Julia W. Brand, Esq. (SBN: 121760)
jbrand@linerlaw.com
Enid M. Colson, Esq. (SBN: 189912)
ecolson@linerlaw.com
LINER YANKELEVITZ
SUNSHINE & REGENSTREIF LLP
1100 Glendon Avenue, 14th Floor
Los Angeles, California 90024-3503
Telephone: (310) 500-3500
Facsimile: (310) 500-3501

Proposed Counsel for Debtors and Debtors-in-Possession

UNITED STATES BANKRUPTCY COURT

SOUTHERN DISTRICT OF CALIFORNIA

In re: STEAKHOUSE PARTNERS, INC., a Delaware corporation, Debtor.	Case No. 08-04147-11 Chapter 11
In re: PARAGON STEAKHOUSE RESTAURANTS, a Delaware corporation, Debtor.	Case No. 08-4152-11 Chapter 11
In re: PARAGON OF MICHIGAN, INC., a Wisconsin corporation, Debtor.	Case No. 08-4153-11 Chapter 11 **FIRST DAY MOTION NO. 3; MOTION FOR ORDER AUTHORIZING PAYMENT OF NON-INSIDER PREPETITION ACCRUED WAGES, SALARIES, COMMISSIONS, EMPLOYEE EXPENSES, WORKERS' COMPENSATION AND EMPLOYEE BENEFITS AND PAYMENT OF RELATED TAXES AND TAX DEPOSITS AND AUTHORIZING AND DIRECTING BANKS TO HONOR PAYROLL ACCOUNT CHECKS AND EXPENSE REIMBURSEMENT CHECKS** Date: TBD Time: TBD Courtroom: 218 Judge: The Honorable James W. Meyers

PLEASE NOTE THAT THIS IS A FIRST-DAY MOTION FILED PURSUANT TO APPENDIX D1 OF THE LOCAL BANKRUPTCY RULES OF THE SOUTHERN DISTRICT OF CALIFORNIA ("LOCAL BANKRUPTCY RULES"). ANY PARTY IN INTEREST WHO OPPOSES THE FIRST-DAY MOTION MUST IMMEDIATELY NOTIFY THE JUDGE'S LAW CLERK, KATHY YOST, BY CALLING (619) 557-3455. NO WRITTEN OPPOSITION SHALL BE FILED TO THE FIRST-DAY MOTION UNLESS THE COURT OTHERWISE DIRECTS.

TO THE HONORABLE JAMES W. MEYERS, UNITED STATES BANKRUPTCY JUDGE, SECURED CREDITORS, THE TWENTY LARGEST UNSECURED CREDITORS AND THE UNITED STATES TRUSTEE:

PLEASE TAKE NOTICE that the above-captioned debtors and debtors in possession (collectively the "Debtors") hereby file this First Day Motion for an order of this Court pursuant to sections 105(a), 507(a)(4) and 507(a)(5) of title 11 of the United States Code (the "Bankruptcy Code") (i) authorizing payment of accrued wages, salaries, commissions, employee expenses, workers' compensation and employee benefits in accordance with the policies and practices established prior to the Petition Date, (ii) authorizing the Debtors to perform and honor all other obligations, practices and policies relating to employees, (iii) authorizing payment of related taxes, tax deposits and processing fees, (iv) authorizing and directing its banks to honor wage and salary related checks, and (v) authorizing and directing Debtors' banks to honor employee expense reimbursement checks (the "Motion").

PLEASE TAKE NOTICE that pursuant to Local Bankruptcy Rule 9014-5 and the "Guidelines for First Day Motions" any party who opposes this Motion shall notify the judge's law clerk of its position by telephone. No opposition shall be filed to a First Day Motion unless the Court otherwise directs. Pursuant to the "Guidelines for First Day Motions" the Court reserves discretion to grant or deny a First Day Motion without a hearing unless the Court otherwise directs.

PLEASE TAKE FURTHER NOTICE that the Motion is based upon the accompanying Memorandum of Points and Authorities and the Declaration of Joseph L. Wulkowicz in support thereof filed under separate cover concurrently herewith. In addition, the Debtors request that the Court take judicial notice of all documents filed with the Court in these cases.

WHEREFORE, the Debtors respectfully request that this Court enter an order authorizing the Debtors to:

1. Pay, in accordance with the policies and practices established prior to the Petition Date, all accrued wages, salaries, commissions, reimbursable employee expenses, workers' compensation and all employee benefits that have been earned and accrued by virtue of the services rendered by the non-insider (as defined in section 101(31)) of the Bankruptcy Code) employees of the Debtors prior to the Petition Date;

2. Pay all applicable federal, state and local taxes, deductions and withholdings pertaining to the payments made pursuant to paragraph 1;

3. Pay the non-insider employees of the Debtors all amounts on account of employee wage and expense checks which may not have been presented for payment or may not have cleared the banking systems as of the Petition Date;

4. Reissue checks as necessary to cover amounts owing on any checks that have been dishonored by any bank and to reimburse employees for any resulting charges; and

5. Granting such other and further relief as is necessary and appropriate in the circumstances.

Dated: May 15, 2008

LINER YANKELEVITZ
SUNSHINE & REGENSTREIF LLP

By: */s/ Enid M. Colson*
Julia W. Brand
Enid M. Colson
Proposed Counsel for Debtors and Debtors-In-Possession

MEMORANDUM OF POINTS AND AUTHORITIES

I.

STATEMENT OF FACTS[1]

A. Jurisdiction and Venue

This Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2). The venue of the chapter 11 cases is proper pursuant to 28 U.S.C. §§ 1408 and 1409 as the Debtors' executive offices are located in San Diego County. The statutory predicate for the relief sought herein are sections 105(a), 507(a)(4) and 507(a)(5) of the Bankruptcy Code and this Court's "Guidelines for First Day Motions."

