency to Lifespace or books an intercompany payable to Lifespace;
- The Cash Management Motion proposed to provide Lifespace with an agreed administrative expense claim for any amount it determines Edgemere underpaid to Lifespace (and it appears Lifespace is deferring and accruing 100% of the monthly estimated payments due from Edgemere during the pendency of these Chapter 11 Cases);
- The Committee has no objection to the cash management system continuing, but objects to providing Lifespace with allowed administrative expense claim now for any amounts Lifespace determines in the future that the Debtors owe it for the underpayment of the actual Lifespace costs allocated by Lifespace to Edgemere. This involves millions of dollars and the eventual allowance of an administrative expense claim should only occur after the Committee and parties in interest have an opportunity to determine the appropriateness of the cost (benefit to the estate) and the fairness of the allocations currently determined by Lifespace.

2. The Committee supports the Debtors' efforts to preserve the status quo and avoid any disruptions in operations and cash flow as debtors-in-possession. The Committee does not oppose the continuation of the Cash Management System or the Intercompany Transactions, *per se*; provided, however, the Committee objects to any preapproved administrative expense claims without the requisite detail provided to support a properly filed application for approval of the same.

II.

PROCEDURAL POSTURE

3. On April 14, 2022 (the "**Petition Date**"), the Debtors each filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code. The Debtors are operating their businesses and managing their properties as debtors in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code.

4. As of the date hereof, no request for the appointment of a trustee or examiner has been made.

5. On April 28, 2022, the United States Trustee for the Northern District of Texas appointed the Committee in these Chapter 11 Cases, as amended on April 29, 2022 and May 2, 2022.

6. On April 19, 2022, the Court approved the Cash Management Motion on an interim basis [Docket No. 93] (the "**First Interim Order**"). After a second interim hearing held on May 11, 2022, the Court approved the Cash Management Motion on a second interim basis pending the Court's rulings at a final hearing.

7. The Committee's response deadline to the Motion is currently set for May 19, 2022 at 4:00 p.m. CT.

8. The Cash Management Motion will be considered for final relief at a final evidentiary hearing currently docketed for May 26, 2022 at 9:30 a.m. CT.

III.
BACKGROUND RELEVANT TO THIS LIMITED OBJECTION

9. In the Cash Management Motion, the Debtors seek authorization, among other things, to operate their current cash management system (the “**Cash Management System**”) and to continue certain Intercompany Transactions. The Intercompany Transactions include certain payments, credits, obligations, transfers and transactions by and/or among, as applicable, the Debtors, certain non-Debtor affiliates and Lifespace within the Corporate Overhead Fee structure and the Intercompany Accounting Protocol, each summarized separately below.

A. Corporate Overhead Fee

10. As described in the Cash Management Motion, the Debtors are included in a group of entities referred to as the “Lifespace Group”. The Lifespace Group is comprised of the Debtors, certain non-Debtor affiliates and Lifespace. Under the Debtors’ Management Services Agreement, Lifespace provides administrative services to the Debtors. Lifespace also provides similar administrative services under similar management services agreements to the non-Debtor affiliates. In exchange for Lifespace providing such administrative services to the Debtors and non-Debtor affiliates, respectively, Lifespace is paid an annual Corporate Overhead Fee.

11. The aggregate amount of the annual Corporate Overhead Fee is estimated and spread across the members of the Lifespace Group based on Lifespace’s historical and anticipated operating costs. Lifespace then allocates the Corporate Overhead Fee to the Lifespace Group members based on various factors. The Lifespace Group members then pay their respective portion of the estimated annual Corporate Overhead Fee to Lifespace on a monthly basis. At the end of each year, the actual amount of the Corporate Overhead Fee due is reconciled against the previously paid monthly estimates and reallocated among the Lifespace Group members to account for any retroactive adjustments.

12. Under the Corporate Overhead Fee structure, the system allows for the possibility that each month the Debtors pay in advance more or less than their actual share of the annual Corporate Overhead Fee due to Lifespace. Conversely, the non-Debtor affiliates in the Lifespace Group could pay in advance more or less than their actual share of the annual Corporate Overhead Fee. Thus, from time-to-time, the Debtors may indirectly cover a share of the non-Debtor affiliates' obligations and vice versa. The projected estimated advance payments are trued up at the end of each year.

13. The Committee cannot consent to preapproved administrative expense claims for Lifespace without first confirming the corroborating amounts, nature, dates, causal benefit to the estates, and related detailed evidence required to diligence such priority.

B. Intercompany Accounting Protocol

14. Separate from the Corporate Overhead Fee, Lifespace also procures certain goods and services for the entirety of the Lifespace Group. In turn, the Lifespace Group members reimburse Lifespace for the cost of such goods and services. In some instances, certain of the Lifespace Group members pay their allocated share of such goods and services directly to the third-party vendor. Lifespace allocates the respective obligations for each member of the Lifespace Group based on various criteria itemized in bullets on pages 7-8 of the Cash Management Motion.

