

**IN THE UNITED STATES DISTRICT COURT  
FOR THE SOUTHERN DISTRICT OF TEXAS  
HOUSTON DIVISION**

<b>SECURITIES AND EXCHANGE</b>	§
<b>COMMISSION,</b>	§
<b>Plaintiff,</b>	§
	§
<b>v.</b>	§
	§
<b>ALBERT FASE KALETA and KALETA</b>	§
<b>CAPITAL MANAGEMENT, INC.,</b>	§
<b>Defendants,</b>	§
	§
<b>and</b>	§
	§
<b>BUSINESSRADIO NETWORK, L.P.,</b>	§
<b>d/b/a BizRadio and DANIEL FRISHBERG</b>	§
<b>FINANCIAL SERVICES, INC., d/b/a</b>	§
<b>DFFS CAPITAL MANAGEMENT, INC.,</b>	§
<b>Relief Defendants,</b>	§
<b>Solely for the purposes</b>	§
<b>of Equitable Relief.</b>	§

**Case No. 4:09-cv-3674**

**RESPONSE TO INVESTORS' OBJECTION TO SALE OF RADIO STATION ASSETS  
AND MOTION FOR CONTINUANCE OF CONFIRMATION HEARING**

South Texas Broadcasting, Inc. ("STB"), a party-in-interest and the Winning Bidder<sup>1</sup> to purchase the Station under the Sale Procedures Order (as defined below), files this response to Investors' Objection to Sale of Radio Station Assets and Motion for Continuance of Confirmation Hearing (the "Objection").

**I. SUMMARY OF RESPONSE**

The Court should enter an order confirming the sale of Station to STB free and clear of all liens, claims, encumbrances and interests because the sale to STB serves the best interests of

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<sup>1</sup> Capitalized terms that are not defined in this Response shall have the meaning ascribed to such terms in the Motion for Entry of Orders (I) Approving Bidding Procedures and Notice for the Sale of Radio Station Assets, (II) Approving Sale of Radio Station Assets Free and Clear of All Liens, Claims Encumbrances and Interests, and (III) Approving Compromise of Controversies and Partial Distribution of Sale Proceeds (the "Sale Motion"), the Sale Procedures Order or the Modified Sale Agreement.

the Receivership Estate and is the result of a robust sale process designed to maximize the value to the Receivership Estate. The Receiver crafted commercially reasonable sale procedures approved by this Court in its Sale Procedures Order<sup>2</sup> to enable potential purchasers in the commercial broadcast market to purchase the Station. Any potential purchaser, including the Investors, could become a Qualified Competing Bidder and submit a Topping Bid that surpassed STB's stalking horse bid. The sale procedures included a mechanism for a public auction to establish the market value for the Station in the event timely Topping Bids were submitted. No one became a Qualified Competing Bidder, so the Receiver did not conduct an Auction and the Receiver has accepted the STB stalking horse bid to purchase the Station.

As described below, the late purported Topping Bid from certain of the Investors does not comply with the terms of the Sale Procedures Order. Additionally, the Investors' purported Topping Bid, which consists solely of an offer by the Investors to cancel certain notes purportedly secured by Station assets<sup>3</sup>, is devoid of any consideration for the purchase of the Station. Contrary to the allegation that certain Investors are "Priority Secured Noteholders" that hold first priority liens on the Station assets, none of the Investors hold any duly perfected, valid or enforceable liens against the Station assets, and do not have any priority over the duly perfected, valid and enforceable liens that STB holds against the Station assets. Therefore, the purported Topping Bid has no value.

As set forth below, the Investors, working through an entity controlled by Messrs. Wallace and Bajjali, claim that they loaned funds to an entity referred to as "Biz Radio" (an entity that has no formal existence). No financing statements were filed in any filing office

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<sup>2</sup> Modified Order Approving Sale Procedures, Fixing Deadlines and Setting Hearing on Sale of Radio Station KTEK Free and Clear of all Liens, Claims, Encumbrances and Other Interests, Approving Compromise and Related Relief entered April 4, 2011 ("Sale Procedures Order").

<sup>3</sup> The Investors have no actual security interest in the Station assets, as explained in this Response.

on behalf of the Investors in order to perfect a security interest in the Station assets and thereby give notice of a security interest in such assets as required by the Texas Business & Commerce Code (the "Texas UCC"). The Investors' loan documents show that any claims they hold are only against Biz Radio Network, LP, an entity that does not own the Station assets or broadcast license. Moreover, as described below, the Investors' claim that they provided "Replacement Financing" under the terms of a Subordination Agreement to which STB, BusinessRadio Houston LLC and Wallace Bajjali Investment Fund II, L.P. are parties fails because there is not an identity of parties, or collateral, and more importantly, the Investors' loans do not comply with the terms for obtaining Replacement Financing status under the Subordination Agreement. Finally, the Investors' claims, if any, are subordinate to STB's interest because they were created after STB made its loan to BusinessRadio Houston LLC and were never perfected through the filing of a financing statement.

For all these reasons, STB submits that the Court should overrule the Objection, deny any further continuance of the sale hearing, and enter an order confirming the sale to STB free and clear of all liens, claims, encumbrances and other interests.

