IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION

In re:	Case No. 24-42473-659
MIDWEST CHRISTIAN VILLAGES, INC., *et al.*,[1]	Chapter 11
Debtors.	Jointly Administered

UNITED STATES' EMERGENCY MOTION FOR STAY PENDING APPEAL OF FINAL ORDER (1) AUTHORIZING DEBTORS IN POSSESSION TO OBTAIN POST-PETITION FINANCING; (2) AUTHORIZING DEBTORS IN POSSESSION TO USE CASH COLLATERAL; (3) PROVIDING ADEQUATE PROTECTION; AND (4) GRANTING LIENS, SECURITY INTERESTS AND SUPERPRIORITY CLAIMS

The United States of America (the "United States"), on behalf of the United States Department of Housing and Urban Development ("HUD"), hereby files this emergency motion (the "Motion"), pursuant to Rule 8007(a) of the Federal Rules of Bankruptcy Procedure for a stay pending appeal, solely as applied to the HUD Debtors (defined below) and their property, of the Final DIP Order (as defined herein). In support hereof, the United States respectfully states as follows:

[1] The address of the Debtors headquarters is 2 Cityplace Dr, Suite 200, Saint Louis, MO 63141-7390. The last four digits of the Debtors' federal tax identification numbers are: (i) Midwest Christian Villages, Inc. [5009], (ii) Hickory Point Christian Village, Inc. [7659], (iii) Lewis Memorial Christian Village [3104], (iv) Senior Care Pharmacy Services, LLC [1176], (v) New Horizons PACE MO, LLC [4745], (vi) Risen Son Christian Village [9738], (vii) Spring River Christian Village, Inc. [1462], (viii) Christian Homes, Inc. [1562], (ix) Crown Point Christian Village, Inc. [4614], (x) Hoosier Christian Village, Inc. [3749], (xi) Johnson Christian Village Care Center, LLC [8262], (xii) River Birch Christian Village, LLC [7232], (xiii) Washington Village Estates, LLC [9088], (xiv) Christian Horizons Living, LLC [4871], (xv) Wabash Christian Therapy and Medical Clinic, LLC [2894], (xvi) Wabash Christian Village Apartments, LLC [8352], (xvii) Wabash Estates, LLC [8743], (xviii) Safe Haven Hospice of Southern Illinois, LLC [7209], (xix) Heartland Christian Village, LLC [0196], (xx) Midwest Senior Ministries, Inc. [3401], (xxi) Shawnee Christian Nursing Center, LLC [0068], and (xxii) Safe Haven Hospice, LLC [6886].

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INTRODUCTION

1. Contemporaneously with filing these chapter 11 cases, the above-captioned debtors (collectively, the "Debtors") filed the DIP Motion[2] seeking post-petition financing on terms that violate the National Housing Act, HUD regulations, and the Regulatory Agreements (as defined below) and where the HUD Debtors have no need for such financing. The United States and the HUD-insured lender (Lument) objected. On September 13, 2024, the Court approved the DIP financing shorn of the United States' statutory and regulatory rights under the National Housing Act and its implementing regulations and policy, finding that the Debtors satisfied the requirements of section 364(d) of the Bankruptcy Code.

2. The United States files this Motion to preserve its right for appellate review. Importantly, the United States seeks only a limited stay of the Final DIP Order as it impacts the HUD Debtors and their property.

3. As discussed more fully below, the factors in evaluating stay pending appeal all weigh in favor of a stay. As to the likelihood of the United States' success on the merits of its appeal, the United States respectfully submits that a reviewing court is likely to determine that the Court erred in approving the DIP Facility on a final basis for at least three reasons. First, the Court approved the Final DIP Order even though the Debtors could not (and cannot) demonstrate that the DIP financing was fair, reasonable, necessary to preserve the HUD Debtors' estates. Second, the Court ordered first-priority, priming liens on the HUD Financed Facilities even though the Housing Act and other applicable federal law do not permit, to insure loans, the non-consensual priming of HUD-insured mortgage liens. Third, the Regulatory Agreements expressly

[2] *Motion for Interim Order and Final Order (1) Authorizing Debtors in Possession to Obtain Post-Petition Financing; (2) Authorizing Debtors in Possession to Use Cash Collateral; (3) Providing Adequate Protection; (4) Granting Liens, Security Interests and Superpriority Claims and (5) Scheduling a Final Hearing* [Dkt. No. 11].

prohibit the Debtors from cross-collateralizing the DIP Obligations with the HUD Debtors' property to fund the operations of the Debtors other than the HUD Debtors.

4. The remaining factors similarly all warrant this limited stay. Consummation of the DIP transaction on the terms embodied in the Final DIP Order harms HUD and HUD lenders in ways that cannot be easily undone. Indeed, this Court's decision threatens to undermine HUD's ability to fulfill its mandate to make credit available to qualified borrowers who might not otherwise have access to capital on favorable terms. The current terms of the Final DIP Order also threatens the financial and regulatory viability of the Section 232 program that is so critical for those in need of access to health care facilities, harming the public interest.

