IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re	:	Chapter 11
	:	
NEWBURY COMMON ASSOCIATES, LLC, *et al.*,	:	Case No. 15-12507 (LSS)
	:	
	:	Jointly Administered
	:	
Debtors.	:	**Objection Deadline: TBD**
	:	**Hearing Date Requested: Prompt**

UNITED STATES TRUSTEE'S MOTION FOR AN ORDER DIRECTING THE APPOINTMENT OF AN EXAMINER

Andrew R. Vara, the Acting United States Trustee for Region 3 (the "U.S. Trustee"), through his counsel, moves the Court for entry of an order pursuant to 11 U.S.C. § 1104(c)(1) directing the appointment of an examiner, and respectfully represents as follows:

I. PRELIMINARY STATEMENT

1. The immediate appointment of an examiner under § 1104(c)(1) is required so that an independent and disinterested person can investigate extensive irregularities in the management of the Debtors' affairs, including purported prepetition wrongdoing, misconduct, and mismanagement, as well as inter-debtor claims and claims that may exist against current or former insiders. The facts and circumstances that support the appointment of an examiner include:

- the prepetition failure of the debtors and their affiliates to maintain proper business records and cash controls, including a disregard of corporate formalities and a failure to maintain the corporate separateness of the various entities;

- the purported mishandling of investor funds prepetition;

- the alleged forging by one insider of other insiders' signatures on financial documents, including personal guarantees, prior to the commencement of these cases;

- the post-petition filing of deficient monthly financial reports;

• the post-petition filing of schedules with multiple disclaimers that call their reliability into question;

• the debtors' post-petition failure to open and maintain appropriate post-petition bank accounts for the various estates in compliance with 11 U.S.C. § 345, and the commingling of estate and non-estate funds, including funds that may be cash collateral of creditors of non-debtors;

• inadequate information regarding the adverse interests of the various bankruptcy estates, posing conflicts among the various debtors and non-debtors, with corresponding problems for the fulfillment of fiduciary responsibilities by estate representatives and professionals.

Debtors' professionals acknowledge many of these facts and circumstances, and have provided extensive information requested by the U.S. Trustee. Irrespective of such cooperation, however, the divergent interests of the various estates, the extreme financial irregularities that have taken place, and the extensive conflicts among the various debtors and their affiliates and insiders, all make the appointment of an independent and disinterested examiner necessary and in the best interests of creditors, any equity security holders and the estates.

II. JURISDICTION

2. The Court has jurisdiction to hear this Objection.

3. Pursuant to 28 U.S.C. § 586, the U.S. Trustee is generally charged with overseeing the administration of chapter 11 cases filed in this District. 28 U.S.C. § 586. Under Section 586 and Section 307 of the Bankruptcy Code, Congress charged the U.S. Trustee with broad responsibilities in chapter 11 cases and the standing to rise and be heard on any issue in any case or proceeding. 11 U.S.C. § 307; *see also United States Trustee v. Columbia Gas Sys., Inc.* (*In re Columbia Gas Sys., Inc.*), 33 F.3d 294, 295-96 (3d Cir. 1994) (the U.S. Trustee has "public interest standing" under 11 U.S.C. § 307, which goes beyond mere pecuniary interest); *Morgenstern v. Revco D.S., Inc.* (*In re Revco D.S., Inc.*), 898 F.2d 498, 500 (6th Cir. 1990) (describing the United States Trustee as a "watchdog").

4. The U.S. Trustee has statutory authority to seek the appointment of an examiner under 11 U.S.C. § 1104(c).

III. BACKGROUND

5. On December 13, 2015 (the "Petition Date"), Newbury Common Associates, LLC and thirteen related affiliates commenced these voluntary chapter 11 cases (D.E. 1). Tag Forest, LLC filed on December 14, 2015. Together, these fifteen related affiliates will be referred to as the "Original Debtors." These fifteen petitions (the "Petitions") were filed with the minimum necessary pleadings to effectuate the filings, a so-called bare bones filing. On February 3, 2016, another ten related affiliates filed voluntary petitions for relief under chapter 11 of the Bankruptcy Code and will be referred to as the "Additional Debtors." Collectively, all of the entities which have filed petitions shall be referred to as "Debtors."