## **II. RULE 8 RESPONSES TO OBJECTION**

1. No response is required to the allegations in paragraph one of the Objection because they are statements summarizing the Investors' objections to the sale. To the extent a response is required, STB denies the allegations in paragraph one as to the reasonableness of the consideration being paid for the Station. Among the Receiver's duties is to maximize the value of the Receivership Estate for the benefit of investors and creditors. STB understands that the Receiver engaged in a thorough process to realize the greatest value for the Station in the marketplace. Toward that end, a material condition that the Receiver insisted on during

negotiations to sell the Station to STB was that other parties would have an opportunity to make higher bids to buy the Station by submitting a Topping Bid and becoming a Qualified Competing Bidder. The Receiver also crafted the sale procedures to allow for a public auction to maximize value to the Receivership Estate. To STB's knowledge, the Receiver complied with all notice and publication requirements under the Sale Procedures Order, and undertook additional efforts to contact potential buyers and radio station brokers. Finally, the Receiver published notice of the opportunity to purchase the Station in recognized industry trade publications.

2. STB denies the allegations in paragraphs two and three. As explained in greater detail in this Response, the self-described "Priority Secured Noteholders," as a matter of law, do not hold duly perfected, valid or enforceable security interests in, or liens on, the Station assets. As a result, the Receiver's request to sell the Station to STB free and clear does not impair the interests of the "Priority Secured Noteholders" or any of the Investors.

3. STB denies the allegations in the first sentence of paragraph four and submits that the Investors' purported Topping Bid described in paragraph four does not comply with the Sale Procedures Order because it was untimely, does not include a \$250,000 cash deposit, or provide evidence reflecting that the Investors meet applicable FCC ownership requirements, and therefore the Investors should not be considered a Qualified Competing Bidder. Moreover, the purported Topping Bid is devoid of any consideration because the debt the Investors propose to cancel to pay for the Station is not secured by the assets being sold. No response is required to the remainder of paragraph four because they are statements of the relief requested by the Investors. STB opposes any additional lengthy continuance to allow the Investors additional time to consider making an untimely offer or conduct due diligence because ample time has been provided to all parties, including the Investors, to submit Topping Bids and to become Qualified

Competing Bidders as provided by the Sale Procedures Order. The Investors failed to follow this Court's procedures by conducting due diligence and making an offer during the time period provided in the Sale Procedures Order, and there is no reason to continue the hearing solely due to the Investors' failure to abide by this Court's order. In addition, further delay would likely cause the existing approval by the Federal Communications Commission ("FCC") of the transfer of the broadcast license by the Receiver to STB to expire. The Receiver has sought and received several extensions from the FCC to postpone the transfer of the broadcast license as a result of this SEC Action and the Receiver's efforts to maximize value through the sale process. FCC counsel for the Receiver has advised STB that the FCC staff has provided no assurance that the FCC will grant any further extension of the July 22, 2011 deadline to file a Notice of Consummation. In such event, the Receiver will be required to restart the lengthy process required to obtain FCC approval of an assignment to STB of the broadcast license. Any further continuance should therefore be denied.

4. STB denies the allegations in paragraph five. Sale of the Station will benefit the Receivership Estate and generate funds for distribution to investors and creditors of the Receivership Estate.

5. STB denies the allegations in paragraphs six and seven insofar as they reflect incorrect statements of the parties and transactions through the loose use of the term "Biz Radio." The Sale Motion provided a precise explanation of the transaction and parties involved in the purchase of the Station to which the Investors have not responded under Rule 8 of the Federal Rules of Civil Procedure, and such allegations are therefore deemed admitted and binding on the Investors. FED. R. CIV. P. 8.

6. The Subordination Agreement referred to in paragraph eight is the best and only evidence of its contents and STB denies all remaining allegations in paragraph eight.

7. STB denies the allegations in paragraph nine.

8. STB admits the allegations in paragraph 10 for the limited purpose of the names, purported note amounts and exhibit numbers to the Objection, but denies that any of the "Priority Secured Noteholders" hold duly perfected, valid or enforceable security interests in, or liens on, the assets to be sold to STB, and lacks information or knowledge to confirm that the Investors actually advanced funds or hold such notes.

9. STB admits the allegations in the first sentence of paragraph 11 and further states that the document is the best and only evidence of its contents. STB denies the remaining allegations in paragraph 11. The Investors' effort to "piggyback" on the financing statement filed by Wallace Bajjali Investment Fund II, L.P. is misplaced and fails as a matter of law, as explained below.

10. STB admits the allegations in paragraphs 12 and 13 insofar as one element of the Purchase Price includes STB's release of its \$1.5 million secured claim owed by BusinessRadio Houston LLC, as the owner of the Station assets being sold. STB denies all remaining allegations in paragraphs 12 and 13.

11. STB lacks sufficient knowledge or information to admit or deny the allegations in paragraph 14; accordingly, they are denied.

12. No response is required to the allegations in paragraph 15 as they are statements of the relief requested.

13. STB denies the allegations in paragraph 16. STB submits that the purported Topping Bid from the "Priority Secured Noteholders" fails to comply with the requirements for

submission of a Topping Bid or for the Investors becoming a Qualified Competing Bidder under the requirements in the Sale Procedures Order and denies that the proposed consideration has any value to the Receivership Estate.

14. STB denies that Investors are entitled to the relief requested in paragraph 17.

### **III. ARGUMENT AND AUTHORITIES**

#### **A. Factual Background**

The Sale Motion seeks to sell assets listed in the Modified Sale Agreement which are owned by BusinessRadio Houston LLC, a Texas limited liability company, and to transfer the FCC broadcast license issued to BusinessRadio Houston Licensee LLC, a Texas limited liability company ("BusinessRadio Licensee") (BusinessRadio Houston LLC and BusinessRadio Licensee are collectively referred to as the "Sellers").