5. Conversely, the Debtors will experience no significant harm as the Final DIP Order will remain unstayed as to all non-HUD Debtors and their property. The non-HUD Debtors remain free to borrow, and UMB Bank remains free to lend to the non-HUD Debtors, under terms of the DIP Facility.

BACKGROUND[3]

6. The Debtors operate a mix of independent, assisted, and skilled nursing campuses in 11 locations across the Midwest (the "Facilities"). The Facilities include: (a) Wabash Estates, located in Carmi, Illinois (the "Wabash Facility") and (b) Washington Village Estates, located in Washington, Illinois (the "WVE Facility," and together with the Wabash Facility, the "HUD Facilities" or "HUD Financed Properties"). Debtor Wabash Estates, LLC ("Wabash Estates") owns the Wabash Facility. Debtor Washington Village Estates, LLC ("WVE Estates", along with Wabash Estates, the "HUD Debtors") owns the WVE Facility.

[3] To avoid redundancy, the United States hereby incorporates all procedural and factual background, statutory framework and arguments set forth in the HUD Objection to the extent applicable. Any capitalized terms used but not otherwise defined herein shall have the meanings ascribed to them in the HUD Objection or the DIP Motion, as applicable.

7. Prior to the Petition Date, the HUD Debtors obtained two loans (the "HUD Loans") from a predecessor of Lument Real Estate Capital, LLC ("Lument" or "HUD Lender"). A Mortgage Note, dated September 1, 2013 (each, as modified or amended, a "HUD Note," and together, the "HUD Notes"), made payable to the order of the HUD Lender evidences each HUD Loan. To secure their respective HUD Notes, each HUD Debtor granted a mortgage lien and security interest in the applicable HUD Facility's real estate, fixtures and related improvements and other assets, including all rents and leases, through a mortgage (each a "HUD Mortgage"). To further secure each HUD Note, each HUD Debtor also executed a Security Agreement, granting security interests to the HUD Lender and HUD in substantially all of such HUD Debtor's personal property. As a condition to insuring the HUD Mortgages, each HUD Debtor also entered into a Regulatory Agreement with HUD (each a "Regulatory Agreement"), which, among other things, requires HUD's consent to transfer, dispose, or encumber the HUD collateral and restricts the use of rents, receivables, and other receipts generated by the HUD Facilities.

8. On July 16, 2024 (the "Petition Date"), the Debtors, other than Safe Haven Hospice, LLC,[4] commenced these cases (together with the chapter 11 case of Safe Haven Hospice, LLC, the "Chapter 11 Cases").

[4] Safe Haven Hospice, LLC, filed its voluntary chapter 11 petition in this Court on August 21, 2024 (Case No. 24-43000) [Dkt. No. 1].

9. Following a first day hearing held on July 17, 2024, the Court entered the First Interim DIP Order.[5] On August 16, 2024, the Court entered the Second Interim DIP Order.[6]

10. On September 4, 2024, the United States objected to the DIP Motion (the "HUD Objection") [Docket No. 271]. The same day, Lument also objected to the DIP Motion [Docket No. 268] (the "Lument Objection").

11. On September 11, 2024, the Court heard evidence and oral argument on the DIP Motion. Evidence included the testimony of Shawn O'Conner, the Debtors' Chief Restructuring Officer, the stipulated facts and admitted exhibits contained in the *Stipulated Facts and Admitted Documents,* filed on September 10, 2024 [Dkt. No. 292].

12. On September 13, 2024, the Court ruled on the DIP Motion on a final basis, approving the DIP Facility and overruling the HUD Objection and the Lument Objection. After the Court's ruling, the United States orally requested a stay pending appeal of the Final DIP Order, solely as to the HUD Debtors and their property. Debtors and UMB Bank opposed. The Court declined to rule on the oral motion and, instead, directed the parties to file written submissions.[7]

[5] *Interim Order (1) Authorizing Debtors in Possession to Obtain Post-Petition Financing; (2) Authorizing Debtors in Possession to Use Cash Collateral; (3) Providing Adequate Protection; (4) Granting Liens, Security Interests and Superpriority Claims; and (5) Scheduling a Final Hearing* [Dkt. No. 60].

[6] *Second Interim Order (1) Authorizing Debtors in Possession to Obtain Post-Petition Financing; (2) Authorizing Debtors in Possession to Use Cash Collateral; (3) Providing Adequate Protection; (4) Granting Liens, Security Interests and Superpriority Claims; and (5) Scheduling a Final Hearing* [Dkt. No. 160].

[7] In lieu of the immediate entry of the Final DIP Order, the Debtors and UMB Bank agreed to propose a further interim order that extends the Debtors' access to cash collateral and the proceeds of previously funded DIP loans through September 20, 2024. On September 14, 2024, the Court approved the interim order [Dkt. No. 309].

