Views from the Bench, 2018



Navigating the Claims-Trading Landscape to Avoid Potential Pitfalls

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AMERICAN BANKRUPTCY INSTITUTE | VIEWS FROM THE BENCH: 2018 "NAVIGATING THE CLAIMS-TRADING LANDSCAPE TO AVOID POTENTIAL PITFALLS"

Topics: (I) Non-Statutory Insiders, (II) Transferred Claims Subject to Preference Challenges, (III) Debt Documents and Claims Trading, and (IV) Strategic Claims Trading

I. Non-Statutory Insiders

Section 101(31) of the Bankruptcy Code provides examples of who qualifies as a statutory "insider," including directors, officers, and controlling persons of a debtor. However, this is a non-exhaustive list. Courts have developed a body of law that encompasses persons not listed in this section, known as "non-statutory insiders." Some courts have developed different tests to determine who qualifies as a non-statutory insider. The Supreme Court has not yet endorsed any of those tests.

In <u>U.S. Bank N.A. ex rel. CW Capital Asset Mgmt. LLC v. Vill. at Lakeridge, LLC</u>, 138 S. Ct. 960 (2018), the Supreme Court granted certiorari to answer a single, narrow issue: whether the Ninth Circuit was right to apply a clear error (rather than *de novo*) standard of review. The opinion does not provide much guidance as to how lower courts should evaluate whether a creditor is a non-statutory insider under the Bankruptcy Code. However, it does show that a number of the Justices have doubts about the Ninth Circuit's test. Until a test is officially endorsed, lower courts will continue experimenting.

In	re The Village at Lakeridge, LLC, 814 F.3d 993 (9th Cir. 2016).
	The Debtor, Village at Lakeridge, LLC (" <u>Lakeridge</u> ") had one member, MBP Equity Partners, LLC (" <u>MBP</u> ").
FACTS & PROCEDURAL HISTORY	Lakeridge had two creditors: (i) secured creditor U.S. Bank, and (ii) unsecured creditor MBP.
mstoki	 After Lakeridge filed for chapter 11 and while it filed its disclosure statement and plan of reorganization, Bartlett, one of MBP's five board members, facilitated the sale of MBP's unsecured claim to Rabkin, with whom she was close, for \$5,000.
	U.S. Bank moved to designate Rabkin's claim and disallow it for plan voting purposes, arguing: (i) that Rabkin was both a statutory and non-statutory insider; and (ii) that the purchase was made in bad faith.
	Bankruptcy Court: designated Rabkin's claim and disallowed it for plan voting purposes on the basis that Rabkin became a statutory insider by virtue of the transferor's insider status (<i>i.e.</i> , the sole member of the LLC). Both parties appealed.
	The Bankruptcy Appellate Panel reversed the decision that Rabkin had become an insider and expressly held that, "insider status cannot be assigned and must be determined for each individual on a case-by-case basis."
ISSUE & HOLDING	 Does an insider's status transfer to a third-party transferee? Question of law, de novo review No. A creditor does not automatically become an insider simply by receiving a claim from a statutory insider.

	 What is the definition of a "non-statutory insider"? Question of law, de novo review A creditor is a non-statutory insider where: (i) the closeness of its relationship with the debtor is comparable to that of the enumerated insider classification in section 101(31) of the Bankruptcy Code; and (ii) the relevant transaction is negotiated at less than arm's length.
PERTINENT ANALYSIS	 Insider status does not transfer with the claim In the Ninth Circuit, a creditor who acquires a claim from a statutory insider is only an insider where two factors are met: (i) the closeness of the acquiring creditor's relationship with the debtor is comparable to that of the enumerated insider classification in section 101(31) of the Bankruptcy Code; and (ii) the relevant transaction is negotiated at less than arm's length. A person does not become a statutory insider solely by acquiring a claim from a statutory insider because (i) insider status only pertains to the claimant, not the claim; and (ii) a person's insider status is a question of fact that must be determined after the claim transfer occurs. And, the clear language of the Bankruptcy Code which indicates that the term "insider" is a noun referring to a person. Lastly, if an insider's status transferred to a third-party transferee, then logic would dictate that an insider could receive "non-insider" status, cleansing an otherwise inappropriate vote, if he received such claim from a non-insider. Defining a non-statutory insider Legislative history indicates that Congress sought to include those with a sufficiently close relationship with the debtor that their conduct is made subject to closer scrutiny than those dealing at arms' length with the debtor.
DISSENT	Judge Clifton concurred in holding that a person does not become a statutory insider solely by acquiring a claim from a statutory insider, so long as, "the interest was acquired by an independent party, for bona fide reasons, uninfected with the unique motivations of the insider," but dissented as to the lower courts abidance by the de novo standard.
	 He disagreed with how the Bankruptcy Court applied the clear error standard of judicial scrutiny, and determined that the court should hold that a creditor is a non-statutory insider in the absence of an arms-length transaction. Accordingly, Judge Clifton argued that Rabkin was clearly a non-statutory insider because the transaction was negotiated at less than arm's length. Judge Clifton also expressed that the majority opinion presents a public policy concern because, under this holding, a savvy debtor can comply with the good faith requirement by following a simple formula: develop a reorganization plan that would provide a payout on the insider claim if approved, and then sell the claim to a friendly third party for a price lower than the payout, enabling the debtor to maneuver the third party into a position where it would be foolish not to vote for approval of the plan, ensuring a "yes" vote and thereby allowing the debtor to effectively avoid the requirement under section 1129(a)(10) that at least one non-insider must approve the plan.

U.S. Bank N.A. ex rel. CW Capital Asset Mgmt. LLC v. Vill. at Lakeridge, LLC, 138 S. Ct. 960 (2018).		
FACTS & PROCEDURAL HISTORY	 As discussed above, In <u>In re The Village at Lakeridge, LLC</u>, the Ninth Circuit Court of Appeals affirmed the Bankruptcy Appellate Panel's holdings that (i) a person does not become a statutory insider solely by acquiring a claim from a statutory insider; (ii) Rabkin was not a non-statutory insider; and (iii) the claim assignment at issue was not made in bad faith. 814 F.3d 993 (9th Cir. 2016). U.S. Bank Appealed to the United States Supreme Court, which granted certiorari on the narrow issue of whether the Circuit Court applied the proper standard of judicial scrutiny. 	
ISSUE & HOLDING	Did the Court of Appeals apply the proper standard in reviewing the Bankruptcy Court's determination that Rabkin, the transferee who acquired a claim from a statutory insider, was not a non-statutory insider? Yes, the question is one of mixed law and fact and the court correctly applied clear error scrutiny because his transaction was conducted at arm's length.	
ANALYSIS	Mixed Question of Law & Fact: The proper standard of scrutiny turns on the question being analyzed. The standard of review applicable to the existence of an arm's length transaction for the purposes of determining whether a party is a non-statutory inside is a mixed question of law and fact that involves: (i) a legal test to determine whether a party is an insider; (ii) a factual analysis to gather information related to the parties' relationship; and (iii) a mixed question of law and fact, at the heart of the case, to determine whether the factual analysis satisfies the legal standard.	
	Court Here Was Weighing Case-Specific Facts: The standard of review applicable to mixed questions of law and fact will depend on whether the situation warrants a court to expound on the law when legal principles need to be developed, or if the court must instead marshal and weigh evidence on case-specific basis.	
	Bankruptcy Court is Best Suited to Make Factual Judgments: Because determining insider status is highly fact specific, the Bankruptcy Court is the best suited to determine how the relationship fits within the bounds of the law because it oversees the presentation of evidence, has heard all the witnesses, and has both the closest and deepest understanding of the record, that is, the Bankruptcy Court.	
	<u>Concurrence</u> : Justice Kennedy reiterated that the Court was not necessarily endorsing the Ninth Circuit's test.	
	Concurrence: Justice Sotomayor's concurrence, joined by Justices Kennedy,	

Thomas, and Gorsuch expressed concern as to whether the Ninth Circuit's test is appropriate, but because certiorari was granted on a narrow question alone, they were unable to evaluate whether the underlying test was correct. A statutory insider does not cease being an insider just because a court finds that a relevant transaction was conducted at arm's length. Under the Ninth Circuit's test, because the two prongs are conjunctive, a court's conclusion that the relevant transaction was conducted at arm's length defeats a finding of non-statutory insider status, regardless of how close a person's relationship is with the debtor or whether he is otherwise comparable to a statutorily enumerated insider.

II. Transferred Claims Subject to Preference Challenge

Because a claim subject to a preference challenge is as disallowable in the hands of a transferee as the hands of the original transferor, it is imperative that appropriate diligence is performed to assess the risk of these claims.

<u>In re KB Toys, Inc.,</u> 736 F.3d 247 (3rd Cir. 2013).		
RELEVANT CODE SECTIONS	Under Section 502(d) of the Bankruptcy Code, the court may disallow "any claim of any entity" for which property is recoverable under various other sections of the Bankruptcy Code or is a transferee of a transfer avoidable under the Bankruptcy Code.	
	Under Section 550(b), a trustee may not recover from a good faith purchaser under an avoidance action.	
FACTS & PROCEDURAL HISTORY:	The Debtor, KB Toys, Inc. (" <u>KB</u> ") filed for chapter 11 relief and filed a SOFA about three months later that disclosed all payments made within the 90 days immediately preceding the petition date.	
	Subsequently, ASM Capital Management (" <u>ASM</u> ") began purchasing claims from various trade creditors, ultimately acquiring nine claims over a span of three years.	
	KB's plan of reorganization established a trust authorized to liquidate and collect certain assets for the benefit of creditors. The KB Chapter 11 Trustee filed an objection with the Bankruptcy Court seeking to disallow the claims that ASM purchased under section 502(d) of the Bankruptcy Code because each original claimant received a preference before transferring its claim to ASM.	
	The Bankruptcy Court disallowed the claims holding that, under section 502(d) of the Bankruptcy Code, "disabilities attach to and travel with the claim." ASM appealed to the U.S. District Court for the District of Delaware.	
	The District Court affirmed, and ASM appealed to the Third Circuit Court of Appeals.	
ISSUE & HOLDING:	• Is a trade claim that is subject to disallowance under section 502(d) of the Bankruptcy Code is disallowable in the hands of a subsequent transferee?	
	Such trade claims are disallowable in the hands of a subsequent transferee, just as if the claims were in the hands of the original claimant.	
	Are purchasers of claims subject to preference challenges under section 502(d) entitled to rely on the good faith defense under section 550(b) of the Bankruptcy Code?	
	No. Purchasers of claims subject to preference may not rely on the good faith defense.	

PERTINENT

Reasoning for claims continuing to be subject to preference despite transfer:

ANALYSIS

- <u>Text of the Statute</u>: provides that the court shall disallow <u>any claim of any entity</u> from which property is avoidable under section 547 of the Bankruptcy Code.
 - Such claims cannot be allowed until the entity who received the avoidable transfer, or the transferee, returns it to the estate. 11 U.S.C. § 502(d)
- Aims of 502(d): to ensure equality of distribution and compelling compliance with
 judicial orders. To hold otherwise would allow claimants to cleanse their
 disallowed claims by selling them. This would also eliminate the court's leverage
 over such claimants

<u>Assumption of Risk</u>: A claim purchaser assumes the risk by voluntarily injecting itself into the bankruptcy process. Here, ASM could have protected itself from the risk of disallowance by reviewing KB's SOFAs, which would have put ASM on notice of the claims' vulnerability to preference attacks.

Reasoning for prohibiting use of good faith defense under section 502(d):

- Not Property of the Estate: The defense only protects good faith transferees who purchase property of the estate that is avoidable and a claim is not property of the estate, but rather a claim against the estate.
- <u>Sophisticated Parties:</u> Claim purchasers are sophisticated entities who knowingly and voluntarily accept the risks and uncertainties associated with the process after conducting extensive due diligence.

III. Debt Documents & Claims Trading

Both In re LightSquared Inc., 511 B.R. 253 (Bankr. S.D.N.Y. 2014) and In re ASHNIC Corp., 736 F.3d 247 (3rd Cir. 2017) illustrate that the contractual language in debt documents must be read in context and with the spirit and purpose of the documents and provisions in mind. Courts will not permit "end runs" around contractual provisions that result in creditors achieving inequitable or unjust results.

The recent result in <u>In re Woodbridge Group of Companies LLC</u>, Case No. 17-12560-KJC (D. Del. 2018), confirms this point. There, and as discussed more fully below, Judge Kevin J. Carey determined that an anti-assignment clause in the underlying debt instrument on which a creditor's claim was based rendered the claim null and void.

Finally, the decision in <u>In re Westinghouse Electric Company LLC</u>, Case No. 17-10751-MEW (Bankr. S.D.N.Y. 2018) illustrates the importance of ensuring claims trades are documented properly to effectuate a valid and enforceable trade. There, the court refused to interpret an email exchange as a binding claims trade.

In re LightSquared Inc., 511 B.R. 253 (Bankr. S.D.N.Y. 2014).		
RELEVANT CODE SECTION & TEST	Under Section 510(c) of the Bankruptcy Code, a bankruptcy court may equitably subordinate a claim to rearrange the priorities of creditors' interests and to place all or part of a wrongdoer's claim in an inferior status to achieve a more just result in the reorganization of a debtor.	
	Under the Mobile Steel Test, a court may equitably subordinate a claim where: (i) the claimant engaged in some type of inequitable conduct, (ii) the misconduct must have resulted in injury to the creditors of the bankruptcy or conferred an unfair advantage, and (iii) equitable subordinate may not be inconsistent with the provisions of the Bankruptcy Code.	
FACTS & PROCEDURAL HISTORY:	 Defendant was the majority shareholder and a board member of the Debtor's competitors. It created a special purpose entity ("SPE") to acquire holdings of the Debtor's debt and eventually came to control a debt class with a blocking position. The Intercreditor Agreement underlying the debt documents contained explicit 	
	prohibitions against competitors acquiring LightSquared's debt. • The Debtor filed a complaint asking the court to (i) determine that the assignment of the claim to the competitor was improper and (ii) enter an order disallowing or equitably subordinating the claim.	
ISSUE & HOLDING:	Was assignment of the claim to the Debtor's competitor's SPE prohibited by the Intercreditor Agreement?	
	No. It was not technically violated because of the use of the SPE as the acquiring entity, and because the competitors had no direct interest in the SPE.	

	 Did the Debtor's competitors actions in acquiring the claim subject it to equitable subordination? Yes. The competitor's actions violated the implied covenant of good faith and fair dealing and engaged in equitable conduct.
PERTINENT ANALYSIS	Equitable Subordination: acquisition of the debt via the SPE violated the purpose of the agreement, which was to prevent competitors from penetrating the Debtors' capital structure. The SPE took inordinate amounts of time to close claim transfer transactions and this caused injury to the creditors by influencing the bankruptcy case while it worked on an acquisition strategy.

In re ASHNIC Corp., 736 F.3d 247 (3rd Cir. 2017).		
FACTS & PROCEDURAL HISTORY:	 A major shareholder, Yucaipa, attempted to circumvent debt covenants that expressly restricted it from acquiring the company's debt. Under the Debtor's Credit Agreement ("CA"), Yucaipa could not be assigned any debt, and was restricted on how much and what type of debt it could acquire. Under the third amendment to the Credit Agreement, which was implemented to extend post-bankruptcy financing to the debtor, Yucaipa was allowed to acquire a limited amount of the Debtor's Term Loan. Aside from the Term Loan, there was a Revolving Loan and a Line of Credit Yucaipa could not participate in. A hedge fund, ComVest Investment Partners III, L.P. purchased approximately 55% of the First Lien Debt under its own name and became a "Requisite Lender" which allowed it to edit the Credit Agreement (entering into the fourth amendment) so as to remove the restrictions on Yucaipa's ability to acquire debt. The hedge fund subsequently sold its full 55% investment in the First Lien Debt to Yucaipa. Yucaipa then became the "Requisite Lender" under the credit agreement with the ability to make amendments moving forward. A group of lenders under the credit agreement, BD/S, sued in New York state court, alleging the fourth amendment was void and that Yucaipa was not the Requisite Lender. They later filed an involuntary bankruptcy proceeding against the Debtor. The Debtor brought an adversary proceeding to determine the identity of the "requisite lenders" under the credit agreement, as they have the power to amend the agreement in certain instances. The Bankruptcy court granted summary judgment in favor of BD/S. Yucaipa appealed. 	
ISSUE & HOLDING:	 Is the third amendment, limiting Yucaipa's ability to acquire the Debtor's debt, valid? ➤ Yes. Unanimous lender consent was not required to pass the amendment. Is Yucaipa the Requisite Lender? ➤ No. Yucaipa was contractually and intentionally limited from properly 	
PERTINENT ANALYSIS	 No. Iucaipa was contractually and imentionally limited from property amassing more than 50% of the outstanding debt. The plain meaning of the agreements was unambiguous, and no extrinsic evidence was necessary "Yucaipa knew it was prohibited from acquiring Line of Credit commitments and that the Third Amendment restricted Yucaipa's rights as Lender. Yucaipa's argument that the express language in the Third Amendment does not exclude [LC] Commitments is an attempted "end run" around the intent to limit Yucaipa's 	

In re Woodbridge Group of Companies, LLC, Case No. 17-12560-KJC (D. Del. 2018)

FACTS & PROCEDURAL HISTORY:

- Prepetition, debtor Woodbridge Mortgage Investment Fund 3A LLC issued three promissory notes to the Berlingers. Each contained an anti-assignment clause.
- The anti-assignment clauses stated that neither the note nor any other instruments
 executed in connection therewith was assignable by the lender without the
 borrower's written consent, and that any attempted assignments absent consent
 would be null and void.
- Post-petition, the Berlingers assigned the notes to Contrarian Funds LLC.
 Contrarian filed a proof of claim for \$75,000. The Debtors objected to this transfer.
- The Debtors also instituted a 90-day moratorium on claims trading.

ISSUE, HOLDING & ANALYSIS:

- Is the anti-assignment clause contained in the promissory note is a valid restriction on assignment rights under Delaware law?
 - > Yes. Under Delaware law, anti-assignment clauses are narrowly construed. The law distinguishes between the power to assign and the right to assign. The null and void language restricted the power to assign, and thus, assignment was null and void.
- Whether a non-breaching party to a promissory note in payment default is still bound by an anti-assignment clause when seeking to enforce the note in bankruptcy through a proof of claim.
 - > Even though the Debtors breached under the note, the anti-assignment clauses are still enforceable. The court applied the same limiting principle as used by Judge Kevin Carey in his KB Toys decision that a non-breaching party may not emerge post-breach with more rights than it had pre-breach.
- Whether the Uniform Commercial Code ("UCC") overrides and nullifies an antiassignment clause in a promissory note
 - ➤ The UCC's restriction on collateral assignments (in Section 9-408 of the UCC) did not prohibit restrictions on the assignment of a security interest in a promissory note.

In re Westinghous	e Electric Company LLC, Case No. 17-10751-MEW (Bankr. S.D.N.Y. 2018).
FACTS & PROCEDURAL HISTORY:	Bestor Westinghouse filed for enapter 11.
ISSUE & HOLDING:	Was there a valid offer and acceptance? Was there a meeting of the minds and an enforceable contract authorizing the trade of certain claims where there was no executed document? The court held that there was never a binding offer and acceptance sufficient to create a contract of any kind, and that alternatively it was clear that neither party had any intent of being bound before the execution of a formal written document.
PERTINENT ANALYSIS	 The court analyzed various emails between the Landstar and Whitebox and determined that no offer was accepted and that there was no "type II" contract: There was no acceptance. The offer that Landstar extended Whitebox was responded to with a counteroffer because it included recourse payment obligations and recourse interest rate terms that were not previously discussed. Landstar's response to Whitebox's transfer was not an acceptance. Therefore, there was no claims trade. There was no "Type II" contract. No Type II Contract existed because Whitebox expressed in its counteroffer that their agreement to pay a particular price was subject to other additional terms, and was not an offer to be bound by a price and negotiate other provisions in good faith, a required component of the Type II Contract. In concluding this, Judge Wiles noted "[i]f claims traders want their customs to be binding when they deal with non-professionals like Ms. Bowers, it is incumbent on them to set forth the terms in a clear and unequivocal way." The court further noted that there was a clear intent not to be bound given that (i) there was no memorialized and executed document, when typically Whitebox had such documents when purchasing claims, and (ii) there was no indication that a binding contract had been formed absent an executed document. Judge Wiles heavily emphasized the use of "subject to" by both parties in their email exchanges.