The entity that the Investors loosely refer to as "Biz Radio" and indentified as Biz Radio Network, LP in the Investors' loan documents does not own anything related to the Station assets. Ownership of the Station license and interests of other entities in the license owner are reflected in ownership reports required by the FCC.<sup>4</sup> Neither "Biz Radio" nor Biz Radio Network, LP is shown in any of these reports as having an interest in an entity that has an interest in the license.

Ownership of the assets by the Sellers traces back to the March 2008 transaction by which BusinessRadio Houston LLC and BusinessRadio Licensee acquired the Station and license, respectively, from STB. In connection with the purchase, BusinessRadio Houston LLC obtained \$4,000,000 in financial accommodations from Wallace Bajjali Investment Fund II, L.P. ("Wallace Bajjali Fund II"), in its capacity as the Administrative Agent for Industrial Info

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<sup>4</sup> Copies of the applicable FCC 323 Ownership Report for Commercial Broadcast Stations are attached as **Exhibits 1 to 5** in the Appendix to this Response.

Resources, Inc. The financial accommodations were memorialized in loan documents dated March 28, 2008 including: (A) a Senior Secured Promissory Note in the amount of \$4,000,000, (B) a Security Agreement by and between BusinessRadio Houston LLC and Wallace Bajjali Fund II, (C) a Subordination and Intercreditor Agreement by and among, Industrial Info Resources, Inc., as Initial Senior Lender, Wallace Bajjali Fund II, as Administrative Agent, and STB, as Subordinate Lender, and (D) a UCC Financing Statement filed on March 28, 2008 with the Delaware Department of State UCC Filing Section under file no. 20081103686, in favor of Wallace Bajjali Fund II, covering the Station assets as collateral, but not the broadcast license.<sup>5</sup>

Subordinate loan documents memorializing the financial accommodations from STB to BusinessRadio Houston LLC dated March 28, 2008 included: (A) Promissory Note A in the amount of \$1,750,000 from BusinessRadio Houston LLC, as borrower, to STB, as lender, (B) Promissory Note B in the amount of \$1,500,000 from BusinessRadio Houston LLC, as borrower, to STB, as lender, (C) a Security Agreement by and between BusinessRadio Houston LLC and STB, and (D) a UCC Financing Statement filed on March 28, 2008 with the Delaware Department of State UCC Filing Section under file no. 20081095627, and a UCC Financing Statement filed on March 28, 2008 with the Texas Secretary of State under file no. 08-0012803686, with each financing statement naming BusinessRadio Houston LLC as

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<sup>5</sup> BusinessRadio Houston Licensee LLC owns the broadcast license, not BusinessRadio Houston LLC or BusinessRadio Network, LP. The FCC has consistently held that a broadcast license may not be encumbered by a mortgage, lien, pledge or lease. *See In re Application of Radio KDAN, Inc.*, 11 F.C.C.2d 934, *recon. denied*, 13 R.R.2d 100 (1968), *aff'd on procedural grounds sub nom., Hansen v. FCC*, 413 F.2d 374 (D.C. Cir. 1969), and *In re Applications of Kirk Merkely, Receiver*, 94 F.C.C.2d 829 (1983), *recon. denied*, 56 R.R.2d 413 (1984), *aff'd sub nom., Merkely v. FCC*, 776 F.2d 365 (D.C. Cir. 1985). The FCC stated, "no right of reversion can attach to a broadcast station license, and the license, as distinguished from a station's physical assets, is not subject to a mortgage, security interest, or lien." *Merkely*, 56 R.R.2d at 416. The rationale for this principle is that the license belongs to the government and such an encumbrance endangers the independence of the licensee who must be at all times responsible and accountable to the FCC.

debtor and STB as secured party, covering the Station assets, but not the broadcast license, as collateral.<sup>6</sup>

The Receiver has advised STB that he has investigated the assets and liabilities of BusinessRadio Houston LLC and reviewed its business and financial records and has confirmed with counsel for Industrial Info Resources, Inc. that all payments owing under the Senior Secured Promissory Note had been paid in full and that no further obligations remain under the loan documents. The Receiver has further determined that all obligations owing to STB under Note A have been paid in full, and that the obligations owing to STB under Note B remain due and payable.

STB is unaware of any other liens, claims, encumbrances or other interests in the Station assets by any other parties, and disputes any further claims of Wallace Bajjali Fund II, or the claims of the objecting Investors, to a duly perfected security interest in, or lien on, the Station assets, or any further rights to have a lien on proceeds from the sale of the Station assets and transfer of the broadcast license. Finally, the Receiver has not advised STB that he is aware of any other duly perfected liens, claims, encumbrances or other interests in the Station assets or the license by any other parties other than certain taxing authority claims described in the Modified Sale Agreement.<sup>7</sup>

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<sup>6</sup> Copies of STB's financing statements filed with the Texas and Delaware Offices of Secretary of State are attached as **Exhibits 6 and 7** to the Appendix.

<sup>7</sup> Attached as **Exhibits 8 and 9** to the Appendix are certificates from the Texas Office of Secretary of State certifying that the financing statement naming STB as secured party and BusinessRadio Houston LLC as debtor is the only financing statement that has been filed and from the Delaware Office of Secretary of State certifying that the financing statements naming STB and Wallace Bajjali Fund II as secured parties and BusinessRadio Houston LLC as debtor are the only financing statements that have been filed.

