

**UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE**

In re: : Chapter 11
: :
EMERGE ENERGY SERVICES LP, *et al.*, : Case No. 19-11563 (KBO)
: :
Debtors. : Jointly Administered
: **Hearing Date: September 5, 2019 at 10:00 a.m. (ET)**
: **Objection Deadline: August 30, 2019 by 4:00 p.m. (ET)**
: :
: **Related Docket Nos. 247 and 269**

**POWNALL SERVICES, LLC’S OBJECTION
TO THE DEBTORS’ DISCLOSURE STATEMENT**

Pownall Services, LLC (“Pownall”), by and through its undersigned counsel, hereby objects (the “Objection”) to the *Disclosure Statement* (the “Disclosure Statement”) for the *First Amended Joint Plan of Reorganization* (the “Plan”) for *Emerge Energy Services LP* and its *Affiliated Debtors Under Chapter 11 of the Bankruptcy Code* [D.I. 269] and the motion to approve the *Disclosure Statement* [D.I. 247] (the “Solicitation Motion”) filed by the above-captioned debtors (the “Debtors”). In support of this Objection, Pownall states as follows:

PRELIMINARY STATEMENT

1. According to the Debtors’ schedules and other publicly available information, there could be as much as \$25 million in mechanic’s liens encumbering the Debtors’ properties. Notwithstanding the magnitude of these obligations—obligations that may be a gating issue to confirmation of any plan—the *Disclosure Statement* does not even mention mechanic’s liens.

2. Even more fundamental to the adequate information needs of all creditors, the *Disclosure Statement* fails to disclose information relating to the Debtors’ valuation of the frac plants in Oklahoma and Texas, any liens or claims against the properties, how mechanic’s liens will be treated under the Debtors’ plan, and the adversary proceeding filed by Pownall seeking declaratory judgment regarding the priority of liens on the Debtors’ Oklahoma plant.



3. Additionally, the Motion should be denied because the Debtors' plan is patently unconfirmable. First, no distribution to junior claims (e.g., unsecured claims) may be made without payment of Pownall's allowed secured claim, and any other allowed "Other Secured Claims" under the Plan. Second, in order for Other Secured Claims to be validly treated as unimpaired, the Plan must be revised to specify that an allowed claim of a mechanic's lien claimant includes attorneys' fees and interest, to the extent provided under applicable nonbankruptcy law. Third, the Plan seeks to reverse the established burden of proof on allowance of claims, which, as to mechanic's lien claims, would apparently allow the Debtors to pay nothing and reserve nothing for mechanic's liens that the Debtors subjectively dispute, and at the same time receive a full release of liens.

4. A disclosure statement should not leave creditors guessing as to their treatment. A disclosure statement should not be allowed to avoid discussing the Debtors' ability to reorganize around threshold issues, such as the mechanic's liens currently encumbering the Debtors' properties. Accordingly, the Solicitation Motion should be denied.

PREPETITION BACKGROUND

5. Pownall is a contractor which provides design, construction, and maintenance services for a variety of industrial processing facilities, including bulk sand handling facilities commonly known as frac sand plants.

6. Debtor Superior Silica Sands LLC (the "Debtor") owns multiple frac sand plants throughout North America, including a plant in Kingfisher, Oklahoma (the "Oklahoma Plant") and in Kosse, Texas (the "Texas Plant").

7. Pownall furnished the Debtor with labor and materials at the Oklahoma and Texas Plants.

8. On or about February 15, 2019, Pownall recorded a mechanic's lien (the "Texas Lien") against the Texas premises in the amount of \$380,054.73, representing the amount due for services rendered by Pownall to the Debtor related to the Texas Plant.

9. On or about April 5, 2019, Pownall recorded a mechanic's lien (the "Oklahoma Lien") against the Oklahoma premises in the amount of \$1,598,738.31, representing the amount due for services rendered by Pownall to the Debtor related to the Oklahoma Plant. Although not specified in in the Disclosure Statement, the first-day declaration filed in these cases, D.I. 14 (the "First-Day Declaration"), provides that the Debtors began construction of the Oklahoma Plant in May 2018, but discontinued work on the project in January 2019.

POSTPETITION BACKGROUND

10. On July 15, 2019 (the "Petition Date"), the Debtors filed their voluntary petitions under chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for the District of Delaware. The Debtors' cases are being jointly administered.

11. On July 25, 2019, the Debtors filed their *Joint Plan of Reorganization for Emerge Energy Services LP and Its Affiliate Debtors Under Chapter 11 of the Bankruptcy Code* [D.I. 98] (the "Plan") and Disclosure Statement.