IV. Strategic Claims Trading

A. Purchasing Claims to Block Confirmation

Earlier this year, the Ninth Circuit held that a creditor could purchase claims for the sole reason of preventing the confirmation of a chapter 11 plan, and that such action did not, on its own, establish "bad faith" warranting vote designation.

<u>In re Fagerdala,</u> 891 F.3d 848 (9th Cir. 2018).		
FACTS & PROCEDURAL HISTORY:	Fagerdala USA – Lompoc, Inc., the debtor, was a California corporation that owned real estate worth approximately \$6 million. Pacific Western Bank held a senior secured claim worth approximately \$4 million, secured on Fagerdala's real estate.	
	Fagerdala filed for chapter 11 and filed a proposed chapter 11 plan of reorganization. Pacific Western Bank was not satisfied with the proposed treatment its secured claim under the proposed plan.	
	The debtor sought to "cram up" its secured lender, Pacific Western Bank, by using the general unsecured claims class to achieve its requirement to have an impaired accepting class vote in favor of the plan. Pacific Western Bank acquired 50% in number of the allowed general unsecured claims. Pacific Western Bank then voted all of its claims – both secured and unsecured – against Fagerdala's chapter 11 plan.	
	Fagerdala moved to designate Pacific Western Banks's votes of the Purchased Claims under section 1126(e) arguing that the Pacific Western Bank had not purchased them in good faith.	
	The bankruptcy court granted Fagerdala's designation motion, resting its decision on (i) the objective fact that Pacific Western Bank did not offer to purchase all general unsecured claims (and therefore purchased in bad faith), and (ii) its finding that failing to designate the Purchased Claims' votes would be highly prejudicial to the remaining creditors in the general unsecured claims class. On appeal, the district court affirmed the bankruptcy court's designation order.	
ISSUE & HOLDING:	 Does the purchase of claims solely for the purpose of blocking confirmation of a chapter 11 plan constitute bad faith justifying vote designation? Purchasing claims to acquire a blocking position in a class to thereby influence the outcome of a chapter 11 plan process is not a per se act of bad faith. A showing of bad faith requires evidence that a party acted with an "ulterior motive" beyond merely pursuing its enlightened self-interest to protect its economic interests. 	
PERTINENT ANALYSIS	In overturning the Bankruptcy Court's decision, the Ninth Circuit relied on the principle that creditors are permitted to utilize the Bankruptcy Code for their own strategic advantage. The court reasoned that such action, absent an ulterior motive, does not constitute bad faith.	

• The court further reasoned that bad faith is evidenced by a creditor attempting to obtain a benefit to which it was not entitled, and that such action was distinguishable from when and where a creditor took an action to protect its own proper interests. "[C]reditors do not need to approach reorganization plans with a high degree of altruism and with the desire to help the debtor and their fellow creditors. . . [m]erely protecting a claim to its fullest extent cannot be evidence of bad faith."

B. Purchasing Claims to Obtain Standing

The Fifth Circuit held that a party could not retroactively create appellate standing by purchasing a debtor claim after a bankruptcy court overruled the party's objection to a retention application.

Matter of Technicool, 896 F.3d 382 (5th Cir. 2018).		
FACTS & PROCEDURAL HISTORY:	Robert Furlough owned the Debtor. Technicool was sued in Texas state court by National Oilwell Varco ("NOV") for claims arising from the sale of "faulty" air conditioner	
	NOV then lodged a \$3 million claim. Later, the trustee sought to consolidate several of Furlough's related businesses and pierce the corporate veil, and filed an application to employ Stacey & Backer, P.C. ("SBPC"). SBPC was counsel for NOV in both the chapter 11 proceedings and the state court proceedings.	
	Furlough objected to the retention of SBPC. The bankruptcy court found he had no standing and ultimately approved SBPC's retention as special counsel.	
ISSUE & HOLDING:	Does an individual have standing to appeal a bankruptcy court's order under the "person aggrieved" test where the creditor claim was purchased after the bankruptcy order, during the pendency of the appeal?	
PERTINENT ANALYSIS	Furlough argued that he had standing because (i) but for NOV's proof of claim, he would stand to receive an estate surplus, and that because SBPC represented NOV, it might fail to disclose any problems with that claim thereby limiting Furlough's possibility of recovery, and (ii) he had standing as a creditor of Technicool because standing is determined as of the commencement of the case.	
	The Fifth Circuit rejected these arguments. The court emphasized that "only those with a direct, financial stake in a given order can appeal it." The court found Furlough's claim of harm was too speculative in nature because the appointment of SBPC as special counsel to the trustee did not directly affect whether the bankruptcy court approved or denied NOV's claim. It further found that a creditor could not obtain standing to appeal retroactively by purchasing a claim while the appeal was pending.	

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:	Chapter 11
WOODBRIDGE GROUP OF COMPANIES, LLC, et al., 1	Case No. 17-12560 (KJC)
Debtors.	(Jointly Administered)

NOTICE REGARDING TRANSFERS OF UNITS OR NOTES

The above-captioned debtors and debtors in possession (collectively, the "<u>Debtors</u>") in these jointly administered chapter 11 cases (collectively, the "<u>Bankruptcy Cases</u>") have received inquiries with respect to the potential sale, purchase, assignment, or other transfer (collectively, "<u>Transfers</u>") of Units or Notes.² In general, the terms of the Debtors' organizational documents and other documents governing such Units and Notes: (i) require the Debtors' consent to any Transfer of Units or Notes; (ii) render any purported Transfer of such Units or Notes null and void in the absence of the Debtors' consent; and (iii) in certain instances may provide for a right of first refusal with respect to any proposed Transfer.

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The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of this information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

As used herein, the terms "Units" and "Notes" have meanings consistent with those used in the Order, Pursuant to Sections 105(a) and 1102 of the Bankruptcy Code and Bankruptcy Rule 9019, Approving the Consensual Resolution of (A) Motion of the Ad Hoc Committee of Holders of Promissory Notes of Woodbridge Mortgage Investment Fund Entities and Affiliates Pursuant to Section 1102(a)(2) of the Bankruptcy Code Directing the Appointment of an Official Committee of Noteholders, (B) Emergency Motion of Official Committee of Unsecured Creditors for Entry of an Order Directing the Appointment of a Chapter 11 Trustee Pursuant to 11 U.S.C. § 1104, (C)Motion by the U.S. Securities and Exchange Commission for Order Directing the Appointment of a Chapter 11 Trustee, (D) Joinder of Additional Noteholders to Motion of the Ad Hoc Committee of Holders of Promissory Notes of Woodbridge Mortgage Investment Fund Entities and Affiliates Pursuant to Section 1102(a)(2) of the Bankruptcy Code Directing the Appointment of an Official Committee of Noteholders, and (E) Motion of the Ad Hoc Committee of Unitholders of Woodbridge Mortgage Investment Fund Entities Pursuant to Section 1102(a)(2) of the Bankruptcy Code Directing Appointment of an Official Committee of Unitholders [Docket No. 357] (the "Settlement Order"), including the term sheet attached as Exhibit 1 thereto.

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The Debtors have discussed the Transfer requests with the Official Committee of Unsecured Creditors, the Ad Hoc Noteholders Committee, and the Ad Hoc Unit Holders Committee (collectively, the "Constituencies"). The Debtors and the Constituencies have given careful consideration to the particular facts and circumstances of these Bankruptcy Cases, including (i) the hope of the Debtors and the Constituencies to make significant progress in the next ninety (90) days toward a plan that can be effectuated by year-end with a significant recovery for noteholders and unitholders, (ii) the necessity to avoid distractions and focus on exiting the chapter 11 process, and (iii) the desire to protect noteholders and unitholders.

At the unanimous request of the Constituencies and after consideration of the matters described in the prior paragraph, the Debtors are providing notice that they will impose a temporary moratorium on consideration of consent to any Transfer of Units or Notes for the next ninety (90) days, and reserve all rights with respect to the invalidity and ineffectiveness of any prior, current, or future attempts to Transfer Units or Notes. No one contemplating the acquisition of Units or Notes should rely on any representation, warranty, or other statement (whether oral or written, and regardless of the identity of the speaker) to the effect that Units or Notes may be Transferred without the consent of the Debtors.

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As used herein, the "Ad Hoc Noteholders Committee" and the "Ad Hoc Unit Holders Committee" are the groups described in the paragraphs 11 and 13 of the term sheet attached to the Settlement Order. The Ad Hoc Noteholders Committee maintains a website at the following address: http://www.omnimgt.com/woodbridge. The Ad Hoc Unit Holders Committee are in the process of finalizing a website, which will be at the following address: www.woodbridgeunitholders.com. The Official Committee of Unsecured Creditors in the Debtors' cases maintains a website at the following address: http://www.pszjlaw.com/creditor-99.html.

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Nothing herein constitutes or shall be deemed to constitute legal or investment advice, and the Debtors reserve all rights, claims, and defenses.

Dated: March 21, 2018

Wilmington, Delaware

/s/ Ian J. Bambrick

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:

WOODBRIDGE GROUP OF COMPANIES, LLC, et al.,

Debtors.

Chapter 11

Case No. 17-12560 (KJC)

(Jointly Administered)

Hearing Date:
June 5, 2018 at 11:00 a.m. (ET)

Response Deadline:

DEBTORS' (I) OBJECTION TO PROOF OF CLAIM NO. 1216 ASSERTED BY PUTATIVE TRANSFEREE CONTRARIAN FUNDS, LLC WITHOUT PREJUDICE TO RIGHT OF PUTATIVE TRANSFERORS ELISSA AND JOSEPH BERLINGER TO ASSERT SUCH CLAIM; AND (II) REQUEST FOR A LIMITED WAIVER OF LOCAL RULE 3007-1(f)(iii), TO THE EXTENT SUCH RULE MAY APPLY

April 30, 2018 at 4:00 p.m. (ET)

Woodbridge Group of Companies, LLC and its affiliated debtors and debtors in possession (collectively, the "Debtors") in the above-captioned chapter 11 cases (the "Chapter 11 Cases") hereby file this objection (this "Objection") seeking entry of an order, substantially in the form attached hereto as **Exhibit A** (the "Proposed Order"), (i) disallowing and expunging Claim No. 1216 (the "Transferred Claim") asserted by Contrarian Funds, LLC ("Contrarian"), without prejudice to the right of Elissa and Joseph Berlinger (the "Berlingers") to assert such claim on their own behalf, as the claim has been duly scheduled by the Debtors, (ii) directing Garden City Group, Inc. (the "Claims Agent") to reflect the foregoing modifications on the official register maintained by the Claims Agent (the "Claims Register"), and (iii) waiving Rule 3007-1(f)(iii) of the Local Rules of Bankruptcy Practice and Procedure of the United States

The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of this information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

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Bankruptcy Court for the District of Delaware (the "Local Rules") to the extent such rule may otherwise bar the assertion of any subsequent substantive objection (if any) to the Transferred Claim or any claim(s) that may be filed by the Berlingers. In support of this Objection, the Debtors rely on the record of these Chapter 11 Cases and the Declaration of Bradley D. Sharp in Support of Debtors' Objection to Claim No. 1216 Asserted by Contrarian Funds, LLC attached hereto as Exhibit B (the "Sharp Declaration") and respectfully states as follows:

I. JURISDICTION AND VENUE

1. The Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 1334(b) and 157 and the *Amended Standing Order of Reference* from the United States District Court for the District of Delaware dated as of February 29, 2012. This is a core proceeding pursuant to 28 U.S.C. § 157(b) and, pursuant to Local Rule 9013-1(f), the Debtors consent to the entry of a final order by the Court in connection with this Objection to the extent that it is later determined that the Court, absent consent of the parties, cannot enter final orders or judgments in connection herewith consistent with Article III of the United States Constitution. Venue is proper before the Court pursuant to 28 U.S.C. §§ 1408 and 1409. The statutory and legal predicates for the relief requested herein are Bankruptcy Code section 502(b), Bankruptcy Rules 3001, 3003, and 3007, and Local Rules 1001-1(c), 3007-1, and 3007-2.

II. BACKGROUND

2. On December 4, 2017, certain of the Debtors commenced voluntary cases under chapter 11 of the Bankruptcy Code, and on February 9, 2018, March 9, 2018, March 23, 2018 and March 27 2018, additional affiliated Debtors commenced voluntary cases under chapter 11 of the Bankruptcy Code (collectively, the "Petition Dates"). Pursuant to sections 1107(a) and 1108 of the Bankruptcy Code, the Debtors are continuing to manage their financial affairs as debtors in possession.

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- 3. The Chapter 11 Cases are being jointly administered pursuant to Bankruptcy Rule 1015(b) and Local Rule 1015-1. As of the date hereof, no trustee has been appointed in the Chapter 11 Cases. An official committee of unsecured creditors (the "Committee") was appointed in the Chapter 11 Cases on December 14, 2017 [D.I. 79]. On January 23, 2018, the Court approved a settlement providing for the formation of an ad hoc noteholder group (the "Noteholder Group") and an ad hoc unitholder group (the "Unitholder Group") [D.I. 357].
- 4. Appended to the Transferred Claim are three promissory notes, dated October 14, 2016, August 8, 2016, and December 15, 2016 (each a "Note" and collectively the "Notes"). See Claim No. 1216. Each of the three Notes indicates that it reflects a loan of \$25,000 from the Berlingers to Debtor Woodbridge Mortgage Investment Fund 3A, LLC (the "Fund"), for a total principal amount of \$75,000 in the aggregate. Id. Each Note states: "Neither this Note, the Loan Agreement of even date herewith between [the Fund] and [the Berlingers], nor all other instruments executed or to be executed in connection therewith (collectively, the 'Collateral Assignment Documents') are assignable by [the Berlingers] without the [Fund's] written consent and any such attempted assignment without such consent shall be null and void." See Note, § 14.
- 5. Also appended to the Transferred Claim is a notarized document, dated February 13, 2018 (the "<u>Transfer Notice</u>"), purporting to transfer "all [the Berlingers'] right, title and interest in and to the [Berlingers'] claim in the amount of \$75,000.00 ... against the [Fund]" to Contrarian. *See* Claim No. 1216. On March 1, 2018, Contrarian filed the Transferred Claim as an asserted secured claim against the Fund in the amount of \$75,000. *Id*.
- 6. The Debtors have not consented and expressly do not consent to the transfer of the Berlingers' Notes to Contrarian. Sharp Decl., ¶ 4. The Debtors' schedules reflect three

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\$25,000 non-contingent, liquidated, and undisputed claims in favor of the Berlingers, for an aggregate total of \$75,000, on account of the Notes. Sharp Decl., ¶ 3.

7. A copy of the Transferred Claim is attached hereto as **Exhibit C**.

III. RELIEF REQUESTED

8. By this Objection, the Debtors seek entry of the Proposed Order (i) disallowing and expunging the Transferred Claim asserted by Contrarian in its entirety, without prejudice to the right of the Berlingers to assert such claim on their own behalf, as the claim has been duly scheduled by the Debtors, (ii) directing the Claims Agent to reflect the foregoing modifications on the Claims Register, and (iii) waiving Local Rule 3007-1(f)(iii) to the extent such rule may otherwise bar the assertion of any subsequent substantive objection (if any) to the Transferred Claim or any claim(s) that may be filed by the Berlingers.²

IV. BASIS FOR OBJECTION

9. Section 502(a) of the Bankruptcy Code provides that a "claim or interest, proof of which is filed under section 501 of this title, is deemed allowed, unless a party in interest ... objects." 11 U.S.C. § 502(a). In adjudicating claim objections, courts apply "a burden-shifting framework." *In re Devonshire PGA Holdings LLC*, 548 B.R. 689, 697 (Bankr. D. Del. 2016). The Third Circuit Court of Appeals described this framework as follows:

Initially, the claimant must allege facts sufficient to support the claim. If the averments in his filed claim meet this standard of sufficiency, it is "prima facie" valid. In other words, a claim that alleges facts sufficient to support a legal liability to the claimant satisfies the claimant's initial obligation to go forward. The burden of going forward then shifts to the objector to produce evidence sufficient to negate the prima facie validity of the filed claim. It is often said that the objector must produce evidence

Although the Debtors do not believe this Objection is one "based on substantive grounds, other than incorrect classification of a claim," Del. Bankr. L.R. 3007-1(f)(iii), and therefore do not believe that the Objection is required to "include all substantive objections to such claim," *id.*, this Objection requests (out of an abundance of caution) a waiver of Local Rule 3007-1(f)(iii) to the extent such rule might otherwise be construed to apply.

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equal in force to the *prima facie* case. In practice, the objector must produce evidence which, if believed, would refute at least one of the allegations that is essential to the claim's legal sufficiency. If the objector produces sufficient evidence to negate one or more of the sworn facts in the proof of claim, the burden reverts to the claimant to prove the validity of the claim by a preponderance of the evidence.

In re Allegheny Int'l Inc., 954 F.2d 167, 173–74 (3d Cir. 1992) (citations omitted).

- 10. Pursuant to Bankruptcy Code section 502(b)(1), a debtor in possession may object to a claim on the grounds that "such claim is unenforceable against the debtor and property of the debtor, under any agreement or applicable law for a reason other than because such claim is contingent or unmatured." 11 U.S.C. § 502(b)(1). An objection challenging the standing of a claimant is proper under § 502(b)(1) "because if a claimant has not proven it is the owner of a claim with a right to payment (i.e. the party with standing), the claim is unenforceable against the debtor under state law." *In re Richter*, 478 B.R. 30, 48–49 (Bankr. D. Colo. 2012). "To have an allowed proof of claim, the claimant must prove an initial fact: that it is the creditor to whom the debt is owed or, alternatively, that it is the authorized agent of the creditor." *In re Kendall*, 380 B.R. 37, 46 (Bankr. N.D. Okla. 2007); *see also In re Gillbreath*, 409 B.R. 84, 121 (Bankr. S.D. Tex. 2009) ("In order to establish the validity of [these] proofs of claim ... over the Debtors' objection, [the putative assignee] had the burden of proving that it actually owns the claims.").
- putative assignee where the putative assignee fails to meet its burden of proving its ownership of the debt by demonstrating a valid assignment of the obligation that would be enforceable under state law or an applicable agreement. *See, e.g., In re Foy*, 469 B.R. 209, 214–15 (Bankr. E.D. Pa. 2012) (sustaining debtor's objections under § 502(b)(1) to certain transferred claims because under applicable state law, the partial assignment of a judgment requires the consent of the judgment debtor and the putative assignee did not obtain such consent, thus the assignments 01:23110985.3

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were "a legal nullity" under state law); *Pursley v. eCast Settlement Corp.* (*In re Pursley*), 451 B.R. 213, 232–34 (Bankr. M.D. Ga. 2011) (sustaining debtor's objection under § 502(b)(1) to claim asserted by assignee on the basis that the assignee failed to prove a valid assignment of the claim that would be enforceable under state law); *In re Gillbreath*, 409 B.R. at 121 (sustaining debtor's objections under § 502(b)(1) to certain transferred claims because the putative assignee failed to establish a valid assignment of the claims and thus the claims were not enforceable under state law); *In re Taylor*, 363 B.R. 303, 310–11 (Bankr. M.D. Fla. 2007) (sustaining debtor's objections under § 502(b)(1) to certain transferred claims because the putative assignee "did not establish it holds a legally enforceable agreement supporting the claim").

for any assignment to be valid. See Note, § 14. Because the Debtors have not consented and do not consent to the assignment to Contrarian, see Sharp Decl. ¶ 4, the putative assignment reflected in the Transfer Notice is unenforceable against the Debtors. See, e.g., In re Spiers, 2015 Bankr. LEXIS 1901, at *9–10 (Bankr. W.D.N.C. June 10, 2015) (concluding where a state court order prohibited the claimant from assigning its claim, the claimant's attempt to transfer such claim to the putative assignee was invalid and legally unenforceable). Accordingly, Contrarian cannot meet its ultimate burden of proving its ownership of the debt pursuant to a valid assignment, and thus has failed to prove that its claim is enforceable against the Debtors or their property. The Objection should be sustained and the Transferred Claim should be disallowed under section 502(b)(1). Cf. In re Kendall, 380 B.R. at 49 ("Because [the putative assignee] has not met its ultimate burden of proving ... its ownership of the debt, [the putative assignee] has failed to prove that its claim is enforceable against [the debtor] or his property, and

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therefore [the debtor's] objection should be sustained and the claim disallowed under 11 U.S.C. § 502(b)(1).").