6. The Original Debtors and their Additional Debtor affiliates are a part of an enterprise that owns commercial, hospitality and residential properties in Stamford, Connecticut (Declaration of Marc Beilinson in Support of Chapter 11 Petitions, D.E. 5 at ¶ 6, "Beilinson Declaration"). Some of the Original Debtors are holding companies owning equity in Additional Debtor subsidiaries which in turn own the various properties. *Id.* The Petitions disclose asset values of $100 to 500 million and liabilities of $100 to 500 million. *See, e.g.*, D.E. 1. Some of the Debtors are entities which have managed one or more of the remaining entities, or have served primarily as conduits for the transfer of cash between the various entities. However, while some of the Debtors may hold interests in other debtor affiliates, there is no ultimate parent entity that owns or controls all of the debtors. As near as the U.S. Trustee has been able to ascertain, the Debtors have not, for example, filed consolidated tax returns.

7. The Debtors represent that Debtor Seaboard Realty, LLC serves as the managing

member of most of the Debtors (D.E. 5 at ¶6). Seaboard Realty, LLC is owned 50% by John DiMenna ("DiMenna"), 25% by Thomas Kelly ("Kelly") and 25% by William Merritt ("Merritt") (D.E. 5 at ¶6). However, the Debtors' Lists of Debtors' Equity Security Holders in Accordance With Bankruptcy Rule 1007 filed on December 21, 2015 (D.E. 26), discloses that Seaboard Realty, LLC, and 300 Main Management, Inc. are owned 50% by Kelly and 50% by Merritt. DiMenna is not identified as an interest holder of either entity. In addition, there are two non-debtor entities owned and controlled by DiMenna, Seaboard Property Management, Inc. and Seaboard Consolidated, LLC into which there has been extensive comingling of cash.

8. Substantially all of the real property owned by the various debtors (with the exception of a Courtyard Hotel (managed by an unaffiliated third party)) is managed by Seaboard Property Management, Inc. ("SPM"), a non-debtor affiliate, which is a property management company owned by DiMenna. *Id.* at ¶ 7. SPM has been responsible for the day-to-day operations of all the real property directly or indirectly owned by the Debtors. *Id.* It was the understanding of the U.S. Trustee in the immediate post-petition period that Debtors were continuing to use the services and accounts of SPM with the expectation that SPM will pay its employees. See paragraphs 18 and 19 of the concurrently filed Declaration of Karen E. Starr, Bankruptcy Analyst, in Support of the United States Trustee's Motion for an Order Directing the Appointment of an Examiner ("Starr Declaration"). Seaboard Property Management, Inc., is not a debtor.

9. On November 20, 2015, Kelly and Merritt allegedly became aware that certain Original Debtors and Additional Debtor affiliates were having difficulty meeting their financial obligations. *Id.* at ¶ 9. Kelly and Merritt concluded that DiMenna was misrepresenting the finances of the Original Debtors and Additional Debtor affiliates. *Id.* At an evidentiary hearing

held before the Court on January 28, 2016 in two adversary proceedings filed by the Original Debtors seeking to impose a litigation stay in favor of, among others, Kelly and Merritt ("Evidentiary Hearing"), the Court heard substantial testimony by members of current management regarding the lack of cash controls, oversight and records. The Chief Restructuring Officer testified that funds of Debtors have been commingled with the funds of non-debtors post-petition and that funds representing the cash collateral of one or more secured creditors had not been segregated in accordance with the Bankruptcy Code.

10. At the Evidentiary Hearing, Kelly and Merritt testified that they became concerned about the affairs of the Debtors when checks distributed to them in connection with the sale of substantially all assets of Tag Forest, LLC bounced (D.E. 152 filed February 1, 2016, Transcript 141:9-141:17; 208:21-209:1, hereinafter "Transcript" or "TR").[1] At the Evidentiary Hearing, each of Kelly and Merritt testified that although they were managing members of Seaboard Realty, they allowed DiMenna to operate the day to day affairs of the Debtors with minimal oversight. Kelly testified that he would attend a bi-monthly meeting where he would review an agenda and discuss things, would receive a P&L when he asked for one, but: "I don't know if they were correct, or incorrect, or what, you know, I don't know that much." (TR 126:9-19). He also testified that there were no audited financial statements (TR at 134:22-135:5). Merritt testified that prior to December 2, 2015, he did not participate in the day to day activities of the Debtors or related entities (TR at 205:4-9).