B. Background Facts

1. History of the Debtors

The three Debtors are related corporations engaged in the operation of 21 full service steakhouse restaurants located in the seven states of Arizona, California, Indiana, Michigan, North Carolina, Ohio and Utah. These restaurants principally operate under the brand names of Hungry Hunter, Hunter Steakhouse, Mountain Jack's and Carvers.

Debtor Steakhouse Partners, Inc. ("Steakhouse Partners") is publicly traded over the counter under the symbol "STKP." In December, 1998, Steakhouse Partners acquired its wholly owned subsidiary, Debtor Paragon Steakhouse Restaurants, Inc. ("Paragon Steakhouse"), which owns and operates the restaurant businesses. Paragon Steakhouse has one wholly owned subsidiary, Debtor Paragon of Michigan, Inc., ("Paragon of Michigan") through which it conducts its restaurant operations in the state of Michigan and holds its intellectual property and trade names. The structural maintenance of Paragon of Michigan is dictated by state alcohol laws; however, the subsidiary operations and financial results are consolidated at the Paragon Steakhouse level.

The Debtors' business income is generated from food and beverage sales from each of the 21 restaurants, which during the Debtors' Fiscal Year 2007 (ending December 25, 2007) generated approximately $45,000,000 in gross revenue (as of the first quarter 2008, two restaurants are no longer

[1] The facts set forth in this Motion are verified in the Omnibus Declaration of Joseph L. Wulkowicz in Support of Chapter 11 Petitions and First Day Motions filed concurrently herewith under separate cover.

operated by the Debtors). Like other restaurant businesses, the Debtors' operations are seasonal, with the overall performance peaking in the 4th quarter.

The Debtors' 21 steakhouses specialize in complete steak and prime rib meals, and also offer fresh fish and other lunch and dinner dishes. The average restaurant check is $27.30 per guest (including alcoholic beverages) and the 21 restaurants serve approximately two million meals annually. Most restaurants are open daily from 4:30 to 9:30 p.m. on weekdays and from 4:00 to 11:00 p.m. on the weekends. Some restaurants are also open for lunch, typically beginning at 11:00 a.m.

Paragon Steakhouse and Paragon of Michigan, as of January 8, 2008 employ in excess of 1,325 full and part time employees, approximately 1,200 of which perform services during any two-week period, and of which approximately 55% are part-time.

Paragon manages six restaurants known as Sirloin Saloon and Dakota Steakhouses in the states of Vermont, Massachusetts, Connecticut and New York pursuant to a Management and Services Agreement between Paragon and the restaurant owners, DWH, I, Pittsfield DWH and Saloon beverages, Inc., entered into effective November, 2007. This Management Agreement provides for termination of Paragon's management services in the event that Paragon's acquires the membership interests in the referenced corporations pursuant to a Membership Purchase Agreement or terminates the transaction pursuant to its terms.

The Debtors maintain an internet website at www.paragonsteak.com. This website offers free access to the Debtors' press releases and Steakhouse Partners' filings with the U.S. Securities and Exchange Commission (the "SEC"), including its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports, as soon as reasonably practicable after these reports are filed with or furnished to the SEC.

2. The Debtors' Prior Bankruptcy Cases

On February 15, 2002, Steakhouse Partners filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for the Central District of California (the "Bankruptcy Court"). On February 19, 2002, Paragon Steakhouse and Paragon of Michigan also filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code in the Bankruptcy Court (together, the "Initial Filing"). Effective December 31, 2003, the Debtors confirmed a Joint Plan of Reorganization (the "2003

Plan"), and on December 28, 2007 the Court entered an Order Regarding Final Report, Accounting and Final Decree.

The Initial Filing was made in response to the maturing of certain notes aggregating $1,734,285, which the Debtors were unable to pay. Throughout the course of the Reorganization, the Debtors sought to retain core locations, eliminate non-competitive leases, restructure their debt, and withdraw from under-performing markets.

The 2003 Plan provided for the creation of the Class 4 Creditor Trust (the "Trust") for general unsecured claimants with claims in excess of $4,000 with a trustee (the "Trustee") for the purpose of collecting, maintaining and distributing the Steakhouse Partners Class 4 Creditors Trust Assets. As part of the Plan, the Trust was granted a lien on the Debtors' leasehold interests. Today, the Trust is the principle secured creditor of the Debtors.

3. Post Plan Confirmation

Since confirmation of the 2003 Plan, the Debtors have experienced difficulty generating sufficient cash to cover operating expenses, deferred maintenance and the extraordinary costs to satisfy reorganization commitments. This inability remained an impediment to implementing long-term strategic changes required to enhance the Debtors' intrinsic value, to increase top line revenue and resulting profit, and to pay long-term debt. As a result, the Debtors' post-confirmation business plans focused on generating increased revenue and profit, but directed attention to programs producing a longer-term focus through debt restructuring and acquisition. Post confirmation, the Debtors sought and reached agreements with both public and private financial institutions to complete certain acquisitions and private equity placements in order to strengthen the core business and provide capital for debt repayment.

Although the Debtors had originally made total payments of approximately $1,200,000 to the Trust, they failed to make certain further payments as required by the 2003 Plan. As a result, the Trustee and the Debtors negotiated a settlement agreement approved by the Court on August 10, 2006 (the "Settlement Agreement"). Under the Settlement Agreement, the Debtors became obligated to make an alternative payment of $5,200,000 (the "Alternative Payment") of which $1,100,000 was to be paid immediately.

In early 2007, the Debtors began a real estate liquidation plan designed to make structured payments on their debt to the Trust. However, because the Debtors had not made the $1,100,000 payment, on or about

May 18, 2007, the Debtors received the Trustee's notice of default as to the Alternative Payment. As a result, the Debtors agreed to enter into a forbearance agreement (the "Forbearance Agreement") with the Trust, which formalized the real estate sale plan already being marketed. The Debtors discuss their efforts and the status of the sales with the Trustee of the Trust on a regular basis.