- Transferred Claim should be without prejudice to the right of the Berlingers to assert such claim on their own behalf, as the claim has been duly scheduled by the Debtors. *See, e.g., In re King*, 2016 Bankr. LEXIS 2443, at *21–23 (Bankr. E.D.N.C. June 30, 2016) (concluding where an attempted assignment of claim was unenforceable, the putative assignor was the proper holder of the claim and not the putative assignee). Such relief will result in an accurate Claims Register and will not prejudice the Berlingers, as they will retain the rights that were never validly alienated from them. Accordingly, the Debtors request that the Transferred Claim be disallowed and expunged in its entirety without prejudice to the right of the Berlingers to assert such claim on their own behalf, as the claim has been duly scheduled by the Debtors.
- 14. The Debtors do not believe this Objection is one "based on substantive grounds, other than incorrect classification of a claim," Del. Bankr. L.R. 3007-1(f)(iii), and therefore do not believe that the Objection is required to "include all substantive objections to such claim," *id*. Nonetheless, out of an abundance of caution, the Debtors request a waiver of Local Rule 3007-1(f)(iii) to the extent such rule might otherwise be construed to apply. Such waiver is authorized by Local Rule 1001-1(c), and will ensure that all rights of the Debtors or any subsequently appointed estate representative to object in the future to the Transferred Claim or to any future claim(s) the Berlingers may assert on account of the Notes on any grounds permitted by bankruptcy or nonbankruptcy law are expressly reserved.

V. RESERVATION OF RIGHTS

15. The Debtors reserve the right to amend, modify, and/or supplement this Objection if necessary. Nothing contained in this Objection or any actions taken by the Debtors pursuant to 01:23110985.3

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the relief requested herein is intended or should be construed as (i) an admission as to the

validity of any claim, (ii) a waiver of the Debtors' rights to dispute any claim on any grounds,

(iii) a promise or requirement to pay any claim, (iv) an implication or admission that any claim is

of a type referenced or defined in this Objection, (v) an implication or admission that any

contract or lease is executory or unexpired, as applicable, (vi) a waiver or limitation of any of the

Debtors' rights under the Bankruptcy Code or applicable law, (vii) a request or authorization to

assume or reject any agreement under Bankruptcy Code section 365, (viii) a waiver of any

party's rights to assert that any other party is in breach or default of any agreement, or (ix) an

implication or admission that any contract or lease is integrated with any other contract or lease.

VI. NOTICE

16. The Debtors have provided notice of this Objection to: (i) the Office of the United

States Trustee for the District of Delaware, (ii) counsel to the DIP Lender, (iii) counsel for the

Committee, (iv) counsel for the Noteholder Group, (v) counsel for the Unitholder Group, (vi) the

Berlingers, (vii) Contrarian, and (viii) all parties that have requested notice in these Chapter 11

Cases pursuant to Local Rule 2002-1. In light of the nature of the relief requested herein, the

Debtors submit that no other or further notice is necessary.

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VII. CONCLUSION

WHEREFORE, for the reasons set forth herein and in the Declaration, the Debtors respectfully requests that the Court enter the Proposed Order granting the relief requested herein and granting such other and further relief as is just and proper.

Dated: April 16, 2018 /s/ Ian J. Bambrick

Wilmington, Delaware YOUNG CONAWAY STARGATT & TAYLOR, LLP

Sean M. Beach (No. 4070) Edmon L. Morton (No. 3856) Ian J. Bambrick (No. 5455) Allison S. Mielke (No. 5934)

Rodney Square, 1000 North King Street

Wilmington, Delaware 19801 Tel: (302) 571-6600 Fax: (302) 571-1253

-and-

KLEE, TUCHIN, BOGDANOFF & STERN LLP

Kenneth N. Klee (*pro hac vice*) Michael L. Tuchin (*pro hac vice*) David A. Fidler (*pro hac vice*) Jonathan M. Weiss (*pro hac vice*) 1999 Avenue of the Stars, 39th Floor Los Angeles, California 90067

Counsel to the Debtors and Debtors in Possession

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:

C

Case No. 17-12560 (KJC)

WOODBRIDGE GROUP OF COMPANIES, LLC, et al., 1

(Jointly Administered)

Debtors.

Hearing Date:

Chapter 11

June 5, 2018 at 11:00 a.m. (ET)

Response Deadline:

April 30, 2018 at 4:00 p.m. (ET)

NOTICE OF DEBTORS' (I) OBJECTION TO PROOF OF CLAIM NO. 1216 ASSERTED BY PUTATIVE TRANSFEREE CONTRARIAN FUNDS, LLC WITHOUT PREJUDICE TO RIGHT OF PUTATIVE TRANSFERORS ELISSA AND JOSEPH BERLINGER TO ASSERT SUCH CLAIM; AND (II) REQUEST FOR A LIMITED WAIVER OF LOCAL RULE 3007-1(f)(iii), TO THE EXTENT SUCH RULE MAY APPLY

TO: (I) THE OFFICE OF THE UNITED STATES TRUSTEE FOR THE DISTRICT OF DELAWARE; (II) COUNSEL TO THE DIP LENDER; (III) COUNSEL FOR THE COMMITTEE; (IV) COUNSEL FOR THE NOTEHOLDER GROUP; (V) COUNSEL FOR THE UNITHOLDER GROUP; (VI) THE BERLINGERS; (VII) CONTRARIAN FUNDS, LLC; AND (VII) ALL PARTIES THAT HAVE REQUESTED NOTICE IN THESE CHAPTER 11 CASES PURSUANT TO LOCAL RULE 2002-1.

PLEASE TAKE NOTICE that Woodbridge Group of Companies, LLC and its affiliated debtors and debtors in possession in the above-captioned cases (collectively, the "<u>Debtors</u>") have filed the attached **Debtors**' (I) Objection to Proof of Claim No. 1216 Asserted by Putative Transferee Contrarian Funds, LLC Without Prejudice to Right of Putative Transferors Elissa and Joseph Berlinger to Assert Such Claim; and (II) Request for a Limited Waiver of Local Rule 3007-1(f)(iii), to the Extent Such Rule May Apply (the "Objection").²

PLEASE TAKE FURTHER NOTICE that responses to the Objection must be filed on or before <u>April 30, 2018 at 4:00 p.m. (ET)</u> (the "<u>Response Deadline</u>") with the United States Bankruptcy Court for the District of Delaware, 3rd Floor, 824 North Market Street, Wilmington,

The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of this information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

² Capitalized terms used but not otherwise defined herein shall have the meanings ascribed to such terms in the Objection.

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Delaware 19801. At the same time, you must serve a copy of any response upon the undersigned counsel to the Debtors so as to be received on or before the Response Deadline.

PLEASE TAKE FURTHER NOTICE THAT A HEARING ON THE OBJECTION WILL BE HELD ON JUNE 5, 2018 AT 11:00 A.M. (ET) BEFORE THE HONORABLE KEVIN J. CAREY IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE, 824 NORTH MARKET STREET, 5TH FLOOR, COURTROOM NO. 5, WILMINGTON, DELAWARE 19801.

PLEASE TAKE FURTHER NOTICE THAT, IF NO RESPONSES TO THE OBJECTION ARE TIMELY FILED, SERVED, AND RECEIVED IN ACCORDANCE WITH THIS NOTICE, THEN THE COURT MAY GRANT THE RELIEF REQUESTED IN THE OBJECTION WITHOUT FURTHER NOTICE OR A HEARING.

Dated: April 16, 2018

Wilmington, Delaware

/s/ Ian J. Bambrick

YOUNG CONAWAY STARGATT & TAYLOR, LLP

Sean M. Beach (No. 4070) Edmon L. Morton (No. 3856) Ian J. Bambrick (No. 5455) Allison S. Mielke (No. 5934)

Rodney Square, 1000 North King Street

Wilmington, Delaware 19801 Tel: (302) 571-6600 Fax: (302) 571-1253

-and-

KLEE, TUCHIN, BOGDANOFF & STERN LLP

Kenneth N. Klee (pro hac vice) Michael L. Tuchin (pro hac vice) David A. Fidler (pro hac vice) Jonathan M. Weiss (pro hac vice) 1999 Avenue of the Stars, 39th Floor Los Angeles, California 90067

Counsel to the Debtors and Debtors in Possession

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EXHIBIT A

Proposed Order

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:	Chapter 11
WOODBRIDGE GROUP OF COMPANIES, LLC, et	Case No. 17-12560 (KJC)
al.,¹ Debtors.	(Jointly Administered)
Deutois.	Re Docket No:

ORDER (I) SUSTAINING DEBTORS' OBJECTION TO PROOF OF CLAIM NO. 1216
ASSERTED BY CONTRARIAN FUNDS, LLC, WITHOUT PREJUDICE TO
RIGHT OF PUTATIVE TRANSFERORS ELISSA AND JOSEPH BERLINGER TO
ASSERT SUCH CLAIM AND (II) WAIVING, TO THE EXTENT APPLICABLE,
LOCAL RULE 3007-1(f)(iii)

Upon the objection (the "Objection")² filed by the above-captioned debtors and debtors in possession (collectively, the "Debtors") in these chapter 11 cases (the "Chapter 11 Cases") seeking entry of an order, pursuant to section 502(b) of the Bankruptcy Code, Bankruptcy Rules 3001, 3003, and 3007, and Local Rules 3007-1 and 3007-2, (i) disallowing and expunging Claim No. 1216 (the "Transferred Claim") asserted by Contrarian Funds, LLC ("Contrarian"), without prejudice to the right of the Berlingers to assert such claim on their own behalf, as the claim has been duly scheduled by the Debtors, (ii) directing the Claims Agent to reflect the foregoing modifications in the Claims Register, and (iii) waiving Local Rule 3007-1(f)(iii) to the extent such rule may otherwise bar the assertion of any subsequent substantive objection (if any) to the

The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of this information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

² Capitalized terms used but not otherwise defined herein shall have the meaning ascribed to such terms in the Objection.

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Transferred Claim or any claim(s) that may be filed by the Berlingers; and upon consideration of the record of these Chapter 11 Cases and the Sharp Declaration; and it appearing that the Court has jurisdiction to consider the Objection in accordance with 28 U.S.C. §§ 157 and 1334 and the *Amended Standing Order of Reference* from the United States District Court for the District of Delaware dated February 29, 2012; and it appearing that the Objection is a core matter pursuant to 28 U.S.C. § 157(b)(2) and that the Court may enter a final order consistent with Article III of the United States Constitution; and it appearing that venue of these Cases and of the Objection is proper pursuant to 28 U.S.C. §§ 1408 and 1409; and it appearing that due and adequate notice of the Objection has been given under the circumstances and that no other or further notice need be given; and after due deliberation, and good and sufficient cause appearing therefor, it is hereby

ORDERED, ADJUDGED, and DECREED THAT:

- 1. The Objection is SUSTAINED as set forth herein.
- The Transferred Claim is hereby disallowed and expunged in its entirety, without prejudice to the right of the Berlingers to assert such claim on their own behalf, as the claim has been duly scheduled by the Debtors.
- The Claims Agent is directed to modify the Claims Register to comport with the relief granted by this Order.
- 4. Nothing in this Order shall affect any party's rights with respect to any claim that the Berlingers may assert on account of the Notes, and all parties' rights with respect to any such claim are reserved, including, the Debtors' or any subsequently appointed estate representative's rights to object in the future to any such claim on any grounds permitted by bankruptcy or nonbankruptcy law. For the avoidance of doubt and to the extent applicable, Local Rule 3007-

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1(f)(iii) is hereby deemed waived with respect to the relief requested in the Objection and

granted by this Order.

5. Nothing in this Order shall be deemed (i) an admission as to the validity of any

claim, (ii) a waiver of the Debtors' rights to dispute any claim on any grounds, (iii) a promise or

requirement to pay any claim, (iv) an implication or admission that any claim is of a type

referenced or defined in the Objection, (v) an implication or admission that any contract or lease

is executory or unexpired, as applicable, (vi) a waiver or limitation of any of the Debtors' rights

under the Bankruptcy Code or applicable law, (vii) a request or authorization to assume or reject

any agreement under Bankruptcy Code section 365, (viii) a waiver of any party's rights to assert

that any other party is in breach or default of any agreement, or (ix) an implication or admission

that any contract or lease is integrated with any other contract or lease.

6. Notwithstanding any applicable provisions of the Bankruptcy Code, the

Bankruptcy Rules, or the Local Rules, this Order shall be effective immediately upon its entry.

7. The Debtors are authorized to take all actions necessary or appropriate to

effectuate the relief granted pursuant to this Order in accordance with the Objection.

8. This Court shall retain jurisdiction and power with respect to all matters arising

from or related to the implementation or interpretation of this Order.

Dated: ______, 2018 Wilmington, DE

KEVIN J. CAREY

UNITED STATES BANKRUPTCY JUDGE

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EXHIBIT B

Sharp Declaration

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:

WOODBRIDGE GROUP OF COMPANIES, LLC, et al.,

Debtors.

Chapter 11

Case No. 17-12560 (KJC)

(Jointly Administered)

DECLARATION OF BRADLEY D. SHARP IN SUPPORT OF DEBTORS' OBJECTION TO CLAIM NO. 1216 ASSERTED BY CONTRARIAN FUNDS, LLC

I, Bradley D. Sharp, hereby declare under penalty of perjury, pursuant to section 1746 of title 28 of the United States Code, as follows:

1. I am President and CEO of Development Specialists, Inc. ("<u>DSI</u>"), located at 333

S. Grand Avenue Suite 4070, Los Angeles, California 90071, and the Chief Restructuring

Officer of WGC Independent Manager LLC, a Delaware limited liability company ("<u>WGC</u>

<u>Independent Manager</u>"), which is the sole manager of debtor Woodbridge Group of Companies,

LLC, a Delaware limited liability company and an affiliate of each of the above-captioned

debtors and debtors in possession (each, a "<u>Debtor</u>" and collectively, the "<u>Debtors</u>"). I submit

this declaration (this "<u>Declaration</u>") in support of the *Debtors' Objection to Claim No. 1216*Asserted by Contrarian Funds, LLC (the "<u>Objection</u>")² concurrently filed herewith by the

The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of this information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

² Capitalized terms used but not otherwise defined herein shall have the meanings ascribed to such terms in the Objection.

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Debtors. All facts set forth in this Declaration are based upon my personal knowledge, and if

called upon to testify, I could and would testify competently to the facts set forth herein.

2. I have reviewed and am familiar with the Objection and the Transferred Claim

that is the subject thereof. Based on that review, the information contained in the Objection is

true and correct to the best of my knowledge and belief.

3. The Debtors' schedules reflect three \$25,000 non-contingent, liquidated, and

undisputed claims in favor of Elissa and Joseph Berlinger (the "Berlingers"), for an aggregate

total of \$75,000, on account of Notes.

4. The Debtors have not consented and expressly do not consent to the transfer of

the Berlingers' Notes to Contrarian.

Pursuant to 28 U.S.C. § 1746, I declare under penalty of perjury that the foregoing is true

and correct.

Dated: April 16, 2018

/s/ Bradley D. Sharp

Bradley D. Sharp

Chief Restructuring Officer, WGC Independent

Manager, LLC

01:23110985.3

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EXHIBIT C

Transferred Claim

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UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE					
Name of Debtor:	Case No.				
	anies, LLC, et al. Case No. 17-12560				



FILED : 01216
DISTRICT OF DELAWARE
WOODBRIDGE GROUP OF COMPANIES, LLC
17-12560/JUDGE KEVIN J. CAREY

Official Form 410

Proof of Claim

04/16

Read the instructions before filling out this form. This form is for making a claim for payment in a bankruptcy case. Do not use this form to make a request for payment of an administrative expense. Make such a request according to 11 U.S.C. § 503.

Filers must leave out or redact information that is entitled to privacy on this form or on any attached documents. Attach redacted copies of any documents that support the claim, such as promissory notes, purchase orders, invoices, itemized statements of running accounts, contracts, judgments, mortgages, and security agreements. Do not send original documents; they may be destroyed after scanning. If the documents are not available, explain in an attachment.

A person who files a fraudulent claim could be fined up to \$500,000, imprisoned for up to 5 years, or both. 18 U.S.C. §§ 152, 157, and 3571.

Fill in all the information about the claim as of the date the case was filed. That date is on the notice of bankruptcy (Form 309) that you received.

	Vho is the current reditor?	CONTRARIAN FUNDS, LLC Name of the current creditor (the person or entity to be paid for this claim) Other names the creditor used with the debtor							
a	las this claim been cquired from omeone else?	☐ No ☑ Yes. From	whom? _ ELIS	SSA K. BI	ERLINGER AND	JOSEPH W. I	BERLINGER	mar Bartila mar a Bartila del region del redri del redri	Academicalian machilido degre an machilinar machili cadhar dhi militar dhi mil
ai ci Fi B	Where should notices ind payments to the reditor be sent? dederal Rule of lankruptcy Procedure FRBP) 2002(g)	Name 411 WEST Number S GREENW City Contact phone Contact email	PUTNAM treet I/ICH C 203-862-8211 AMUMOLA@CC	S, LLC AVENUE T State 1 (ALISA M DITRARIANCE	O6830 ZIP Code	CONTRAL Name ATTN: 392 Number S PITTSBU City Contact phone Contact email	Street	LLC SS STREE	T 154-0455 15262 ZIP Code
	Does this claim amend one already filed?	V2 No ☐ Yes. Claim number on court claims registry (if known) Filed on MM / DD / YYYY							
е	Do you know if anyone else has filed a proof of claim?	✓ No ☐ Yes. Who	made the earlie	er filing? _	104-de 1 (104-0) 404-t 1 de 1 (104-1 (104-1	0.000mm 6 - 1 &		and a deep desired of the	

Official Form 410

Proof of Claim

page 1

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. Do you have any number you use to identify the debtor?	No Yes. Last 4 digits of the debtor's account or any number you use to identify the debtor:						
. How much is the claim?	\$ 75,000.000 Does this amount include interest or other charges? ✓ No → Yes. Attach statement itemizing interest, fees, expenses, or other charges required by Bankruptcy Rule 3001(c)(2)(A).						
What is the basis of the claim?	Examples: Goods sold, money loaned, lease, services performed, personal injury or wrongful death, or credit card. Attach redacted copies of any documents supporting the claim required by Bankruptcy Rule 3001(c). Limit disclosing information that is entitled to privacy, such as health care information. PROMISSORY NOTES						
. Is all or part of the claim secured?	Yes. The claim is secured by a lien on property. Nature of property: ☑ Real estate. If the claim is secured by the debtor's principal residence, file a Mortgage Proof of Claim Attachment (Official Form 410-A) with this Proof of Claim. ☐ Motor vehicle ☐ Other. Describe: Basis for perfection: Attach redacted copies of documents, if any, that show evidence of perfection of a security interest (for example, a mortgage, lien, certificate of title, financing statement, or other document that shows the lien has been filed or recorded.) Value of property: \$ unknown Amount of the claim that is secured: \$ 75,000.00 Amount of the claim that is unsecured: \$ 0 (The sum of the secured and unsecured amounts should match the amount in line 7.) Amount necessary to cure any default as of the date of the petition: \$ 75,437.50 Annual Interest Rate (when case was filed) % *SEE ATTACHED						
10. Is this claim based on a lease?	✓ Fixed Variable						
11. Is this claim subject to a right of setoff?	☐ Yes. Amount necessary to cure any default as of the date of the petition. \$						
Official Form 410	Proof of Claim page 2						

