

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF WISCONSIN**

In re:	§	Chapter 11
	§	
CAPITOL LAKES, INC., ¹	§	Case No. 16-10158
	§	
Debtor.	§	Hon. Robert D. Martin

MOTION OF DEBTOR FOR ENTRY OF AN ORDER (I) AUTHORIZING THE DEBTOR TO (A) MAINTAIN EXISTING INSURANCE POLICIES AND PAY ALL OBLIGATIONS ARISING THEREFROM, AND (B) RENEW, REVISE, EXTEND, SUPPLEMENT, CHANGE, OR ENTER INTO NEW INSURANCE POLICIES AND (II) GRANTING CERTAIN RELATED RELIEF

Capitol Lakes, Inc., the above-captioned debtor and debtor in possession (the “Debtor”), by and through its undersigned proposed attorneys, hereby submits this motion (this “Motion”) for entry of an order pursuant to sections 105(a), 363, 1107, and 1108 of title 11 of the United States Code (the “Bankruptcy Code”) and rules 6003 and 6004 of the Federal Rules of Bankruptcy Procedure (the “Bankruptcy Rules”) (i) authorizing the Debtor to (a) maintain existing insurance policies and pay all obligations arising therefrom, and (b) renew, revise, extend, supplement, change, or enter into new insurance policies as needed in its business judgment; and (ii) granting certain related relief. In support of this Motion, the Debtor respectfully states as follows:

JURISDICTION AND VENUE

1. The Court has jurisdiction over the Debtor, its estate, and this matter pursuant to 28 U.S.C. §§ 157 and 1334, and the General Order of Reference from the United States District Court for the Western District of Wisconsin, dated June 12, 1984. This matter is a core proceeding within the meaning of 28 U.S.C. § 157(b)(2).

2. Venue in this Court is proper pursuant to 28 U.S.C. §§ 1408 and 1409.

¹ The debtor in this chapter 11 case, along with the last four (4) digits of its taxpayer identification number, is: Capitol Lakes, Inc. (2320). The mailing address of the debtor, solely for purposes of notices and communications, is: 333 W. Main Street, Madison, WI 53703.

3. The statutory bases for the relief requested herein are sections 105(a), 363, 1107 and 1108 of the Bankruptcy Code, and Bankruptcy Rules 6003 and 6004.

BACKGROUND

4. On January 20, 2016 (the "Petition Date"), the Debtor commenced this case by filing a voluntary petition for relief under chapter 11 of the Bankruptcy Code.

5. The Debtor remains in possession of its assets and continues to operate and manage its business as a debtor in possession pursuant to Bankruptcy Code sections 1107 and 1108.

6. No trustee, examiner, or committee of creditors has been appointed in this case.

7. The factual background regarding the Debtor, including its current and historical business operations and the events precipitating this chapter 11 filing, is set forth in detail in the *Declaration of Tim Conroy in Support of Chapter 11 Petition and First Day Motions of Capitol Lakes, Inc.* (the "Conroy Declaration"), filed contemporaneously herewith and incorporated herein by reference.

The Debtor's Insurance Policies

8. As more fully set forth in the Conroy Declaration, the Debtor contracts with Pacific Retirement Services, Inc., an Oregon nonprofit corporation ("PRS"), as its sole member, to provide support, management, and other services to the Debtor.

9. Pursuant to that certain Affiliate Management and Support Services Agreement, dated as of March 18, 2014 (as amended, the "PRS Management Agreement"), subject to certain conditions, PRS is required to obtain and keep in full force and effect, "property and liability insurance policies, including general liability, professional liability, directors and officers liability, employment practices liability, workers' compensation, employers liability, employee benefits liability, and automobile liability coverage, including non-owned and hired automobile liability coverage, and any other insurance coverage as determined by PRS from time to time."

