

UNITED STATES BANKRUPTCY COURT  
DISTRICT OF MINNESOTA

In re:

Chapter 11 Bankruptcy

Intrepid U.S.A., Inc.,  
and Jointly Administered Cases,

Case No. 04-40416-NCD

Case No. 04-40462-NCD

Case No. 04-40418-NCD

Debtors.

Case Nos. 04-41924 – 04-41988-NCD

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**LIMITED OBJECTION OF CAPITALSOURCE FINANCE LLC TO MOTION FOR  
ORDER GRANTING EXPEDITED HEARING AND AUTHORIZING DEBTOR  
INTREPID USA, INC. TO ENTER INTO INSURANCE CONTRACTS  
AND INSURANCE PREMIUM FINANCE AGREEMENT**

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CapitalSource Finance LLC (“CapitalSource Finance”), the DIP lender to the above-captioned debtors and debtors-in-possession (collectively, the “Debtors”), submits this limited objection (the “Limited Objection”) to the Debtors’ Motion for Order Granting Expedited Hearing and Authorizing Debtor Intrepid USA, Inc. to Enter into Insurance Contracts and Insurance Premium Finance Agreement (the “Motion”) and, in support hereof, respectfully states as follows:

**SUMMARY OF OBJECTION**

1. By their eleventh hour Motion, the Debtors seek authority, on an expedited basis, to enter into certain insurance contracts and to pay for such contracts with insurance premium financing because the Debtors have insufficient cash or borrowings under their DIP credit facility with CapitalSource Finance to pay the premiums in full. (Motion, ¶15.) The Debtors seek authority to grant the proposed finance company a first priority lien on the financed insurance premium payments by contending that such property of the estate is unencumbered and not otherwise subject to a lien.<sup>1</sup>

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<sup>1</sup> According to the Debtors’ Motion, in the event of default under the applicable premium financing agreement, the premium finance companies would have the right to cancel the policy and receive and apply any returned premium to the loan. (Motion, ¶ 16.)

2. CapitalSource Finance objects to the terms of the proposed insurance premium financing arrangement on three primary grounds. First, CapitalSource Finance already has a prior valid, perfected, first priority security interest in and blanket lien upon all of the Debtors' assets, including the financed insurance premium payments, which are clearly "general intangibles" covered by CapitalSource's blanket lien. Second, the terms and conditions of the DIP Credit Agreement (as defined herein) prohibit the Debtors' attempt to incur the indebtedness contemplated by the insurance premium financing arrangement absent a waiver from CapitalSource Finance. Third, the terms and provisions of the Final DIP Financing Order (as defined herein) and the DIP Credit Agreement prohibit the Debtors from granting to any finance company any lien (and not just a priming lien) on the financed insurance premium payments absent CapitalSource Finance's consent. While CapitalSource Finance has endeavored to negotiate the necessary waiver and consents requested by the Debtors on extremely short notice, it has been unable to reach an agreement with the Debtors as of the filing of this Limited Objection.

### **BACKGROUND**

3. The petitions commencing the Debtors' cases were filed on January 29, 2004 and April 12, 2004. These cases are now pending in this Court. The Debtors continue to operate their business as debtors-in-possession under sections 1107(a) and 1108 of the Bankruptcy Code. The Court has ordered, for procedural purposes only, joint administration of the Chapter 11 cases.

4. On April 29, 2004, the Debtors and CapitalSource Finance entered into that certain Post-Petition Revolving Credit and Security Agreement (as amended, the "DIP Credit Agreement"), subject to the terms and conditions of which CapitalSource Finance agreed to make certain loans and other financial accommodations to the Debtors.

5. On April 30, 2004, this Court approved the terms and conditions of the DIP Credit Agreement and entered that certain Final Order Authorizing Debtors to Enter Into Post-Petition

Financing Agreement and Obtain Post-Petition Financing Pursuant to Sections 105, 362 and 364 of the Bankruptcy Code, and Granting Liens, Security Interests and Superpriority Claims (the “Final DIP Financing Order”).

6. On Tuesday, October 28, 2004, the Debtors filed their Motion and provided CapitalSource Finance with service thereof. A hearing on the Motion is presently scheduled for Thursday, September 30, 2004 at 2:30 p.m.