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2. Is all or part of the claim	12 No			· · · · · · · · · · · · · · · · · · ·				
entitled to priority under 11 U.S.C. § 507(a)?	Yes. Check	one:		• •		Amount entitled to priority		
A claim may be partly priority and partly	☐ Domestic support obligations (including alimony and child support) under 11 U.S.C. § 507(a)(1)(A) or (a)(1)(B).							
nonpriority. For example, in some categories, the law limits the amount entitled to priority.	Up to \$2,850* of deposits toward purchase, lease, or rental of property or services for personal, family, or household use. 11 U.S.C. § 507(a)(7).							
endiced to priority.	☐ Wages, salaries, or commissions (up to \$12,850*) earned within 180 days before the bankruptcy petition is filed or the debtor's business ends, whichever is earlier. 11 U.S.C. § 507(a)(4).							
	Taxes o	or penalties owed to gov	ernmental units. 11 U.	.S.C. § 507(a)(8).		\$		
	☐ Contributions to an employee benefit plan. 11 U.S.C. § 507(a)(5).							
	☐ Other. Specify subsection of 11 U.S.C. § 507(a)() that applies.							
	* Amounts are subject to adjustment on 4/01/19 and every 3 years after that for cases begun on or after the date of adjustment.							
THE STATE OF THE PARTY OF THE P	de de la manuel de	gagge infrastrumente e que y eperage y MFF fredericamente annoque	ere - Service valida di misi soni soni soniste e prigo. Netti	ar mana. May applicated through a true designation	MARKET TOTAL SECURITY SECURITY OF SECURITY			
Part 3: Sign Below	·							
The person completing this proof of claim must	Check the appro	opriate box:						
sign and date it.	☑ I am the creditor.							
FRBP 9011(b).	am the creditor's attorney or authorized agent.							
If you file this claim	I am the trustee, or the debtor, or their authorized agent. Bankruptcy Rule 3004.							
electronically, FRBP 5005(a)(2) authorizes courts to establish local rules	l am a guarantor, surety, endorser, or other codebtor. Bankruptcy Rule 3005.							
specifying what a signature is.	I understand that an authorized signature on this <i>Proof of Claim</i> serves as an acknowledgment that when calculating amount of the claim, the creditor gave the debtor credit for any payments received toward the debt.							
A person who files a fraudulent claim could be fined up to \$500,000, imprisoned for up to 5	and correct.							
years, or both. 18 U.S.C. §§ 152, 157, and 3571.	I declare under penalty of perjury that the foregoing is true and correct. Executed on date 02/26/2018							
3311.								
	CONTRARIA	MM / DD / YYYY	۸					
•	BY: CONTRARIAN OF PITAL MANAGEMENT, LLC AS MEMBER							
			1					
	Signature		3					
	Print the name of the person who is completing and signing this claim:							
		JANICE	М.		STANTON			
	Name	First name	Middle nam		Last name			
	Title	MEMBER				-		
	Company	CONTRARIAN F	UNDS, LLC					
	COMPANIAN FUNDS, LLC Identify the corporate servicer as the company if the authorized agent is a servicer.							
•	Address	411 WEST PUT	NAM AVENUE, SUI	TE 424				
	,	Number Stree						
		GREENWICH		СТ	06830			
		City		State	ZIP Code			
•	Contact phone	203-862-8211 (AL	LISA MUMOLA)	Email	AMUMOLA	CONTRARIANCAPITAL.COM		
	Contact prioric			Linds				

Official Form 410 Proof of Claim

page 3

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SUPPLEMENT TO PROOF OF CLAIM FILED BY CONTRARIAN FUNDS, LLC

- 1. Contrarian Funds, LLC ("Creditor") submits this Proof of Claim and Supplement (together with all exhibits, the "Proof of Claim") in the amount of at least \$75,000.00, against Woodbridge Group of Companies, LLC ("Debtor") in the case In re Woodbridge Group of Companies, LLC, et al., Case No. 17-12560 (KJC) (Jointly Administered) under Chapter 11 of Title 11 of the United States Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the District of Delaware.
- 2. This Proof of Claim is not intended to be, and shall not be, construed as (i) an election of remedies, (ii) a waiver of any defaults or (iii) a waiver or limitation of any rights, remedies, claims or interests of Creditor.
- 3. Creditor expressly reserves the right to amend, modify and/or supplement this Proof of Claim at any time and from time to time and in any respect, including, but not limited to, for purposes of fixing, increasing or amending in any respect the amounts referred to herein.
- 4. This Proof of Claim is filed without prejudice to Creditor's rights under the Bankruptcy Code or otherwise, including, but not limited to, any and all rights of setoff and recoupment. Creditor expressly preserves all of its rights and claims against Debtor under the Bankruptcy Code and applicable non-bankruptcy law.

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EVIDENCE OF TRANSFER OF CLAIM

TO:

United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court") Attention: Court Clerk

AND TO:

Woodbridge Group of Companies, LLC, et al. (the "Debtor") Case No. 17-12560 (the "Case")

Elissa K. Berlinger and Joseph W. Berlinger ("Seller"), for good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, does hereby certify that it has unconditionally and irrevocably sold, transferred and assigned unto:

Contrarian Funds, LLC ("Buyer" 411 West Putnam Avenue, Suite 425 Greenwich, CT 06830

and its successors and assigns all Seller's right, title and interest in and to the Seller's claim in the amount of \$75,000.00 (the "Claim") against the Debtor, to which claim number has been assigned.

Seller hereby waives any objection to the transfer of the Claim to Buyer on the books and records of the Debtor and the Bankruptcy Court, and hereby waives to the fullest extent permitted by law any notice or right to a hearing as may be imposed by Rule 3001 of the Federal Rules of Bankruptcy Procedure, the Bankruptcy Code, applicable local bankruptcy rules or applicable law. Seller acknowledges and understands, and hereby stipulates that an order of the Bankruptcy Court may be entered without further notice to Seller transferring to Buyer the Claim and recognizing the Buyer as the sole owner and holder of the Claim.

You are hereby directed to make all future payments and distributions, and to give all notices and other communications, in respect of the Claim to Buyer.

IN WITNESS WHEREOF, the undersigned has duly executed this Evidence of Transfer of Claim by its duly authorized representative dated Feb 13, 2018.

> ALLISON ROSE STEVENS Notary Public, State of Florida Commission# FF 237295 My comm. expires June 3, 2019

CONTRARIAN FUNDS, LLC

as mahager By:

Name

Title:

By: Contrarian Capital Management, L.L.C.,

JANICE M. STANTON

MEMBER

ELISSA K. BERLINGER

Name: Elissa K. Berlinger Title: Individual

Sworn to before me this

day of February, 2018

Name: Joseph W. Berlinger

JOSEPH W. BERLINGER

Title: Individual

Sworn to before me this

13 day of February, 2018

Notary Public

ALLISON ROSE STEVENS Notary Public, State of Florida Commission# FF 237295 My comm. expires June 3, 2019

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FOR YOUR RECORDS

Property ID : Pacific Coast Highway - Malibu, CA Principal : \$25,000.00

Int. Rate : 6.50%

PROMISSORY NOTE State Commence

October 14, 2016 Sherman Oaks, California

\$25,000.00

FOR VALUE RECEIVED, the undersigned, WOODBRIDGE MORTGAGE INVESTMENT FUND 3A, LLC, a Delaware limited liability company having an office and a mailing address at 14225 Ventura Boulevard, Suite 100, Sherman Oaks, California 91423 (hereinafter referred to as the "Borrower") does hereby promise to pay to the order of ELISSA K. BERLINGER AND JOSEPH W. BERLINGER, individuals having an address of 7940 Amethyst Lake Point, Lake Worth, Florida 33467 (hereinafter together referred to as "Lender"), at such place as the Lender may designate by written notice to Borrower, the principal sum of Twenty-Five Thousand and 00/100 Dollars (\$25,000.00), together with interest on all unpaid balances beginning as of the date hereof, at the fixed rate per annum as set forth in Section 1 hereof.

- Interest Rate. The unpaid balance of the principal sum of Twenty-Five Thousand and 00/100 Dollars (\$25,000.00) shall bear interest from the date hereof through November 1, 2017, at a fixed rate of interest equal to six and 50/100 percent (6.50%) per annum. After November 1, 2017, the unpaid balance of this Note shall bear interest at a fixed rate equal to nine and 00/100 percent (9.00%) per annum. The rate of interest charged hereunder shall never exceed the maximum amount, if any, allowable by law. Interest shall be charged on the principal balance from time to time outstanding on the basis of the actual number of days elapsed computed on the basis of a 360 day year.
- Default Interest Rate. During the continuance of any Event of Default (as more particularly defined in Paragraph 6 below) under this Note by acceleration or otherwise, interest shall accrue from and after such Event of Default at four (4) percentage points above the interest rate then in effect hereunder (the "Default Interest Rate").
- Repayment. Borrower promises to pay the interest and principal on this Note, as set forth below:

Monthly payments of interest shall be made commencing on November 1, 2016 and continuing on the same day of each and every month to occur thereafter, both before and after maturity by acceleration or otherwise.

The entire principal balance plus accrued and unpaid interest thereon, and all other sums and charges due to the Lender hereunder, unless sooner paid, shall be due and payable on February 1, 2018 (the "Maturity Date"). Upon and after the eighth (8th) day following Borrower's receipt of written notice from Lender of Borrower's failure to pay the entire principal balance plus accrued and unpaid interest on the Maturity Date as required, any outstanding amounts due under this Note shall bear interest at a fixed rate of twenty-four and 00/100 percent (24.00%) per annum.

- 4. Application of Payments. All payments pursuant to this Note shall be made in legal tender of the United States of America and shall be applied first to the payment of delinquency or late charges, if any; second, to the payment of accrued and unpaid interest on this Note; and third, the balance on account of the principal of this Note.
- Cure Period and Notice of Default. Failure of Borrower to pay by its due date any installment of the principal or of interest within thirty (30) days from the date the same becomes due and payable, shall constitute a "Payment Default" under this Note. Borrower shall have a cure period of not less

Case 17-12560-KJC Doc 1563-4 Filed 04/16/18 Page 8 of 18

Property ID : Pacific Coast Highway - Malibu, CA Principal : \$25,000.00 Int. Rate : 6.50%

than thirty (30) days after receipt of written notice ("Notice of Default") of any alleged breach or Payment Default under the terms of this Note to cure the same.

6. <u>Event of Default</u>. Any alleged breach or Payment Default under this Note that is not fully cured following the expiration of the applicable cure period specified in a given Notice of Default shall constitute an event of default ("<u>Event of Default</u>") under this Note.

7. Waiver of Rights.

- a. BORROWER HEREBY WAIVES TRIAL BY JURY IN ANY COURT AND IN ANY SUIT ACTION OR PROCEEDING OR ANY MATTER ARISING IN CONNECTION WITH OR IN ANY WAY RELATED TO THE FINANCING TRANSACTIONS OF WHICH THIS NOTE OR THE COLLATERAL ASSIGNMENT DOCUMENTS (AS DEFINED BELOW) ARE A PART AND/OR THE ENFORCEMENT OF ANY OF LENDER'S RIGHTS AND REMEDIES. BORROWER ACKNOWLEDGES THAT IT MAKES THIS WAIVER KNOWINGLY, VOLUNTARILY AND ONLY AFTER EXTENSIVE CONSIDERATION OF THE RAMIFICATIONS OF THIS WAIVER.
- b. Borrower hereby waives diligence, demand, presentment for payment, protest and notice of protest, and notice of any renewals or extensions of this Note, and agrees that the time for payment of this Note may be changed and extended at Lender's sole discretion, without impairing its liability thereon, and further consents to the release of any party liable for this obligation, or the release of all or any part of the collateral given as security for the payment of this Note, without affecting its liability with respect hereto.
- 8. <u>Lender's Rights</u>. Lender's rights hereunder shall be cumulative and not exclusive and may be exercised at the sole discretion of Lender with respect to priority, order and type of collateral or security realized upon or applied toward the indebtedness evidenced hereby until this Note and all accrued and unpaid interest and other sums and charges due hereunder shall have been paid in full. Further, no failure on the part of Lender to exercise any right or remedy hereunder, whether before or after the occurrence of an Event of Default hereunder, shall constitute a waiver thereof, and no waiver of any past default shall constitute waiver of any future default or of any other default.
- 9. <u>Prepayment.</u> The Borrower shall have the right to prepay this Note in whole or in part at any time without penalty.
- Binding Effect. This Note shall bind the successors and assigns of Borrower and shall inure to the benefit of the Lender, its successors and assigns.
- 11. <u>Captions and Section Headings</u>. The captions and section headings used in this Note are for convenience only and shall not be used to interpret, modify or affect in any way the covenants and agreements herein contained.
- 12. <u>Severability</u>. In the event that any one or more of the provisions of this Note shall for any reason be held to be invalid, illegal or unenforceable, in whole or in part, or in any respect, or in the event that any one or more of the provisions of this Note shall operate or would prospectively operate, to invalidate this Note, then the remaining provisions of this Note shall remain operative and in full force and effect, shall be valid, legal and enforceable and shall in no way be affected, prejudiced or disturbed thereby.

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Property ID : Pacific Coast Highway - Malibu, CA Principal : \$25,000.00 Int. Rate : 6.50%

- 13. Governing Law. This Note shall be governed by and construed in accordance with the laws of the State of Delaware.
- 14. <u>No Assignment.</u> Neither this Note, the Loan Agreement of even date herewith between Borrower and Lender, nor all other instruments executed or to be executed in connection therewith (collectively, the "Collateral Assignment Documents") are assignable by Lender without the Borrower's written consent and any such attempted assignment without such consent shall be null and void.
- 15. <u>Commercial Transaction</u>. Lender and Borrower each acknowledge and stipulate that the Loan is a commercial transaction.
- 16. <u>Security</u>. This Note will be secured <u>inter alia</u> by the Collateral Assignment Documents upon execution thereof.

WOODBRIDGE MORTGAGE
INVESTMENT FIRED LLC

By:
Robert Reed
Its Authorized Representative

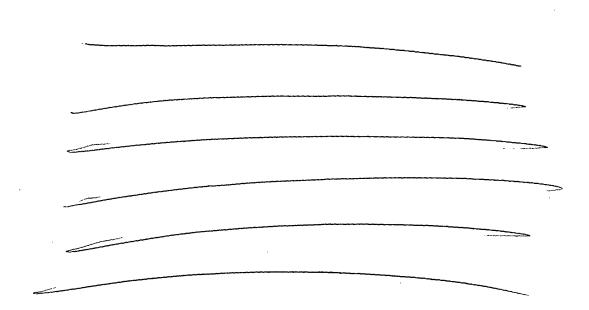
Accepted and Agreed to by Lender:

ELISSAK. BERLINGER

JOSEPH'W. BERLINGER

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ECTORAL SHOW HOW

Property ID : Owlwood Estates - Holmby Hills, CA

Principal : \$25,000.00 Int. Rate : 6.25%

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PROMISSORY NOTE

August 8, 2016 Sherman Oaks, California

\$25,000.00

FOR VALUE RECEIVED, the undersigned, WOODBRIDGE MORTGAGE INVESTMENT FUND 3A, LLC, a Delaware limited liability company having an office and a mailing address at 14225 Ventura Boulevard, Suite 100, Sherman Oaks, California 91423 (hereinafter referred to as the "Borrower") does hereby promise to pay to the order of ELISSA K. BERLINGER AND JOSEPH W. BERLINGER, individuals having an address of 7940 Amethyst Lake Point, Lake Worth, Florida 33467 (hereinafter together referred to as "Lender"), at such place as the Lender may designate by written notice to Borrower, the principal sum of Twenty-Five Thousand and 00/100 Dollars (\$25,000.00), together with interest on all unpaid balances beginning as of the date hereof, at the fixed rate per annum as set forth in Section 1 hereof.

- 1. <u>Interest Rate</u>. The unpaid balance of the principal sum of Twenty-Five Thousand and 00/100 Dollars (\$25,000.00) shall bear interest from the date hereof through September 1, 2017, at a fixed rate of interest equal to six and 25/100 percent (6.25%) per annum. After September 1, 2017, the unpaid balance of this Note shall bear interest at a fixed rate equal to nine and 00/100 percent (9.00%) per annum. The rate of interest charged hereunder shall never exceed the maximum amount, if any, allowable by law. Interest shall be charged on the principal balance from time to time outstanding on the basis of the actual number of days elapsed computed on the basis of a 360 day year.
- 2. <u>Default Interest Rate</u>. During the continuance of any Event of Default (as more particularly defined in Paragraph 6 below) under this Note by acceleration or otherwise, interest shall accrue from and after such Event of Default at four (4) percentage points above the interest rate then in effect hereunder (the "Default Interest Rate").
- 3. Repayment. Borrower promises to pay the interest and principal on this Note, as set forth below:

Monthly payments of interest shall be made commencing on September 1, 2016 and continuing on the same day of each and every month to occur thereafter, both before and after maturity by acceleration or otherwise.

The entire principal balance plus accrued and unpaid interest thereon, and all other sums and charges due to the Lender hereunder, unless sooner paid, shall be due and payable on December 1, 2017 (the "Maturity Date"). Upon and after the eighth (8th) day following Borrower's receipt of written notice from Lender of Borrower's failure to pay the entire principal balance plus accrued and unpaid interest on the Maturity Date as required, any outstanding amounts due under this Note shall bear interest at a fixed rate of twenty-four and 00/100 percent (24.00%) per annum.

- 4. <u>Application of Payments</u>. All payments pursuant to this Note shall be made in legal tender of the United States of America and shall be applied first to the payment of delinquency or late charges, if any, second, to the payment of accrued and unpaid interest on this Note; and third, the balance on account of the principal of this Note.
- 5. <u>Cure Period and Notice of Default.</u> Failure of Borrower to pay by its due date any installment of the principal or of interest within thirty (30) days from the date the same becomes due and payable, shall constitute a "<u>Payment Default</u>" under this Note. Borrower shall have a cure period of not less

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Property ID : Owlwood Estates - Holmby Hills, CA Principal : \$25,000.00 Int. Rate : 6.25%

than thirty (30) days after receipt of written notice ("Notice of Default") of any alleged breach or Payment Default under the terms of this Note to cure the same.

6. <u>Event of Default</u>. Any alleged breach or Payment Default under this Note that is not fully cured following the expiration of the applicable cure period specified in a given Notice of Default shall constitute an event of default ("<u>Event of Default</u>") under this Note.

7. Waiver of Rights.

- a. BORROWER HEREBY WAIVES TRIAL BY JURY IN ANY COURT AND IN ANY SUIT ACTION OR PROCEEDING OR ANY MATTER ARISING IN CONNECTION WITH OR IN ANY WAY RELATED TO THE FINANCING TRANSACTIONS OF WHICH THIS NOTE OR THE COLLATERAL ASSIGNMENT DOCUMENTS (AS DEFINED BELOW) ARE A PART AND/OR THE ENFORCEMENT OF ANY OF LENDER'S RIGHTS AND REMEDIES. BORROWER ACKNOWLEDGES THAT IT MAKES THIS WAIVER KNOWINGLY, VOLUNTARILY AND ONLY AFTER EXTENSIVE CONSIDERATION OF THE RAMIFICATIONS OF THIS WAIVER.
- b. Borrower hereby waives diligence, demand, presentment for payment, protest and notice of protest, and notice of any renewals or extensions of this Note, and agrees that the time for payment of this Note may be changed and extended at Lender's sole discretion, without impairing its liability thereon, and further consents to the release of any party liable for this obligation, or the release of all or any part of the collateral given as security for the payment of this Note, without affecting its liability with respect hereto.
- 8. <u>Lender's Rights</u>. Lender's rights hereunder shall be cumulative and not exclusive and may be exercised at the sole discretion of Lender with respect to priority, order and type of collateral or security realized upon or applied toward the indebtedness evidenced hereby until this Note and all accrued and unpaid interest and other sums and charges due hereunder shall have been paid in full. Further, no failure on the part of Lender to exercise any right or remedy hereunder, whether before or after the occurrence of an Event of Default hereunder, shall constitute a waiver thereof, and no waiver of any past default shall constitute waiver of any future default or of any other default.
- 9. <u>Prepayment.</u> The Borrower shall have the right to prepay this Note in whole or in part at any time without penalty.
- 10. <u>Binding Effect.</u> This Note shall bind the successors and assigns of Borrower and shall inure to the benefit of the Lender, its successors and assigns.
- 11. <u>Captions and Section Headings</u>. The captions and section headings used in this Note are for convenience only and shall not be used to interpret, modify or affect in any way the covenants and agreements herein contained.
- 12. <u>Severability</u>. In the event that any one or more of the provisions of this Note shall for any reason be held to be invalid, illegal or unenforceable, in whole or in part, or in any respect, or in the event that any one or more of the provisions of this Note shall operate or would prospectively operate, to invalidate this Note, then the remaining provisions of this Note shall remain operative and in full force and effect, shall be valid, legal and enforceable and shall in no way be affected, prejudiced or disturbed thereby.