13. On September 16, 2024, the Debtors filed a further revised version of the proposed Final DIP Order [Dkt. No. 313, Ex. A].[8] Like prior versions of the proposed Final DIP Order, this most recent proposed Final DIP Order (not yet entered by the Court): (a) makes the HUD Debtors liable for the obligations (other than the Roll-Up Obligations) of the non-HUD Debtors under the DIP Credit Agreement [Final DIP Order, ¶ 9(ii)]; (b) grants priming Post-Petition Liens in favor of the DIP Lender [Id., ¶¶ 16, 21(i), & 21(ii)] on the HUD Debtors' property; (c) finds that the DIP Lender, Trustee, and certain others acted in "good faith" [See, e.g., id., ¶¶ FF, GG, 4, & 39]; (d) subjects the HUD Mortgages and HUD Collateral to the terms of the Carve-Out [Id., ¶¶ 40-41]; and (e) waives the equitable remedy of marshaling [Id., ¶¶ 30 & 35(ii)].

BASIS FOR RELIEF

14. Bankruptcy Rule 8007(a)(1)(A) authorizes a party to seek "a stay of a judgment, order, or decree of the bankruptcy court pending appeal" from this Court. To determine whether to issue a stay pending appeal, courts consider four factors: (1) whether the party seeking the stay has demonstrated a strong likelihood of success on the merits; (2) whether the party seeking the stay will be irreparably injured without a stay; (3) whether a stay would substantially injure other parties; and (4) the public interest. *See Org. for Black Struggle v. Ashcroft*, 978 F.3d 603, 607 (8th Cir. 2020) (citing *Brakebill v. Jaeger*, 905 F.3d 553, 557 (8th Cir. 2018)). Although courts in the Eighth Circuit give the most weight to the appellant's likelihood of success on the merits, the Court must consider the relative strength of the four factors, "balancing them all." *Brady v.*

[8] Unless otherwise noted, all references herein to the "Final DIP Order" refer to the version thereof filed at Docket No. 313, Exhibit A.

Nat'l Football League, 640 F.3d 785, 789 (8th Cir. 2011) (quoting *Fargo Women's Health Org. v. Schafer,* 18 F.3d 526, 538 (8th Cir. 1994)).

15. The Court should stay the Final DIP Order as it applies to the HUD Debtors or their property, as the balancing of all four factors establishes the United States' entitlement to a stay. First, the United States has a strong likelihood of prevailing on appeal. Second, HUD will suffer irreparable harm absent a stay, given the risks that its appeal may be rendered equitably moot or barred by section 364(e) of the Bankruptcy Code. Third, the limited stay as to the HUD Debtors and their property will not harm the Debtors. Finally, a stay of Final DIP Order serves the public interests, given the repercussions that the Final DIP Order may have on eligible borrowers' access to credit under the section 232 program.

A. The United States Has a Strong Likelihood of Prevailing on the Merits of the Appeal.

16. In deciding whether to grant a stay, courts analyze whether success on appeal is "likely." *Iowa Utils. Bd. v. F.C.C.,* 109 F.3d 418, 423 (8th Cir. 1996). A movant "need not establish an absolute certainty of success" on the merits. *Id.* When "[t]he legal issues raised . . . are serious", the Eighth Circuit has granted a stay pending appeal "[w]ithout expressing an opinion on the merits" based on its determination that the "balance of the equities favors the United States." *James River Flood Control Ass'n v. Watt,* 680 F.2d 543, 544 (8th Cir. 1982). Here, the United States raises serious legal issues and has a strong likelihood of success on the merits.

1. <u>The DIP Facility s not fair, reasonable, or necessary for the HUD Debtors and not in the best interests of the HUD Debtors' estates.</u>

17. The Court erred in determining the DIP Facility is fair, reasonable, or necessary for the HUD Debtors and is in the best interests of the HUD Debtors' estates. *See In re Farmland Indus., Inc.*, 294 B.R. 855, 879–80 (Bankr. W.D. Mo. 2003), *appeal dismissed*, No. 03-00472

(W.D. Mo. Jan. 9, 2004); *In re Los Angeles Dodgers LLC*, 457 B.R. 308, 312 (Bankr. D. Del. 2011) ("In seeking approval of [DIP financing], the Debtors have the burden of proving that . . . the terms of the transaction are fair, reasonable, and adequate, given the circumstances of the debtor-borrower and the proposed lender."); *In re Mid-State Raceway, Inc.*, 323 B.R. 40, 60 (Bankr. N.D.N.Y. 2005). Postpetition credit should not be authorized if its primary purpose is to benefit or improve the position of a particular secured lender. *See, e,g.*, *In re Aqua Assocs.*, 123 B.R. 192, 195–96 (Bankr. E.D. Pa. 1991) ("[C]redit should not be approved when it is sought for the primary benefit of a party other than the debtor."); *In re Ames Dep't Stores, Inc.*, 115 B.R. 34, 39 (Bankr. S.D.N.Y. 1990) ("[A] proposed financing will not be approved where it is apparent that the purpose of the financing is to benefit a creditor rather than the estate.").