10. Accordingly, PRS arranges for the Debtor's coverage under several insurance policies and surety contracts (the "Insurance Policies"). The Insurance Policies are administered by several third-party insurance carriers (collectively, the "Insurance Policy Carriers") and collectively provide coverage for, among other things, (a) general liability, (b) professional liability, (b) automobile liability, (c) storage tank liability, (d) property, (e) crime, (f) director and officer liability, (g) workers' compensation, and (f) employer's liability. PRS also arranges for the Debtor to maintain contracts with sureties (the "Surety Parties," and together with the Insurance Policy Carriers, the "Insurance Carriers") to post patient trust bonds and unemployment surety bonds on behalf of the Debtor, as required by applicable law. A schedule of the Insurance Policies (which include the surety agreements), (including the Insurance Carrier, the named insured, and the payor) is attached hereto as Exhibit A and incorporated herein by reference.² Continuation of the Insurance Policies is essential to the preservation of the value of the Debtor's business, properties, and assets. Moreover, in many cases, the coverage provided by the Insurance Policies is required by the regulations, laws, and contracts that govern the Debtor's business activities.

11. The Debtor makes various payments to the Insurance Carriers as payment for the Insurance Policies and to PRS as reimbursement for the Insurance Policy costs paid by PRS (the "Premium Payments"), which are set forth in detail (including the due date and amount of the next Premium Payment) on Exhibit A.

² Concurrently with this Motion, the Debtor has filed a motion for an order authorizing payment of prepetition (i) wages, salaries and other compensation of employees, (ii) employee medical and similar benefits, (iii) reimbursable employee expenses, and (iv) other miscellaneous employee expenses and benefits (the "Wage Motion"). One or more of the insurance policies discussed in this Motion are provided for the benefit of employees of the Debtor, and are therefore addressed concurrently in the Wage Motion.

RELIEF REQUESTED

12. By this Motion, the Debtor requests an order (i) authorizing the Debtor to (a) maintain the existing Insurance Policies and pay all obligations arising therefrom, including any Premium Payments, and (b) renew, revise, extend, supplement, change, or enter into new insurance policies as needed in its business judgment; (ii) authorizing and directing banks and other financial institutions to receive, process, honor, and pay all checks issued and electronic payment requests made related to the foregoing; and (iii) granting such other and further relief as may be appropriate.

BASIS FOR RELIEF

A. Maintaining the Insurance Policies and Paying Obligations Related Thereto is Required by the Bankruptcy Code and the U.S. Trustee

13. The Insurance Policies are essential to preserve the value of the Debtor's business, properties, and assets. Not only are some of the Insurance Policies required by the various regulations, laws, and contracts that govern the Debtor's commercial activities, but section 1112(b)(4)(C) of the Bankruptcy Code provides that "failure to maintain appropriate insurance that poses a risk to the estate or to the public," is "cause" for mandatory conversion or dismissal of a chapter 11 case. 11 U.S.C. § 1112(b)(4)(C). Moreover, the *Chapter 11 Operating Instructions and Reporting Requirements* issued by the U.S. Trustee (the "UST Guidelines") also require a debtor to maintain insurance coverage throughout its chapter 11 case.

14. Payment of the Premium Payments owing in connection with the Insurance Policies and the renewal, revision, extension, supplementation, or change of existing Insurance Policies and entering into new insurance policies as needed in the Debtor's business judgment are necessary to protect and safeguard the Debtor's ongoing operations and ensure compliance with the UST Guidelines.

B. Payment of the Insurance Obligations Are Permitted as Ordinary Course Expenses

15. Section 105(a) of the Bankruptcy Code provides, in pertinent part, that “[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title.” 11 U.S.C. § 105(a).

16. Section 363(c) of the Bankruptcy Code provides, in pertinent part:

If the business of the debtor is authorized to be operated under section . . . 1108 . . . of this title and unless the court orders otherwise, the trustee may enter into transactions, including the sale or lease of property of the estate, in the ordinary course of business, without notice or a hearing, and may use property of the estate in the ordinary course of business without notice or a hearing.

11 U.S.C. § 363(c). The insurance obligations that the Debtor seeks to pay by this Motion are clearly within the definition of payments made in the ordinary course of business contemplated by section 363(c).