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Property ID : Owlwood Estates - Holmby Hills, CA
Principal : \$25,000.00
Int. Rate : 6.25%

- 13. <u>Governing Law</u>. This Note shall be governed by and construed in accordance with the laws of the State of Delaware.
- 14. <u>No Assignment</u>. Neither this Note, the Loan Agreement of even date herewith between Borrower and Lender, nor all other instruments executed or to be executed in connection therewith (collectively, the "<u>Collateral Assignment Documents</u>") are assignable by Lender without the Borrower's written consent and any such attempted assignment without such consent shall be null and void.
- 15. <u>Commercial Transaction</u>. Lender and Borrower each acknowledge and stipulate that the Loan is a commercial transaction.
- 16. <u>Security</u>. This Note will be secured <u>inter alia</u> by the Collateral Assignment Documents upon execution thereof.

WOODBRIDGE MORTGAGE INVESTMENT FUND 3A, LLC

By: David E. Golden

Its Authorized Representative

Accepted and Agreed to by Lender:

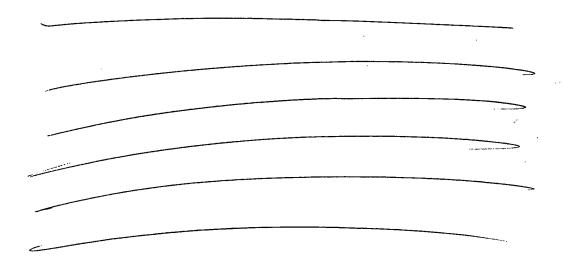
ELISSAK. BERLINGER

JOSÉPH W. BERLINGER

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Property ID : Carla Ridge Two Construction -

Beverly Hills. CA

Principal : \$25,000.00

Int. Rate

FOR YOUR RECORDS

PROMISSORY NOTE

B.L. COTTONS Alim on \$25,000.00

December 15, 2016 Sherman Oaks, California

FOR VALUE RECEIVED, the undersigned, WOODBRIDGE MORTGAGE INVESTMENT FUND 3A, LLC, a Delaware limited liability company having an office and a mailing address at 14225 Ventura Boulevard, Suite 100, Sherman Oaks, California 91423 (hereinafter referred to as the "Borrower") does hereby promise to pay to the order of ELISSA K. BERLINGER AND JOSEPH W. BERLINGER, individuals having an address of 7940 Amethyst Lake Point, Lake Worth, Florida 33467 (hereinafter together referred to as "Lender"), at such place as the Lender may designate by written notice to Borrower, the principal sum of Twenty-Five Thousand and 00/100 Dollars (\$25,000.00), together with interest on all unpaid balances beginning as of the date hereof, at the fixed rate per annum as set forth in Section 1 hereof.

- 1. Interest Rate. The unpaid balance of the principal sum of Twenty-Five Thousand and 00/100 Dollars (\$25,000.00) shall bear interest from the date hereof through January 1, 2018, at a fixed rate of interest equal to seven and 25/100 percent (7.25%) per annum. After January 1, 2018, the unpaid balance of this Note shall bear interest at a fixed rate equal to nine and 00/100 percent (9.00%) per annum. The rate of interest charged hereunder shall never exceed the maximum amount, if any, allowable by law. Interest shall be charged on the principal balance from time to time outstanding on the basis of the actual number of days elapsed computed on the basis of a 360 day year.
- 2. Default Interest Rate. During the continuance of any Event of Default (as more particularly defined in Paragraph 6 below) under this Note by acceleration or otherwise, interest shall accrue from and after such Event of Default at four (4) percentage points above the interest rate then in effect hereunder (the "Default Interest Rate").
- 3. Repayment. Borrower promises to pay the interest and principal on this Note, as set forth below:

Monthly payments of interest shall be made commencing on January 1, 2017 and continuing on the same day of each and every month to occur thereafter, both before and after maturity by acceleration or otherwise.

The entire principal balance plus accrued and unpaid interest thereon, and all other sums and charges due to the Lender hereunder, unless sooner paid, shall be due and payable on April 1, 2018 (the "Maturity Date"). Upon and after the eighth (8th) day following Borrower's receipt of written notice from Lender of Borrower's failure to pay the entire principal balance plus accrued and unpaid interest on the Maturity Date as required, any outstanding amounts due under this Note shall bear interest at a fixed rate of twenty-four and 00/100 percent (24,00%) per annum.

- 4. Application of Payments. All payments pursuant to this Note shall be made in legal tender of the United States of America and shall be applied first to the payment of delinquency or late charges, if any; second, to the payment of accrued and unpaid interest on this Note; and third, the balance on account of the principal of this Note.
- 5. Cure Period and Notice of Default. Failure of Borrower to pay by its due date any installment of the principal or of interest within thirty (30) days from the date the same becomes due and payable,

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Property ID : Carla Ridge Two Construction -

Beverly Hills, CA

Principal : \$25,000.00 Int. Rate : 7.25%

shall constitute a "Payment Default" under this Note. Borrower shall have a cure period of not less than thirty (30) days after receipt of written notice ("Notice of Default") of any alleged breach or

Payment Default under the terms of this Note to cure the same.

6. Event of Default. Any alleged breach or Payment Default under this Note that is not fully cured following the expiration of the applicable cure period specified in a given Notice of Default shall constitute an event of default ("Event of Default") under this Note.

7. Waiver of Rights.

- a. BORROWER HEREBY WAIVES TRIAL BY JURY IN ANY COURT AND IN ANY SUIT ACTION OR PROCEEDING OR ANY MATTER ARISING IN CONNECTION WITH OR IN ANY WAY RELATED TO THE FINANCING TRANSACTIONS OF WHICH THIS NOTE OR THE COLLATERAL ASSIGNMENT DOCUMENTS (AS DEFINED BELOW) ARE A PART AND/OR THE ENFORCEMENT OF ANY OF LENDER'S RIGHTS AND REMEDIES. BORROWER ACKNOWLEDGES THAT IT MAKES THIS WAIVER KNOWINGLY, VOLUNTARILY AND ONLY AFTER EXTENSIVE CONSIDERATION OF THE RAMIFICATIONS OF THIS WAIVER.
- b. Borrower hereby waives diligence, demand, presentment for payment, protest and notice of protest, and notice of any renewals or extensions of this Note, and agrees that the time for payment of this Note may be changed and extended at Lender's sole discretion, without impairing its liability thereon, and further consents to the release of any party liable for this obligation, or the release of all or any part of the collateral given as security for the payment of this Note, without affecting its liability with respect hereto.
- 8. <u>Lender's Rights</u>. Lender's rights hereunder shall be cumulative and not exclusive and may be exercised at the sole discretion of Lender with respect to priority, order and type of collateral or security realized upon or applied toward the indebtedness evidenced hereby until this Note and all accrued and unpaid interest and other sums and charges due hereunder shall have been paid in full. Further, no failure on the part of Lender to exercise any right or remedy hereunder, whether before or after the occurrence of an Event of Default hereunder, shall constitute a waiver thereof, and no waiver of any past default shall constitute waiver of any future default or of any other default.
- 9. <u>Prepayment.</u> The Borrower shall have the right to prepay this Note in whole or in part at any time without penalty.
- 10. <u>Binding Effect.</u> This Note shall bind the successors and assigns of Borrower and shall inure to the benefit of the Lender, its successors and assigns.
- 11. <u>Captions and Section Headings</u>. The captions and section headings used in this Note are for convenience only and shall not be used to interpret, modify or affect in any way the covenants and agreements herein contained.
- 12. <u>Severability</u>. In the event that any one or more of the provisions of this Note shall for any reason be held to be invalid, illegal or unenforceable, in whole or in part, or in any respect, or in the event that any one or more of the provisions of this Note shall operate or would prospectively operate, to invalidate this Note, then the remaining provisions of this Note shall remain operative and in full force and effect, shall be valid, legal and enforceable and shall in no way be affected, prejudiced or disturbed thereby.

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Property ID : Carla Ridge Two Construction -

Beverly Hills, CA

Principal : \$25,000.00 Int. Rate : 7.25%

- 13. <u>Governing Law</u>. This Note shall be governed by and construed in accordance with the laws of the State of Delaware.
- 14. <u>No Assignment.</u> Neither this Note, the Loan Agreement of even date herewith between Borrower and Lender, nor all other instruments executed or to be executed in connection therewith (collectively, the "<u>Collateral Assignment Documents</u>") are assignable by Lender without the Borrower's written consent and any such attempted assignment without such consent shall be null and void.
- 15. <u>Commercial Transaction</u>. Lender and Borrower each acknowledge and stipulate that the Loan is a commercial transaction.
- 16. <u>Security</u>. This Note will be secured <u>inter alia</u> by the Collateral Assignment Documents upon execution thereof.

WOODBRIDGE MORTGAGE INVESTMENT FUND 3A. LLC

By:

Robert Reed
Its Authorized Representative

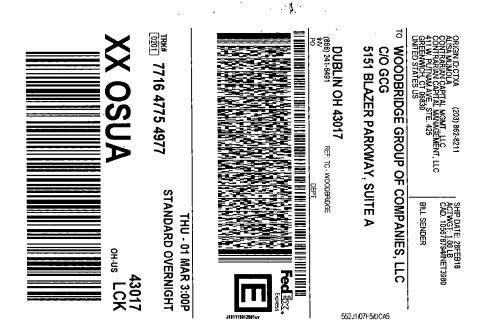
Accepted and Agreed to by Lender:

12. 2 / / \

ELISSA K. BERLINGER

JOSEPH W. BERLINGER

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0IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

Debtors.	Ref. Docket Nos. 890, 1585, 1656		
et al., ¹	(Jointly Administered)		
WOODBRIDGE GROUP OF COMPANIES, LLC,	Case No. 17-12560 (KJC)		
In re:	Chapter 11		

THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS' JOINDER AND STATEMENT IN SUPPORT OF DEBTORS' OBJECTION TO MOTION TO QUASH OF CONTRARIAN FUNDS, LLC

The Official Committee of Unsecured Creditors (the "<u>Committee</u>") appointed in the above-captioned cases, through the Committee's undersigned counsel, hereby joins and files this statement in support of the *Debtors' Objection to Motion to Quash of Contrarian Funds*, *LLC* [Docket No. 1656] (the "<u>Objection</u>").² The Committee joins in the Objection for the reasons set forth therein.

Background

- On April 3, 2018, Contrarian Funds, LLC ("<u>Contrarian</u>") filed its *Motion* for Authority to Acquire Promissory Notes [D.I. 890] (the "<u>Notes Motion</u>").
- 2. On April 10, 2018, the Debtors filed its notice to conduct a Rule 30(b)(6) deposition of a representative of Contrarian [D.I. 954] (the "Deposition Notice").

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¹ The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of such information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting counsel for the Debtors.

² Capitalized terms not defined herein shall have the meaning as provided by the Objection.

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- 3. In response, on April 18, 2018, Contrarian filed a *Motion to Quash of Contrarian Funds, LLC* [D.I. 1585] (the "Motion to Quash") seeking to quash the Deposition Notice.
- 4. Contemporaneously therewith, Contrarian also filed its *Motion to Shorten*Notice with Respect to Motion to Quash of Contrarian Funds, LLC [D.I. 1586] (the "Motion to

 Shorten") seeking to schedule the Motion to Quash to be heard during the previously scheduled omnibus hearing on May 1, 2018, at 11:00 a.m., and to shorten the period for notice of the hearing, with objections, if any, to be filed by 4:00 p.m. on April 26, 2018.
- On April 19, 2018, the Debtors filed their Response to the Motion to
 Shorten and, among other things, consented to the Motion to Quash being heard on May 1, 2018
 (as requested in the Motion to Shorten). On April 26, 2018, the Debtors filed the Objection.

Joinder

- 6. The Committee joins in the Objection and agrees that the Motion to Quash should be denied and that the Debtors be permitted to take the discovery requested with respect to the Notes Motion.
- 7. The Committee is committed to protecting the interests of investors who were defrauded by the Debtors' former principal, Robert Shapiro. To this end, the Committee supported a moratorium on claims trading in order to ensure that investors are not prejudiced by unscrupulous claims traders who may be preying on investors.

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- 8. For the reasons set forth in the Objection, the Committee believes that a full factual record must be developed before a hearing on the merits of the Notes Motion is conducted.
- 9. Accordingly, the Committee requests that the Court: (i) deny the Motion to Quash; (ii) permit the Debtors to take discovery concerning the Notes Motion; and (iii) grant such other and further relief as the Court deems appropriate.

Dated: April 30, 2018 PACHULSKI STANG ZIEHL & JONES LLP

/s/ Colin R. Robinson

Richard M. Pachulski (CA Bar No. 90073) James I. Stang (CA Bar No. 94435) Jeffrey N. Pomerantz (CA Bar No. 143717) Bradford J. Sandler (DE Bar No. 4142) Colin R. Robinson (DE Bar No. 5524) 919 North Market Street, 17th Floor P.O. Box 8705

Wilmington, DE 19899 (Courier 19801)

Telephone: 302-652-4100 Facsimile: 302-652-4400

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Counsel for the Official Committee of Unsecured Creditors

DOCS DE:219278.2 94811/002

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:

WOODBRIDGE GROUP OF COMPANIES LLC, et al. ¹

Debtors.

Chapter 11

Case No. 17-12560 (KJC)

Jointly Administered

Re: Dkt. Nos. 890, 1585, 1656

JOINDER OF THE OFFICAL AD HOC COMMITTEE OF UNITHOLDERS TO DEBTORS' OBJECTION TO MOTION TO QUASH OF CONTRARIAN FUNDS, LLC

The Official Ad Hoc Committee of Unitholders (the "<u>Unitholders' Committee</u>") of Woodbridge Mortgage Investment Fund Entities,² by and through its undersigned counsel, hereby submits this Joinder to the *Debtors' Objection to Motion to Quash of Contrarian Funds, LLC* [Dkt. No. 1656] (the "<u>Objection</u>"), and in support thereof, respectfully states as follows:

- 1. On April 3, 2018, Contrarian Funds, LLC ("Contrarian") filed its *Motion for Authority to Acquire Promissory Notes* [Dkt. No. 890] (the "Notes Motion").
- 2. On April 10, 2018, the Debtors filed its notice to conduct a Rule 30(b)(6) deposition of a representative of Contrarian [Dkt. No. 954] (the "Deposition Notice").
- 3. In response, on April 18, 2018, Contrarian filed a *Motion to Quash of Contrarian Funds*, *LLC* [Dkt. No. 1585] (the "Motion to Quash"), seeking to quash the Deposition Notice.

¹ The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14225 Ventura Boulevard, #100, Sherman Oaks, California 91423. A complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses may be obtained on the website of the Debtors' claims and noticing agent at www.gardencitygroup.com/cases/WGC.

² The Funds consist of the following Debtors: (i) Woodbridge Mortgage Investment Fund 1, LLC; (ii) Woodbridge Mortgage Investment Fund 2, LLC; (iii) Woodbridge Mortgage Investment Fund 3, LLC; (iv) Woodbridge Mortgage Investment Fund 3A, LLC; (v) Woodbridge Mortgage Investment Fund 4, LLC; (vi) Woodbridge Commercial Bridge Loan Fund 1, LLC; and (vii) Woodbridge Commercial Bridge Loan Fund 2, LLC.

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4. At a hearing held on April 23, 2018, the Court scheduled the Motion to Quash for

hearing on May 1, 2018, and the Notes Motion for hearing on June 5, 2018.

5. On April 26, 2018, the Debtors filed the Objection [Dkt. No. 1656].

6. The Unitholders' Committee joins the Objection and supports the Debtors' ability

to seek limited discovery from Contrarian in connection with the Notes Motion.

7. For all the reasons set forth in the Objection, the Unitholders' Committee

respectfully requests that this Court: (i) deny the Motion to Quash; (ii) permit the Debtors to take

targeted, appropriate discovery concerning the Notes Motion; and (iii) grant such other and further

relief as is just and appropriate.

Dated: April 26, 2018

Wilmington, Delaware

VENABLE LLP

/s/ Jamie L. Edmonson

Jamie L. Edmonson (No. 4247) Daniel A. O'Brien (No. 4897)

1201 N. Market Street, Suite 1400

Wilmington, Delaware 19801

Telephone: 302-298-3535

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Andrew J. Currie 600 Massachusetts Avenue, NW Washington D.C. 20001 Telephone: 202-344-4586 Facsimile: 202-344-8300

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Counsel to the Official Ad Hoc Unitholders' Committee

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:

WOODBRIDGE GROUP OF COMPANIES, LLC, et al., ¹

Debtors.

Chapter 11

Case No. 17-12560 (KJC)

(Jointly Administered)

Re: Dkt. Nos. 890, 1585

DEBTORS' OBJECTION TO MOTION TO QUASH OF CONTRARIAN FUNDS, LLC

Woodbridge Group of Companies, LLC and its affiliated debtors and debtors in possession (collectively, the "Debtors") in the above-captioned chapter 11 cases (the "Chapter 11 Cases") hereby object (this "Objection") to the Motion to Quash of Contrarian Funds, LLC [Docket No. 1585] (the "Motion to Quash"), filed by Contrarian Funds, LLC ("Contrarian"), which seeks to bar all discovery in connection with the Motion of Contrarian Funds, LLC for Authority to Acquire Promissory Notes Against the Debtors [Docket No. 890] (the "Note Motion"). As set out below, Contrarian's arguments for precluding discovery in connection with the Note Motion lack merit, and the Motion to Quash should be denied.

PRELIMINARY STATEMENT

1. In its Note Motion, Contrarian seeks sweeping injunctive and declaratory relief – the very relief for which a full adversary proceeding is required under Rule 7001(7) and (9) of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules"). Specifically, Contrarian asks the Court to enjoin the Debtors from enforcing anti-assignment provisions in approximately

The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of such information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

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9,000 prepetition Notes by categorically declaring that "[e]ach and any Noteholder shall be and hereby is authorized to freely assign or otherwise transfer its right, title and interest in the Notes and attendant claims against the Debtors free of any restrictions or requirements set forth in the Notes and any related agreement or document" Note Mot. Ex. A (Proposed Order) ¶ 2.

2. Bankruptcy Rule 7001 is no mere procedural nicety. It exists to ensure that requests for certain types of relief – including the injunctive and declaratory relief requested by Contrarian – are initiated, heard, and determined with appropriate procedural protections commensurate to the issues at stake. Such protections are vital where, as here, the sweeping and unprecedented relief at issue portends profound effects on the Debtors and these Chapter 11 Cases, and may even implicate potential violations of federal or state law. The federal Securities and Exchange Commission (the "SEC") has alleged that the very Notes at issue in Contrarian's Note Motion are unregistered securities that were unlawfully offered and sold in violation of the Securities Act of 1933 (the "Securities Act") and the Securities Exchange Act of 1934 (the "Exchange Act") prepetition. See generally Complaint for Injunctive and Other Relief, SEC v. Shapiro, et al., No. 1:17-cv-24624 (S.D. Fla., filed Dec. 20, 2017) (the "SEC Complaint"). Yet Contrarian proposes that these same instruments be declared "freely assignable and transferable" (Note Mot. ¶ 18) by *ipse dixit* – without any input of the SEC or any of the state regulators who have made allegations similar to those set out in the SEC Complaint, a shred of discovery, or even one on-point precedent from any court anywhere granting this type of relief.²

An adversary proceeding would, among other things, provide appropriate mechanisms for formal joinder or intervention of interested regulators or others, *see* Fed. R. Bankr. P. 7019 & 7024, full discovery, *see* Fed. R. Bankr. P. 7026–7037, robust briefing and argument that engages with the facts uncovered in discovery, *see* Fed. R. Bankr. P. 7056, and other well-settled standards and procedures. As the Debtors will argue in their forthcoming opposition to the Note Motion, Contrarian cannot sidestep the proper procedural rules, and its Note Motion can and should be denied on the basis that Contrarian has not complied with Bankruptcy Rule 7001. The Debtors will further demonstrate that the Note Motion is procedurally infirm for a second reason: lack of standing. Contrarian's putative standing rests on its assertion that it "has acquired certain Notes" and has filed "one proof of claim against *(footnote continued)*

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- 3. The Motion to Quash marshals two basic arguments in opposition to discovery: First, that the information the Debtors seek is confidential (albeit neither legally privileged nor otherwise protected from disclosure), and second, that Contrarian's legal arguments on the merits of the Note Motion are so strong that no facts the Debtors adduce in discovery could possibly have any bearing on the proper disposition of the Note Motion. Neither point is well-taken.
- 4. As to confidentiality, Contrarian maintains that the details of its attempts to acquire Notes in violation of the anti-assignment provisions is "sensitive, confidential commercial information that any investor would be reluctant to divulge." Mot. to Quash ¶ 2. Perhaps. But no claim is made that any of the information sought is legally privileged or otherwise protected from disclosure. Nor does Contrarian argue that there would be any particular burden (let alone an undue burden) in providing the requested discovery (which is modest and narrowly-tailored). The Debtors have offered to enter into an appropriate protective order to shield proprietary or competitively-sensitive information from Contrarian's competitors both at the production/deposition stage and in any filings in which such material may be referenced. This Court, its staff, and the attorneys who practice before it are all well-accustomed to dealing with sensitive information, and there is no reason to believe that the established practices and procedures employed to address these types of concerns in countless other cases before this Court will be inadequate here. See infra ¶¶ 23–25.

the Debtors" on account of such allegedly acquired Notes. Mot. to Quash ¶ 13 (citing Claim No. 1216 (the "Contrarian Proof of Claim")). But – as the Notice of Debtors' (I) Objection to Proof of Claim No. 1216 Asserted by Putative Transferee Contrarian Funds, LLC Without Prejudice to Right of Putative Transferors Elissa and Joseph Berlinger to Assert Such Claim; and (II) Request for a Limited Waiver of Local Rule 3007-1(f)(iii), to the Extent Such Rule May Apply [Docket No. 1563] (the "Claim Objection") demonstrates – Contrarian's purported acquisition of the Notes is null, void, and of no effect, and Contrarian is nothing more than a potential purchaser of Notes. These issues will be briefed and argued in the context of Contrarian's Note Motion, but the Debtors flag them now to foreclose any future argument by Contrarian that the Debtors have somehow acquiesced in Contrarian's standing or procedural missteps or that it would be unfair to require Contrarian (or a proper plaintiff with actual standing) to start afresh with an adversary complaint following the June 5, 2018 hearing on the Note Motion. Contrarian can and should withdraw its Note Motion now rather than proceed down the dead-end path of a motion that ought to be an adversary proceeding and a movant that ought to be a plaintiff with proper standing.