### ARGUMENT

**A. CapitalSource Finance Has a Valid, Perfected, First Priority Security Interest in and Lien on the Debtors’ General Intangibles, which Includes any Contractual Rights under the Debtors’ Insurance Policies, including the Return of Unearned Premiums.**

7. In their Motion and supporting memorandum, the Debtors seek to grant the proposed finance company a lien on the financed insurance premium payments by contending that such property of the estate is unencumbered and not otherwise subject to a lien. The Debtors are wrong. CapitalSource Finance already has a prior valid, perfected, first priority security interest in and blanket lien upon all of the Debtors’ assets, including the financed insurance premium payments, which are clearly “general intangibles” covered by CapitalSource Finance’s blanket lien.

8. Pursuant to Section 2.9 of the DIP Credit Agreement, the Debtors granted CapitalSource Finance a continuing security interest in and blanket lien (the “DIP Liens”) upon all of the Debtors’ “now owned or hereafter acquired” assets to secure the indebtedness under the DIP Credit Agreement, including without limitation, “all present and future” “General Intangibles (including, without limitation, . . . contract rights, . . . )” and “insurance proceeds,” as set forth in greater detail therein (the “Collateral”). CapitalSource Finance’s DIP Liens were deemed perfected by operation of law upon entry of the Final DIP Financing Order. (Final DIP Financing Order, ¶ 13(a).)

9. Debtors often grant security interests in policies of insurance by, among other things, granting security interests in their “general intangibles,” including “contract rights.” Moreover, bankruptcy and district courts applying state law have long considered unearned insurance premiums to be general intangibles. In re Megamarket of Lexington, Inc., 207 B.R. 527, 533 (Bankr. E.D.Ky. 1997) (“A prepaid insurance account, i.e., the right to receive a refund of an unearned insurance premium, is a ‘chase in action’ or a ‘thing in action,’ which falls under the category of a general intangible.”); In re Matter of Maplewood Poultry Co., 2 B.R. 550, 554 (Bankr. D. Me. 1980) (“the collateral is not the insurance policies themselves, but the unearned premium, a general intangible”); In re Gross-Feibel Co., Inc., 21 B.R. 648 (Bankr. S.D. Ohio 1982); Duke Roofing Co., Inc., 47 B.R. 990, 992 (E.D. Mich. 1985); Budget Premium Co. v. American Casualty Co., 483 N.E.2d 389, 391 (Ill. App. Ct. 1985.) This case is no exception.

10. The Debtors clearly assigned to CapitalSource Finance their interests in general intangibles, which includes insurance policies (and their proceeds) and any and all contractual rights thereunder, including without limitation the right to the return of unearned insurance premiums under such policies. Accordingly, the Debtors’ attempt to grant a finance company a priming lien on any financed insurance premium payments pursuant to 11 U.S.C. § 364(c)(2) by arguing, incorrectly, that such premiums are unencumbered property of the estate must fail. Any security interest in the financed premium payments would be subordinate in rights, interest and payment to CapitalSource Finance’s DIP Liens.

**B. The Debtors Must Obtain a Waiver from CapitalSource Finance to Incur the Additional Indebtedness Contemplated by the Insurance Premium Financing**

11. The Debtors contend that the proposed premium financing agreements are “in the ordinary course of their business and, therefore, Court approval is not necessary.” (Motion, ¶ 20.) Such contention is belied by the clear and unambiguous terms of the DIP Credit Agreement, which prohibits the Debtors’ attempt to incur the indebtedness contemplated by the premium

financing arrangement absent a waiver from CapitalSource Finance. (DIP Credit Agreement, § 7.2.)