**B. The Investors Made Loans to Wallace Bajjali Development Partners, L.P. and/or Biz Radio Network, LP**

According to the loan documents attached to the Objection, the Investors purported to provide loans to Wallace Bajjali Development Partners, L.P., a Texas limited partnership, or Biz Radio Network, LP, a Texas limited partnership, as the borrower(s). *See* Exhibits 3-20 to the Objection. Each note is payable either to the order of an individual payee, or Wallace Bajjali Development Partners, L.P., a Texas limited partnership, as Agent for the individual payees as lender to Biz Radio Network, LP. Security agreements from Biz Radio Network, LP to Wallace Bajjali Development Partners, L.P. and/or certain of the borrowers purport to grant the lenders security interests in the collateral described in those security agreements. Despite bargaining for a security interest in favor of the Investors, neither the Investors in their individual capacities, nor Wallace Bajjali Development Partners, L.P., as agent, took action to perfect security interests by filing financing statements with either the Texas or Delaware Secretary of State naming Biz Radio Network, LP as debtor.<sup>8</sup>

**C. The Investors do not have duly perfected, valid or enforceable security interests in, or liens on, the Station assets**

1. The Investors have not filed financing statements

The framework of Article 9 reflects a series of bright-line rules to provide commercial certainty, commercial efficiency, commercial reliance and promote the flow of commerce. *See* BARKLEY CLARK, THE LAW OF SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE, ¶ 3.01 at 3-1 (3d ed. 2010). Financing statements are critical instruments for purposes of perfection of a creditor's lien rights under the comprehensive notice filing framework of Article 9

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<sup>8</sup> Attached as **Exhibits 10 and 11** to the Appendix are certificates from the Delaware and Texas Offices of Secretary of State certifying that no financing statements naming "Biz Radio Network, LP" have been filed of record.

of the Texas UCC. The fundamental principle of secured transactions is that "a financing statement must be filed to perfect all security interests" unless there is an exception (such as possession or control), none of which apply to this case. Texas UCC § 9.310(a).

The Investors' loan documents name "Biz Radio Network, LP, a Texas limited partnership" as the debtor. Putting aside for the moment that Biz Radio Network, LP, a Texas limited partnership, does not exist as a registered entity, none of the Investors or Wallace Bajjali Development Partners, L.P., as agent, has filed financing statements. Without a filed financing statement, the objectors do not hold a perfected security interest under the Texas UCC and do not have priority over a creditor that has filed a financing statement.

2. Any financing statement filed by the Investors would be ineffective

A financing statement is sufficient to perfect a security interest in collateral only if it: 1) *provides the name of the debtor*; 2) provides the name of the secured party or a representative of the secured party; and 3) indicates the collateral covered by the financing statement. Texas UCC § 9.502(a)(1)-(3) (emphasis added). Section 9.503(a)(1) of the Texas UCC confirms that a financing statement sufficiently provides the name of a debtor, "if the debtor is a registered organization, only if the financing statement provides the name of the debtor indicated on the debtor's formation documents that are filed of public record in the debtor's jurisdiction of organization . . ." Comment 2 to Section 9.503 of the Texas UCC explains, "[t]he requirement that a financing statement provide the debtor's name is particularly important. Financing statements are indexed under the name of the debtor, and those who wish to find financing statements search for them under the debtor's name."

In any case, had the Investors filed a financing statement naming "Biz Radio Network, LP", it would be ineffective to create a security interest in Station assets. The Investors' loan

documents name "Biz Radio Network, LP, a Texas limited partnership" as the debtor. Biz Radio Network, LP, a Texas limited partnership, does not exist according to the records of the Texas and Delaware Offices of Secretary of State.<sup>9</sup> Thus, any financing statement that would name Biz Radio Network, LP as the debtor, even if filed, would be insufficient to perfect a security interest in collateral.

3. No minor error exists to make any financing statement, even if filed, sufficient

The Investors may not claim that use of the name "Biz Radio" is a minor error that might otherwise support an effective financing statement. Section 9.506(a) of the Texas UCC contemplates that a financing statement that substantially satisfies the requirements of UCC Article 9 will be effective, even if there are minor errors or omissions, unless the errors or omissions make the financing statement seriously misleading. A financing statement that fails sufficiently to provide the name of the debtor as required by Section 9.503(a) is "seriously misleading." Texas UCC § 9.506(b).

The actual registered entity closest in name to the Biz Radio Network, LP debtor named in the Investors' loan documents is BusinessRadio Network, LP, a Texas limited partnership. Assuming that the name "Biz Radio" is a trade name for BusinessRadio Network, LP, "a financing statement that provides only the debtor's trade name does not sufficiently provide the name of the debtor." Texas UCC § 9.503(c). *See generally, In re Jim Ross Tires, Inc.*, 379 B.R. 670 (Bankr. S.D. Tex. 2007) (J. Isgur). If a search of the records of the filing office under the debtor's correct name, using the filing office's standard search logic, would disclose a financing statement that fails to sufficiently name the debtor as required by Section 9.503(a), the name provided does not make the statement seriously misleading. Texas UCC § 9.506(c). Thus,

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<sup>9</sup> Attached as **Exhibits 12 and 13** to the Appendix are certificates from the Offices of the Secretary of State of Texas and Delaware reflecting the non-existence of "Biz Radio Network, LP."

the name on the financing statement must be so similar to the debtor's correct name that searches of filing office records using standard search logic with the correct name will also disclose the filing under the incorrect name.