C. Payment of the Insurance Obligations is Warranted Even if not Considered Ordinary Course Expenses

17. To the extent that the Court determines that the payment of the Insurance Premiums is not within the scope of the ordinary course of business of the Debtor, such payments are permitted under sections 105(a), 363(b), 1107(a), and 1108 of the Bankruptcy Code.

18. Pursuant to sections 1107(a) and 1108 of the Bankruptcy Code, “a debtor in possession . . . is a fiduciary holding the bankruptcy estate and operating the business for the benefit of its creditors and (if the value justifies) equity owners.” In re CoServ, L.L.C., 273 B.R. 487, 497 (Bankr. N.D. Tex. 2002). Inherent in the fiduciary duties of a debtor in possession is the obligation to “protect and preserve the estate, including an operating business’s going-concern value,” which, in certain instances, can be fulfilled “only . . . by the preplan satisfaction of a prepetition claim.” Id. Indeed, the court in CoServ specifically noted that the preplan satisfaction of prepetition claims

would be a valid exercise of the debtor's fiduciary duty when the payment "is the only means to effect a substantial enhancement of the estate . . ." Id.

19. Consistent with a debtor's fiduciary duties, where there is a sound business purpose for the payment of prepetition obligations and where the debtor is able to "articulate some business justification, other than the mere appeasement of major creditors," courts have authorized debtors to make such payments under section 363(b) of the Bankruptcy Code. See, e.g., Institutional Creditors of Cont'l Air Lines, Inc. v. Cont'l Air Lines, Inc. (In re Cont'l Air Lines, Inc.), 780 F.2d 1223, 1226 (5th Cir. 1986) ("[T]here must be some articulated business justification for using, selling, or leasing the property outside the ordinary course of business."); In re Ionosphere Clubs, Inc., 98 B.R. 174, 175 (Bankr. S.D.N.Y. 1989) (stating that a sound business justification existed to pay prepetition wages). Once a debtor articulates a valid business justification for a particular form of relief, that relief "should be approved by the court unless it is shown to be 'so manifestly unreasonable that it could not be based upon sound business judgment, but only on bad faith, whim, or caprice.'" In re Aerovox, Inc., 269 B.R. 74, 80 (Bankr. D. Mass. 2001) (quoting In re Logical Software, Inc., 66 B.R. 683, 686 (Bankr. D. Mass. 1986)).

20. Failure to pay amounts related to the Insurance Policies as they come due may harm the Debtor's estate in several ways. Specifically, there is the potential for insurance coverage to be terminated.³ Such termination would likely place additional strain on the Debtor's relationships with key employees who benefit from the Debtor's insurance coverage, and would also eviscerate the Debtor's ability to prevent loss in value caused by casualty, natural disaster, or another unforeseen event. The continuation of the Debtor's Insurance Policies is especially important in the healthcare sector. In the event of termination of insurance coverage, the Debtor

³ With respect to policies where the Debtor is not responsible for paying the Insurance Carriers directly, if the Debtor does not reimburse PRS, PRS can potentially terminate insurance coverage.

would need to obtain replacement insurance, likely at a higher price. The cancellation of key Insurance Policies would threaten to halt the Debtor's operations altogether. In light of the importance of maintaining insurance coverage with respect to its business activities, the Debtor submits it is in the best interest of its estate to maintain the Insurance Policies and to pay related amounts as described herein under the Bankruptcy Code. In addition, to the extent applicable, the Debtor should be authorized to renew, revise, extend, supplement, or change existing Insurance Policies, or enter into new insurance policies as needed in the Debtor's business judgment, to ensure that appropriate insurance coverage is maintained during this chapter 11 case and that the Debtor is fulfilling its fiduciary duties.