4. <u>The Debtors' Situation in 2008</u>

Although the Debtors have attempted to complete all of the sales contemplated by their agreement with the Trust, a combination of variables causing deteriorating financial performance and third-party reticence to consent to transfers have stymied the Debtors' efforts to live up to their commitments to the Trust.

Since mid-2007, the Debtors' financial results have deteriorated as a result of a combination of rising costs and declining sales and guest frequency. By the end of March 2008, the deterioration rapidly accelerated. Specifically, cost increases have been unprecedented. By way of example:

- The price of prime rib alone has increased by around 5%, chiefly as a result of the Midwest diversion of corn products from the cattle feed market to the production of alternate fuel sources such as ethanol. Thus, the feed available to ranchers has spiked in price, forcing them to charge more per pound of beef. Further, in response to their own cost pressures, the ranchers have reduced herd sizes, further driving up commodity costs due to lack of available product. The Debtors only serve corn fed beef as it is the over whelming preference of their core guests.
- Similarly, the nationwide oil and gas price increases have forced purveyors to assess "fuel charges" on all products (whether produce, dairy, staples or alcohol), adding almost $500,000 annually to the Debtors' operating cost.
- During 2007, the Debtors incurred increased payroll costs of around $400,000 as a direct result of state minimum wage increases. During first quarter 2008, an additional $100,000 in increased wages were paid as new minimum wage increases took effect.

Administrative and accounting costs necessary to comply with new federal regulations, public company filing requirements and the increases in medical benefit and workman's compensation costs added another $100,000 to the costs of business.

Unfortunately, the above cost increases come in the middle of an economic downturn in which Americans are spending less on "elective items" such as dining out, making it nearly impossible to raise menu prices. According to the restaurant industry reports, unemployment, economic uncertainty and instability in the housing market are the greatest contributors to declining restaurant revenue in all segments.

As a result of this reduced revenue-increased cost environment, the Debtors have been unable to generate sufficient cash to timely pay their bills on an ongoing basis and still sell real estate to satisfy the Trust obligations. As the spiral has accelerated, landlords are unwilling to consent to transfers when payments are not current, and state authorities will not allow transfer of single units until all state obligations are current.

As such, the Debtor seeks to complete its liquidation commitments within the protection of chapter 11 cases to gain sufficient time to sell assets for their highest and best price as going concerns. In the past six years, the Debtors have sold and assigned more than 20 restaurants. In each case, the Debtors were able to sell its leasehold interest, alcohol license, personal property and inventory for cash. In contrast, two restaurants have been closed and offered for sale. In each case, no sale has been consummated because the building offers no "going concern" value. A restaurateur does not want the property, because the inventory and operating licenses (including liquor) are not available, and the "dark building" offers no built in customer base. Alternate use buyers have shied away from purchase, because a restaurant building requires extensive remodeling (especially with approximately 40% of the square footage allocated to the kitchen) or razing to be suitable for alternative use.

Beginning in the week of May 11, 2008, the Debtors have started to receive 3-day notices from some of their landlords. Other landlords have made statements to the Debtors that they may commence eviction proceedings but have not yet served formal 3-day notices.

The Debtors believe that they can maximize cash available for distribution to creditors by offering for sale their assets as operating "going concerns" while under the court's protection. They believe this can be accomplished expeditiously and efficiently given the sales programs and leads already in place. However, it cannot be accomplished without this Court's protection from parties seeking to block sales by seeking preferential payment in front of senior creditors.

The remaining units will produce sufficient cash to support operations until sold. During the coming ninety days, the restaurants the Debtor expects to continue to operate until sales are consummated should produce a positive EBITDA.

C. <u>Relief Requested</u>

By this Motion, the Debtors respectfully request the entry of an order authorizing the Debtors to pay certain prepetition amounts and to honor certain prepetition obligations to their non-insider employees, including accrued wages, salaries, commissions and employee benefits and all applicable taxes, tax deposits and processing fees associated therewith.

D. <u>Factual Basis for Relief Requested</u>

1. <u>The Debtors' Employees</u>

As of May 11, 2008, Debtor Steakhouse Partners employs three persons, each of whom is salaried and an executive officer of the Debtor. <u>The compensation of these three persons is not the subject of this Motion as they are insiders of the Debtor within the meaning of 11 U.S.C. § 101(31)</u>. As of the May 15 2008, Debtor Paragon Steakhouse employs approximately 950 employees, of which approximately 70 are salaried and the remainder are paid wages at an hourly rate. As of May 15, 2008 Debtor Paragon of Michigan employs approximately 147 employees, of which approximately eight are salaried and the remainder are paid wages at an hourly rate.

The Debtors, for purposes of payroll and benefit issues, place their employees into two different categories: (i) Production Employees; and (ii) Administrative Employees. Production Employees include any and all non-managerial restaurant employees and Administrative Employees include all other employees. Restaurant Management (approximately 67 of the Administrative Employees) receives compensation in two forms, a base salary and performance based compensation, more fully described below.

Prior to the Petition Date, and in the ordinary course of the Debtors' business, employees were owed or had accrued various sums for wages, salaries and commissions in their rendition of services. In addition, some of the employees were entitled to reimbursement of business expenses. Furthermore, the Debtors have always and remain obligated to pay federal, state and local withholding and employer payroll taxes due on prepetition employee wages and salaries.

The Debtors also subsidize certain employee benefits such as medical, dental and vision insurance, disability insurance, accidental death and dismemberment, and life insurance. To maintain these benefits, the Debtors are required to make contributions to insurance providers and plan administrators, as discussed in more detail below. In addition, well before the Petition Date, the Debtors adopted a Paid Time Off plan pursuant to which employees may take vacation and sick days.