12. Pursuant to Section 7.2 of the DIP Credit Agreement, the Debtors covenanted and agreed that, until full performance and satisfaction, and indefeasible payment in full in cash, of all of the obligations under the DIP Credit Agreement, they shall not create, assume or suffer to exist any additional indebtedness except for the specifically enumerated exceptions of “Permitted Indebtedness.” Section 7.2(vi) permits the borrower to incur borrowings in the ordinary course of business not to exceed \$150,000 in the aggregate outstanding at any one time and mandates that any such permitted borrowings be on an unsecured basis, subordinated to the right of repayment and remedies to all of the obligations and to all of CapitalSource Finance’s rights pursuant to a subordination agreement in form and substance satisfactory to CapitalSource Finance. Assuming arguendo that the proposed premium financing is incurred in the ordinary course of business, such proposed financing arrangement far exceeds the permitted amounts, if any, under the DIP Credit Agreement and impermissibly attempts to grant a priming lien on CapitalSource Finance’s interest in such Collateral – a clear breach of the Debtors’ negative covenants under the DIP Credit Agreement and a violation of the Final DIP Financing Order. Accordingly, the proposed premium financing arrangement is prohibited absent a limited waiver from CapitalSource Finance of the relevant negative covenants.

**C. The Debtors Cannot Grant to the Finance Companies a Priming Lien on the Financed Premium Payments Absent CapitalSource Finance’s Consent**

13. The Debtors cannot grant to any finance company any lien on any of CapitalSource Finance’s Collateral, including the premium finance payments, absent CapitalSource Finance’s consent. Pursuant to Section 7.3 of the DIP Credit Agreement, the Debtors covenanted and agreed “not to create, incur, assume or suffer to exist any Lien upon, in or against, or pledge of any of the Collateral . . . , whether now owned or hereafter acquired . . . .” Therefore, any attempt by the Debtors to unilaterally grant or create any lien upon the proposed

premium finance payments is a clear breach by the Debtors of their negative covenant under the Section 7.3 of the DIP Credit Agreement and a violation of the Final DIP Financing Order.

14. In addition, the Debtors cannot grant to any finance company a priming lien on the financed insurance premium payments absent CapitalSource Finance's consent. Pursuant to Paragraph 6(b) of the Final DIP Financing Order, the Debtors acknowledged and agreed "that until such time that all DIP Obligations are indefeasibly paid in full, in cash, and the Revolving Facility is terminated in accordance with the terms of the DIP Loan Agreement, the Debtors shall not in any way prime or seek to prime (i.e., cause to be subordinated) the liens provided to [CapitalSource Finance] under this Final Order by offering a subsequent lender or any party-in-interest a superior or pari passu lien, interest or claim pursuant to section 364(d) of the Bankruptcy Code or otherwise."

15. Moreover, Section 7.2 of the DIP Credit Agreement provides that any permitted borrowings by the Debtors "shall be on an unsecured basis, subordinated to the right of repayment and remedies to all of the obligations and to all of [CapitalSource Finance's] rights pursuant to a subordination agreement in form and substance satisfactory to [CapitalSource Finance]."

16. The Debtors have attempted to circumvent both the Final DIP Financing Order and terms and conditions of the DIP Credit Agreement, which prohibit the incurrence of the proposed premium financing and the priming lien, by arguing that the financed insurance premiums are unencumbered property. As explained above, the financed insurance premiums would be encumbered because the Debtors have already granted CapitalSource Finance a prior valid, perfected, first-priority security interest in and blanket lien upon the Debtors' then-owned or thereafter acquired general intangibles, which includes the financed premium payments.

17. Finally, as a policy matter, the position urged by the Debtors is troubling. While the Debtors do not assert in the Motion that they seek to grant the finance company a purchase money security interest, the net effect of their proposed grant of a security interest would have

that same impact given CapitalSource Finance's prior DIP Liens. However, purchase money security interests can be granted solely in goods and software, not general intangibles, a requirement that neither the Debtors nor the finance company can meet. Moreover, the Debtors' presumed equitable argument that it should be entitled to grant a priming security interest to the finance company in insurance premiums which it financed is no different than a trade creditor hopelessly arguing that it should be able to recover, in a reclamation action, the products it supplied, and there is no dispute that a secured lien trumps a reclamation claim in the same collateral. In re Phar-Mor, Inc., 301 B.R. 482, 495 (Bankr. N.D. Ohio 2003).