Again, no financing statement has been filed whatsoever. This is fatal to the Investors' case as there is no financing statement that will be disclosed in a search of the filing office records. Assuming that BusinessRadio Network, LP is the correct name of the debtor, a search for "BusinessRadio" in the records of the Texas Secretary of State using standard search logic would not return a financing statement that lists the debtor as "Biz Radio." Similarly, a search of the Texas and Delaware filing offices using the term "Biz Radio" does not turn up a financing statement naming "Biz Radio" as debtor. Thus, the use of "Biz Radio Network, LP" is seriously misleading and would be insufficient to allow the Investors to claim that they hold a perfected security interest even if a financing statement using that name had been filed. *See Jim Ross Tires*, 379 B.R. at 679 (illustrating the necessity of correctly naming the debtor so that a financing statement is not seriously misleading under Section 9.506(c)).

**D. The Investors Do Not "Stand in the Shoes" of the Interest Formerly Held by Wallace Bajjali Fund II**

Since the Investors failed to file their own financing statements, they argue that they now stand in the first priority "shoes" of Wallace Bajjali Fund II. The Investors argue that they should be considered "other senior lenders" under the financing statement filed by Wallace Bajjali Fund II to secure the Industrial Info Resources, Inc. loan to BusinessRadio Houston LLC. As explained below, the Investors are not "other senior lenders" under the financing statement. They are lenders to an entity foreign to the March 28, 2008 transaction.

1. The Investors do not have a perfected interest as "other senior lenders" under the financing statement filed by Wallace Bajjali Fund II

Wallace Bajjali Fund II filed a financing statement as administrative agent for Industrial Info Resources, Inc. (the original Senior Lender), and "other senior lenders." *See* Exhibit 1 to the Objection. Wallace Bajjali Development Partners, L.P. acted as agent for the Investors. *See* Exhibits 3-20 to the Objection. The records of the Texas Office of Secretary of State reflect that these two Wallace Bajjali entities have separate and distinct legal status.<sup>10</sup>

Neither Wallace Bajjali Development Partners, L.P., as agent, nor the Investors in their individual capacities, can base their position of being "Priority Secured Noteholders" on the financing statement filed by Wallace Bajjali Fund II, as agent for Industrial Info and "other secured parties." Section 9.502(a)(2) of the Texas UCC provides that a financing statement is effective only if it "provides the name of the secured party or a representative of the secured party." On its face, the Wallace Bajjali Fund II financing statement refers to its status as representative of Industrial Info, but does not specifically name the Investors as "other secured parties" as required by Section 9.502(a)(2) for the Investors to be able to rely on this financing statement. Similarly, the financing statement does not refer to Wallace Bajjali Development Partners, L.P., as agent or otherwise. Accordingly, the Investors do not hold perfected security interests as "other secured parties" because Wallace Bajjali Development Partners, L.P. is a separate entity from Wallace Bajjali Fund II, which does not serve as agent for Wallace Bajjali Development Partners, L.P., who is agent for the Investors.

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<sup>10</sup> Attached as **Exhibits 14 and 15** to the Appendix are certificates from the Texas Office of Secretary of State reflecting the separate certificates of formation for the two Wallace Bajjali entities.

2. The Investors do not hold perfected security interests where the secured parties are related or unrelated, because each secured party, or its representative, must file a separate financing statement that names the secured party or its representative

The Investors cannot overcome the absence of a financing statement that specifically names them or their representative based on the argument that Wallace Bajjali Fund II and Wallace Bajjali Development Partners, LP are related entities. An interest in collateral perfected in the name of one secured creditor is not perfected for the benefit of another creditor, even if the entities are related. The Fifth Circuit has held that a "related" entity cannot base its claim for perfection on a financing statement filed by a related entity under the UCC. *Matter of E.A. Fretz Co.*, 565 F.2d 366 (5th Cir. 1978). In *E.A. Fretz*, the court concluded that subsidiaries of a secured creditor could not rely on a financing statement filed by their parent company against the same debtor to claim priority over the claims of the bankruptcy trustee.

In *E.A. Fretz*, the parent company filed a financing statement as secured creditor in its name only. Later, two subsidiaries of the secured creditor obtained security interests from the same debtor but never filed financing statements. After the common debtor filed bankruptcy, the subsidiaries assigned their claims to their parent company that had filed a financing statement. *Id.* at 369. However, because neither of the subsidiaries was named as a secured party in the parent company's financing statement, the court concluded that the subsidiaries did not hold perfected security interests under the parent company's filed financing statement. *Id.* In reaching this conclusion, the Fifth Circuit refused to endorse the concept that the subsidiaries could become "an open-ended class of creditors with unsecured and unperfected interests who, after the debtor's bankruptcy, can assign their claims to a more senior lienor and magically secure and perfect their interests under an omnibus security agreement and financing statement." *Id.* The Fifth Circuit further explained that naming the secured party has consequences insofar as the

statute [formerly §9.402 now §9.502] does not allow for "secured party, and anyone in the world who subsequently assigned a claim to the secured party without ever filing a proper financing statement" and that "[p]lacing our imprimatur on floating secured parties would undercut 'Article Nine's perfection requirement (which) reflects a Code policy against secret security.'" *Id.* at 370-71.

Just as the related subsidiaries in *E.A. Fretz* could not rely on the financing statement of their parent company to claim a perfected security interest, none of the Investors can claim to hold perfected security interests in the Station assets by claiming that Wallace Bajjali Fund II and Wallace Bajjali Development Partners, L.P. are "related entities" and thereby rely on a financing statement that does not name them as a secured party and magically turn themselves into "floating secured parties."