21. Courts in this jurisdiction and others have approved relief similar to the relief requested in this Motion. See, e.g., In re ITR Concession Co., Case No. 14-34284 (Bankr. N.D. Ill. Sept. 23, 2014) (authorizing debtors to pay prepetition insurance premiums); In re Hi-Way Equipment Company, LLC, Case No. 13-41498 (RFN) (Bankr. N.D. Tex. Apr. 4, 2013) (authorizing debtors to continue prepetition insurance coverage and maintain financing of insurance premiums); In re Vertis Holdings, Inc., Case No. 12-12821 (CSS) (Bankr. D. Del. Nov. 1, 2012) (authorizing debtors to maintain, extend, and renew existing insurance programs and pay all insurance obligations including premiums, deductibles, retrospective adjustments, expenses, taxes, fees, etc.); In re Bicent Holdings LLC, Case No. 12-11304 (KG) (Bankr. D. Del. Apr. 24, 2012) (same); In re Airadigm Commc'ns, Inc., Case No. 06-10930 (RDM) (Bankr. W.D. Wis. May 10, 2006) (authorizing debtor to maintain existing insurance policies and make payments related thereto).

D. Cause Exists to Authorize and Direct the Debtor's Financial Institutions to Honor Checks and Electronic Fund Transfers

22. The Debtor also requests that all applicable banks and other financial institutions be authorized to receive, process, honor, and pay all checks presented for payment, and to honor all electronic payment requests made by the Debtor related to the obligations described herein, whether such checks were presented or electronic requests are submitted prior to, on, or after the Petition Date.⁴ The Debtor further requests that all such banks and financial institutions be authorized to rely on the Debtor's designation of any particular check or electronic payment request as approved pursuant to this Motion. The Debtor represents that it has sufficient availability of funds to pay the amounts described herein by virtue of funds to be made available under the Debtor's proposed access to cash collateral and the budget contemplated thereby. Also, under the Debtor's existing cash management system, the Debtor represents that checks or wire transfer requests can be readily identified as relating to an authorized payment made with respect to the Insurance Policies. Accordingly, the Debtor believes that checks or wire transfer requests, other than those relating to authorized payments, will not be honored inadvertently and that all applicable financial institutions should be authorized and directed, when requested by the Debtor, to receive, process, honor, and pay any and all checks or wire transfer requests with respect to the Insurance Policies.

E. The Requirements of Bankruptcy Rule 6003 are Satisfied.

23. As described above, the Debtor seeks authority to pay the Insurance Premiums that will become due and owing to the Insurance Carriers and PRS as such amounts become due in the ordinary course as specified on Exhibit A. Under Bankruptcy Rule 6003, the Court may authorize

⁴ Concurrently with this Motion, the Debtor has filed a motion for an order authorizing the Debtor to (i) continue to use its existing cash management system, (ii) maintain its existing bank accounts, (iii) continue to use its existing business forms, and (iv) maintain its existing investment practices.

the Debtor to satisfy the amounts related to the Insurance Premiums within the 21-day period after the Petition Date because such relief is necessary to avoid immediate and irreparable harm to the Debtor's estate. See Fed. R. Bankr. P. 6003(b).

24. The Debtor submits that for the reasons already set forth herein, the relief requested in this Motion is necessary to avoid immediate and irreparable harm. As discussed above, if the Debtor does not obtain the relief requested in the Order, it would suffer immediate and irreparable harm because (a) the Debtor would not be able to continue its operations if an Insurance Policy was terminated due to nonpayment of premiums; (b) the Debtor would be at severe risk of jeopardizing its assets if they did not have adequate coverage; and (c) the Debtor's assets would be harmed by the subsequent need to obtain replacement insurance at a likely higher price. Accordingly, the Debtor respectfully submits that it has satisfied the "immediate and irreparable harm" standard of Bankruptcy Rule 6003 and seeks authority to pay the amounts related to the Insurance Policies pursuant to the Order.

F. Waiver of Bankruptcy Rules Regarding Notice and Stay

25. To implement the foregoing successfully, the Debtor seeks a waiver of the notice requirements under Bankruptcy Rule 6004(a) and any stay of an order granting the relief requested herein pursuant to Bankruptcy Rules 6004(h), 7062, 9014, or otherwise. Pursuant to Bankruptcy Rule 6004(h), "[an] order authorizing the use, sale, or lease of property other than cash collateral is stayed until the expiration of 14 days after entry of the order, unless the court orders otherwise." Fed. R. Bankr. P. 6004(h). As explained above, the immediate payment of all amounts identified in this Motion is essential to prevent potentially irreparable damage to the Debtor's operations and value. Accordingly, the Debtor submits that cause exists to justify a waiver of the 14-day stay imposed by Bankruptcy Rule 6004(h), if it even applies.