11. At the Evidentiary Hearing, each of Kelly and Merritt testified to DiMenna's allegedly having obtained multiple secured loans of millions of dollars over an extended period of time without proper authority and by allegedly forging Kelly's and Merritt's signatures (TR

[1] A copy of the Transcript is attached hereto as Exhibit "A".

129:6-130:11; 198:22-200:20). At the Evidentiary Hearing, counsel for the Debtors acknowledged to the Court that the Debtors received and used the funds from the alleged fraudulently obtained loans (TR 237:23-25). Merritt testified that he should never have to answer in court or to an investigator about his involvement and any responsibility he may have in connection with the Debtors (TR 202:22-203:4).

12. On December 2, 2015, DiMenna voluntarily resigned from his managing position and duties.

13. Kelly testified that in late November or early December of 2015, he transferred an investment account in his sole name with a balance in excess of $1 million to an account in his wife's sole name (TR 166:14-167:17).

14. Kelly and Merritt hired Anchin, Block & Anchin, LLP as forensic accountants sometime between November 20, 2015 and the Petition Date. D.E. 5 at ¶ 10.

15. On or about December 10, 2015, Kelly and Merritt hired Marc Beilinson as Chief Restructuring Officer ("Beilinson" or "CRO") for the Original Debtors and Additional Debtors and to conduct an investigation into the Debtors' assets and liabilities. *Id.* In a status report filed with the Court on January 12, 2016 (D.E. 47, "Status Report"), Beilinson stated: "Prior to the Petition Date there was limited internal and external financial and accounting reporting. There were insufficient internal controls, financial reporting to management, and accounting process in place, and the Debtors had minimal formal or systematic processes for maintaining books and records." (D.E. 47 at ¶ 16).

16. At the Evidentiary Hearing, Beilinson gave the following testimony:

> "Well, I mean, when I went in, the first thing you look for is management reporting, which is typical in virtually in company of this size (sic). You look at what controls they have over their financial processes, and what I found was shocking to me. It was something that I hadn't seen in 35 years. There

> was no management booklet, which would contain the normal things that you would expect to see like profit-and-loss statements, budgets, P&Ls, reports, you know, with regard to leasing activity, et cetera. And it was clear that there wasn't sufficient- well, they were completely lacking in financial controls. And as I investigated it further, it was clear that money was being comingled and used for whatever purpose Mr. DiMenna decided to use it for, whether appropriate or not." (TR 18:21-19:9).

Beilinson provided a preliminary conclusion: "And the preliminary conclusion, just looking at 2015, what we have today, is that they didn't and, you know, the money wasn't coming in from the properties to pay for distributions. It must have come from some other sources, whether that's mezz debt or investors." (TR 22:13-17).

17. As of February 4, 2016 no Debtor has opened a debtor-in-possession bank account. In the Status Report, Beilinson, stated: "…all of the cash to operate the enterprise is currently maintained in Bank Accounts with Newbury Common Member Associates, LLC, One Atlantic Investor Associates, LLC or Century Plaza Investor Associates, LLC." These entities subsequently became debtors on February 3, 2016. Beilinson testified that post-petition he has deposited the funds of the various Debtors into one consolidated account but could not remember the name of the account (TR 88:1-88:17). He testified revenues of the entities are being used to pay the expenses of Debtors and non-Debtors (TR 108:1-108:17). In response to questioning by the Court, Beilinson stated that one reason he had not segregated cash post-petitions was: "…because at one point in time, there wasn't sufficient cash in some of the properties to pay normal operating expenses." (TR 109:7-9).