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- 5. Next, the Motion to Quash identifies three legal arguments that, by Contrarian's telling, are so compelling as to render any factual discovery irrelevant. Specifically, Contrarian argues that Bankruptcy Rule 3001 "[i]mplement[s] a broad policy in favor of the free transfer of claims" such that "only the transferor and not the Debtor may object to the transfer of a claim," Mot. to Quash ¶ 2; that "Section 9-408 of the UCC renders ineffective a contractual provision that requires the consent of a maker of a promissory note before the note may be transferred," *id.* ¶ 24; and that "the Debtors cannot be heard to enforce a non-assignment provision under Notes that they have materially breached through non-payment," *id.* ¶ 26. Each of these three arguments fails:
 - Rule 3001 does not indeed, *cannot*, under the Rules Enabling Act, 28 U.S.C. § 2075 override the anti-assignment provisions in the Debtors' Notes. The pertinent authority is not Bankruptcy Rule 3001 (which deals solely with the mechanics of transfers), but is instead Bankruptcy Code section 502(b)(1), which provides for the disallowance of any claim that is "unenforceable against the debtor and property of the debtor, under any agreement or applicable law for a reason other than because such claim is contingent or unmatured." Notes that have purportedly been acquired in violation of their anti-assignment provision are unenforceable in the hands of the putative transferee. Rule 3001 does not factor into the analysis. *See infra* ¶ 27–30.
 - Contrarian's Uniform Commercial Code ("<u>UCC</u>") argument rests on the wrong section of the UCC. The section that Contrarian cites (9-408) applies only to security interests in notes, not to sales of notes. The applicable section is 9-406(e), which makes clear that anti-assignment provisions in promissory notes

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may indeed be enforced to prohibit sales of notes. *See, e.g., Day v. White*, 2017 U.S. Dist. LEXIS 90135, at *18–23, 2017 WL 2563234, at *7–9 (D.V.I. June 12, 2017). *See infra* ¶ 31–37.

- One party's breach even a material breach does not render a contract's anti-assignment provision unenforceable. See, e.g., In re Diamondhead Casino Corp., 2016 Bankr. LEXIS 2450, at *45–46, 2016 WL 3284674, at *15 (Bankr. D. Del. June 7, 2016). If it did, no debtor could ever enforce any provision in an executory contract or unexpired lease if the debtor had defaulted prepetition. That is not the law. See infra ¶¶ 38–42.
- 6. Even beyond the lack of merit in the legal arguments identified in Contrarian's Motion to Quash, several additional factors independently establish the relevance of the discovery at issue in the Motion to Quash:
- 7. *First*, the Note Motion explicitly invokes "equity" and "public policy" in support of the relief sought, *see* Note Mot. ¶ 17, and therefore invites scrutiny of Contrarian's motives, conduct, and good faith. *See, e.g., In re Mission of Care, Inc.*, 164 B.R. 877, 880 (Bankr. D. Del. 1994) ("He who seeks equity must do equity. Equity will not grant affirmative relief to one with unclean hands, where the misconduct directly relates to the legal controversy."). Especially in light of indications already apparent even before discovery, 3 it is manifestly appropriate for the Debtors to make targeted inquiries that are reasonably calculated to lead to the discovery of misrepresentations, sharp practices, or unfair dealing by Contrarian. *See infra* ¶ 44–45.

See Ex. A to Debtors': (I) Response to Motion to Shorten Notice With Respect to Motion to Quash of Contrarian Funds, LLC; and (II) Cross-Motion for Continuance of Hearing on [Note Motion] [Docket No. 1593] (the "Scheduling Response & Cross-Motion") (an "offer of 82 cents per dollar" for Notes contingent on the Debtors acquiescing in an argument they have disputed from the first day of these Chapter 11 Cases).

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- 8. **Second**, as much as Contrarian seeks to portray the issue as whether there is free trading of bankruptcy claims generally, the fact remains that the nearly 9,000 instruments at issue here are Notes that each contain a presumptively valid term (the anti-assignment provision) that has not to date been voided by any order of this Court. Contrarian's Note Motion asks the Court to take the drastic and unprecedented step of altering these nearly 9,000 Notes. It is not too much to ask that the Debtors (who are, unlike Contrarian, actually party to the Notes) be allowed to take discovery prior to the hearing and determination of the Note Motion. Among other things, the Ponzi-scheme-specific issues in these Chapter 11 Cases raise important questions about how prepetition "interest" (which was not, in fact, interest it was another victim's money) will be taken into account in connection with distributions to Noteholders. As detailed below, the Debtors have reason to believe that Noteholders are being induced to make representations regarding the ultimate amount of their allowed claims that may in fact be false. See infra ¶¶ 46–48.
- 9. *Finally*, the specific Notes that Contrarian seeks to buy, sell, and otherwise freely trade and transfer have been alleged by the SEC to be unregistered securities that were unlawfully offered and sold in violation of the Securities Act and the Exchange Act. The purchase or sale of securities without a registration statement or applicable exemption risks Securities Act liability, and any material misrepresentation, omission, or deception in connection with the purchase or sale of securities risks Exchange Act liability. In addition to further distinguishing these Chapter 11 Cases from the vast majority of chapter 11 cases in which all types of claims are actively traded, these circumstances support discovery of what exactly Noteholders are being asked to represent as part of any sale of their Notes and what if any representations are being made to Noteholders to induce them to sell. *See infra* ¶ 49–50.

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10. For all these reasons, and as more particularly set out below, discovery is necessary and appropriate here and the Motion to Quash should accordingly be denied.

FACTUAL BACKGROUND

A. The Chapter 11 Cases

- 11. On December 4, 2017, a total of 279 Debtors commenced voluntary cases under chapter 11 of the Bankruptcy Code. Thereafter, on February 9, 2018, March 9, 2018, March 23, 2018, and March 27, 2018, additional affiliated Debtors (27 in total) commenced voluntary cases under chapter 11 of the Bankruptcy Code. Pursuant to sections 1107(a) and 1108 of the Bankruptcy Code, the Debtors are continuing to manage their financial affairs as debtors in possession.
- 12. The Chapter 11 Cases are being jointly administered pursuant to Bankruptcy Rule 1015(b) and Local Rule 1015-1. As of the date hereof, no trustee has been appointed. An official committee of unsecured creditors (the "<u>Unsecured Creditors' Committee</u>") was appointed on December 14, 2017 [Docket No. 79].
- 13. On December 20, 2017, the SEC commenced an action styled SEC v. Robert H. Shapiro, Woodbridge Group of Companies, LLC, et al., Case No. 17-24624, via the SEC Complaint, in the U.S. District Court for the Southern District of Florida. The Debtors have filed a motion seeking this Court's approval to resolve the SEC Complaint by agreeing to a permanent injunction barring them from violating the Securities Act and Exchange Act. See Debtors' Motion for Entry of an Order, Pursuant to Section 105(a) of the Bankruptcy Code and Bankruptcy Rule 9019, Authorizing and Approving the Debtors' Entry into a Consent and Judgment with the Securities and Exchange Commission [Docket No. 1615].

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- 14. On January 23, 2018, the Court approved a settlement providing for the formation of an ad hoc noteholder group (the "Ad Hoc Noteholders' Committee") and an ad hoc unitholder group (the "Ad Hoc Unit Holders' Committee" and together with the Unsecured Creditors' Committee and the Ad Hoc Noteholders' Committee, the "Constituencies") [Docket No. 357]. In addition, the settlement provided that the Debtors would replace their Board of Managers with three new members (the "New Board"). The New Board subsequently selected a new Chief Executive Officer and Chief Restructuring Officer.
- 15. In March 2018, the Debtors' counsel hosted representatives of and counsel for the Constituencies at its offices in Los Angeles for multiple full-day meetings. At these meetings, the parties engaged in extensive debate and discussion regarding key legal issues in the Chapter 11 Cases, including, among other things, whether the Notes are secured by valid, perfected security interests, the relative rights and treatment of holders of Notes and Units, and whether substantive consolidation of the Estates is warranted under the circumstances. The negotiations were ultimately fruitful, as they culminated with the signing of a *Summary Plan Term Sheet*, dated as of March 22, 2018 [Docket No. 828] (the "Plan Term Sheet").
- 16. The Plan Term Sheet memorializes a broad agreement in principle regarding the fundamental terms of a chapter 11 plan, while providing a basis for further discussion regarding the specific details of the plan and related transactions (which details remain subject to further review and approval). "The Plan will admit and acknowledge that the Debtors were operating a Ponzi scheme since at least August 2012 and that the date of discovery of such scheme was in December 2017." Plan Term Sheet § C(2)(c). Thus, the consideration that will ultimately be distributed in respect of any Note will take into account the prepetition "interest" received by the Noteholder. *See* Plan Term Sheet Ex. A (definition of "Note Distribution Formula"). This is a

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consequence of how Ponzi schemes operate: One victim's "interest" is actually money that was procured by fraud from another, later-in-time victim. This fact is important, because the Debtors are aware that certain claims buyers are inducing Noteholders to make representations about their ultimate recovery entitlement that are untrue.

B. Contrarian's Note Motion

- 17. Each of the nearly 9,000 prepetition Notes issued by the Debtors contain antiassignment provisions that are clear and conspicuous:
 - 14. <u>No Assignment.</u> Neither this Note, the Loan Agreement of even date herewith between Borrower and Lender, nor all other instruments executed or to be executed in connection therewith (collectively, the "Collateral Assignment Documents") are assignable by Lender without the Borrower's written consent and any such attempted assignment without such consent shall be null and void.
- 18. Each Note also contains a choice-of-law provision specifying that Delaware law governs. Under Delaware law, the anti-assignment provisions in the Notes are valid and enforceable, *see*, *e.g.*, *Se. Chester Cnty. Refuse Auth. v. BFI Waste Servs. of Pa., LLC*, 2017 Del. Super. LEXIS 312, at *13 (Del. Sup. Ct. June 27, 2017); *Paul v. Chromalytics Corp.*, 343 A.2d 622, 625–26 (Del. Super. Ct. 1975), which means that the Debtors' express written consent is required before any Note may be transferred or assigned and that any purported transfer or assignment without such express written consent is null and void. Although Contrarian's Note Motion seeks to invalidate the anti-assignment provisions in the Notes, to date the provisions remain operative and in effect.
- 19. In the exercise of their business judgment, and in close consultation with the Constituencies, the Debtors provided notice on March 21, 2018 that "that they will impose a temporary moratorium on consideration of consent to any Transfer of Units or Notes for the next ninety (90) days" in order to, *inter alia*, avoid distractions and focus on exiting the chapter 11 process. *See Notice Regarding Transfers of Units or Notes* [Docket No. 799] (the "Transfer 01:23149956.1

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Notice"). The Transfer Notice did not purport to create rights that the Debtors do not already have under the Notes themselves. Instead, the Transfer Notice put the marketplace on notice that the Debtors had determined not to consider or approve any Note transfers at this time. That way, if any claim buyer induced a Noteholder to make a false representation that the Noteholder had the unilateral power to convey good title to a Note, the claim buyer could not later claim reasonable reliance on such a representation.

- 20. On April 3, 2018, Contrarian filed the Note Motion. In it, Contrarian seeks what is in essence an injunction barring the Debtors from enforcing the anti-assignment provisions in the Notes. As grounds for such extraordinary relief, Contrarian makes several assertions of fact, including that Noteholders are being affirmatively harmed, *see* Note Mot. ¶ 2 ("Preventing liquidity perversely causes further harm to the same defrauded creditors the Debtors claim to want to protect."), *id.* ¶ 10 ("Restricting the transfer of the Notes only makes matters worse for [the Noteholders]."), and that the Debtors are acting unfairly vis-à-vis their creditors, *see id.* ¶ 11 ("The Debtors have not considered each Noteholder's liquidity needs or risk tolerance, and for the Debtors to impose their views on a global class of creditors is highly restrictive and patently unfair to the creditors that do want to sell their Notes."). Further, the Note Motion explicitly appeals to public policy and equitable considerations as grounds for voiding the anti-assignment provisions, *see id.* ¶ 17, thus bringing into play considerations of unclean hands.
- 21. On April 4, 2018 (the day after the Note Motion was filed), the Debtors sent a letter to Contrarian's counsel seeking informal discovery with respect to the Note Motion, with a response requested by April 10, 2018. *See* Scheduling Response & Cross-Mot. Ex. B. The same day that Contrarian declined to provide such discovery, *see* Scheduling Response & Cross-Mot. Ex. C, the Debtors served a deposition notice (the "Deposition Notice," attached as Exhibit A to

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Contrarian's Motion to Quash), followed the next day by the document requests that mirrored the informal discovery requests (the "Requests for Production," attached as Exhibit D to the Scheduling Response & Cross-Motion).

22. On April 18, 2018, Contrarian filed its Motion to Quash, which seeks an order quashing the Deposition Notice. With regard to the Requests for Production, the Motion to Quash observes that "Contrarian will serve a response and objections ... in accordance with the Bankruptcy Rules," Mot. to Quash ¶ 15 n.3, which presumably means on May 10, 2018 (*i.e.*, 30 days after the requests were served).

ARGUMENT

- A. Contrarian's Confidentiality Concerns Can Be Addressed by Entry of an Appropriate Protective Order; They Are Not a Basis to Quash Discovery
- 23. Most motions to quash or for protective orders argue that the discovery being resisted is either privileged or protected from disclosure or would impose "undue burden or expense." Fed. R. Civ. P. 26(c)(1). Not so with Contrarian's Motion to Quash. Instead, Contrarian asserts only that the Debtors seek "sensitive, confidential commercial information that any investor would be reluctant to divulge." Mot. to Quash ¶ 2. This same formulation appears three more times in the Motion to Quash, *see also id*. ("highly sensitive and confidential"); *id*. ¶ 3 ("sensitive and confidential commercial information"); *id*. ¶ 28 ("sensitive, confidential details of Contrarian's transactions or communications"), yet never is paired with an argument that the discovery sought is legally privileged or otherwise protected from disclosure, or that there would be any undue burden or expense in providing the discovery.
- 24. Contrarian's concerns about confidentiality can be addressed with an appropriate protective order to shield proprietary or competitively-sensitive information from Contrarian's competitors, both at the production/deposition stage and in any filings in which such material

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may be referenced. Such orders are common in this Court and other courts across the country, and the Debtors are ready, willing, and able to agree to the entry of an appropriate protective order here. Indeed, the Debtors recently negotiated such an order with Comerica Bank to govern the production of sensitive financial information that may be subject to statutory and regulatory confidentiality regimes that are likely at least as stringent (if not more stringent) than any requirements that might be implicated by the Debtors' Deposition Notice and Requests for Production to Contrarian. See Order Regarding Stipulation and Protective Order Regarding Confidentiality [Docket No. 1609] (the "Stipulated Protective Order").

25. Finally in this regard, Contrarian is presumably making offers to large numbers of Noteholders. With nearly 9,000 Notes outstanding, it is not surprising that examples of such solicitations have been making the rounds. In addition to the exemplar included as Exhibit A to the Scheduling Response & Cross-Motion (Contrarian's supposed 82-cent "offer"), an example from another claims trader is discussed below. *See infra* ¶ 47 & Ex. A hereto. Commercial solicitations and communications in wide circulation are not so sensitive or secret as to be beyond the reach of ordinary discovery.

B. Contrarian's Three Merits Arguments Do Not Foreclose Discovery

26. The primary thrust of the Motion to Quash is Contrarian's argument that the discovery sought by the Debtors does not "bear on ... the Note Motion." Mot. to Quash ¶ 19. That is, by Contrarian's telling, three of its arguments in support of the Note Motion are pure issues of law, and no facts adduced in discovery will have any bearing them. But this attempt to resist discovery of the facts fails because the merits arguments Contrarian proffers do not, in fact, have any merit.

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(1) Rule 3001(e) Does Not Mean What Contrarian Says It Means

- 27. Contrarian asserts that Bankruptcy Rule 3001(e) "[i]mplement[s] a broad policy in favor of the free transfer of claims [by] severely limit[ing] standing to challenge the transfer of claims." Mot. to Quash ¶ 2. That is not accurate. Bankruptcy Rule 3001(e) "merely establish[es] who is entitled to file a proof of claim and not what evidence is necessary to prove its ownership." *In re Kincaid*, 388 B.R. 610, 617 (Bankr. E.D. Pa. 2008). It is purely a procedural device that ensures the proper recording of those claims that have been validly transferred under applicable law. *See id*.
- 28. As a rule of procedure, Bankruptcy Rule 3001 does not indeed, *cannot*, under the Rules Enabling Act override the anti-assignment provisions in the Debtors' Notes. The Rules Enabling Act provides that the Bankruptcy Rules "shall not abridge, enlarge, or modify any substantive right." 28 U.S.C. § 2075. Any Bankruptcy Rule that dictates a substantive result, rather than a matter of procedure, it is invalid under section 2075. *See, e.g., Tenn. Student Assistance Corp. v. Hood*, 541 U.S. 440, 454 (2004) (noting that an obligation "which is required only by the [Bankruptcy] Rules" and could preclude a party from exercising a statutory right "would give the Rules an impermissible effect"). If Bankruptcy Rule 3001(e) did what Contrarian claims it does, then it would be invalid under the Rules Enabling Act.
- 29. Far from supporting Contrarian's argument that Bankruptcy Rule 3001(e) overrides anti-assignment provisions in instruments such as promissory notes, the three cases

Accord Caudill v. N.C. Mach., Inc. (In re Am. Eagle Mfg., Inc.), 231 B.R. 320, 331 (B.A.P. 9th Cir. 1999) (holding that former Bankruptcy Rule 2003(d) was invalid since it "would clearly abridge and modify the substantive rights of creditors" under the statute); In re Nat'l Store Fixture Co., 37 B.R. 481, 489–90 (Bankr. W.D. Mo. 1984) (invalidating former Bankruptcy Rule 5002 because "it abridges and modifies substantive rights"); see also Sibbach v. Wilson & Co., 312 U.S. 1, 14 (1941) ("The test must be whether a rule really regulates procedure, – the judicial process for enforcing rights and duties recognized by substantive law and for justly administering remedy and redress for disregard or infraction of them.").