18. As the Debtors' Chief Restructuring Officer admitted, the HUD Debtors here simply have no need for the DIP Facility for the expected duration of these cases.[9] WVE owns and operates a thriving, financially stable senior living facility. The Debtors' own fiscal year 2023 audited financial statements establish that WVE has generated substantial positive and self-sustaining cash flow both before and after servicing its HUD Loan, WVE's only long-term debt. As of the Petition Date, WVE had approximately $1,081,964 of cash (the "WVE Cash") [Dkt. No. 292 at ¶ 33], and current accounts receivable (*i.e.,* 90 days or less) totaling more than $376,685 (the "WVE A/R") [Dkt. No. 191]. The WVE Cash and the WVE A/R are and were, available, to be used to service WVE's HUD Loan and to satisfy the facility's operational and repair obligations. Indisputably, WVE and Wabash Estates have no need for funding from the DIP Facility or intercompany transfers from any other Debtor to operate and survive.

[9] *See Stipulated Facts and Admitted Documents* [Dkt. No. 292], Admitted Exhibit No. 3 [Deposition of Shawn O'Conner on Sept. 4, 2024 at 65:22-66:5; 88:9-13].

19. The Debtors also failed to consider the separate and distinct interests of the HUD Debtors during the negotiation and drafting of the DIP Facility's terms. "Neither Washington Village Estates nor Wabash Estates was separately represented by counsel or other professionals (other than counsel or other professionals that were representing all of the Debtors) in connection with the negotiation or documentation of the DIP Facility's terms."[10] Further, "[s]ince at least May 1, 2024, there have been no individuals serving in an officer, director, or managing agent capacity for Washington Village Estates that were not simultaneously also holding one or more such roles for Midwest Christian Villages, Inc. or an entity that is a member of the [non-HUD Debtors]."[11] Midwest Christian Villages is the parent holding company for all of the Debtors, including all the non-HUD Debtors.

20. Given the terms of the DIP Facility and the failure to protect the distinct interests of the HUD Debtors in negotiating and drafting the DIP Facility, a reviewing court is likely to find that this Court committed reversible error in determining that the DIP Facility and Final DIP Order terms are in the best interests of the HUD Debtors and their estates.

2. <u>The Priming of the existing HUD Mortgages violates applicable federal law, including the Housing Act, its regulations, and the regulatory agreements.</u>

a. The Housing Act, HUD regulations, and required regulatory agreements mandate a first mortgage.

21. The Housing Act only permits HUD to insure first mortgage liens. Specifically, the Housing Act requires that, to be insurable, a HUD-insured mortgage be a "***first*** mortgage on real estate in fee simple." 12 U.S.C. § 1715w(b)(4) (emphasis added). Granting priming first-priority liens on the real property of the HUD Debtors therefore directly contravenes this

[10] *Id.*, ¶ 48.

[11] *Id.*, ¶ 51. *See also id.*, ¶ 52 (containing same admission as to Wabash Estates).

Housing Act requirement. On this ground alone, the Court should have denied approval of non-consensual priming liens on the HUD Financed Properties.

22. Besides the statutory first mortgage requirement, the HUD regulations require that a HUD project "be free and clear of all liens other than the insured mortgage, except that the property may be subject to an inferior lien as provided by terms and conditions established by the Commissioner for an inferior lien." 24 C.F.R § 200.71 (2024). The HUD regulations also require HUD to "regulate the mortgagor by means of a regulatory agreement providing terms, conditions and standards established by the Commissioner, or by such other means as the Commissioner may prescribe." 24 C.F.R § 200.105(a) (2024). Consequently, HUD required the HUD Debtors to enter into the Regulatory Agreements. These Regulatory Agreements expressly prohibit *any* liens on the HUD Financed Properties and other collateral without HUD's prior written approval. *See* Regulatory Agreements, ¶ 6(a) ("Owners shall not without the prior written approval of the Secretary . . . encumber any of the mortgaged property, or permit . . . encumbrance of such property.").

23. The bankruptcy proceedings do not relieve the HUD Debtors from complying with the Regulatory Agreements. While the Regulatory Agreements are, at base, security instruments that created liens on the HUD Debtors' real and personal property, they also function as regulatory devices that aid HUD in regulating the HUD Debtors. *See* 24 C.F.R. § 200.105(a) ("As long as the Commissioner is the insurer or holder of the mortgage, the Commissioner shall regulate the mortgagor by means of a regulatory agreement providing terms, conditions and standards established by the Commissioner, or by such other means as the Commissioner may prescribe."); *Indian Motorcycle Assocs. III Ltd. Partnership v. Massachusetts Housing Finance Agency*, 66 F.3d 1246, 1250 (1st Cir. 1995) ("Every court which has considered the question has

determined that the [Housing Act] empowers HUD to enforce its prepetition rights under a Regulatory Agreement notwithstanding the initiation of a chapter 11 proceeding by or against the [Housing Act] borrower."). Here, HUD has not consented to encumber the HUD Financed Properties or the HUD Debtors' other assets with liens in favor of the DIP Lender. The Final DIP Order, which grants priming liens in favor of the DIP Lender, therefore violates the Housing Act, its related regulations, and the terms of each HUD Debtor's Regulatory Agreement.

b. Section 364 of the Bankruptcy Code does not trump the Housing Act's requirements.