18. The Debtors have represented that Debtor Tag Forest, LLC sold substantially all its assets prior to the Petition Date. The Debtors do not specify when Tag Forest, LLC sold its assets. *See id.* at 3 n.2. The Debtors initially represented to the U.S. Trustee there were no bank accounts. On December 21, 2015, however, the Debtors disclosed an account for Tag Forest

with approximately $226,000 on deposit. *See* Starr Declaration at ¶ 12-13. The Debtors provided the U.S. Trustee with an alleged closing statement dated December 3, 2015. The closing statement is not a HUD-1 form. Debtor Tag Forest, LLC filed its Schedules of Assets and Liabilities (D.E. 76, "Tag Forest Schedules") and Statement of Financial Affairs (D.E. 77, "Tag Forest Statements") on January 12, 2016. The Tag Forest Statements do not disclose the prepetition sale of assets. The Tag Forest Statements disclose that $195,000 was paid to Anchin, Block and Anchin and to Beilinson Advisory Group on December 14, 2015. The Tag Forest Schedules disclose $1,324.08 on hand as of the filing.

19. The Seaboard Realty, LLC Statement of Affairs (D.E. 51, "Seaboard Statement of Affairs") reports no income for 2015 in response to Question 1 but reports insider distributions aggregating approximately $1 million in the year preceding the filing at Question 4. Question 1 of the Seaboard Realty Statement reports negative gross income of $2,070,502 for 2014 and negative gross income of $1,544,620 for 2013.[2]

20. On December 17, 2015, Seaboard Realty appointed Howard Altschul of Waterbridge Advisers to act as an Independent Managing Member for a monthly fee of $17,500 and a minimum guaranteed fee of $210,000. See the Notice of Appointment of Independent Managing Member (D.E. 17). At the Evidentiary Hearing, Kelly testified that he and Merritt continue to serve as Managing Members of Seaboard Realty, LLC. Kelly also testified that if there is a dispute between him, Merritt and Altschul, Altschul's decision would control although there is no written document evidencing this apparent abdication of responsibility (TR 149:6-

[2] On page 7 of the Global Notes and Statements of Limitations, Methodology, and Disclaimer Regarding the Original Debtors' Schedules of Assets and Liabilities and Statements of Financial Affairs that were filed on January 12, 2016 (D.E. 48-77*)*, the Original Debtors state: Schedule E/F – Creditors Who Have Unsecured Claims – Intercompany payables are not included on Schedule E/F. SOFAs Question 4 – Payments or Other Transfers of Property Made Within 1 Year Before Filing This Case That Benefitted Any Insider – SOFA question 4 does not include any intercompany transfers. The disclosures that have been made are not complete.

149:17). Altschul did not testify at the Evidentiary Hearing.

21. As of February 4, 2016 the Debtors have still not opened a single DIP bank account.[3] *See* Starr Declaration at ¶ 11. The Initial Monthly Operating Report tardily filed with the Court on January 29, 2016 (D.E. 135, "IMOR") names as the primary insured Seaboard Property Management, Inc., a non-debtor entity owned and controlled by DiMenna. Debtors and non-debtors are included in the Insurance Certificate. On January 29, 2016, the Debtor filed its first monthly operating reports for the Debtors. The reports show little to no financial activity and do not appear to have accounted for the post-petition handling of estate funds with the funds of non-debtors as was admitted at the Evidentiary Hearing.

22. Beilinson indicated at an Initial Debtor Interview conducted by the U.S. Trustee during the first days of the case that Seaboard Property Management, Inc., a non-debtor owned by DiMenna, was invoicing the Debtors for its services and Beilinson was paying the invoices with the expectation that SPM would pay the employees performing services for the debtors. Starr Declaration at ¶ 19. In the Status Report, Beilinson reported that he was not using an account for Seaboard Property Management, but the accounts of three non-debtors (which subsequently became debtors on February 3, 2016), through which he has reportedly been tracking disbursements. See paragraph 17 above.

IV. ARGUMENT

23. Pursuant to 11 U.S.C. § 1104(c), the court shall order the appointment of an examiner:

[3] On December 21, 2015, the Debtors disclosed to the U.S. Trustee the existence of 35 bank accounts with a balance on hand of not less than $731,000 as of December 10, 2015. Of those accounts at the time, 13 were Debtors' accounts holding approximately $276,000. It is impossible from those documents to determine how the money flows between the entities. *See* Starr Declaration at ¶ 13.