STB had no knowledge of the purported loans made through Wallace Bajjali Development Partners, L.P. until it received Exhibits 3 to 20 of the Objection. Even if STB had knowledge, the Fifth Circuit teaches that prudent lenders that seek priority must file a financing statement because anything else would turn Article 9 on its head. "But knowledge cannot provide a substitute for creating valid security interests and perfecting them in accordance with Code provisions. Treating knowledge as controlling would turn Article 9 on its head." *E.A. Fretz*, 565 F.2d at 371.

Creditors that are "not related" also cannot piggyback on another named secured creditor's prior filed financing statement. In *In re Morgan*, 291 B.R. 795, 797 (Bankr. E.D. Tenn. 2003), a debtor purchased a vehicle that was financed through a lender that debtor granted a lien on the vehicle. The debtor refinanced the loan with a second lender that provided funds to the debtor to be used to satisfy the first lender's note. *Id.* The debtor later filed bankruptcy and

was involved in an automobile accident, after which she conveyed title to the vehicle to her insurance company, who paid the second lender in full satisfaction of its note. *Id.* The bankruptcy trustee demanded proof of the second lender's perfected security interest in the vehicle and argued that the second lender did not hold a perfected security interest and was therefore subordinate to the bankruptcy trustee's strong arm lien rights such that the insurance proceeds were property of the bankruptcy estate. *Id.* The second lender argued it was equitably subrogated to the perfected security interest of the first lender since its funds were used to pay off the claim of the first lender. *Id.* The bankruptcy court disagreed and found that the second lender was required to perfect its own interest and could not piggyback on the financing statement filed by the first lender. *Id.* at 803.

Here, the Investors cannot piggyback on the financing statement filed by Wallace Bajjali Fund II by claiming that they are "other secured lenders"; they are not perfected because they have never filed financing statements in their own names or through a representative in order to be effective under Article 9 of the Texas UCC.

The Investors cite Section 9.503(d) of the Texas UCC for the proposition that the statement "other senior lenders" in the Wallace Bajjali Fund II Financing Statement properly identifies the Investors. However, Section 9.503(d) deals only with failure to indicate the "representative capacity" of a secured party (e.g., stating "XYZ Bank" but failing to state "XYZ Bank, as Trustee"). The official comment to Section 9.503 explains:

3. **Secured Party's Name.** New subsection (d) makes clear that when the secured party is a representative, a financing statement is sufficient if it names the secured party, whether or not it indicates any representative capacity. Similarly, a financing statement that names a representative of the secured party is sufficient, even if it does not indicate the representative capacity.

Because the Investors have not filed a financing statement that specifically names either the Investors or Wallace Bajjali Development Partners, L.P., as agent, as required by Section 9.502(a)(2) of the Texas UCC, they do not hold a perfected interest in the Station assets and Section 9.503(d) does not apply.

A more recent case demonstrating the problem of "floating secured creditors" is *In re Adirondack Timber Entp., Inc.*, No. 08-12553, 2010 WL 1741378 (Bankr. N.D.N.Y. 2010). In *Adirondack Timber*, a debtor bought tractors from Deere & Company, who financed the transaction and entered into a security agreement. The debtor also had a revolving line of credit from Farm Plan, a wholly owned subsidiary of Deere & Company. *Id.* The security agreement signed by the debtor indicated it was to "secure the obligation evidenced by this contract and any other obligation that I may owe to [Deere] *or to [Deere's] affiliates*, I grant [Deere] a Security Interest in the Goods described..." *Id.* at 3 (emphasis added).

When the debtor filed bankruptcy, Farm Plan argued it was a secured creditor under the original security agreement because it was an "affiliate" of Deere & Company. *Id.* The court found that the Farm Plan was not expressly listed as a creditor under the security agreement and thus was not a secured creditor simply because it was an "affiliate" of the named Secured Creditor that had filed a financing statement. *Id.* Citing *E.A. Fretz*, the court confirmed that while the UCC contemplates "floating collateral" and "floating debt," it contains no provision for "floating creditors." *Id.* As such, the Investors cannot claim that Wallace Bajjali Development Partners, L.P., as their agent, hold a perfected security interest in the Station assets by relying on the financing statement filed by Wallace Bajjali Fund II. Failure to file a financing statement, let alone a correct one that meets all of the requirements of Article 9, is fatal to the arguments presented by the Investors.

3. The debtor that granted Wallace Bajjali Fund II a security interest is a different entity than the debtor that obtained loans from the Investors

The Investors hold an interest, if any, in the collateral of a different entity than BusinessRadio Houston LLC, the debtor listed in the March 28, 2008 UCC Financing Statement. The loan documents attached to the Objection reflect that the Investors made loans to Biz Radio Network, LP, a Texas limited partnership. This is an entity separate from the debtor listed in the initial Security Agreement, Financing Statement, and the Subordination Agreement, which all name BusinessRadio Houston LLC, a Delaware limited liability company, as the debtor. Therefore, the Investors have unperfected security interests in the assets of BusinessRadio Network, LP, assuming that it used the trade name Biz Radio Network, LP. As discussed in detail above, a debtor must be properly named for a financing statement to be effective. Texas UCC § 9.503(a). The Investors' security interests in the assets of another entity cannot be perfected by relying on a financing statement that names a different debtor. *Id.*

**E. No Replacement Financing Was Accomplished Under the Terms of the Subordination Agreement**

Although Section 6 of the Subordination Agreement provided a mechanism for Replacement Financing that might enjoy the original priority against the assets of BusinessRadio Houston LLC, no replacement financing was exercised in the manner provided by the Subordination Agreement. Section 6 of the Subordination Agreement states, in relevant part:

Borrower intends to obtain additional financing secured by the Shared Collateral and use the proceeds of such financing to, among other things, satisfy Borrower's obligations under the Subordinate Loan and under the Initial Senior Loan (the "**Replacement Financing**,"...)