24. The Bankruptcy Code does not relieve the Debtors of their existing obligations under the Housing Act, the related regulations, and the Regulatory Agreements or, in this context, supplant their requirements. Rather, "when two statutes are capable of coexistence, . . . it is the duty of the courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective." *In re Am. River Transp. Co.*, 800 F.3d 428, 433 (8th Cir. 2015) (quoting *Morton v. Mancari*, 417 U.S. 535, 551 (1974)) (internal quotations omitted). Courts routinely apply "a federal statute to bankruptcy suits despite the existence of another, bankruptcy-specific statute covering the same ground." *Simon v. FIA Card Servs., N.A.*, 732 F.3d 259, 275 (3d Cir. 2013) (citing *Connecticut National Bank v. Germain*, 503 U.S. 249 (1992)). To determine whether the Bankruptcy Code supplants another federal statute, "the proper inquiry . . . is whether the [federal statute] raises a direct conflict between the Code or Rules and the [federal statute] or whether both can be enforced." *Simon*, 732 F.3d at 274 (finding that there is "a presumption against the implied repeal of one federal statute by another"); *see also Wood v. Fiedler*, 548 F.2d 216, 219 (8th Cir. 1977) (in bankruptcy context, declining to abrogate a federal statute absent "a clear or manifest congressional intent").

25. Section 364 of the Bankruptcy Code does not directly address the portions of the Housing Act and its regulations at issue here. *Compare In re Welker*, 163 B.R. 488, 489 (Bankr. N.D. Tex. 1994) ("The Bankruptcy Code does not authorize the court to employ § 363 to supersede or preempt [HUD guidelines] or the compelling public policy interests behind the housing acts."), *with In re Pulaski Highway Express, Inc.*, 41 B.R. 305, 309-10 (Bankr. M.D. Tenn. 1984) ("courts addressing conflicts between ERISA and the Bankruptcy Code have concluded that the Bankruptcy Code controls because of the explicit language of § 1144(d)"). Accordingly, the Court must enforce both the Housing Act and the Bankruptcy Code consistent with each other. The granting of priming first-priority liens on the HUD Debtors' real property is inconsistent with the Housing Act's requirements that, to be insurable, the loan be secured by a "***first*** mortgage". 12 U.S.C. § 1715w(a)(4) (emphasis added). Thus, to give effect to the Housing Act and the regulations promulgated thereunder, the Court should have denied the final approval of the DIP Motion with respect to the HUD Debtors and their property.

26. In the Court's September 13 ruling, the Court appears to have deemed "first mortgage" requirement wholly inapplicable to the issue of whether priming liens may be approved pursuant to section 364(d) of the Bankruptcy Code. In this regard, in approving the requested priming lien at Washington Village Estates, the Court stated that the federal government is not entitled to any special treatment under section 364(d).

27. This, however, is inconsistent with applicable federal law. Courts must approach the construction of the applicable provisions of the Housing Act and the Bankruptcy Code as "holistic endeavors". *See U.S. Nat'l Bank of Or. v. Indep. Ins. Agents of Am., Inc.,* 508 U.S. 439, 455 (1993) ("Statutory construction 'is a holistic endeavor,' and, at a minimum, must account for a statute's full text, language as well as punctuation, structure, and subject matter.") (quoting

United Savings Ass'n of Tex. v. Timbers of Inwood Forest Assocs., Ltd., 484 U.S. 365, 371 (1988)); *Beal v. Outfield Brew House, LLC,* 29 F.4th 391, 394 (8th Cir. 2022).

28. Section 1715w(a)(4) of title 12 is not the only provision of the Housing Act and regulations that speak to whether other liens encumbering property subject to a HUD-insured mortgage are permissible. For example, 12 U.S.C. § 1715w(d)(1) requires a mortgage to be executed by a mortgagor approved by the HUD Secretary, and 24 C.F.R. § 232.3 specifies that "[t]he borrower shall be a single asset entity acceptable to the Commissioner." HUD regulations further require that a HUD-insured project "be free and clear of all liens other than the insured mortgage, except that the property may be subject to an inferior lien as provided by terms and conditions established by the Commissioner for an inferior lien." 24 C.F.R. § 200.71. *See also, e.g.,* Regulatory Agreements, ¶ 6(a) ("Owners shall not without the prior written approval of the Secretary . . . encumber any of the mortgaged property, or permit . . . encumbrance of such property."). Especially telling of Congress's expectation that the "first mortgage" requirement would continue after the initial act of insuring the HUD mortgage is that Congress has established a federal cause of action for DOJ on behalf of HUD to recover any assets or income "used by any person" in violation of a regulatory agreement or any applicable regulation. *See* 12 U.S.C. § 1715z-4a(a)(1). If Congress had intended the "first mortgage" requirement to be of no consequence after HUD insured the mortgage, it would have had no reason to create this enforcement mechanism.