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Contrarian cites – *Preston Trucking Co. v. Liquidity Solutions, Inc.(In re Preston Trucking Co.)*, 333 B.R. 315 (Bankr. Md. 2005), *In re Lynn*, 285 B.R. 858 (Bankr. S.D.N.Y. 2002), and *Viking Associates, LLC. v. Drewes (In re Olson)*, 120 F.3d 98 (8th Cir. 1997), *see* Mot. to Quash ¶ 20–21 – have nothing to do with anti-assignment provisions. *In re Preston Trucking Co.* involved laid-off workers' assignment of their priority wage claims and WARN Act claims to a claims buyer for 35-cents-on-the-dollar – a deal the workers tried to re-trade when the assigned claims were thereafter paid in full. *See* 333 B.R. at 319–20. In *In re Lynn*, someone with personal animosity toward the debtor paid \$50 in exchange for a \$177,107.50 claim in the debtor's chapter 7 case, allegedly for the sole purpose of harassing the debtor. 285 B.R. at 860–61. And in *In re Olson*, disappointed bidders for an asset of the estate purchased all outstanding unsecured claims in an attempt to have the bankruptcy dismissed so that they could buy the asset they wanted from the debtor herself rather than negotiate with the chapter 7 trustee. 120 F.3d at 100. None of the claims at issue in these cases had restrictions on assignability.

30. The mechanism by which the Debtors can enforce the anti-assignment provisions in the Notes is not by objecting to claim transfers under Bankruptcy Rule 3001(e). Instead, "a challenge to the standing of a claimant is a substantive objection under § 502(b)(1), which provides a claim may be disallowed to the extent the claim is unenforceable against a debtor under any applicable law, including state law." *In re Richter*, 478 B.R. 30, 48 (Bankr. D. Colo. 2012). That is why the Claim Objection to the Contrarian Proof of Claim rests on Bankruptcy Code section 502(b)(1), and cites persuasive authority from around the country sustaining objections to claims that were invalid in the hands of the transferees who held them because the transfer was invalid. *See, e.g., In re King*, 2016 Bankr. LEXIS 2443, at *21–23, 2016 WL 3648524, at *7–8 (Bankr. E.D.N.C. June 30, 2016) (where an attempted assignment of claim was

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unenforceable, the putative assignor, not the putative assignee, was the proper holder of the claim); *In re Spiers*, 2015 Bankr. LEXIS 1901, at *9–10 (Bankr. W.D.N.C. June 10, 2015) (where a state court order prohibited the claimant from assigning its claim, the claimant's attempt to transfer such claim to the putative assignee was invalid and legally unenforceable); *In re Foy*, 469 B.R. 209, 214–15 (Bankr. E.D. Pa. 2012) (sustaining debtor's objections under § 502(b)(1) to certain transferred claims because under applicable state law, the partial assignment of a judgment requires the consent of the judgment debtor and the putative assignee did not obtain such consent, thus the assignments were "a legal nullity" under state law); *Pursley v. eCast Settlement Corp.* (*In re Pursley*), 451 B.R. 213, 232–34 (Bankr. M.D. Ga. 2011) (sustaining debtor's objection under § 502(b)(1) to claim asserted by assignee on the basis that the assignee failed to prove a valid assignment of the claim that would be enforceable under state law); *see also In re Gillbreath*, 409 B.R. 84, 121 (Bankr. S.D. Tex. 2009) ("In order to establish the validity of [these] proofs of claim ... over the Debtors' objection, [the putative assignee] had the burden of proving that it actually owns the claims.").

(2) UCC Section 9-408 Does Not Void Anti-Assignment Provisions in Promissory Notes

31. Contrarian cites no authority whatsoever in support of its assertion that "Section 9-408 of the UCC renders ineffective a contractual provision that requires the consent of the maker of a promissory note before the note may be transferred." Mot. to Quash ¶ 24. That is not surprising, because Contrarian's interpretation is wrong. It is contrary to the statutory text, the official comments, and the case law, all of which make clear that section 9-408 applies only to transactions involving the grant or transfer of a *security interest* in a promissory note, not an outright *sale* of a promissory note.

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32. Section 9-408(a) of the Delaware Uniform Commercial Code provides:

Except as otherwise provided in subsection (b), a term in a promissory note [that] prohibits, restricts, or requires the consent of the person obligated on the promissory note ... to the assignment or transfer of, or creation, attachment, or perfection of a security interest in, the promissory note ... is ineffective to the extent that the term:

- (1) would impair the creation, attachment, or perfection of a security interest; or
- (2) provides that the assignment or transfer or the creation, attachment, or perfection of the security interest may give rise to a default, breach, right of recoupment, claim, defense, termination, right of termination, or remedy under the promissory note [Del. Code Ann. tit. 6, § 9-408(a).]
- 33. Section 9-408(b), in turn, limits the scope of section 9-408(a): "Subsection (a) applies to a security interest in a payment intangible or promissory note" *Id.* § 9-408(b). "Security interest' means an interest in personal property or fixtures which secures payment or performance of an obligation." *Id.* § 1-201(35).

"Security interest" means an interest in personal property or fixtures which secures payment or performance of an obligation. "Security interest" includes any interest of a consignor and a buyer of accounts, chattel paper, a payment intangible, or a promissory note in a transaction that is subject to Article 9. "Security interest" does not include the special property interest of a buyer of goods on identification of those goods to a contract for sale under § 2-401, but a buyer may also acquire a "security interest" by complying with Article 9. Except as otherwise provided in § 2-505, the right of a seller or lessor of goods under Article 2 or 2A to retain or acquire possession of the goods is not a "security interest", but a seller or lessor may also acquire a "security interest" by complying with Article 9. The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer under § 2-401 is limited in effect to a reservation of a "security interest." Whether a transaction in the form of a lease creates a "security interest." Whether a transaction in the form of a lease creates a "security interest" is determined pursuant to § 1-203.

Del. Code Ann. tit. 6, § 1-201(35). In context, it is clear that a security interest is an interest that secures repayment of a debt or performance of an obligation. The second sentence of the definition merely indicates that a lender can *(footnote continued)*

The Motion to Quash misleadingly suggests that any purchased promissory note is somehow itself a "security interest" – even when there is no repayment or performance to secure. *See* Mot. to Quash ¶ 23 ("Section 1-201 of the UCC defines 'security interest' to include 'any interest of ... a buyer of ... a promissory note in a transaction that is subject to Article 9." (ellipses in original)). In fact, the pertinent portion of the definition has two sentences: the first (quoted in the text above) states what the term security interest "means," and the second (selectively quoted, with plenty of ellipses, in the Motion to Quash) indicates what the term may "include[,]" depending on the circumstances. The full definition is as follows:

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- 34. Here, Section 9-408(a) does not apply because Contrarian does not hold any security interest in the Notes. Contrarian did not lend money to the Noteholders at all let alone lend any money for which the repayment obligation is secured by a Noteholder's interest in his or her own Note (as would be required for Contrarian's interest in the Notes to qualify as a security interest, rather than the straightforward title that Contrarian purports to hold). The Debtors dispute that any valid purchase was effected (given that the anti-assignment provision renders "null and void" any purported transfer made without the Debtors' consent), but regardless, Contrarian cannot seriously contend that it holds a security interest in any Notes. Accordingly, section 9-408 has no applicability.
- 35. The official comments confirm that section 9-408(a) does not apply to a sale of a promissory note out of which no security interest arises. *See* Del. Del. Code Ann. tit. 6, § 9-408, cmt. 4 ("Subsection[] (a) ... render[s] ineffective restrictions on assignments only 'to the extent' that the assignments restrict the 'creation, attachment, or perfection of a security interest,' including sales of payments intangibles and promissory notes. This section does not render ineffective a restriction on an assignment that does not create a security interest."). And the case law is in accord. *See Day*, 2017 U.S. Dist. LEXIS 90135, at *22–23, 2017 WL 2563234, at *8 (holding that "§ 9-408 would be implicated if the [Bank] granted or transferred a security interest in the promissory note to a third party In reality, the [Bank] has not granted or transferred a security interest in the [promissory note], it has purportedly assigned, transferred, and set over the Promissory Note to [Plaintiffs]." (emphasis, internal quotation marks, and alterations omitted)).

acquire a security interest in a promissory note "in a transaction that is subject to Article 9" (such as by lending money in a transaction in which repayment is secured by the borrower's interest in a promissory note).

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- Contrarian does not cite. In certain situations, subsection (d) of that section can override contractual restrictions on the sale of promissory notes, *see* Del. Code Ann. tit. 6, § 9-406(d) ("a term in ... a promissory note is ineffective to the extent that it ... prohibits restricts, or requires the consent of the ... person obligated on the promissory note to the assignment or transfer of, or the creation, attachment, perfection, or enforcement of a security interest in the ... promissory note ..."), but it does not apply here by virtue subsection (e): "Subsection (d) does not apply to the sale of a payment intangible or promissory note, other than a sale pursuant to a disposition under Section 9-610 or an acceptance of collateral under Section 9-620." *Id.* § 9-406(e). Thus, the relevant provision in the UCC that Contrarian neglects to cite (§ 9-406) upholds the enforceability of anti-assignment provisions in the sale of promissory notes, and the provision on which Contrarian rests its argument (§ 9-408) applies only to grants of security interests.
- 37. In short, the Uniform Commercial Code does not render anti-assignment clauses in promissory notes null and void. If it did, then the case law would not be replete with promissory notes containing anti-assignment provisions, *see, e.g., Gragert v. Lake*, 541 F. App'x 853, 858 (10th Cir. 2013) (promissory note's anti-assignment provision rendered it illiquid and thus not an available "resource" for purposes of social insurance program eligibility); *Davis v. United States*, 961 F.2d 53, 55 (5th Cir. 1991); *Dzikowski v. Moreno (In re V.O.C. Analytical Labs., Inc.)*, 263 B.R. 156, 158 (S.D. Fla. 2001), and Contrarian would have some case law authority in support of its UCC argument.

The referenced sections 9-610 and 9-620 pertain to sales by a secured party post-default and retention of collateral by a secured party post-default, respectively. Del. Code Ann. tit. 6, §§ 9-610 & 9-620. Neither is implicated here.

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(3) A Counter-Party's Material Breach Does Not Void the Anti-Assignment Provisions in Promissory Notes (Or Any Other Contracts)

38. Contrarian asserts that "by failing to pay principal and interest when due, ... the Debtors have materially breached the terms of the Notes" and therefore "cannot enforce other terms of the Notes to the detriment of the non-breaching Noteholders." Mot. to Quash ¶ 27. This is not an accurate statement of the law. To be sure, the doctrine sometimes referred to as "failure of consideration" or "first material breach" does in certain circumstances prohibit a party that is itself in material breach of a contractual obligation from insisting on due performance from its non-breaching counterparty. See generally Restatement (Second) of Contracts § 237; 14 Williston on Contracts § 43:1. If, for example, the underlying loan agreements between the Debtors and the Noteholders purported to require a second round of funding from the Noteholders (they do not), then a material breach by the Debtors would be a defense to the Noteholders' obligation to advance even more funds to the Debtors. It is that proposition – which has no applicability here – that is described in the two cases cited by Contrarian. See Mot. to Quash ¶ 26 (citing BioLife Sols., Inc. v. Endocare, Inc., 838 A.2d 268, 278 (Del. Ch. 2003), and Hipcricket, Inc. v. mGage, LLC, No. CV 11135-CB, 2016 WL 3910837, at *1 & *11 (Del. Ch. July 15, 2016)).7

Neither case cited by Contrarian is on-point. The court in *BioLife* concluded that one party's failure to timely deliver certain assets under the parties' agreement was not a material breach that would excuse the other party's performance, reasoning that "a slight breach by one party, while giving rise to an action for damages, will not necessarily terminate the obligations of the injured party to perform under the contract." 838 A.2d at 278–82. In *Hipcricket*, the court enforced a choice of law provision in a breached contract, *see* 2016 WL 3910837, at *12, but refused to enforce the portion of the breached contract that would have prevented the non-breaching party (a salesperson who did not receive the commissions he had been promised) from soliciting customers from the breaching party (his former employer). *See* 2016 WL 3910837, at *15. This result is entirely consistent with the first-material-breach rule articulated in the Restatement: Having materially breached its obligations to pay its former employee the commissions he was owed, the employer could not simultaneously insist on due performance from the former employee. The employer was therefore not entitled to an order enforcing the agreement by barring the former employee from soliciting customers or employees of the former employer.

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- 39. One party's material breach of a contract does not mean that the contract itself—including its standard choice of law, choice of forum, anti-assignment, and other similar provisions somehow disappears. If it did, no debtor could ever enforce any provision in an executory contract or unexpired lease if the debtor had defaulted prepetition. Judge Silverstein's decision in *Diamondhead*, 2016 Bankr. LEXIS 2450, 2016 WL 3284674, is characteristically apt. There, the involuntary debtor asserted that one of the petitioning creditors' claims was the subject of a bona fide dispute because, *inter alia*, the claim was based on a promissory note that was assigned to it in violation of an anti-assignment provision in the note. 2016 Bankr. LEXIS 2450, at *40–41, 2016 WL 3284674, at *14. The petitioning creditors argued that the debtor was in material breach of the note based on its failure to pay and therefore could not enforce the anti-assignment provision in the note. 2016 Bankr. LEXIS 2450, at *45, 2016 WL 3284674, at *15. Judge Silverstein rejected this argument as "untenable," reasoning that the debtor's breach did not improve its counter-party's contractual rights. 2016 Bankr. LEXIS 2450, at *46, 2016 WL 3284674, at *15.
- 40. Diamondhead comports with the Restatement's first-material-breach rule, which treats one party's due performance as an implied condition of the counter-party's due performance. "A material failure of performance," then, affects only "the other party's remaining duties of performance with respect to the exchange. It prevents performance of those duties from becoming due, at least temporarily, and it discharges those duties if it has not been cured during the time in which performance can occur." Id. cmt. a (emphasis added); accord id. cmt. e ("Under the rule stated in this Section, only duties with respect to the performances to be exchanged under the particular exchange of promises are affected by a failure of one of those performances."). Here, the Debtors are not demanding further "performance" from their non-

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breaching counter-parties (as would be the case if, for example, the Debtors attempted to insist that Noteholders lend *more* money pursuant to the loan agreements). As such, the first-material-breach rule is not implicated.

41. The Fourth Circuit's decision in *Monster Daddy, LLC v. Monster Cable Products*, 483 F. App'x 831 (4th Cir. 2012), is instructive. There, the parties had entered into a settlement agreement that required any action against one another to be brought in a South Carolina court. *Id.* at 833. When Cable Products filed an action against Monster Daddy in California, Monster Daddy (which was in material breach of the trademark terms in the contract) relied on the forum selection clause to argue that the case had to be heard in South Carolina. *Id.* at 833–34. Cable Products responded that the forum selection clause was unenforceable on account of Monster Daddy's breach. *Id.* at 834. The Fourth Circuit rejected that argument:

Cable Products' reliance on the prior material breach doctrine is misplaced.... Here, performance under the forum selection clause was not dependent upon the performance of any other contract provision contained in the settlement agreement. In fact, the unambiguous language of the forum selection clause does not mention any other term, clause, or obligation in the settlement agreement.... Accordingly, because the forum selection clause was an independent promise bearing no relationship to the alleged prior material breach, the 'first material breach' doctrine was inapplicable as a defense in this case. [*Id.* at 835–36.]

42. Just as the Fourth Circuit concluded that Monster Daddy's alleged material breach of the trademark terms in its contract with Cable Products did not render unenforceable the forum selection clause in the parties' agreement, there is no basis for this Court to hold that even a material breach by the Debtors of their payment obligations under the Notes vitiates the anti-assignment provision in the Notes.⁸

Here, too, there is also a standing problem: Contrarian is not a party to any of the Notes or the loan agreements, and thus has no standing to argue the respective rights of the Noteholders. *See supra* note 2 (preserving all standing and other procedural arguments, which will be raised in opposition to the Note Motion itself).

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C. Discovery Is Permissible and Appropriate in Any Event

43. Contrarian implies that the relief it seeks in the Note Motion is wholly customary and will merely bring these Chapter 11 Cases in line with other bankruptcy cases around the country. *See, e.g.*, Note Mot. ¶ 17 ("The assignment of claims is extremely common in bankruptcy cases and promotes greater liquidity."). Not so. The Debtors have not attempted and are not attempting to restrict anyone from transferring anything that is routinely transferred in bankruptcy cases. Trade vendors, counter-parties to rejected leases and executory contracts, and other holders of other general unsecured claims against the Debtors are and always have been free to trade their claims as they see fit, just as in any other case. What is at issue in the Note Motion is something else entirely: The Notes themselves contain express anti-assignment provisions that are presumptively valid and have not been invalidated by any statute, rule, or order, and Contrarian seeks to void those restrictions on the grounds of, *inter alia*, "public policy" and "equity." The tailored discovery sought by the Debtors is necessary and appropriate to develop a proper factual record against which the Court can evaluate Contrarian's request.

(1) The Note Motion's Appeals to Equity and Public Policy Open Contrarian's Good Faith and Fair Dealing to Discovery

44. The Note Motion places Contrarian's good faith and the terms on which Contrarian is attempting to acquire Notes squarely at issue by, *inter alia*, explicitly appealing to equitable considerations as grounds for voiding the anti-assignment provisions. *See* Note Mot. ¶ 17 ("[A]s a matter of public policy, the consent provisions should not be enforced [and] the Court should, as a matter of equity, authorize the transfer of Notes without the Debtor's consent in view of the policy favoring assignability of claims."). Contrarian has thus invited scrutiny of its motives, its conduct, and its "conscience and good faith." *Precision Instrument Mfg. Co. v. Auto. Maint. Mach. Co.*, 324 U.S. 806, 814–15 (1945); *accord Root Ref. Co. v. Universal Oil*

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Prod. Co., 169 F.2d 514, 534–35 (3d Cir. 1948) ("No principle is better settled than the maxim that he who comes into equity must come with clean hands and keep them clean throughout the course of the litigation, and that if he violates this rule, he must be denied all relief whatever may have been the merits of his claim.").

45. As previewed in a recent filing that pertained to scheduling, the Debtors are aware of one particular solicitation made by Contrarian purporting to be an "offer of 82 cents per dollar for your Note, which must be recognized and allowed by the Debtor." *See* Scheduling Response & Cross-Mot. Ex. A. It appears that the actual price Contrarian is offering is in the 20- to 25-cent range, and that the 82-cent "offer" in the solicitation is conditioned on the Debtors agreeing that the Notes are secured – a position the Debtors have disputed since literally the first day in these Chapter 11 Cases. At best, this appears to be a bait-and-switch-type solicitation (piquing interest with a headline number – 82 cents – that in reality will never be paid). At worst, the solicitation may be intentionally and materially misleading. Either way, it "has immediate and necessary relation to the equity that [Contrarian] seeks in respect of the matter in litigation," *Keystone Driller Co. v. Gen. Excavator Co.*, 290 U.S. 240, 245 (1933), and is thus a proper topic of discovery.

(2) The Anti-Assignment Provisions Are Presently In Place and Effective

46. Although Contrarian seeks to invalidate the anti-assignment provisions in the Notes, to date the provisions remain operative and effective and enforceable by the Debtors. It is therefore perfectly proper to permit discovery into Contrarian's efforts to acquire Notes in violation of the anti-assignment provisions. This discovery is necessary to test the disputed factual assertions Contrarian has offered in support of its attempt to void the anti-assignment provisions, including in particular Contrarian's claim that the Debtors are "perversely caus[ing] further harm to the same defrauded creditors the Debtors claim to want to protect," Note Mot.

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 \P 2, and even "inflict[ing] a second injury upon the Noteholders," *id*. \P 15. These assertions are material to the Note Motion (otherwise Contrarian would not have made them), and the Debtors have reason to believe that there is evidence to be adduced in discovery that contradicts them.