18. To the extent the Debtors obtain the necessary consents and waivers from CapitalSource Finance to borrow the contemplated insurance premium payments, any security interest created or granted to the financing company in the unearned financed insurance premium payments must be subject to and inferior to CapitalSource Finance's Liens and such finance company shall be entitled to payment from such collateral only after CapitalSource Finance's Liens are satisfied in full.

### **CONCLUSION**

19. The Debtors' assignment to CapitalSource Finance of its interest in general intangibles, including insurance policies and their proceeds and contract rights, became valid, perfected, and enforceable as of the entry of the Final DIP Financing Order, much earlier than the Debtors' contemplated assignment of its interest in the same collateral to a finance company. The DIP Credit Agreement clearly prohibits the Debtors from incurring the indebtedness contemplated by the proposed insurance premium financing agreements. The Final DIP Financing Order further prohibits the Debtors from granting to any finance company any lien, whether a priming or subordinate lien, on the financed insurance premium payments.

20. While CapitalSource Finance has endeavored to negotiate the necessary waivers and consents requested by the Debtors with respect to the contemplated insurance premium financing on extremely short notice, it has been unable to reach agreement with the Debtors on

these issues as of the filing of this Limited Objection. Absent such an agreement, CapitalSource Finance reserves all of its rights and remedies under the DIP Credit Agreement, the Final DIP Financing Order, and the DIP Loan Documents as well as the right to submit supplemental written objections to the Court with respect to the Motion and gives notice that it may call a representative of the Debtors to testify at any hearing on said Motion.

Dated: September 29, 2004

Respectfully submitted,

KATTEN MUCHIN ZAVIS ROSENMAN  
Kenneth J. Ottaviano, Esq. (IL 06237822)  
Jeffrey L. Elegant, Esq. (IL 3124280)  
Jeffrey A. Chadwick, Esq. (IL 6274686)  
525 West Monroe, Suite 1800  
Chicago, Illinois 60661  
Telephone: (312) 902-5200

RIDER BENNETT LLP

By: /e/ Steven J. Kluz, Sr.  
Steven J. Kluz, Sr., Esq. (MN 56765)  
333 South Seventh Street  
Suite 2000  
Minneapolis, MN 55402

Attorneys for CapitalSource Finance LLC

UNITED STATES BANKRUPTCY COURT  
DISTRICT OF MINNESOTA

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In re:

Chapter 11 Bankruptcy

**INTREPID U.S.A., INC.**  
**INTREPID OF GOLDEN VALLEY, INC.**  
**F.C. ACQUISITION CORPORATION,**

Debtors.

BKY No.: 04-40416  
BKY No.: 04-40462  
BKY No.: 04-40418  
Bky Nos. 04-41924 – 04-41988

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**UNSWORN CERTIFICATE OF SERVICE**

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I, Daniel J. McGarry, declare under penalty of perjury that on September 29, 2004, I served a copy of the LIMITED OBJECTION OF CAPITALSOURCE FINANCE LLC TO MOTION FOR ORDER GRANTING EXPEDITED HEARING AND AUTHORIZING DEBTOR INTREPID USA, INC. TO ENTER INTO INSURANCE CONTRACTS AND INSURANCE PREMIUM FINANCE AGREEMENT by facsimile on the following entities:

Mike Fadlovich  
U.S. Trustee's Office  
1015 US Courthouse  
300 South Fourth Street  
Minneapolis, MN 55415  
612-664-5516

Clint Cutler, Esq.  
Fredrickson & Byron  
1100 International Centre  
900 Second Avenue South  
Minneapolis, MN 55402-3397  
612-492-7077

George H. Singer, Esq.  
Lindquist & Vennum  
4200 IDS Center  
80 South 8th Street  
Minneapolis, MN 55402  
612-371-3207

Jeffrey K. Garfinkle  
Paul S. Arrow  
Buchalter, Nemer, Fields & Younger  
895 Dove Street, Suite 400  
Newport Beach, CA 92660-2917  
949-720-0182

RIDER BENNETT, LLP

By \_\_\_\_\_ /e/ Daniel J. McGarry \_\_\_\_\_  
Daniel J. McGarry

333 South Seventh Street  
Suite 2000  
Minneapolis, MN 55402  
(612) 340-7978

Dated: September 29, 2004