

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

In re: §
§
NORTH BAY GENERAL HOSPITAL, INC., § CASE NO. 08-20368
§ (Chapter 11)
Debtor. §

**SUPPLEMENT TO DISCLOSURE STATEMENT
REGARDING SALE AND CLOSING POSSIBLE SETTLEMENT
OF LITIGATION WITH NORTHERN HEALTHCARE CAPITAL, LLC**

COMES NOW, North Bay General Hospital, Inc. (“Hospital”) and files this, its Supplement to Disclosure Statement and would show as follows:

1. On January 13, 2010, the Hospital caused the Hospital’s Solicitation Package¹ to be mailed to all pre and post petition creditors of the Hospital. Since then, two significant events have occurred: i) the Buyer has changed the date it will close on the real estate from the 36th month to the 48th month after Consummation of the Sale; and ii) the Hospital and Northern Healthcare Capital, LLC (“NHC”) are believed to be very close to a compromise of the litigation brought by the Hospital against NHC which is described on pages 13, 17-18 of the Disclosure Statement.

Sale Terms

2. The terms of the sale of the Real Property are substantially the same as previously disclosed in the Disclosure Statement; however, the Buyer requested to have the flexibility of another year of renting the Real Property prior to being required to purchase same. The purchase price has remained \$4,500,000.00; the rent will be as follows:

¹ Unless defined herein, capitalized terms used herein have the meaning given to them in the Plan, Disclosure Statement or Code.

Months 1-5	\$17,500.00
Months 6-36	\$25,000.00
Months 37-48	\$20,000.00

The Buyer has agreed that the rental income will be paid for at least 30 months. On or before the end of the 36th month, the Buyer will pay the Estate \$500,000.00 (“R.E. Payment”) toward the \$4,500,000.00 purchase price for the Real Property. As described below, any future rental, if received, due to the Buyer’s request to extend the Real Property sale date, will be used to fund the increased Claim of the San Patricio Taxing Authorities; NHC’s pre-petition Secured Claim; to pay costs of administration; and Administrative Claims.

Settlement with NHC

3. As is disclosed in the Disclosure Statement, the Hospital filed a Complaint against NHC. The Hospital and NHC have been negotiating a possible resolution of the Litigation. That settlement, if finally reached, and which is subject to Bankruptcy Court approval, after notice and an opportunity for hearing, is summarized below:

NHC’s Administrative Claim – NHC has asserted an Administrative Claim in the amount of \$1,775,000.00. To resolve NHC’s Administrative Claim, the parties have agreed that of the \$1,775,000.00 of the NHC Escrowed Funds, NHC will receive \$790,000.00 within five (5) business days (“Pay Date”) after the Confirmation Date.

The Administrative Claims of the IRS and the Texas Workforce Commissions regarding post-petition payroll taxes (estimated in the aggregate amount of \$790,000.00) will be paid out of the NHC Escrowed Funds. The IRS has agreed to waive its post-petition penalties in exchange for the prompt payment of its post-petition claim, which benefits the Estate in the approximate amount of \$100,000.00. The balance of the NHC Escrow of approximately \$195,000.00 will be available to pay costs to liquidate the Estate and pay Administrative Claims.

NHC will receive \$316,000.00 out of the Settlement Proceeds towards its Administrative Claim on the Pay Date, and in the 36th month after the initial closing with the Buyer, NHC will receive \$474,000.00 within five (5) days of the Estate's receipt of the R.E. Payment which will satisfy NHC's Administrative Claim.

NHC's Pre-Petition Claim - NHC filed a secured proof of claim in the amount of \$5,131,765.67 plus interest, fees and costs. Under the settlement currently being negotiated, NHC will be allowed a pre-petition secured claim of \$3,825,768.00 which claim will be subordinated and junior to: a) Administrative Claims in an amount up to \$1,000,000.00 (inclusive of NHC's \$474,000.00 Administrative Claim); b) a \$120,000.00 distribution for the Class 16 Unsecured Creditors; and c) \$3,600,000.00 on its secured claim another \$120,000.00 to the Unsecured Creditors (after NHC collects). NHC will also have an allowed \$805,997.67 unsecured claim which shall be subordinate to all other Class 16 Unsecured Creditors. NHC's secured claim will be paid with \$90,000.00 from the anticipated lease payments to be received in months 37-48 and the balance of NHC's secured claim will be paid from the proceeds received by the Estate from the sale of the Real Property, the closing of which is anticipated between the 37th and 48th month after the initial closing of the Sale.