> to conduct such an investigation of the debtor as is appropriate, including an investigation of any allegations of fraud, dishonesty, incompetence, misconduct, mismanagement, or irregularity in the management of the affairs of the debtor of or by current or former management of the debtor, if—
> (1) such appointment is in the interests of creditors, any equity security holders, and other interests of the estate; or
> (2) the debtor's fixed, liquidated, unsecured debts, other than debts for goods, services, or taxes, or owing to an insider, exceed $5,000,000.

11 U.S.C. § 1104(c)(2).

24. The moving party has the burden to demonstrate that an examiner should be appointed. *See In re Dewey & LeBoeuf LLP*, 478 B.R. 627, 636 (Bankr. S.D.N.Y. 2012).

25. The language in section 1104(c)(1) of the Bankruptcy Code calling for the appointment of an examiner if "such appointment is in the interest of creditors, any equity security holders, and other interests of the estate" reflects the language contained in section 1104(a)(2) with regard to the appointment of a trustee. An examiner "typically investigate[s] the debtor's business . . . , but do[es] not replace the debtor in possession in handling the day-to-day affairs of the business." *In re Gliatech, Inc., et al.*, 305 B.R. 832, 835 (Bankr. N.D. Ohio 2004), quoting *United States v. Schilling* (*In re Big Rivers Elec. Corp.*), 355 F.3d 415, 422 (6th Cir. 2004).

26. A request for the appointment of an examiner must be supported by the given facts and circumstances. *See In re Gliatech*, 305 B.R. at 836 (citing *In re Mechem Fin. Of Ohio, Inc.*, 92 B.R. 760, 761 (Bankr N.D. Ohio 1988)). The facts and circumstances of this case compel the appointment of an examiner.

27. The existence of significant commingling between debtor and non-debtor estates generally constitutes grounds for the appointment of a trustee. *In re Hotel Associates, Inc.*, 3 B.R. 343, 345 (Bankr. E.D. Pa. 1980) ("due to the failure of the debtor to keep adequate books and records, to properly maintain the hotel while it was within its control and in order to open the

possibility of other plans being presented, the appointment of a trustee is clearly in the interests of creditors"). "[B]ecause of the failure of the debtor to keep adequate books and records, the commingling of the debtor's assets . . ., and the admittedly adverse interest between the operator of the debtor by its managing official . . . and the alleged equity holders . . ., we conclude that it is in the best interests of creditors, equity holders and all other parties in interest, to appoint a trustee . . . ." *In re Philadelphia Athletic Club, Inc.*, 15 B.R. 60, 63 (Bankr. E.D. Pa. 1981). "[W]here there are questionable inter-company financial transfers and the principals of the debtor occupy conflicting positions in the transferee companies, a trustee should be appointed in the best interests of creditors and all parties in interest in order to investigate the financial affairs of the debtor." *In re McCorhill Pub., Inc.*, 73 B.R. 1013, 1017 (Bankr. S.D.N.Y. 1987).

28. The appointment of an examiner is necessary and would benefit all parties-in-interest in this matter. *See In re New Century TRS Holdings, Inc.*, 407 B.R. 558, 566 (Bankr. D. Del. 2009) ("The Examiner performs his duties at the request of the Court, for the benefit of the debtor, its creditors and shareholders"); *In re Fibermark*, 339 B.R. 321, 325 (Bankr. D. Vt. 2006) ("The benefit of appointing an independent examiner is that he or she will act as an objective nonadversarial party who will review the pertinent transactions and documents, thereby allowing the parties to make an informed determination as to their substantive rights."); *In re Apex Oil Co.*, 101 B.R. 92, 99 (Bankr. E.D. Mo. 1989) ("The Examiner is appointed to act as an independent party to review without monetary interest, transaction and documents. Disclosure and transparency are fundamental tenants of bankruptcy, and a crucial requirement to the effective functioning of the federal bankruptcy system. *See In re Kane*, 628 F.3d 631, 636 (3d Cir. 2010). The examiner is first and foremost disinterested and nonadversarial. The benefit of

the examiner's investigative efforts flow solely to the debtor and to its creditors and shareholders.") (internal citations omitted).