The Debtors believe that in order to achieve success in these chapter 11 cases, they must honor their obligations to employees. Without loyal employees who know and understand the business, the Debtors will be at a serious disadvantage with respect to ensuring the maximization of the value of their assets in these chapter 11 cases.

The Debtors believe that without the relief requested its employees would be faced with tremendous hardship. A failure to pay accrued employee wages, salaries, expenses, benefits, and other employee-related obligations, or even a delay in such payment, would have a significant negative impact on employee morale. The Debtors' employees could not reasonably be expected to continue their employment and assist with the Debtors' efforts to maximize their value while at the same time enduring personal financial difficulties.

The Debtors believe that the requested relief will enable them to maintain their current business operations without interruption and, at the same time, maintain employee morale until their assets can be liquidated. The Debtors' employees are vital to the Debtors' efforts and provide essential services, without which the Debtors would be unable to function. Without the relief requested, the Debtors' ability to preserve their assets for the benefit of all creditors and equity security holders will be impaired, and the goals of these chapter 11 cases will be thwarted.

The amount of compensation (including wages, salaries, commissions, vacation, severance and sick leave pay and applicable benefits) to be paid to the Debtors' employees for their accrued prepetition services will average less than $10,950 per employee. At the present time, the Debtors are not seeking authority to pay their officers and directors (or any other insiders within the meaning of section 101(31)) for their accrued prepetition services but reserve the right to do so on a non-emergency basis in the future.

2. Salary, Wages and Commissions

Under the Debtors' standard payroll procedure, the Debtors pay their salaried and hourly employees on a bi-weekly basis by check drawn on a payroll account at Union Bank, as processed by the Debtor's third-party payroll processing Company, RealTime Computer Systems ("RealTime"). Employees are paid the wages or salaries earned during a bi-weekly period one week after the end of the pay period. Therefore, on any given payday, there will still be one week of accrued and unpaid wages and salaries outstanding. All of the Debtors' employees are paid by check (except for certain terminating restaurant employees (less than 10 per pay period) who are paid cash upon termination in compliance with state wage & hour laws.) The most recent payroll was made on May 13, 2008 for the pay period ending May 6, 2008. This payroll totaled $334,694.11 and the Debtors believe that, at most, approximately 50% of this payroll will not have cleared the bank and will remain owing to its employees for wages and salaries earned prepetition (including overtime). The next payroll will occur May 27, 2008 for wages and salary earned through May 20, 2008.

In addition, Paragon Steakhouse and Paragon of Michigan provide restaurant leadership with compensation tied to performance. This compensation, payable to less than 70 persons, is based upon achieving certain sales and profit goals during the respective four-week accounting period. Under the program, employees are paid one part of their performance compensation with the fourth payroll following the respective accounting period an another piece on a quarterly basis. On average, Paragon and its subsidiaries pay approximately $25,000 in performance compensation to these employees each period based on the results ended two periods ago (in other words, there would typically be as much as a two month lag period). However, the Debtors have not paid these wages for periods 12/2007 and periods 1, 2, 3 and 4 / 2008, each of which is currently due and/or payable. The quarterly compensation for Period 1, 2008 is also unpaid. Paragon Steakhouse and Paragon of Michigan, however, estimate that no more than the numbers below are owed in the future for results that arose from prepetition services rendered:

Period 12, 2007	$53,734
Period 1, 2008	$16,754
Period 2, 2008	$28, 775
Period 3, 2008	$29,293
Period 4, 2008	$18,194
1Q2008	$40,121

The Debtors pay their employees by check. As a result of the timing of the filing of these chapter 11 cases, employee paychecks previously issued may not yet have been presented for payment or may not yet have cleared the banking system and, accordingly, may be dishonored unless the Court authorizes and directs the bank in which the Debtors maintain their payroll account to honor these checks. The Debtors believe that in addition to the payroll released May 13, 2008, approximately $40,000 of paychecks may be outstanding as of the Petition Date (dating to 2005).

3. Reimbursable Expenses

Many of the Debtors employees regularly incur certain out-of-pocket, business-related expenses, such as necessary and authorized travel expenses (i.e. airfare, lodging, rental cars, meals, etc.). Employees are reimbursed upon the submission of expense reports and supporting documentation. Such reports are normally submitted within two weeks after the employee incurs the expense and, after review and approval of the expense report, the Debtors reimburse the employee by check drawn on the Union Bank Concentration Account. The Debtors estimate that they have no more than $10,000 (other than to Executive Officers) of accrued prepetition employee expenses that were not reimbursed prior to the Petition Date. (All have been paid, but not all checks have been presented to the issuing banks). However, because some employees submit reimbursement requests up to one month after incurring the expense, there may be significantly more employee expenses that the Debtors are unable to quantify at the present time.

4. Withholding Taxes

Attendant to the payment of employee wages, salaries, commissions and expenses is the Debtors' obligation to pay federal, state and, in some instances, city withholding taxes and employer payroll taxes such as FICA, FUTA, SUTA and state/local disability taxes/insurance ("Withholding Taxes"). Such taxes accrue as wages are earned and are calculated based upon a statutorily mandated percentage of gross wages employees earn.

The Debtors currently use the services of a third-party payroll service, RealTime, to process all of its payroll obligations and uses Payroll Tax Management Company ("PTM") to process and remit its Withholding Taxes nationwide. For each pay period, the Debtors remit a list of employees to RealTime, and RealTime then sends an electronic report to PTM and the Debtors reflecting their Withholding Tax obligation for that pay period. The Debtors, based on this report, thereafter remit funds for the Withholding Taxes to PTM, who in turn remits the Withholding Taxes to the applicable taxing authority after the disbursement of funds to employees.