This settlement would resolve the single most significant contingency contained in the Plan. Based on the Hospital's current best estimate, the potential settlement allows all Administrative Claims to be paid in full, with approximately 50% paid once all of the Administrative Claims have been filed and approved by the Court and the balance to be paid from the recovery of Avoidance Actions and the sale of the Real Property.

The potential settlement, subject to the sale of the Real Property occurring, also quantifies the return to Class 16 Unsecured Creditors. The Hospital estimated, in the Disclosure

Statement, that in the event the Hospital succeeded in its litigation claims against NHC, the return to Unsecured Creditors would be approximately one to five percent (1%-5%). This settlement would obtain for the Unsecured Creditors an estimated initial Distribution of two and a half percent (2.5%) with the prospect of an additional Distribution of two and a half percent (2.5%) once NHC recovers \$3.6 million on its Allowed pre-petition secured claim. In the event the Hospital is more successful than presently anticipated in the recovery of Avoidance Actions, the Distribution to Unsecured Creditors could exceed five percent (5%).

4. In Article IV of the Plan, certain parties are to be released from various claims of creditors, and creditors are enjoined from pursuing certain claims against the Debtor and Insiders of the Debtor. Notwithstanding these provisions in the Plan, there is no intention to a) restrict the IRS or the Texas Workforce Commission from asserting claims against “responsible third parties”; b) restrict the right of recoupment, if any, of the Texas Medicaid or Federal Medicare Authorities; and c) interfere with or restrict the contractual rights of creditors with non-debtor parties. Nothing in the Plan shall restrict any right or remedy that NHC may have pursuant to any guarantee executed by Thomas McNaull for the benefit of NHC.

5. Due to the accrual of interest during the pendency of the Case on the San Patricio Taxing Authorities’ Claims, their Secured Claims were understated in the Disclosure Statement. By agreement reached with the San Patricio Taxing Authorities, the amortization of those Secured Claims was extended in conjunction with the Buyer’s request for an additional year of rent. Therefore, the anticipated cash flow of the initial 36 months under the Plan remains approximately the same as previously disclosed; however, the San Patricio Taxing Authorities’ Secured Claims are now payable over 48 months. A revised chart reflecting the payments to be

made under the Plan, as modified, to Secured Creditors from the anticipated rental income is on www.hirshwest.com under the North Bay General Hospital tab.

6. Monthly operating reports will be filed through the date of the Sale (anticipated to occur shortly after the Confirmation Date); thereafter, the Disbursing Agent will file with the Court quarterly reports of receipts and disbursements. US Trustee fees will continue to accrue and be payable as long as the Case remains open.

7. Due to the changes to the Plan necessitated by the change in the terms of the sale of the Real Property and the possible settlement with NHC, the definition of the Effective Date of the Plan has been changed to be “the date that is thirty (30) days after the date the Buyer pays the \$4,500,000.00 for the purchase of the Real Property”. **All holders of Administrative Claims will be required to file an Administrative Claim prior to the Administrative Bar Date.** An Administrative Claim form will be approved by the Court at Confirmation and served on each Creditor believed to have an Administrative Claim.

8. The Plan has been modified to include these changes. A copy of the NHC settlement agreement, the Motion to Compromise Controversy and the Modification can be viewed at www.hirschwest.com under the North Bay General Hospital tab. Due to the fact that the settlement was has not been agreed to, those documents may be changed from time to time prior to the Confirmation in the event the settlement fails or is changed.

9. The Hospital is proposing that Jay Stacy initially serve as the Disbursing Agent to assist the Estate with the litigation against NHC, if necessary; to assist with the prosecution of the Avoidance Actions; and the filing of tax returns, monthly operating reports and cost reports.

10. Any Creditor, who previously cast a Ballot accepting or rejecting the Plan and who believes the Plan, as now modified, substantially changes their prior decision, may alter their earlier vote by delivering a revised Ballot via first class mail, facsimile or e-mail to

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700 Louisiana, Suite 2550
Houston, Texas 77002
Attn.: Barbara Howell
E-mail: bhowell@hirschwest.com
Fax: (713) 223-9319

so that the revised Ballot is received on or before 5:00 p.m. central time February 24, 2010.

11. The Confirmation Hearing has been continued until February 25, 2010 at 1:00 p.m. central time.

WHEREFORE, PREMISES CONSIDERED, the Debtor files this, Supplement to the Disclosure Statement and seeks confirmation of the Plan as modified and for such other and further relief as is just.

HIRSCH & WESTHEIMER, P.C.

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