29. An examiner must act as the term suggests, for the purpose of conducting an examination, not to act as a protagonist in the case. *See In re Loral Space & Communications Ltd., et al*., 313 B.R. 577, 583 (Bankr. S.D.N.Y. 2004), *rev'd*, 2004 U.S. Dist. LEXIS 25681. It is generally understood that an "investigation" pursuant to Section 1104(c) is for the purpose of conducting a study "of any allegations of fraud, dishonesty, incompetence, misconduct, mismanagement or irregularity in the management of the affairs of the debtor" of or by current or former management of the debtor, as the statute so clearly states. *See id*. at 585 (internal quotation marks omitted). The statute has been interpreted to provide for an investigation "of a particular transaction or series of transactions, in order to reveal ways and means to protect or augment the estate." *Id*. (citing *In re Gliatech*, 305 B.R. at 835).

30. Under 11 U.S.C. § 1106, a court-appointed examiner performs the duties set forth in 11 U.S.C. § 1106(a), which provides in relevant part that an examiner shall:

> (3) except to the extent that the court orders otherwise, investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and the desirability of the continuance of such business, and any other matter relevant to the case or to the formulation of a plan;
>
> (4) as soon as practicable—
>
> (A) file a statement of any investigation conducted under paragraph (3) of this subsection, including any fact ascertained pertaining to fraud, dishonesty, incompetence, misconduct, mismanagement, or irregularity in the management of the affairs of the debtor, or to a cause of action available to the estate; and
>
> (B) transmit a copy or a summary of any such statement to any creditors' committee or equity security holders' committee, to any indenture trustee, and to such other entity as the court designates[.]

11 U.S.C. § 1106(a) (emphasis added).

31. The broad mandate of section 1106 of the Bankruptcy Code plainly includes the more limited powers that the United States Trustee seeks for an examiner in this case. *See* 11 U.S.C. § 1106 (an examiner shall "investigate . . . any other matter relevant to the case or to the formulation of a plan."); *see also The Official Comm. Of Unsecured Creditors of Cybergenics Corp. v. Chinery*, 330 F.3d 548, 577 (3d Cir. 2003) ("An examiner's duties include investigation of the debtor, the debtor's business, and 'any other matter relevant to the case or to the formation of a plan.'").

32. The evidence overwhelming supports the appointment of an examiner. Two members of current management, Kelly and Merritt, comprise fifty percent of the Debtors' pre-petition management. The testimony of each at the Evidentiary Hearing was that each paid little or no attention to the daily affairs of the Debtors. Before November 2015, they appear to have examined financial data only when it was given to them. Although Kelly and Merritt allege that DiMenna obtained millions of dollars in loans over a period of time without their alleged approval and by way of forged signatures, even a cursory review by them of the Debtors' finances showing the debt service they never agreed to should have been more than sufficient to alert them to the alleged improprieties much sooner than the bouncing of their distribution checks from Tag Forest in November 2015 (Transcript at 141:9-17; 208:21-209:2).

33. The Debtors' representatives have admitted to serious improprieties committed by members of management pre-petition, including the lack of any financial controls. Post-petition, comingling has continued by current management and current management has failed to comply with the Bankruptcy Code and Rules of Procedure.

34. The appointment of an examiner in this case will ensure the integrity of the chapter 11 process, help maintain confidence in the bankruptcy system, and in the process provide a valuable contribution to this case that will serve all constituents, creditors and shareholders alike. The prompt appointment of an examiner is required to:

(1) investigate the assets, liabilities and financial condition of the Debtors;

(2) investigate the background and events that led to this bankruptcy filing;

(3) probe the specific allegations against DiMenna;

(4) investigate the extent to which Kelly and Merritt were involved in mismanagement of the Debtors' financial affairs, including any commingling and transfers of assets;

(5) examine the operation of the Debtors' businesses (including how the Debtors are funding this case).

V. CONCLUSION

WHEREFORE, for the reasons stated above, the U.S. Trustee respectfully requests that this Court enter an order directing the appointment of an examiner, and such other and further relief as the Court deems just, fair, and equitable.

Dated: February 4, 2016
Wilmington, Delaware

Respectfully submitted,

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