*See* Exhibit 2 to the Objection. The "Borrower" under the Subordination Agreement, BusinessRadio Houston LLC, never obtained any additional financing. The Investors appear to have loaned funds to the entity Biz Radio Network, LP through Wallace Bajjali Development

Partners, L.P. The Investors bear the burden of proof that they have priority, which is not supported by the Investors' instruments.

Section 6 of the Subordination Agreement provided a mechanism to allow for amendment of the Subordination Agreement to include additional Senior Lenders.

Upon request of the lender that intends to provide Replacement Financing, Subordinate Lender and each existing Senior Lender in good faith shall enter into an addendum, amendment or replacement of this Agreement to reflect the addition of such lender as a Senior Lender and the inclusion of such Replacement Financing as a Senior Loan for all purposes hereunder, provided that Subordinate Lender shall be under no obligation to execute and deliver subordination documents that contain commercially unreasonable terms.

No amendments have been provided to BusinessRadio Houston LLC or STB to indicate that replacement loans entitled to priority were ever affected. Notice of any such additional loans to STB was a material element of the agreement given the opportunity for other senior debt to subordinate the interests of STB. The notice procedure avoids the type of claims the Investors now advance.

Indeed, in *E.A. Fretz*, the Fifth Circuit anticipated the problems that might confront a junior secured creditor like STB that must deal with the uncertainty associated with purported floating secured creditors:

Surely floating debt and floating collateral provide all of the uncertainty any creditor should be required to suffer. When floating secured parties are wading in the wings, clairvoyance, not mere knowledge, would be essential. We are unwilling to impose on any junior secured creditor, with knowledge or without, the additional risk that, at a date subsequent to his perfection, any affiliate of the senior creditor or any stranger to it unnamed as secured parties in a security agreement or financing statement could be metamorphosed into senior secured parties by virtue of an assignment or otherwise, pre- or post-bankruptcy. We also decline to impose upon a junior secured creditor the burden of a frequent check to determine whether any unsecured parties have secretly assigned their claims to a senior secured party whose interest has been perfected.

*E.A. Fretz*, 565 F.2d at 372. Simply put, the Fifth Circuit's rationale confirms that this Court should not impose on STB's perfected priority interest in a case where the mechanism established by the Subordination Agreement to memorialize Replacement Financing has not been followed and a financing statement was never filed.

Section 7 of the Subordination Agreement includes additional protections for the benefit of STB so that it would receive written notice of any "modifications, amendments, extensions . . . or changes to the Senior Loan Documents." STB has received no such notices from BusinessRadio Houston LLC, Industrial Info, Wallace Bajjali Fund II, as agent, Wallace Bajjali Development Partners, L.P., as agent for the Investors, or from any of the individual Investors.

Indeed, Section 14 of the Subordination Agreement requires any Senior Lender (which the Investors claim to be) to promptly notify STB of "the granting of a further encumbrance against the Shared Collateral" for which the Senior Lenders must obtain the prior written consent of STB. As with the failures under Sections 6 and 7 of the Subordination Agreement to follow the notice procedures, neither Industrial Info (the original Senior Lender) nor Wallace Bajjali Fund II, as administrative agent, ever notified STB that a replacement loan was being made or that "a further encumbrance of the Shared Collateral" was being sought by any other lenders. Equally telling is the undisputed fact that none of the Investors, or their agent, Wallace Bajjali Development Partners, L.P., have ever notified STB that a further encumbrance, or refinancing of the Senior Loan was sought, nor has there ever been any request that STB grant its written consent to additional or replacement senior loans as required by the Subordination Agreement.

STB is entitled to rely on these material contract terms under the bargain it reached with Industrial Info and BusinessRadio Houston LLC. These are important contractual terms protect STB from the type of argument being advanced by Investors that want the status of "floating

secured lenders" which *E.A. Fretz* holds cannot be imposed on a junior secured lender. Without such contractual protections, it is easy to envision opportunities for the debtor (or any party foreign to the original transaction) to incur significant additional debts that would destroy the priority interests that STB bargained for in the Subordination Agreement and thereby prevent it from being paid what it was owed by BusinessRadio Houston LLC.

It is also important to note that none of the Investors' loan documents provide any evidence that their loans would be considered Replacement Financing under the terms of the Subordination Agreement. The documents contain no reference to the Industrial Info Resources loan, the March 28, 2008 financing statement filed by Wallace Bajjali Fund II, or that the security interests being granted would rely on such financing statement for purposes of perfection.

If "any lender who provided new funds to pay down the IIR indebtedness or the STB indebtedness would stand in the shoes of IIR with a priority security interest," as Investors argue, one would expect each of the Investors' promissory notes and/or Security Agreements to refer to the Industrial Info Security Agreement, or the financing statement filed by Wallace Bajjali Fund II, or to the Subordination Agreement. None of the promissory notes or corresponding Security Agreements contain any reference to the Industrial Info Security Agreement, the Wallace Bajjali Fund II Financing Statement, or the Subordination Agreement. In fact, certain of the Investors' loan documents refer to a lender pool and that the funds would be used for the purpose of investing in real estate and private equity interests, not a commercial radio station.