29. Conversely, section 364(d)(1) of the Bankruptcy Code does not affirmatively mandate the bankruptcy court grant a priming lien for postpetition financing whenever the trustee (or DIP) meets the section's requirements. Had Congress intended that result, it would have used mandatory language such as "the court . . . [***shall***] authorize the obtaining of credit or

the incurring of debt secured by a senior or equal lien on property of the estate that is subject to a lien . . . " in section 364(d).[12] Instead, Congress used the permissive language "may authorize."

30. Thus, it is likely that a reviewing court will grant the United States' appeal on the basis that the Court erred in allowing the HUD-insured mortgage to be primed.

3. The DIP Facility impermissibly obligates the HUD Debtors for obligations of the non-HUD Debtors and cannibalizes the HUD Debtors' assets to support lending to the non-HUD Debtors.

31. The Housing Act delegates discretion to the HUD Secretary to specify the characteristics of a HUD-insured mortgage and mortgagor. *See* 12 U.S.C. § 1715w(d)(1). HUD regulations mandate that the HUD Debtors "***shall*** be a single asset entity acceptable to the Commissioner." 24 C.F.R. § 232.3 (emphasis added). Thus, the "mortgaged healthcare facility must be the only asset of the [HUD Debtors]." U.S. DEP'T OF HOUS. & URB. DEV., HEALTHCARE MORTGAGE INSURANCE PROGRAM HANDBOOK, § II, ch. 2.5 (Jan. 19, 2017) ("Program Handbook").[13] Further, funds from HUD insured projects cannot be used to operate facilities that have no HUD-insured loans. *See Id.* at § II, ch. 15.3(J) ("The AR Lender cannot use the accounts receivable or any other collateral related to the included FHA-insured projects to secure or pay loans to non-FHA projects/Operators, or to secure or pay debts of FHA-insured projects not approved for inclusion in the AR line."). HUD's regulations and guidance limiting use of project assets and income for only certain permitted purposes are central to the functioning of the FHA

[12] *See, e.g., Lopez v. Davis,* 531 U.S. 230, 241 (2001) ("Congress' use of the permissive 'may' in § 3621(e)(2)(B) contrasts with the legislators' use of a mandatory 'shall' in the very same section. Elsewhere in § 3621, Congress used 'shall' to impose discretionless obligations . . . ."); *Kingdomware Techs, Inc., v. U.S.,* 579 U.S. 162, 172 (2016) ("When a statute distinguishes between 'may' and 'shall,' it is generally clear that 'shall' imposes a mandatory duty."); *LeMay v. U.S.P.S.,* 450 F.3d 797, 799 (8th Cir. 2006) ("[A]s a general rule of statutory construction, 'may' is permissive, whereas 'shall' is mandatory.").

[13] The Program Handbook is available at: www.hud.gov/program_offices/administration/hudclips/handbooks/hsgh/42321

mortgage insurance system and essential to Congress's policy goals. Congress created the FHA "to insure private lenders against loss on . . . mortgage loans, thereby making those loans more widely available to a greater portion of the population." *Capital Mortgage Bankers v. Cuomo*, 222 F. 3d 151, 152 (4th Cir. 2000); *Housing Study Group v. Kemp*, 732 F. Supp. 180, 182 (D.D.C. 1990) (FHA does not make loans but "rather it operates programs to insure private lenders against loss on mortgage loans"). Congress crafted the Housing Act "to prevent money of federally insured housing projects from being diverted to purposes other than actual and necessary expenses . . . ." *United States v. Norris*, 749 F.2d 1116, 1120 (4th Cir. 1984).

32. The Regulatory Agreements implement these directives and mandates. The Regulatory Agreements expressly forbid the HUD Debtors from distributing project assets or income (including the mortgaged property), except for surplus cash, or incurring liabilities or obligations not connected with the project. Reg. Agree., ¶ ¶ 6(e)(1) – (4), 6(f), and 13(n) (contained in each LEAN Rider). Bankruptcy does not eliminate these restrictions. *See Stumpf v. Albarcht*, 982 F.2d 275, 277 (8th Cir. 1992) (noting that the trustee succeeds to only the prebankruptcy rights of the debtor). The Final DIP Order violates HUD regulations, HUD policy, and Regulatory Agreements by (1) obligating the HUD Debtors to become borrowers under the DIP Facility or otherwise be jointly and severally liable for the DIP Obligations and (2) enabling, through encumbrance, the use of the HUD Debtors' property for the non-HUD Debtors' benefit in contravention of the Regulatory Agreements' use restrictions.

33. In its September 13 ruling, the Court considered only whether the HUD Debtors' cases are jointly administered with the cases of non-HUD Debtors and whether the HUD Debtors' cases were subject to dismissal under section 1112(b) of the Bankruptcy Code as bad faith filings. As discussed above, when, as here, a debtor has no need for the proposed

postpetition financing facility, it is almost never proper to allow that debtor to incur those liabilities and to pledge its assets to secure their repayment.