RESERVATION OF RIGHTS

26. Nothing contained herein is intended or should be construed as an admission as to the validity of any claim against the Debtor, a waiver of the Debtor's rights to dispute any claim, or an approval or assumption of any agreement, contract, or lease under section 365 of the Bankruptcy Code. Additionally, nothing contained herein is intended or should be construed as an admission as to the validity of any claim against the Debtor. The Debtor expressly reserves its rights to contest any claim or billing dispute. Likewise, if this Court grants the relief sought herein, any payment made pursuant to the Court's order is not intended and should not be construed as an admission as to the validity of any claim or a waiver of the Debtor's rights to subsequently dispute such claim.

27. To the extent that any of the Insurance Policies or the PRS Management Agreement may be deemed executory contracts within the meaning of 11 U.S.C. § 365, the Debtor does not at this time seek authority to assume the contracts. The Debtor simply requests authorization to continue to pay the obligations related to the Insurance Policies as necessary to keep the respective Insurance Policies in force.

NOTICE

28. Notice of this Motion has been provided to (a) the Office of the United States Trustee for the Western District of Wisconsin; (b) the Office of the Attorney General of the State of Wisconsin; (c) the Wisconsin Office of the Commissioner of Insurance; (d) each of the Debtor's twenty (20) largest unsecured creditors; (e) U.S. Bank, N.A. as trustee; (f) counsel to Santander Bank, N.A.; (g) counsel to KBC Bank N.V.; (h) the Insurance Carriers; and (i) the Internal Revenue Service and state taxing authorities. The Debtor submits that, in light of the nature of the relief requested, no other or further notice is necessary or required.

CONCLUSION

WHEREFORE, for the reasons set forth herein, the Debtor respectfully requests that the Court enter an Order (i) authorizing the Debtor to (a) maintain the existing Insurance Policies and pay all obligations arising thereunder, including any Insurance Premium payments, and (b) renew, revise, extend, supplement, change, or enter into new insurance policies as needed in its business judgment; (ii) authorizing and directing banks and other financial institutions to receive, process, honor, and pay all checks issued and electronic payment requests made related to the foregoing; and (iii) granting such other and further relief as may be appropriate.

Dated: January 21, 2016

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Proposed Counsel for the Debtor and Debtor in Possession

Exhibit A

Insurance Policies

Insurance Policies

COVERAGE TYPE	NAMED INSURED	CARRIER	POLICY NUMBER	PREMIUM PAID BY CAPITOL LAKES OR REIMBURSEMENT TO PRS	PAYOR (PRS OR CAPITOL LAKES)
General/Professional Liability—Primary and Excess Coverage	Capitol Lakes, Inc., is named insured to PRS' master policy	Caring Communities Reciprocal Risk Retention Group	CCRRRG-0015-16	<ul style="list-style-type: none"> Annual Premium: \$90,035.24 (paid by PRS in four quarterly premium payments) Next payment due: 4/1/2016 Term: 1/1/2016 to 1/1/2017 	Paid by PRS, Capitol Lakes reimburses PRS for full annual premium in January, and PRS pays out quarterly installments when due
Automobile Liability	Capitol Lakes, Inc., is named insured to PRS' master policy	Church Mutual Insurance Company	03033709728 246	<ul style="list-style-type: none"> Annual Premium: \$5,927 (paid annually) Next payment due: 3/1/2016 Term: 3/1/2015 to 3/1/2016 	Paid by Capitol Lakes directly
Automobile Excess Liability	Capitol Lakes, Inc., is named insured to PRS' master policy	Caring Communities Reciprocal Risk Retention Group	CCRRRG-0015-16	<ul style="list-style-type: none"> Premium included in General/Professional Liability premium above Next payment due: 4/1/2016 Term: 1/1/2016 to 1/1/2017 	
Storage Tank Liability	Capitol Lakes, Inc.	Ace American Insurance Company	G24666086	<ul style="list-style-type: none"> Annual Premium: \$350.00 (paid) Next payment due: 4/23/2016 Term: 4/23/2015 to 4/23/2016 	Paid by PRS, reimbursed by Capitol Lakes
Property Liability	Capitol Lakes, Inc., is named insured to PRS' master policy	Travelers Property Casualty Company of America	KTJCMB2305 N08715	<ul style="list-style-type: none"> 12-Month Premium \$79,504.02 (paid annually—paid); 6-Month Premium: \$39,668.50 (due 3/1/2016—not yet paid) Term: 3/1/2015 to 9/1/2016 (18-month policy period) 	Paid by Capitol Lakes directly
Crime	Capitol Lakes, Inc., is named insured to PRS' master policy	Travelers Property Casualty Company of America	105699312	<ul style="list-style-type: none"> Annual Premium: \$0 Next payment due: 10/1/2016 (premium TBD) Term: 10/1/2015 to 10/1/2016 	Historically paid by PRS (going forward, to be reimbursed by Capitol Lakes 10/1/2016)