12. On August 9, 2019, the Debtors filed their schedules and statements of financial affairs. The schedules show that mechanic's liens will be a significant issue in the Debtors' cases. See, e.g., Schedules of Superior Silica Sands LLC, Schedule D, Part 1 Attachment (disclosing sixteen "construction liens," aggregating to over \$13 million). Pownall's Texas and Oklahoma Liens are inexplicably not included in the Debtors' schedules,¹ and other mechanic's liens not

¹ At the 341 meeting of creditors on August 14, 2019, the Debtors' witness testified that he was aware of the Texas and Oklahoma Liens, but had no explanation of why these were not reflected on the Debtors' schedules.

reflected on the Debtor's schedules have been asserted through notices filed on the docket, see, e.g., D.I. 159 (reflecting a \$15,571.76 mechanic's lien of Anchor Technical Services, LLC), D.I. 252 (reflecting a \$1,195,911.89 mechanic's lien of A-1 Excavating, Inc.); D.I. 254 (reflecting a \$8,802,159.22 mechanic's lien of Market & Johnson, Inc.). Accordingly, based on the limited information to date, mechanic's liens on the Debtors' property could exceed \$25 million.²

13. At the 341 meeting of creditors on August 14, 2019, the Debtors' witness testified that the Debtors had not yet determined whether to complete construction of the Oklahoma Plant.

14. On August 16, 2019, Pownall filed a complaint in this Court against the Debtor and HPS Investment Partners, LLC (the prepetition lender and DIP lender), initiating an adversary proceeding captioned *Pownall Services, LLC v. Superior Silica Sands LLC, et al.*, Adv. Pro. No. 19-50295 (the "Pownall Action"), requesting a declaratory judgment that Pownall is a secured creditor and that the Oklahoma Lien is senior to the "Prepetition Liens" of HPS, as defined in the final DIP order [D.I. 209]. The complaint was served on both defendants on August 16 and, as of the date hereof, neither defendant has responded.

OBJECTIONS

A. The Disclosure Statement Does Not Provide Adequate Information Regarding Mechanic's Liens.

15. A disclosure statement must contain "adequate information," defined as information that would allow a hypothetical investor to make an informed judgment regarding the plan. See 11 U.S.C. § 1125(a)(1). The Third Circuit has stated, "[W]e cannot overemphasize the debtor's obligations to provide sufficient data to satisfy the [Bankruptcy] Code standard of 'adequate information.'" Oneida Motor Freight, Inc. v. United Jersey Bank, 848 F.2d 414, 417 (3d Cir. 1988).

² Pownall does not stipulate or admit to the validity of any liens other than its own liens and specifically reserves the right to object to the validity of any such liens.

16. Here, the Disclosure Statement is so facially deficient of “adequate information” that creditors cannot make an informed decision about the Plan. Specifically, the Disclosure Statement:

- fails to disclose any information relating to the Debtors’ valuation of the Oklahoma and Texas Plants;
- provides no discussion regarding the Debtors’ plans regarding the Oklahoma Plant (e.g., whether the Debtors intend to complete construction);
- does not detail (even in a summary fashion) the \$25 million³ mechanic’s liens filed on the Debtors’ properties and is ambiguous regarding the treatment thereof; and
- provides financial projections and a liquidation analysis too vague and speculative for parties-in-interest to make an informed decision regarding the Plan.

17. Despite mechanic’s liens being front-and-center in these bankruptcy cases—and maybe even a gating issue to confirmation—the Disclosure Statement is barren of any information relating to mechanic’s liens. In Article II.C of the Disclosure Statement—the “Prepetition Indebtedness” subsection of the background—the Debtors describe HPS’ first lien debt, the second lien debt, and unsecured trade debt, but make no mention of any mechanic’s liens or any other liens.

18. Buried in the fine print of the liquidation analysis, attached to the Disclosure Statement as Exhibit D, footnote AC provides that lien claims against the Oklahoma Plant may be listed as Other Secured Claims and liquidation value is based on an assumed sale of “those

³ As discussed above, the \$25 million figure for mechanic’s liens are based on (1) the Debtor’s schedules, (2) the amount asserted in Pownall’s Oklahoma and Texas Liens, and (3) the undersigned’s interpretation of notices filed on the docket to date.

particular assets.” See Disclosure Statement, Liquidation Analysis, n. AC (“Lien claims listed as other secured primarily relate to specific assets at the Kingfisher, OK plant (under construction). Any assumed recovery is related specifically to any potential proceeds from the sale of those particular assets.”). In the “Summary of Expected Recoveries” portion, the Disclosure Statement provides that the expected total recovery to “Other Secured Claims,” is “Expected Amount: \$[441,000].”