34. For all these reasons, the United States has a strong likelihood of prevailing on appeal.

B. The United States Will Suffer Irreparable Injury Absent a Stay.

35. A stay prevents irreparable harm to the United States. A stay is appropriate when "irreparable injury is *likely* [not merely possible] in the absence of [a] [stay]." *See Winter v. Natural Res. Def. Council, Inc.,* 555 U.S. 7, 22 (2008) (emphasis in text). For irreparable harm, the Supreme Court's use of "likely" means "more apt to occur than not." *In re Revel AC*, 802 F.3d at 569, citing *Michigan v. U.S. Army Corps of Engineers*, 667 F.3d 765, 788 (7th Cir.2011) (for harm to be likely "there must be more than a mere possibility that harm will come to pass . . . *but the alleged harm need not be occurring or be certain before a court may grant relief*") (citation omitted) (emphasis added).

36. Courts consistently find that an appellant satisfies the irreparable harm requirement when the appellant's right would be vitiated absent a stay. For example, in *ACC Bondholder Group v. Adelphia Commc'ns Corp. (In re Adelphia Commc'ns Corp.)*, 361 B.R. 337 (S.D.N.Y. 2007), in staying the bankruptcy court's confirmation order pending appeal, the district court emphasized the loss of appellate review is a "quintessential form of prejudice." *Id.* at 347-48. The court concluded that "where the denial of a stay pending appeal risks mooting *any* appeal of *significant* claims of error, the irreparable harm requirement is satisfied." *Id*. at 348; *see also Manges v. Seattle-First Nat'l Bank (In re Manges*), 29 F.3d 1034, 1039 (5th Cir. 1994); *In re Texas Equip. Co., Inc.*, 283 B.R. 222, 228 (Bankr. N.D. Tex. 2002) (unless the party obtains a stay of a sale order, there would be no effective remedies).

37. Here, the United States faces irreparable harm from the likely elimination of its appeal rights if the Final DIP Order as it relates to the HUD Debtors and their property is not stayed. The Debtors have already borrowed $3 million under the DIP Facility and are budgeted to draw another $1.9 million during the week ending September 21, 2024. Under the terms of the Final DIP Order, the HUD Debtors will be liable for these obligations even though the HUD Debtors have no need for such funding during these cases. If the Final DIP Order is afforded the protections in section 364(e) of the Bankruptcy Code (as well as the enhanced protections drafted into the Final DIP Order), the United States will be denied the means for effective review of the Final DIP Order.

C. The Debtors Will Not Be "Substantially Injured" by a Stay Pending Appeal.

38. As the Eighth Circuit has stated, "there can be little harm to other parties where a stay preserves the status quo. . ." *Ashcroft*, 978 F.3d at 609 (internal citation and quotation omitted). In considering whether a stay would cause substantial injury to others, courts balance the harm of one party against another. *See Iowa Utils. Bd.*, 109 F.3d at 426 (finding the inconvenience to the party seeking to avoid a stay was "outweighed by the harm and difficulties" to the other party).

39. With respect to the non-HUD Debtors, there is no harm if the Court grants the DIP financing as to those Debtors only without obligating the HUD Debtors and without priming the HUD Financed Properties. It defies credulity that UMB Bank would cut off the non-HUD Debtors' access to cash collateral and deny them postpetition financing if it does not obtain the windfall of obligating the HUD Debtors and encumbering their assets.[14] According to the

[14] This is especially so, given that HUD and Lument have not opposed granting the DIP Lender and Trustee senior liens on the HUD Debtors' accounts receivable or junior liens on the HUD Debtors' already encumbered real property and other assets.

Debtors, these Chapter 11 Cases were filed to implement a bankruptcy sale process to maximize value for their creditors.[15] The primary creditor beneficiaries of this sale process are UMB Bank and other holders of the Master Obligations that the Debtors have stipulated exceeded $75 million in outstanding principal as of the Petition Date.[16] Final DIP Order, ¶ O. Logic dictates that UMB Bank will not follow through with its threats to withhold funding to the non-HUD Debtors over the failure to have its way as to the HUD Debtors and their property, given that to do so would be to destroy going concern value of which UMB Bank and the holders of the Master Obligations would otherwise be the primary beneficiaries The non-HUD Debtors will still be entitled to the financing and the benefits provided with the Final DIP Order. Only the HUD Debtors will be impacted with the stay. Because the HUD Debtors, as explained above, have no need for the DIP Facility, the HUD Debtors will suffer no "substantial" injury, much less any injury at all.