Through the Petition Date, to the best of their knowledge, the Debtors were current on all Withholding Tax obligations relating to disbursed prepetition payrolls. The Withholding Tax to be transmitted relating to the May 13, 2008 payroll was paid as required by wire transfer.

5. Employee Benefits

The Debtors provide employees with certain benefits, including medical, dental and vision insurance coverage, disability insurance, accidental death and dismemberment, and life insurance, for which the Debtors makes certain contributions. The Debtors also pay compensation for certain periods of its employees' vacation and sick leave.

The Debtors subsidize some of these benefits, which are an integral and important part of each employee's total compensation package. Interruption of such benefits caused by the filing of the Debtors' voluntary petitions would affect the morale of the employees adversely and would undermine the Debtors' business operations. For these reasons, the Debtors are requesting the authority to pay the prepetition amounts attributable to such benefits as and when such amounts come due in the ordinary course of their business.

6. Medical, Dental and Vision Insurance

Each Debtor provides medical and dental insurance to its full time employees and its full time employees' dependents, if they elect to subscribe to the plan offered. The Debtors' medical and dental plan is a standard HMO or PPO medical and dental health plan provided through Blue Shields (medical) and Cigna (dental) and their affiliates in seven states, covering a percentage of medical costs (with such dollar amounts varying based on choice of HMO or PPO). The monthly premium for the medical health insurance plans varies, depending on the number of employees enrolled and the number of dependents covered, and averages $37,000 per month, of which approximately 50% represents withholdings from employee wages to cover the cost of their portion of the premium. The monthly premium for the dental plan is approximately $3,300, half of which is obtained through withholdings from employee wages. The Debtors offer Vision Case through VSP Insurance to their administrative employees only, at an annual cost of approximately $9,000, half of which premium is paid by the employees. The Debtors have paid for their medical, dental and vision insurance plans, including the employee withholdings portion, through April 2008.

7. Disability Insurance, Life Insurance and AD&D Policies

Long term-disability insurance is made available to all administrative full-time employees; employees pay 75% of the premium costs of $15,768 annually. Pursuant to these policies, the employee may receive 60% of their earnings if the employee is unable to perform material duties of their position due to disability. Unum underwrites the long-term disability policies.

The Debtors provide life insurance and accidental death and dismemberment for its administrative employees and its employees' dependents. In conjunction with the Debtors' medical policy, one times base salary of term life insurance is provided to the employees at no cost. Additionally, the Debtors provide term life insurance benefits up to five times an employee's salary. United Health Care underwrites benefits for these programs. At the employee's option, additional term life insurance can be purchased from United Health Care via payroll deduction. Employees may also purchase accidental death and dismemberment from UNUM Insurance. The annual premium for life insurance and accidental death and dismemberment is approximately $24,588, all of which is employee paid except as stated above.

8. Paid Time Off

The Debtors have established a VEBA Trust for the purpose of providing vacation related benefits, by which, depending upon the length of service, employees are eligible to earn paid time off for purposes of vacation.

For administrative employees, after one year of service, an employee may be paid for one week off annually, increasing as the length of the employee's service increases, up to a maximum of four weeks days per year after 15 years of service. For production employees, after one year of service, employees receive a check equal to 30 hours of pay in the event that they work at least 1,560 hours in one year.

All administrative employees also have the opportunity to earn paid "sick days". After being employed for one year, employees earn one-half day of paid sick time per month. Employees are not paid at termination for any unused sick days.

Almost all administrative employees may have accrued "paid time off" based upon work performed prior to the Petition Date. The aggregate obligation for Debtors' "paid time off" policy is approximately $592,167.92 for "sick days" and $346,665.24 for vacation pay.

II.

LEGAL ARGUMENT

A. The Bankruptcy Code and the "Necessity Doctrine" Authorize the Employee Payments Proposed Herein

Bankruptcy courts have authorized debtors-in-possession to pay employees' prepetition claims, just like those described herein, under section 105(a) of the Bankruptcy Code. That section provides that the court "may issue any order process, or judgment that is necessary or appropriate to carry out the provisions of this title." § 105(a). The purpose of this section is "to assure the bankruptcy courts power to take whatever action is appropriate or necessary in aid of the exercise of their jurisdiction." 2 Collier on Bankruptcy, ¶ 105.01 at 105-6 (15th rev. ed. 2004). Essentially, section 105(a) codifies the bankruptcy court's inherent equitable powers. *See*, Matter of Management Tech. Corp., 56 B.R. 337, 339 (Bankr. D.N.J. 1985) (court's equitable power is derived from section 105).

In In re Ionosphere Clubs, Inc., the bankruptcy court permitted Eastern Air Lines to pay its current employees' prepetition wages, salaries, benefits and business expense claims finding that it was critical to pay these employee claims to preserve and protect the debtor's business and to retain current employees and maintain their morale. In re Ionosphere Clubs, Inc., 98 B.R. 174, 175 (Bankr. S.D.N.Y. 1989). That court also held that the payments of prepetition obligations to current employees was justified under the "necessity of payment" rule first enunciated by the Supreme Court in Miltenberger v. Logansport Railroad Co., 106 U.S. 286, 1 S.Ct. 140 (1882). The Ninth Circuit has recognized and approved of the necessity of payment doctrine. In re Adams Apple, Inc., 829 F.2d 1484, 1490 (9th Cir. 1987). This doctrine recognizes that paying certain prepetition claims may be necessary to realize a successful chapter 11 in which the value of the debtor-in-possession is maximized for the benefit of all its creditors and employees. Just for Feet, 242 B.R. 821, 825-26 (D. Del. 1999); In re Chateaugay Corp., 80 B.R. 279 (S.D.N.Y. 1987) (approving bankruptcy court order authorizing debtor to pay prepetition wages, salaries, employee reimbursement expenses and benefits);In re Gulf Air, Inc., 112 B.R. 152 (Bankr. W.D. La. 1989) (authorizing debtor in possession to pay prepetition employee wages and benefits, and health, life and workers' compensation insurance premiums).