COVERAGE TYPE	NAMED INSURED	CARRIER	POLICY NUMBER	PREMIUM PAID BY CAPITOL LAKES OR REIMBURSEMENT TO PRS	PAYOR (PRS OR CAPITOL LAKES)
Employment Practices and Director and Officer Liability/Excess Coverage/ Director and Officer Liability—Excess Side A Coverage	Capitol Lakes, Inc., is named insured to PRS' master policy	Wesco Insurance Company/Westchester Fire Insurance Company/RSUI Indemnity Company	WIC—EUW1082284 02/WFIC—G2434334000 4/NHS665596	<ul style="list-style-type: none"> Annual Premium: \$27,891.75 Next payment due: 12/1/2016 Term: 12/1/2015 to 12/1/2016 	Paid by Capitol Lakes directly
Workers' Compensation	Capitol Lakes, Inc., is named insured to PRS' master policy	Alaska National Insurance Company/Old Republic Insurance Company	Alaska National—15JWS09338	<ul style="list-style-type: none"> \$40,253 Annual Deposit and then monthly premium of approximately \$21,500 per month Next payment due: 2/5/2016 Term: 10/1/2015 to 10/1/2016 	Deposit paid by PRS, reimbursed by Capitol Lakes; monthly premium paid directly by Capitol Lakes
Employer's Liability	Capitol Lakes, Inc., is named insured to PRS' master policy	Caring Communities Reciprocal Risk Retention Group	CCRRRG-0015-16	<ul style="list-style-type: none"> Included in Annual General/Professional Liability premium above Next payment due: 4/1/2016 Term: 1/1/2016 to 1/1/2017 	
Patient Trust Surety Bond—Terraces	Capitol Lakes, Inc.	North American Specialty Insurance Co.	2179101	<ul style="list-style-type: none"> Annual Premium: \$106.00 Next payment due: 3/2016 Term: 3/26/2015 to 3/26/2016 	Paid by Capitol Lakes directly
Patient Trust Surety Bond—Health Center	Capitol Lakes, Inc.	North American Specialty Insurance Co.	2179102	<ul style="list-style-type: none"> Annual Premium: \$122.00 Next payment due: 3/2016 Term: 3/26/2015 to 3/26/2016 	Paid by Capitol Lakes directly
Unemployment Surety Bond	Capitol Lakes, Inc.	Hartford Fire Insurance Company	52BSBFG2612	<ul style="list-style-type: none"> Original Premium: \$18,496 (paid in 7/2014) Next payment due: Original Premium paid until 12/31/2019; however, WI Unemployment Dept. requires annual one-year continuation extensions payable annually of approximately \$4,352-last payment 7/2015 Term: 1/1/14 to 12/31/2019 	Paid by Capitol Lakes directly