40. The Debtors and UMB Bank also attempt to hide behind the specter of residents of the Debtors' senior living facilities being ejected into the streets if the Debtors' facilities are forced to cease operations. This is a highly improbable scenario. In any event, virtually every state in which the Debtors operate senior living facilities has the ability to exercise oversight over, or assume control of, a facility's closing process when necessary to protect the welfare of its residents. For example, if the Illinois Department of Public Health, which controls the licensure of a nursing home, determines that the nursing home facility is closing without enough

[15] *See Declaration of Kathleen (Kate) Bertram,* dated July, 16, 2024, ¶ 118 [Dkt. 3] ("Upon careful consideration and in consultation with their professionals, the Debtors have determined that selling substantially all of their assets in one or more going-concern sales will maximize the value of the Debtors' estates and creditor recoveries."); *DIP Motion,* ¶ 6 ("The Debtors filed chapter 11 cases to pursue one or more going concern sales and/or going concern affiliates for each of their facilities.").

time to transfer the residents or it determines that an emergency exists that would be a threat to the health, safety, or welfare of the residents, the Department can place an agent to monitor the facility and assist with the closure and/or transfer of residents. 77 Ill. Adm. Code § 300.270.

D. Granting a Stay Pending Appeal Serves the Public Interest.

41. A district court in the Eighth Circuit has noted that the "government's interest is in large part presumed to be the public's interest." *United States v. Reed*, No. C07-4087-MWB, 2009 WL 10727786, at *2 (N.D. Iowa May 12, 2009) (quoting *U.S. v. Rural Elec. Convenience Cooperative Co.*, 922 F.2d 429, 440 (7th Cir. 1991)). The Section 232 program, established by HUD to fulfill its mandates under the Housing Act, focuses on promoting construction and substantial rehabilitation of nursing homes, intermediate care facilities, and board and care homes, as well as the acquisition or refinancing of such facilities. 12 U.S.C. § 1715w. To execute this program, "Congress authorized the Secretary of HUD to insure the mortgage loans by which eligible projects were acquired, refinanced, constructed, or rehabilitated." *Hous. Study Grp. v. Kemp*, 732 F. Supp. 180, 182 (D.D.C. 1990). Since HUD may lose money on many defaulted loans and too many lenders submit claims to cover those losses, Congress directed the Secretary of HUD "to take appropriate actions to reduce losses under the [Housing] Act." *Capitol Mortg. Bankers, Inc. v. Cuomo*, 222 F.3d 151, 152 (4th Cir. 2000) (internal quotation omitted). *See also* 12 U.S.C. §§ 1715z-4a(a)(2) & (c) (giving the United States the ability "to recover any assets or income used by any person in violation of (A) a regulatory agreement that applies to a multifamily project, nursing home, . . .[or] assisted living facility. . . whose mortgage is . . . insured or held by the Secretary . . . ; or (D) any applicable regulation" and imposing double damages liability on responsible parties). In pursuit to this Congressional directive, HUD has established regulations and mandated the use of regulatory agreements that prohibit any liens and encumbrances on the HUD-insured borrower's property without HUD's prior written approval

and that confine the use of a HUD borrower's property (except for "surplus cash" not available here) for operating and repairing the project subject to the HUD-insured mortgage. *See* Reg. Agree., ¶¶ 6(e), 6(f) & 13(n); 24 C.F.R. §§ 200.71, 200.105(a), & 232.3.

42. Granting liens of senior or equal priority with HUD-insured mortgages risks the HUD mortgage insurance for the mortgage loans. *See* Lument Objection, ¶¶ 4 & 50-52 & n.7 (citing 24 C.F.R. § 207.258(b)(3) regarding representations and warranties that must be made to HUD for a valid mortgage insurance claim).[17] Even assuming *arguendo* that Lument could be adequately protected in these cases, if such relief is granted here, there will be many other cases where the loss of the HUD mortgage insurance exposes commercial lenders to loss upon borrower default. This would inevitably chill private lenders, such as Lument, from extending section 232 loans on favorable terms (or, much worse, on any terms at all) to the detriment of the American public. *See e.g., Johnson v. U.S. Dep't of Hous. & Urb. Dev.*, 911 F.2d 1302, 1304 (8th Cir. 1990) (HUD insures mortgages against default and subsidizes below-market interest rates in exchange for certain conditions); *Overton v. John Knox Ret. Tower, Inc.*, 720 F. Supp. 934, 937 (M.D. Ala. 1989) (explaining that the Housing Act offers programs to private sponsors who are otherwise unable to arrange funding from other sources upon terms and conditionals equally as favorable as those offered by HUD). The public interest thus would be served by the requested stay.

[17] "[T]he mortgagee shall warrant that: . . . (iii) The mortgage is prior to all liens and encumbrances which may have attached or defects which may have arisen subsequent to the recording of the mortgage, except such liens or other matters as may be approved by the Commissioner." 24 C.F.R. § 207.258(b)(3).

CONCLUSION

WHEREFORE, the United States respectfully requests that this Court grant this Motion, issue a stay pending appeal as requested herein, and grant the United States such other and further relief as is just and proper.

Dated: September 16, 2024

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on September 16, 2024, a copy of the foregoing was served by CM/ECF on each of the parties that have filed an appearance in this case.

/s/ Gregory W. Werkheiser
GREGORY W. WERKHEISER