It is critically important that the Debtors be permitted to pay their non-insider employees the prepetition wages, salaries, commissions, personal/sick leave, vacation and other pay that has accrued, and to honor existing employee benefits policies in the ordinary course of business. Not only will this assist in maintaining the continuity of the Debtors' businesses and preserve the morale of their labor force, but a potential loss (or delay in receipt) of benefits or earned wages would work a hardship on the Debtors' employees. The Debtors' ability to preserve their businesses and assets will be affected adversely if they are unable to retain the support and loyalty of their employees.

In addition, the authority to continue to pay the Debtors' employees and to maintain the current employee benefits programs is necessary to ensure that the Debtors can retain employees knowledgeable about the Debtors' businesses, to provide an incentive for the Debtors' employees to continue to provide quality services to the Debtors at a time when they clearly are needed and to allow the Debtors to remain competitive in the job markets in which they maintain operations. The Debtors operate in a very competitive market for certain of their employees, and, in the ordinary course, there tends to be a lot of movement of employees. The Debtors continue to try to keep this to a minimum and believe that the relief requested is critical to that objective.

The adequate staffing of the Debtors' operations without excessive turnover is essential to the Debtors' ability to conduct business and obtain the highest value for the sale of their assets. If the Debtors are unable to assure their employees that they will be paid timely, or if employees are not immediately assured of uninterrupted critical benefits payments to which they are entitled, the Debtors' operations could suffer immediate and irreparable harm due to employee resentment, resignations and loss of goodwill. The Debtors' failure to honor accrued obligations and benefits and to maintain the Debtors' employee benefits package would create great concern and discontent among their employees and adversely affect their ability to retain them. This, in turn, would likely cause a slowdown or cessation of the Debtors' operations which would severely hinder their efforts to maximize the value of their operations and assets.

Moreover, for the Debtors to identify whether and to what extent individual employees hold priority or general unsecured claims for employee benefits, and to modify benefit policies to enforce these distinctions, would be disruptive, time-consuming and expensive. This would lead to further discontent among the Debtors' employees and hamper business operations.

In short, to maintain the continuity of the Debtors' businesses and to preserve the morale of employees, the Debtors should be permitted to pay and honor any accrued but unpaid prepetition wages, vacation days, personal/sick leave days, short-term disability, retirement plan benefits and other employee benefits in the ordinary course of their businesses. Accordingly, the payment of the prepetition employee-related obligations, described above, and the continuation of employee compensation and benefits is essential to the Debtors' efforts.

B. These Employee Payments Will Not Prejudice Other Unsecured Creditors

Bankruptcy Code section 507(a)(4) grants a fourth priority to employee claims for wages, salaries, or commissions, including vacation, severance, and sick leave pay, earned during the 180 days before the bankruptcy, up to $10,950 per employee. 11 U.S.C. § 507(a)(4). Section 507(a)(5) grants a fifth priority to all claims for contributions to employee benefit plans, such as insurance plans, based on services performed during the 180 days before bankruptcy, up to a total of $10,950 times the number of covered employees, less the aggregate amount of priority wage claims under section 507(a)(4).

Here, the Debtors believe the amounts to be paid to the Debtors' 1,325 employees for accrued but unpaid prepetition services is far below the $10,950 to which each employee is entitled to priority payment under section 507(a)(4) and (a)(5). The only difference is that he Debtor proposes to pay them now, instead of at the end of the case. Thus these payments will not prejudice unsecured creditors and will avert potential hardship to the employees. Equally important, by insuring employee loyalty and morale, these payments will benefit other creditors and preserve the value of the Debtors' estates.

C. Notice of This Motion Complies With This Court's Requirements and Is Appropriate

Pursuant to this Court's Guidelines for First Day Motions, this Motion has been served by facsimile, or personal service, or email (where consent was granted) or, where necessary, by express or overnight mail on all known secured creditors and the twenty largest unsecured creditors in each of the Debtors' cases and the United States Trustee. Because of the exigent circumstances, the Debtors respectfully submit, and request that this Court find that no further notice of this Motion is required.

D. **<u>The Court May Grant this First Day Motion Without A Hearing</u>**.

Bankruptcy Code section 102(1)(A) provides in pertinent part: "(1) 'after notice and a hearing' . . . means after such notice as is appropriate in the particular circumstances, and such opportunity for hearing as is appropriate in the particular circumstances." Furthermore, section 102(1)(B)(i) of the Bankruptcy Code "authorizes an act without actual hearing if such notice is given properly and such a hearing is not requested timely by a party in interest."

This Motion is brought as a First Day Motion in accordance with the Guidelines for First Day Motions which provide that certain matters must be addressed immediately after the commencement of a chapter 11 case in order to ensure the least possible disruption to the debtor's ongoing business operations and thereby enhance the chances for success in chapter 11. Pursuant to the Guidelines, the Court reserves discretion to grant or deny a First Day Motion without a hearing unless the Court otherwise directs. The Debtors believe that under section 102(1) of the Bankruptcy Code and the Guidelines, and with the need for immediate approval of this Motion, it would be appropriate to dispense with a hearing on the Motion.

III.