Further evidence suggesting that the Investors were not making replacement loans is reflected in the Investors' security agreements stating that the lenders would have perfected secured interests in the listed collateral "upon the due filing of UCC financing statements."

Because there is no reference to the Wallace Bajjali Fund II Financing Statement, which reference could have easily been made, it appears that the various security agreements contemplated the filing of separate financing statements naming Biz Radio Network, LP as debtor.<sup>11</sup>

**F. The Investors' Security Interests, if any, are Subordinate to STB's Interest because they were Created Later in Time and were Never Perfected**

Assuming *arguendo* that the Investors hold valid security interests in the Station assets, which STB specifically denies, the Investors' interests would necessarily be subordinate to STB's interest, and remain unperfected.

A security interest becomes enforceable, and thus attaches to collateral, when value is given by the secured party, the debtor has rights in the collateral, and the debtor has authenticated a security agreement that provides a description of the collateral. Texas UCC § 9.203. Thus, value must be conveyed in order for a security interest to attach. When the initial security agreement was executed, value was given by Industrial Info. As such, Industrial Info had a security interest perfected when it filed the financing statement. However, no value was given by the Investors at the time the March 28, 2008 financing statement was filed. Thus, the Investors could not have any rights under the Industrial Info financing statement until they made their respective loans, at which time their security interests, if any, could have attached to the collateral. Therefore, the security interests of the Investors, if any (which STB denies), would necessarily be inferior to the interest of STB because STB caused attachment of its collateral to occur and perfected its security interest on March 28, 2008, well before any security interest of

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<sup>11</sup> Indeed, even if the Investors' loan documents made reference to the same, the mere reference would not suffice because the underlying loans were made to Biz Radio Network, LP, not BusinessRadio Houston LLC, and neither the Investors nor their agent, Wallace Bajjali Development Partners, L.P. are named in that financing statement.

the Investors could attach to collateral if all requirements for an effective financing statement had been satisfied.

As discussed above, Section 9.310 of the Texas UCC requires that a financing statement must be filed to perfect a security interest in collateral. Perfected security interests rank according to priority in time of filing or perfection. Texas UCC § 9.322(a)(1). A perfected security interest has priority over a conflicting unperfected security interest. Texas UCC § 9.322(a)(2).<sup>12</sup> The time of perfection of a security interest is most significant in determining priorities among competing interests. *See In re McBee*, 714 F.2d 1316 (5th Cir. 1983).

STB's interest was perfected on March 28, 2008 by filing its UCC Financing Statements with both the Texas and Delaware Secretaries of State. The only interest that is superior to STB's interest is the interest of Wallace Bajjali Fund II, which was perfected by filing the financing statement with the Delaware Secretary of State that same day. Any subsequent security interest in the same collateral, whether perfected or not, would be subordinate to STB's interest. *See Texas UCC § 9.322(a)(2)*.

The references in the titles of some of the Investors' loan documents and in the bodies of such documents that purport to represent "perfected first priority" or "senior" interests fail to provide such status. These types of statements simply do not override the law granting priority to a party with a properly perfected security interest in collateral. *See Texas UCC § 9.322(a)(1)*. Priority of security interests are determined according to the statutory provisions governing priority and not based upon language in a security agreement stating it is a senior or first priority interest.

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<sup>12</sup> Comment 3 to Section 9.322 of the Texas UCC explains, "The rules may be regarded as adaptations of the idea, deeply rooted in common law, of a race of diligence among creditors. The first two rules are based on precedence in the time as of which the competing secured parties either filed their financing statements or perfected security interests."

Further, Section 5 of the Investors' security agreements expresses the intent that the security interests be perfected by filing:

...the Security Interest in the Collateral granted to the Secured Party hereunder shall constitute at all times a valid and perfected first priority security interest vested in the Secured Party in and upon the Collateral ... which Security Interest shall be perfected...*upon the due filing of UCC financing statements...*

*See* Exhibits 3-20 to the Objection (emphasis added). Searches of the UCC records of the filing offices of the Texas and Delaware Secretary of State reveal that no security interest has ever been filed against Biz Radio Network, LP (the debtor under the Investors' loan documents) or for that matter, BusinessRadio Houston LLC or BusinessRadio Houston Licensee LLC as reflected in the exhibits attached to the Appendix. Therefore, the security interests, if any, of the Investors are not perfected and are thus subordinate to STB's perfected security interest under Sections 9.322(a)(2) and 9.310 of the Texas UCC.

#### **IV. PRAYER**

South Texas Broadcasting, Inc. requests that the Court grant the Receiver's motion in all respects, and enter a Confirmation Order approving the sale of the radio station assets to STB pursuant to the Modified Sale Agreement, and grant such other relief the Court may deem just and equitable.

Dated June 24, 2011

Respectfully submitted,

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**ATTORNEYS FOR SOUTH TEXAS  
BROADCASTING, INC.**

**CERTIFICATE OF SERVICE**

On June 24, 2011, I electronically submitted the foregoing document with the clerk of the court of the U.S. District Court, Southern District of Texas, using the electronic case filing system of the court. I hereby certify that I have served all counsel and/or *pro se* parties of record listed on the attached service list, electronically or by another manner authorized by Federal Rule of Civil Procedure 5(b)(2).

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*/s/ Joseph G. Epstein*

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Joseph G. Epstein