19. Without more detail, this \$441,000 valuation of the Oklahoma Plant raises more questions than it provides answers. Among other questions: What is the basis for the valuation? At the 341 meeting, the Debtors’ witness testified that he was aware of no valuations of the property, so is this some new valuation performed during the last two weeks? Is the reference to “lien claims” in footnote AC an admission that HPS does not, as asserted in Pownall’s adversary proceeding, have a lien on the Oklahoma Plant? What would be the value of the Oklahoma Plant as a going-concern, taking into account the cost to complete the project?

20. Nor does the Disclosure Statement shed any light as to the treatment of mechanic’s lien claims. Section 2 of the Financial Projections, attached to the Disclosure Statement as Exhibit C, provides that “Other Secured Claims relating to claimants with valid M&M liens are reinstated as secured debt and amortized over a 24 month period.” Is this an indication of how the Debtors actually intend to treat Other Secured Claims? If so, who will be paid, how much, and at what effective discount rate?

21. Compounding the risk and uncertainty to mechanic’s lien claimants, the Disclosure Statement fails to describe how lien claims will be resolved and, if valid, paid under the Plan. Any liens will be fully released on the Debtors’ property as of the effective date of the Plan, see Disclosure Statement Art. IV.D.11, but apparently no requirement that a reserve or other fund to

satisfy the liens need be funded in order for the Plan to go effective, see Disclosure Statement Art IV.G.4 (providing that a reserve for disputed claims “may” be established if the Debtors, the reorganized debtors, or the distribution agent so determine, “in their respective sole discretion”).

22. Finally, the Disclosure Statement fails to disclose any claims against the estate and the existence, likelihood, and possible success of nonbankruptcy litigation. Specifically—and notable for all creditors of the Debtors’ estate, not just mechanic’s lien claimants—the Disclosure Statement fails to disclose the Pownall Action, which seeks a declaratory judgment that the Oklahoma Lien and other mechanics’ liens have priority over any prepetition liens of HPS on the Oklahoma Facility.

23. Accordingly, the Disclosure Statement fails to provide the information necessary to inform parties-in-interest about the current status of the estates and to allow them to make an informed judgment regarding the Plan, and the Solicitation Motion should be denied.

B. The Plan Is Patently Unconfirmable.

24. An objection to a disclosure statement should be sustained “where it is obvious at the disclosure statement stage that a later confirmation hearing would be futile because the plan described by the disclosure statement is patently unconfirmable.” In re American Capital Equipment, LLC, 688 F.3d 145, 154 (3d Cir. 2012). For the reasons stated below, the Debtors’ Plan is patently unconfirmable, and therefore the Solicitation Motion should be denied.

25. First, the Debtors’ Plan is patently unconfirmable because it violates the absolute priority rule. No party has yet contested that Pownall’s Liens are secured claims that are entitled to payment in full before unsecured creditors are entitled to a single penny. Pursuant to the absolute priority rule, junior creditors are not entitled to receive payment on account of their claim unless and until senior creditors are paid in full. 11 U.S.C. § 1129(b)(2). In order to respect the absolute

priority rule, the Plan must require also that, in the absence of payment in full of all allowed mechanic's liens, any distribution made under the Plan is subject to disgorgement. Absent such a provision, payments to any claimant, including secured claims, unsecured claims, and administrative expenses, would violate the absolute priority rule and the Plan would be neither fair nor equitable.