CONCLUSION

For the foregoing reasons, the Debtors respectfully request that this Court enter an order authorizing the Debtors to:

1. Pay, in accordance with the policies and practices established prior to the Petition Date, all accrued wages, salaries, commissions, reimbursable employee expenses, workers' compensation and all employee benefits that have been earned and accrued by virtue of the services rendered by the non-insider employees for the Debtors prior to the Petition Date;

2. Pay all applicable federal, state and local taxes, deductions and withholdings pertaining to the payments made pursuant to paragraph 1;

3. Pay the non-insider employees of the Debtors all amounts on account of employee wage and expense checks which may not have been presented for payment or may not have cleared the banking systems as of the Petition Date;

4. Reissue checks as necessary to cover amounts owing on any checks that have been dishonored by any bank and to reimburse employees for any resulting charges; and

5. Granting such other and further relief as is necessary and appropriate in the circumstances.

Dated: May 15, 2008

LINER YANKELEVITZ
SUNSHINE & REGENSTREIF LLP

By: */s/ Enid M. Colson*
Julia W. Brand
Enid M. Colson
Proposed Counsel for Debtors and
Debtors-In-Possession

Exhibit A

CSD 1001A [11/15/04]
Name, Address, Telephone No. & I.D. No.

Julia W. Brand, Esq. (SBN: 121760)
Enid M. Colson, Esq. (SBN: 189912)
Liner Yankelevitz Sunshine & Regenstreif LLP
1100 Glendon Ave., 14th Floor
Los Angeles, CA 90024-3503
(310) 500-3500

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF CALIFORNIA
325 West "F" Street, San Diego, California 92101-6991

In Re
STEAKHOUSE PARTNERS, INC., a Delaware corporation,

Debtor.

BANKRUPTCY NO.
08-04147-11
Date of Hearing:
Time of Hearing:
Name of Judge: James W. Meyers

ORDER ON FIRST DAY MOTION NO. 3; MOTION FOR ORDER AUTHORIZING PAYMENT OF NON-INSIDER PREPETITION ACCRUED WAGES, ETC

IT IS ORDERED THAT the relief sought as set forth on the continuation pages attached and numbered two (2) through ________ with exhibits, if any, for a total of ________ pages, is granted. Motion/Application Docket Entry No. ________

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DATED:

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Judge, United States Bankruptcy Court
James W. Meyers

Signature by the attorney constitutes a certification under Fed. R. of Bankr. P. 9011 that the relief in the order is the relief granted by the court.

Submitted by:

Liner Yankelevitz Sunshine & Regenstreif LLP
(Firm name)

By: /s/ Enid M. Colson
Attorney for [X] Movant [ ] Respondent
Enid M. Colson

The Debtors and Debtors-in-Possession Steakhouse Partners, Inc., Paragon Steakhouse Restaurants and Paragon of Michigan (the "Debtors"), having properly filed and provided the required notice of its First Day Motion No: 3 "Motion for Order Authorizing Payment of Non-Insider Prepetition Accrued Wages, Salaries, Commissions, Employee Expenses, Workers' Compensation and Employee Benefits and Payment of Related Taxes and Tax Deposits and Authorizing and Directing Banks to Honor Payroll Account Checks and Expense Reimbursement Checks" ("Payroll Motion") and the Omnibus Declaration of Joseph L. Wulkowicz filed in support of the Debtors' First Day Motions, the Court having determined that the legal and factual bases set forth in the Payroll Motion establish just cause for the relief requested, and it appearing that such relief is in the best interests of the Debtors' estates, and after due deliberation and sufficient good cause appearing therefor,

IT IS HEREBY ORDERED AS FOLLOWS:

1. The Debtors' Motion for Order Authorizing Payment of Non-Insider Prepetition Accrued Wages, Salaries, Commissions, Employee Expenses, Workers' Compensation and Employee Benefits and Payment of Related Taxes and Tax Deposits and Authorizing and Directing Banks to Honor Payroll Account Checks and Expense Reimbursement Checks is granted;

2. The Debtors are authorized to pay, in accordance with the policies and practices established prior to the Petition Date, all accrued wages, salaries, commissions, reimbursable employee expenses, workers' compensation and all employee benefits that have been earned and accrued by virtue of the services rendered by the non-insider (as defined in section 101(31)) of the Bankruptcy Code) employees of the Debtors prior to the Petition Date;

3. The Debtors are authorized to pay all applicable federal, state and local taxes, deductions and withholdings pertaining to the payments made pursuant to paragraph 2;

4. The Debtors are authorized to pay the non-insider employees of the Debtors all amounts on account of employee wage and expense checks which may not have been presented for payment or may not have cleared the banking systems as of the Petition Date; and

5. The Debtors are authorized to reissue checks as necessary to cover amounts owing on any checks that have been dishonored by any bank and to reimburse employees for any resulting charges; and

IT IS SO ORDERED

CSD 1001A [11/15/04]
Name, Address, Telephone No. & I.D. No.
Julia W. Brand, Esq. (SBN: 121760)
Enid M. Colson, Esq. (SBN: 189912)
Liner Yankelevitz Sunshine & Regenstreif LLP
1100 Glendon Avenue, 14th Floor
Los Angeles, California 90024-3503
310.500.3500

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF CALIFORNIA
325 West "F" Street, San Diego, California 92101-6991

In Re
PARAGON STEAKHOUSE RESTAURANTS, a Delaware corporation

Debtor.

BANKRUPTCY NO.
08-3152-11
Date of Hearing:
Time of Hearing:
Name of Judge: James W. Meyers

ORDER ON FIRST DAY MOTION NO. 3; MOTION FOR ORDER AUTHORIZING PAYMENT OF NON-INSIDER PREPETITION ACCRUED WAGES, ETC.

IT IS ORDERED THAT the relief sought as set forth on the continuation pages attached and numbered two (2) through ______ with exhibits, if any, for a total of ______ pages, is granted. Motion/Application Docket Entry No. ______

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DATED:

____
Judge, United States Bankruptcy Court
James W. Meyers

Signature by the attorney constitutes a certification under Fed. R. of Bankr. P. 9011 that the relief in the order is the relief granted by the court.