15. Under the Intercompany Accounting Protocol, each member of the Lifespace Group (comprised of the Debtors and their non-Debtor affiliates) either (a) directly pays third-party vendors, or (b) reimburses Lifespace for the remainder of costs allocated to such member of the Lifespace Group.

16. Despite the description of the reimbursement system and an itemized list of the allocation criteria, the details remain unclear as to exactly how much and when the reimbursements under the Intercompany Accounting Protocol are paid either to Lifespace or the third-party vendors

and how much of such reimbursements are allocated among the Debtors and non-Debtor affiliates in the Lifespace Group.

17. Again, as with the Corporate Overhead Fee, the Lifespace Group reimbursement allocation structure under the Intercompany Accounting Protocol creates a scenario where Lifespace may (i) incur costs on behalf of the Debtors and not collect from the Debtors, or (ii) collect such incurred costs from a non-Debtor affiliate on behalf of the Debtors. Either way, potential insider administrative claims may be created. The allowed amount of any administrative expense claim should be subjected to notice and an opportunity for review before being allowed in advance in an undetermined amount.

18. The payments, obligations, transfers, transactions, and/or credits made or incurred among the Debtors, non-Debtor affiliates and/or Lifespace within the Corporate Overhead Fee structure and the Intercompany Accounting Protocol are defined by the Cash Management Motion as the “**Intercompany Transactions**”.

IV. **LIMITED OBJECTION TO RELIEF REQUESTED**

19. The Committee does not object to the Debtors’ continued use of its Cash Management System generally, as the Committee recognizes that use of such a system is necessary to preserve and maximize the value of the Debtors’ estates. The Committee further understands that the Intercompany Transactions are necessary to maintain uninterrupted business services.

20. Accordingly, the Committee’s objection to the Cash Management Motion is limited to the preapproved administrative expense priority awarded to the Debtors’ insiders and affiliates in advance of any such Intercompany Transactions being made and without any independent corroboration of the evidence satisfying the criteria under 503(b)(1) to justify administrative expense priority for such Intercompany Transactions.

21. The Fifth Circuit requires a party seeking administrative expense priority to file a separate application to allow such a claim. *See In re Taco Bueno Rest., Inc.*, 606 B.R. 289, 301 (Bankr. N.D. Tex. 2019) (citing *In re Jack Kline Co.*, 440 B.R. 712, 735 (Bankr. S.D. Tex. 2010) (The Fifth Circuit has concluded that a party must request administrative expenses by a separate application.) (citing *NL Indus., Inc. v. GHR Energy Corp.*, 940 F.2d 957, 966 (5th Cir. 1991)). Under 503(b), the applicant bears the burden to show reasonableness, necessity and benefit to the bankruptcy estate. *See Taco Bueno Rest., Inc.*, 606 B.R. at 302. Requiring that a § 503 administrative expense be in a separate application also ensures that the bankruptcy court will have an opportunity to pass judgment on the administrative expense and prevent any unreasonable, unnecessary, and non-beneficial claims from being charged to the estate. *See id.*

22. If the Debtors' general ledger system functions as most such systems do, it will generate a substantial number of balancing entries, some of which may reflect economic reality but others of which will merely reflect the exigencies and requirements of the general ledger system itself. It will therefore be highly prejudicial to unsecured creditors, and to creditors that may have, or subsequently acquire, administrative claims in these cases, to allow in a prospective manner an ill-defined and potentially quite large number of transactions administrative status at this early stage in these proceedings.

23. Precisely because they maintain records of the transactions in question, there is no reason why the Debtors or their non-Debtor affiliates cannot seek administrative status at a later time for the transactions they believe are entitled to such status. At such time, the transactions can be described retrospectively with the requisite supporting detail, and creditors and parties in interest will be in a better position to judge whether those transactions satisfy the criteria of Section 503(b)(1).

24. The Committee recognizes the Debtors' needs to continue operating in the ordinary course of business and to minimize cash flow disruption. In recognition of these issues, the Committee's proposed solution to the Intercompany Transactions problems identified in this Objection is to defer allowance of any administrative expense priority for Intercompany Transactions until corroborating evidence is presented to diligence such claims in a formal application for allowance under 503(b) filed with the Court. The Court should therefore deny the preapproved administrative expense claims for the Intercompany Transactions, as defined in the Cash Management Motion, without prejudice to future application for such administrative expense claims, with all parties' rights reserved.

V.
RESERVATION OF RIGHTS

25. The Committee expressly reserves all of its rights to assert additional objections to the Cash Management Motion or to amend or supplement this Objection at any time prior to or at any hearing on the Cash Management Motion.

WHEREFORE, for the reasons set forth above, the Committee objects to the relief sought in the Cash Management Motion, and respectfully requests that this Court: (i) limit the relief sought by the Debtors in the Cash Management Motion to the extent provided for herein; and (ii) grant such other and further relief as the Court may deem just and proper.

[signature page follows]

Dated: May 19, 2022

Respectfully submitted,

FOLEY & LARDNER LLP

/s/ Thomas C. Scannell

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served electronically by
the Court's PACER system on May 19, 2022.

/s Thomas C. Scannell

Thomas C. Scannell