26. Second, the treatment of "Class 2 – Other Secured Claims" should be revised to make clear that the allowed claims of such parties includes any attorneys' fees and interest, to the extent provided under applicable nonbankruptcy law. At least as to interest, the Plan currently seeks to cut off those rights. See Plan Art. I.C. ("The term 'Allowed Claim' shall not, for purposes of computing distributions under this Plan, include interest on such Claim from and after the Petition Date, except as provided in sections 506(b) or 511 of the Bankruptcy Code, or otherwise expressly set forth in this Plan or a Final Order of the Bankruptcy Court."); Plan Art. VII.B. (providing that postpetition interest shall not accrue on claims "[u]nless otherwise specifically provided for in this Plan, the Confirmation Order or Final Order of the Bankruptcy Court, or required by applicable bankruptcy law"). As a mechanic's lien claimant under Oklahoma and Texas state law, Pownall is entitled to attorneys' fees and interest. See, e.g., Okl. Stat. tit. 12, § 727.1 (providing for pre- and post-judgment interest); Okla. Stat. tit. 42, § 176 (2019) ("In an action brought to enforce any lien the party for whom judgment is rendered shall be entitled to recover a reasonable attorney's fee, to be fixed by the court, which shall be taxed as costs in the action."); Tex. Prop. Code Ann. § 53.156 (West 2019) ("In any proceeding to foreclose a lien . . . or in any proceeding to declare that any lien or claim is invalid or unenforceable in whole or in part, the court shall award costs and reasonable attorney's fees as are equitable and just."); Tex. Fin. Code Ann. § 304.002 (providing for prejudgment interest); id. § 304.003 (providing for

postjudgment interest); William M. Graham Oil & Gas Co. v. Oil Well Supply Co., 264 P. 591, 601 (Okla. 1927) (affirming trial court, and holding that approval of attorneys' fees awards in ranges between 10% and 25% of mechanic's lien claim amount were reasonable and "involved the exercise of a sound judicial decision"). It is likely that other mechanic's lien creditors will make similar claims. Given the importance of mechanic's liens in the Debtors' chapter 11 cases, the treatment of Other Secured Claims in the Plan should be revised accordingly. Such treatment should be a condition to the Other Secured Claims being treated as unimpaired under the Plan.

27. Third, the Plan is unconfirmable because it seeks to revise the Bankruptcy Code's presumption that a timely filed, properly documented proof of claim is deemed allowed, absent an objection. Through a series of defined terms, the Plan apparently allows the Debtors to unilaterally treat a claim as disputed (notwithstanding the fact a creditor may have an allowed claim under the Bankruptcy Code, because, for example, it filed a proper proof of claim by the bar date) and not pay distributions on account of that claim. See Plan Art. 1.C. (defining "Allowed Claim" as "any Claim that is not a Disputed Claim or a Disallowed Claim"); Plan Art. 1.C. (defining "Disallowed Claim" as "a Claim, or any portion thereof, that . . . is scheduled at zero, in an unknown amount or as contingent, disputed or unliquidated"); Plan Art. 1.C. (defining "Disputed Claim" to include a claim (i) to which an objection has been filed, (ii) "which is otherwise disputed by any Debtor in accordance with applicable law," or (iii) "that is otherwise disputed by any Debtor in accordance with the provisions of this Plan or applicable law, which dispute has not been withdrawn, resolved or overruled by Final Order"). This potentially allows for mischief for mechanic's liens, because the property of the Debtors is vested free and clear of liens as of the effective date of the Plan, see Plan Art. V.D., and for any claims to be released on the effective date, see Plan Art. V.K., but allows the Debtors to withhold paying or otherwise honoring a lien claim on the effective date if

the lien claim is not “Allowed” as of the effective date of the plan, see Plan Art. III.B.2(b) (providing that “Other Secured Claims” receive, among other possible treatment, cash, collateral, or other treatment such that they will be not be impaired, but only after such claim becomes “Allowed”), see also Plan Art. VII.A. (“Distributions on account of Disputed Claims that first become Allowed Claims after the Effective Date shall be made pursuant to Article VIII hereof.”). The Plan should be revised to specify that a creditor with an “Other Secured Claim” retains its liens until the creditor receives one of the treatments specified in Article III.B.2, of the Plan. Otherwise, the loss of a lien without appropriate payment or other appropriate treatment is a clear impairment under section 1124 of the Bankruptcy Code.

CONCLUSION

WHEREFORE, Pownall respectfully requests that the Court deny the Solicitation Motion, and condition approval upon amendment of the Disclosure Statement and the Plan to address the objections raised herein.

Dated: August 30, 2019

SAUL EWING ARNSTEIN & LEHR LLP

/s/ Lucian B. Murley

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**UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE**

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EMERGE ENERGY SERVICES LP, *et al.*, : Case No. 19-11563 (KBO)
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Debtors. : Jointly Administered

CERTIFICATE OF SERVICE

I, Lucian B. Murley, hereby certify that on August 30, 2019, I caused a copy of the *Pownall Services, LLC's Objection to the Debtor's Disclosure Statement* to be served electronically with the Court and served through the Court's CM/ECF system upon all registered electronic filers appearing in this case who consented to electronic service and via Electronic Mail and First Class Mail on the parties on the attached service list.

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Dated: August 30, 2019

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