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Senior Living Properties, LLC

Creditor claimed insurer was bankrupt debtor's de facto partner

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Decision (P)	Liability only
CASE	In Re: Senior Living Properties, LLC, et al., Debtors. Dan B. Lain, Trustee of Senior Living Properties, LLC, Trust v. ZC Specialty Insurance Co., No. 02-34243-SAF-11; adversary no. 03-3262
COURT	United States Bankruptcy Court, Northern District, Dallas, TX
JUDGE	Steven A. Felsenthal
DATE	4/22/2004
PLAINTIFF ATTORNEY(S)	David T. Marks (lead), The Marks Firm, Houston, TX Henry P. Giessel, The Marks Firm, Houston, TX David H. Hill, Wellborn, Houston, Adkison, Mann, Sadler & Hill, Henderson, TX Marvin Isgur, Floyd, Isgur, Rios & Wahrlich, Houston, TX Andrew E. Jillson, Jenkens & Gilchrist, Dallas, TX David R. Jones, Floyd, Isgur, Rios & Wahrlich, Houston, TX Tim Lee, Ware, Snow, Fogel & Jackson, Houston, TX Lynnette R. Warman, Jenkens & Gilchrist, Dallas, TX
DEFENSE ATTORNEY(S)	Ronald D. Betman, Winston & Strawn, Chicago, IL Monica Blacha, Winston & Strawn, Chicago, IL Patricia Bronte, Jenner & Block, Chicago, IL Jack J. Crowe, Winston & Strawn, Chicago, IL Mark K. Thomas, Jenner & Block, Chicago, IL
FACTS & ALLEGATIONS	On Aug. 8, 2003, plaintiff Dan B. Lain became trustee of the assets of bankruptcy debtor Senior Living Properties LLC (SLP), a nursing home company. Lain's duties included liquidating the assets and using the proceeds to satisfy claims against SLP, including claims by unsecured creditors and personal injury claimants. Lain sued a surety of SLP's, ZC Specialty Insurance Co., a subsidiary of Zurich Financial Services Group, alleging that ZC was SLP's partner in the nursing home business and therefore liable for SLP's debts. Lain alleged that, in February 1998, ZC engineered the purchase of about 88 nursing homes in Texas and Illinois for $246 million. ZC arranged a GMAC loan of $226 million with subordinated loans of $20 million. Lain further alleged that, for its role in the transaction, ZC contracted to receive the first $4 million of the annual profit of the nursing homes, plus at least 70% of the fair market value of the homes if later sold; and to have sole discretion over hiring and firing a nursing-home management company. Lain claimed that the 70% terms later increased to 90%. ZC also required liability insurance to be maintained on the nursing homes, with ZC as a named insured; required that GMAC be paid each month before any other payments were made; and had the right to examine the nursing homes' books and records at any time. Lain alleged that, at the closing of the transaction in February 1998m ZC for the first time identified SLP, a company with no assets or capital, as the "buyer" and henceforth the "nominee owner" of the nursing homes. ZC contended that SLP was a bankruptcy-remote entity required by GMAC for REMIC (real estate mortgage investment conduit) participation and that SLP had been identified as such an entity as early as 1997. The transaction documents identified SLP as the buyer and ZC as a surety – ZC had provided a $146 million surety bond on the GMAC loan. The documents expressly stated that no partnership was created. ZC claimed that it was merely a surety of SLP, not an owner or partner in the nursing homes business. ZC argued that it had the protections typically given to a secured lender, but did not share in the profits or losses. Lain alleged that ZC was at least as much of a buyer and subsequent owner as SLP. SLP's principals, who put up $200 for the loans totaling $246 million, testified that SLP was the owner in name only. Further, Lain argued that all the key transaction documents and terms were negotiated and controlled by ZC with no involvement by and in the absence of SLP. Lain alleged that, as business began to sour, ZC began to exercise even greater control in the business and go even further beyond the typical role of a surety. ZC contended that it had and exercised the normal rights of a creditor. Lain argued that it was very unlikely that SLP, a company with practically no assets in February 1998, could have obtained $246 million in loans while putting up only $200 in capital, if it had no partner. Internal modeling documents of ZC referred to its equity-like return, "profit share," and other premiums, which were indicia of partnership, Lain argued. ZC argued that such premiums were common the surety industry when the risk was as enormous as ZC's. Some ZC personnel also testified that they had used certain terms loosely, which Lain argued was unlikely for people sophisticated in financial affairs.
INJURIES/DAMAGES	Lain sought a declaration that ZC was a partner of SLP and therefore liable for SLP's debts.
RESULT	After a bench trial, Judge Felsenthal found that ZC was a de facto partner of SLP and liable for SLP's debts. The opinion is 110 pages. Felsenthal found not credible some testimony from ZC witnesses. He described one former ZC director's testimony as "Clintonesque" in it evasiveness.
Plaintiff Expert(s)	Richard Clark Abbott, finance, Houston, TX John Dolan, J.D., loans, Detroit, MI Neil Cohen, J.D., loans, Brooklyn, NY
Defense Expert(s)	James Hass, finance, Washington, DC Donald Thomas, CPA, finance, Allen, TX
Post-Trial	ZC is appealing the decision. On April 27, trustee Lain filed a Complaint for Money Judgment against ZC in this court, seeking $421 million, plus attorney fees, costs and interest. This amount includes $90 million in claims by ZC and its affiliates as creditors of SLP and $205 million for that part of the GMAC loan independently guaranteed by the ZC surety bond. ZC is asserting defenses to the damages claims. On Dec.14, ZC settled with the trust for $47.5 million, subject to the court.
Editor's Note	The creditors committee, Lain's predecessor, authorized The Marks Firm to pursue this claim against ZC on behalf of all SLP creditors, and Judge Felsenthal approved the authorization.