Submitted by:

Liner Yankelevitz Sunshine & Regenstreif LLP
(Firm name)

By: */s/ Enid M. Colson*
Attorney for [X] Movant [ ] Respondent
Enid M. Colson

The Debtors and Debtors-in-Possession Steakhouse Partners, Inc., Paragon Steakhouse Restaurants and Paragon of Michigan (the "Debtors"), having properly filed and provided the required notice of its First Day Motion No: 3 "Motion for Order Authorizing Payment of Non-Insider Prepetition Accrued Wages, Salaries, Commissions, Employee Expenses, Workers' Compensation and Employee Benefits and Payment of Related Taxes and Tax Deposits and Authorizing and Directing Banks to Honor Payroll Account Checks and Expense Reimbursement Checks" ("Payroll Motion") and the Omnibus Declaration of Joseph L. Wulkowicz filed in support of the Debtors' First Day Motions, the Court having determined that the legal and factual bases set forth in the Payroll Motion establish just cause for the relief requested, and it appearing that such relief is in the best interests of the Debtors' estates, and after due deliberation and sufficient good cause appearing therefor,

IT IS HEREBY ORDERED AS FOLLOWS:

1. The Debtors' Motion for Order Authorizing Payment of Non-Insider Prepetition Accrued Wages, Salaries, Commissions, Employee Expenses, Workers' Compensation and Employee Benefits and Payment of Related Taxes and Tax Deposits and Authorizing and Directing Banks to Honor Payroll Account Checks and Expense Reimbursement Checks is granted;

2. The Debtors are authorized to pay, in accordance with the policies and practices established prior to the Petition Date, all accrued wages, salaries, commissions, reimbursable employee expenses, workers' compensation and all employee benefits that have been earned and accrued by virtue of the services rendered by the non-insider (as defined in section 101(31)) of the Bankruptcy Code) employees of the Debtors prior to the Petition Date;

3. The Debtors are authorized to pay all applicable federal, state and local taxes, deductions and withholdings pertaining to the payments made pursuant to paragraph 2;

4. The Debtors are authorized to pay the non-insider employees of the Debtors all amounts on account of employee wage and expense checks which may not have been presented for payment or may not have cleared the banking systems as of the Petition Date; and

5. The Debtors are authorized to reissue checks as necessary to cover amounts owing on any checks that have been dishonored by any bank and to reimburse employees for any resulting charges; and

IT IS SO ORDERED

Name, Address, Telephone No. & I.D. No.
Julia W. Brand, Esq. (SBN: 121760)
Enid M. Colson, Esq. (SBN: 188912)
Liner Yankelevitz Sunshine & Regenstreif, LLP
1100 Glendon Avenue, 14th Floor
Los Angeles, California 90024-3503
310.500.3500

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF CALIFORNIA
325 West "F" Street, San Diego, California 92101-6991

In Re
PARAGON OF MICHIGAN, INC., a Wisconsin corporation

Debtor.

BANKRUPTCY NO.
08-4153-11
Date of Hearing:
Time of Hearing:
Name of Judge: James W. Meyers

ORDER ON FIRST DAY MOTION NO. 3; MOTION FOR ORDER AUTHORIZING PAYMENT OF NON-INSIDER PREPETITI ACCRUED WAGES, ECT

IT IS ORDERED THAT the relief sought as set forth on the continuation pages attached and numbered two (2) through ________ with exhibits, if any, for a total of ________ pages, is granted. Motion/Application Docket Entry No. ________

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DATED:

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Judge, United States Bankruptcy Court
James W. Meyers

Signature by the attorney constitutes a certification under Fed. R. of Bankr. P. 9011 that the relief in the order is the relief granted by the court.

Submitted by:

Liner Yankelevitz Sunshine & Regenstreif, LLP
(Firm name)

By: */s/ Enid M. Colson*
Attorney for [X] Movant [ ] Respondent
Enid M. Colson

The Debtors and Debtors-in-Possession Steakhouse Partners, Inc., Paragon Steakhouse Restaurants and Paragon of Michigan (the "Debtors"), having properly filed and provided the required notice of its First Day Motion No: 3 "Motion for Order Authorizing Payment of Non-Insider Prepetition Accrued Wages, Salaries, Commissions, Employee Expenses, Workers' Compensation and Employee Benefits and Payment of Related Taxes and Tax Deposits and Authorizing and Directing Banks to Honor Payroll Account Checks and Expense Reimbursement Checks" ("Payroll Motion") and the Omnibus Declaration of Joseph L. Wulkowicz filed in support of the Debtors' First Day Motions, the Court having determined that the legal and factual bases set forth in the Payroll Motion establish just cause for the relief requested, and it appearing that such relief is in the best interests of the Debtors' estates, and after due deliberation and sufficient good cause appearing therefor,

IT IS HEREBY ORDERED AS FOLLOWS:

1. The Debtors' Motion for Order Authorizing Payment of Non-Insider Prepetition Accrued Wages, Salaries, Commissions, Employee Expenses, Workers' Compensation and Employee Benefits and Payment of Related Taxes and Tax Deposits and Authorizing and Directing Banks to Honor Payroll Account Checks and Expense Reimbursement Checks is granted;

2. The Debtors are authorized to pay, in accordance with the policies and practices established prior to the Petition Date, all accrued wages, salaries, commissions, reimbursable employee expenses, workers' compensation and all employee benefits that have been earned and accrued by virtue of the services rendered by the non-insider (as defined in section 101(31)) of the Bankruptcy Code) employees of the Debtors prior to the Petition Date;

3. The Debtors are authorized to pay all applicable federal, state and local taxes, deductions and withholdings pertaining to the payments made pursuant to paragraph 2;

4. The Debtors are authorized to pay the non-insider employees of the Debtors all amounts on account of employee wage and expense checks which may not have been presented for payment or may not have cleared the banking systems as of the Petition Date; and

5. The Debtors are authorized to reissue checks as necessary to cover amounts owing on any checks that have been dishonored by any bank and to reimburse employees for any resulting charges; and

IT IS SO ORDERED