In addition to the 82-cent "offer" described previously, see supra ¶ 45 (discussing Exhibit A to the Scheduling Response & Cross-Motion), the Debtors are aware of other solicitations in the marketplace that require Noteholders to make certain representations as a condition to acceptance - representations that are factually inaccurate. Attached hereto as **Exhibit A** is a recent (April 10, 2018) solicitation sent by another claim buyer (Fair Harbor Capital) that conditions its acceptance on the selling Noteholder "represent[ing], warrant[ing] and covenant[ing]" that the Noteholder will provide "good title" to the Note, that "no objection ... has been filed or threatened," and that the Debtor "has no basis to assert ... any defense" or argue for "disallowance ... whether on contractual, legal or equitable grounds" Those representations are untrue: As demonstrated by the Debtors' Claim Objection with respect to the Note Contrarian purported to purchase in violation of the anti-assignment provisions, the Debtors do in fact have a Bankruptcy Code section 502(b)(1) objection to each and every claim that rests on a Note that has been transferred in violation of the anti-assignment provisions, and the Debtors do intend to raise those objections. To the extent the claims buyer has an "out" in the event the representations it seeks from Noteholders prove untrue, the entire transaction has a heads-I-win-tails-you-lose quality: The claims trader can attempt to stand by those transactions that it ultimately finds beneficial yet walk away from transactions that do not ultimately work out in its favor.9

See Ex. A at p. 2, under the heading Representations; Warranties and Covenants ("Seller acknowledges and unconditionally agrees any misrepresentation or breach by Seller may cause Purchaser irreparable harm and accordingly, Purchaser shall be entitled to all available remedies as may be available to Purchaser for any such (footnote continued)

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- 48. Likewise, the specific facts of these Chapter 11 Cases – which involve a massive and long-running Ponzi scheme – raise key questions about the representations Noteholders are being induced to make to claim buyers concerning the value of their Notes. Under the Plan Term Sheet, the consideration that will ultimately be distributed in respect of any Note will take into account the prepetition "interest" received by such Noteholder. See Plan Term Sheet at pp. 8–9 (definition of "Note Distribution Formula"). That is because in a Ponzi scheme, one victim's "interest" is actually money that was procured by fraud from another, later-in-time victim. 10 Thus, the holders of two Notes that are identical in face amount and that are scheduled in identical amounts may ultimately receive different distributions, depending on the amount of prepetition "interest" that was paid. Thus, depending on the representations that claim buyers such as Contrarian may be inducing Noteholders to make, it is entirely possible Noteholders could be exposed to claims for breach. See supra note 9. There may also be misrepresentations or omissions concerning the material tax benefits with respect to timing-of-losses that Noteholders may enjoy as a result of the stipulated December 2017 discovery date of the Ponzi scheme. At a bare minimum, these are fair topics for discovery.
 - (3) The Fact That the SEC Has Alleged That the Notes Are Unlawfully Unregistered Securities Counsels in Favor of More Information (Not Less) About Potential Material Representations and Omissions in Connection with Attempted Purchases and Sales of the Notes
- 49. Finally, it bears emphasis that the specific Notes that Contrarian seeks to buy, sell, and otherwise freely trade and transfer have been alleged by the SEC to be unregistered

misrepresentation, breach or threatened breach, including but not limited to immediate recovery of money damages ('Restitution') including without limitation a 'Restitution Payment', as further defined below.").

See, e.g., Perkins v. Haines, 661 F.3d 623, 627 (11th Cir. 2011); Donell v. Kowell, 533 F.3d 762, 770-72 (9th Cir. 2008); AFI Holding, Inc. v. Mackenzie, 525 F.3d 700, 708-09 (9th Cir. 2008); Geltzer v. Barish (In re Geltzer), 502 B.R. 760, 770 (Bankr. S.D.N.Y. 2013); Fisher v. Sellis (In re Lake States Commodities, Inc.), 253 B.R. 866, 871-72 (Bankr. N.D. Ill. 2000).

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Exchange Act. They are thus different in kind from ordinary claims in chapter 11 cases. The proposed purchase and sale of instruments the SEC has alleged are securities without a registration statement or valid exemption could create exposure under the Securities Act, and any misrepresentations Noteholders may be induced to make in connection with the purchase or sale of instruments that the SEC has alleged are securities could create exposure under the Exchange Act. These circumstances make it all the more important to permit appropriate, tailored discovery designed to reveal precisely what is going on in the marketplace – *especially* in the absence of a single on-point authority or comparable instance in which relief of this nature (a wholesale voiding of anti-assignment restrictions in thousands of individual instruments that federal and state regulators have charged are unlawfully unregistered securities) has ever been granted by any bankruptcy court in the country.

50. In short, if the marketplace has been contaminated with misrepresentations, deceptions, or sharp practices of the sort suggested by the (admittedly limited) solicitations and transfer terms of which the Debtors are currently aware, discovery into the scope and extent of such matters is necessary to, *inter alia*, test Contrarian's allegations that enforcement of the anti-assignment provisions "perversely caus[es] further harm to the same defrauded creditors the Debtors claim to want to protect," Note Mot. ¶ 2, and "inflict[s] a second injury upon the Noteholders," *id.* ¶ 15. The actual facts adduced in discovery may demonstrate that far from harming or re-victimizing Noteholders, enforcement of the anti-assignment provisions in the Notes is preventing violations of the Securities Act and Exchange Act.

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CONCLUSION

51. For all of the foregoing reasons, the Debtors respectfully request that the Court deny the Motion to Quash and permit the Debtors to take targeted, appropriate discovery concerning the Note Motion.

Dated: Wilmington, Delaware

April 26, 2018

YOUNG CONAWAY STARGATT & TAYLOR, LLP

/s/ Edmon L. Morton

Sean M. Beach (No. 4070) Edmon L. Morton (No. 3856) Ian J. Bambrick (No. 5455) Allison S. Mielke (No. 5934)

Rodney Square

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-and-

KLEE, TUCHIN, BOGDANOFF & STERN LLP

Kenneth N. Klee (*pro hac vice*) Michael L. Tuchin (*pro hac vice*) David A. Fidler (*pro hac vice*) Jonathan M. Weiss (*pro hac vice*) 1999 Avenue of the Stars, 39th Floor Los Angeles, California 90067

Counsel for the Debtors and Debtors in Possession

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Exhibit A

Sequence Number 1035

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1841 Broadway, 10th Floor, New York, New York 10023

www.FairHarborCapital.com

Tel 212 967 4035. Fax 212 967 4148

Tuesday, April 10,2018

NOTE HOLDER

1.35

Limited Allocation - CASH Out

RE:

Woodbridge Mortgage Investment Fund 3A, LLC

Part of the Bankruptcy fo Woodbridge Group of Companies, LLC, et al.

U.S. Bankruptcy Court, District of Delaware Bankruptcy Petition #: 17-12780 (KJC)

<u> Ալովիկիդիկինիկին արագարությունի իրականի անկանի</u>

Dear Sir or Madam:

We are writing you to express indication of our interest in purchasing your claim of \$36,000.00 for a cash payment of \$7,740.00. If you are interested in selling your claim please:

- Sign the attached Claim Purchase Agreement in where indicated,
- Attach copies of Promissory Note and Loan Agreement, and
- Return the entire document to us by fax (212) 967-4148, or email (proposals@fairharborcapital.com) and mail the original.

URGENT - This indication expires at the close of business on May 5th, 2018 and is subject to acceptance, further due diligence, and mutually agreeable documents of transfer. If accepted, payments are typically sent by mail within 10 business days (unless noted alternatively above). Funds may be sent by overnight delivery for a nominal charge.

This indication of interest is on a first-come, first-serve basis and the allocation for this case is limited and may be rescinded for any reason whatsoever without further notice or obligation from either party. Please do not delay. Please note that Fair Harbor Capital, LLC is not obligated to file any application, motion, Proof of Claim or other document with the Bankruptcy Court with regard to your claim.

Please do not hesitate to call at (866) 967 4035 with any questions or email at vknox@fairharborcapital.com.

Sincerely,

Victor Knex

Fair Harbor Capital, LLC*

Please note, Fair Harbor Capital, LLC is an independent investment company not affiliated with or hired by the Debtor or the Bankruptcy Court.

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FL 33434. for good and valuable consideration in the sum of \$7,740.00 (the "Purchase Price"), does hereby absolutely and unconditionally sell, convey, and transfer to Fair Harbor Capital, LLC, and any of its successors, assign or designees (hereinafter "Purchaser") all of Seller's right, title, benefit and interest in and to any and all of Seller's pre-petition claim or claims, as more specifically set forth as any right to payment (the "Claim"), against Woodbridge Mortgage Investment Fund 3A, LLC ("the "Debtor"), in bankruptcy proceedings in the United States Bankruptcy Court for the District of Delaware (the "Court"). Case No. 17-12780 (KJC) Jointly administered under the main case, 17-12560 (the "Case"); and includes any Proof of Claim (defined below), along with voting and any other rights and benefits which may now exist, or come into existence in regards the Claim, all cash securities, instruments and other property, to be paid or issued by Debtor or any other party, directly or indirectly, in connection with or satisfaction of the Claim, including without limitation "cure" amounts related to the assumption of an executory contract and any rights to receive all payments in respect thereof, and all rights to receive interest, penalties, fees and any damages from any cause of action, litigation or rights of any nature against Debtor, its affiliates, any guarantor or other third party, which may be paid or issued with respect to and/or in satisfaction of the Claim (the "Recovery"). This Claim Purchase Agreement (the "Agreement") shall be deemed an unconditional purchase of the Claim for the purpose of collection and shall not be deemed to create a security interest. Seller represents the Claim is manount not less than \$36,000.00 (the "Claim Amount"). In the event that any Recovery related to the claim is made payable or addressed to the Seller hereby authorizes Purchaser to deposit such Recovery into Purchaser's bank as if such Recovery was made payable or in the name of Purchaser.

Proof of Claim. Seller represents and warrants that (check one)

(i) a proof of claim in the amount of ______ (the "Proof of Claim Amount") has been duly and timely filed in the Case; or

(ii) no proof of claim has been filed. For the avoidance of doubt, the term "Proof of Claim" shall include, unless expressly agreed to otherwise,

(a) any and all multiple Proofs of Claim filed at any time, whether before or after the date of execution of this Agreement, by or on behalf of Seller in respect of the Claim and (b) any and all of Seller's documentation supporting the Claim. The parties agree that if the Proof of Claim Amount is less than the Claim Amount, the Purchase Price shall be reduced such that Seller shall be paid the pro rata share of the Purchase Price based on the lower Proof of Claim Amount.

Representations; Warranties and Covenants, Seller represents, warrants and covenants that, (a) Seller owns and has sole title to the Claim free and clear of any and all liens, security interests or encumbrances of any kind or nature whatsoever, including without limitation pursuant to any factoring agreement, and upon the sale of the Claim to Purchaser, Purchaser will receive good title to the Claim; (b) Seller has not previously sold, assigned, transferred, or pledged the Claim, in whole or in part, to any third party; (c) the basis for the Claim is amounts validly due from and owing by the Debtor, (d) the Claim is a valid, undisputed, liquidated, enforceable, and non-contingent claim against the Debtor for which the Debtor has no defenses and no objection to the Claim has been filed or threatened; (e) Seller has not engaged in any acts, conduct or omissions that might result in Purchaser receiving, in respect of the Claim, proportionately less payments or distributions or any less favorable treatment than other similarly situated creditors; (f) Debtor, or any other third party, has no basis to assert the Claim is subject to any defense, claim or right of setoff, reduction, impairment, disallowance, subordination or avoidance, including preference actions, whether on contractual, legal or equitable grounds;(g) that Seller is not "insolvent" within the meaning of Section 1-201 (23) of the Uniform Commercial Code or within the meaning of Section 101 (32) of the Bankruptcy Code; and (h) Seller is not an "insider" of the Debtor, as set forth in the United States Bankruptcy Code § 101(31), or a member of any official or unofficial committee in connection with the Case. Seller acknowledges and unconditionally agrees any misrepresentation or breach by Seller may cause Purchaser irreparable harm and accordingly, Purchaser shall be entitled to all available remedies as may be available to Purchaser for any such misrepresentation, breach or threatened breach, including but not limited to the immediate recovery of money

Execution of Agreement. This Agreement shall become effective and valid when (a) Seller executes this Agreement and it is received by Purchaser and (b) the Agreement is executed by a proper representative of Purchaser.

Consent and Waiver. Seller hereby acknowledges and consents to all of the terms set forth in this Agreement and hereby waives its right to raise any objections thereto pursuant to Rule 3001 of the Rules of Bankruptcy Procedure.

Claim or Recovery Impaired or Allowed for an Amount Less than Claim Amount or Case Conversion/Dismissal, If all or any part of the Claim or Claim Amount is (a) avoided, disallowed, subordinated, reclassified, reduced, objected to, or otherwise impaired, for any reason whatsoever including without limitation a breach of any of the terms or conditions of this Agreement; or (b) the Claim is subsequently scheduled by Debtor or is amended such that all or any portion of the Claim is listed on the Debtor's amended schedule of liabilities as unliquidated, contingent or disputed or in a lesser amount than the Claim Amount (each (a) and (b) a "Disallowance"), then Seller, shall make immediate Restitution and repayment of the proportional Purchase Price equal to the ratio of the amount of the Disallowance divided by the Claim Amount multiplied by the Purchase Price ("Restitution Payment"), no later than 30 days after receiving notice of such Disallowance. Such Restitution Payment shall be made together with interest, calculated at the rate of five (5%) percent per annum, from the date of Seller's execution of this Agreement until the date that such Restitution Payment is received by Purchaser. For clarity purposes, this paragraph pertains only to the validity of the Claim and not the Recovery. Notwithstanding the foregoing, in the event that the Debtor's bankruptcy case is dismissed or converted to a case under Chapter 7 of the Bankruptcy Code, ownership of the Claim shall revert back to the Seller and all monies paid by Purchaser shall remit to Purchaser.

Notices (including Voting Ballots) Received by Seller; Further Cooperation. Seller agrees to immediately forward to Purchaser any and all notices received from Debtor, the Court or any other court or governmental entity or any third party regarding the Claim assigned herein and to take such other action, with respect to the Claim, as Assignee may request from time to time. More specifically, Seller shall take such further action as may be necessary or desirable to effect the transfer of the Claim and to direct any payments or distributions, or any form of Recovery on account of the Claim to Purchaser, including the execution of appropriate voting ballots, transfer powers and consents at Purchaser's sole discretion.

Recovery (including Cure Payments) Received or Delayed by Seller, In the event Seller, (i) receives any interim or final distribution of the Recovery, or any portion thereof, made payable on or after the date of Seller's execution of this Agreement; or (ii) delays or impairs Purchaser's right to Recovery for any reason (each (i) and (ii) a "Delayed Recovery Event"), then Seller agrees to (a) accept any Recovery the same as Purchaser's agent and to hold the same in trust on behalf of and for the sole benefit of Purchaser and shall promptly deliver the same forthwith to Purchaser in the same form received, or in a form reasonably requested by Purchaser, free of any withholding, set-off, claim or deduction of any kind and/or (b) settle or cure the reason for the Delayed Recovery Event (each(a) and (b) a "Settlement") within ten (10) business days of the Delayed Recovery Event (the "Settlement Date"). Seller shall pay Purchaser interest, calculated at the rate of five (5%) percent per annum of any amount or portion of Recovery that incurs a Delayed Recovery Event, for each day after the Settlement Date until such Recovery is received by Purchaser.

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0IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

Debtors.	Ref. Docket Nos. 1585, 1586, 1593
et al., 1	(Jointly Administered)
WOODBRIDGE GROUP OF COMPANIES, LLC,	Case No. 17-12560 (KJC)
In re:	Chapter 11

THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS'
JOINDER AND STATEMENT IN SUPPORT OF DEBTORS' (I) RESPONSE
TO MOTION TO SHORTEN NOTICE WITH RESPECT TO MOTION TO
QUASH OF CONTRARIAN FUNDS, LLC; AND (II) CROSS-MOTION FOR
CONTINUANCE OF HEARING ON MOTION OF CONTRARIAN FUNDS, LLC
FOR AUTHORITY TO ACQUIRE PROMISSORY NOTES AGAINST THE DEBTORS

The Official Committee of Unsecured Creditors (the "<u>Committee</u>") appointed in the above-captioned cases, through the Committee's undersigned counsel, hereby joins and files this statement in support of the *Debtors'* (*I*) *Response to Motion to Shorten Notice With Respect to Motion to Quash of Contrarian Funds, LLC; and (II) Cross-Motion for Continuance of Hearing on Motion of Contrarian Funds, LLC for Authority to Acquire Promissory Notes Against the Debtors* [Docket No. 1593] (the "<u>Response</u>").² The Committee joins in the Response for the reasons set forth therein.

Background

On April 3, 2018, Contrarian Funds, LLC ("<u>Contrarian</u>") filed its *Motion* for Authority to Acquire Promissory Notes [D.I. 890] (the "<u>Notes Motion</u>").

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¹ The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of such information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting counsel for the Debtors.

² Capitalized terms not defined herein shall have the meaning as provided by the Response.

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- 2. On April 10, 2018, the Debtors filed its notice to conduct a Rule 30(b)(6) deposition of a representative of Contrarian [D.I. 954] (the "Deposition Notice").
- 3. In response, on April 18, 2018, Contrarian filed a *Motion to Quash of Contrarian Funds, LLC* [D.I. 1585] (the "Motion to Quash") seeking to quash the Deposition Notice.
- 4. Contemporaneously therewith, Contrarian also filed its *Motion to Shorten*Notice with Respect to Motion to Quash of Contrarian Funds, LLC [D.I. 1586] (the "Motion to Shorten") seeking to schedule the Motion to Quash to be heard during the previously scheduled omnibus hearing on May 1, 2018, at 11:00 a.m., and to shorten the period for notice of the hearing, with objections, if any, to be filed by 4:00 p.m. on April 26, 2018.
- 5. On April 19, 2018, the Debtors filed their Response consenting to the Motion to Quash being heard on May 1, 2018 (as requested in the Motion to Shorten) if the hearing on the Notes Motion is continued to June 5, 2018.

<u>Joinder</u>

- 6. The Committee joins in the Response and agrees that the Motion to Quash should be heard on May 1, 2018 and the Notes Motion continued to June 5, 2018.
- 7. Since its appointment, the Committee has been committed to protecting the interests of investors who were defrauded by the Debtors' former principal, Robert Shapiro.

 To this end, the Committee supported a moratorium on claims trading in order to ensure that investors are not prejudiced by unscrupulous claims traders who may be preying on investors.

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8. The Committee is deeply concerned about what appears to be deliberately misleading solicitations by claims traders such as Contrarian (see Ex. A to the Response). The Committee supports the relief requested in the Response because a full factual record must be developed before there is a hearing on the merits of the Notes Motion.

9. Accordingly, the Committee requests that the Court: (i) schedule the Motion to Quash for May 1, 2018; (ii) continue the Notes Motion to June 5, 2018; and (iii) grant such other and further relief as the Court deems appropriate.

Dated: April 19, 2018 PACHULSKI STANG ZIEHL & JONES LLP

/s/ Colin R. Robinson

Richard M. Pachulski (CA Bar No. 90073) James I. Stang (CA Bar No. 94435) Jeffrey N. Pomerantz (CA Bar No. 143717) Bradford J. Sandler (DE Bar No. 4142) Colin R. Robinson (DE Bar No. 5524) 919 North Market Street, 17th Floor P.O. Box 8705

Wilmington, DE 19899 (Courier 19801) Telephone: 302-652-4100

Counsel for the Official Committee of Unsecured Creditors

DOCS DE:219112.2 94811/002

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:

Chapter 11

WOODBRIDGE GROUP OF COMPANIES, LLC, et al.,

Case No. 17-12560 (KJC) (Jointly Administered)

Debtors.

Objection Deadline: April 24, 2018 at 4:00 p.m. (EDT) Hearing Date: May 1, 2018 at 11:00 a.m. (EDT)

MOTION OF CONTRARIAN FUNDS, LLC FOR AUTHORITY TO ACQUIRE PROMISSORY NOTES AGAINST THE DEBTORS

Contrarian Funds, LLC ("<u>Contrarian</u>"), by and through its undersigned counsel, submits this motion (the "<u>Motion</u>") for entry of an order authorizing it to acquire, and the Noteholders (as defined below) to freely assign, all rights, title and interests in the promissory notes (the "<u>Notes</u>") they hold against the above-captioned debtors and debtors in possession¹ (the "<u>Debtors</u>") without further order of this Court or obtaining prior consent from the Debtors, and in support of this Motion, respectfully represents as follows:

Introduction

- 1. Having been victimized by a very broad and significant Ponzi scheme perpetrated by the Debtors, certain of the Noteholders (defined below) have elected to sell their Notes, whether because of a need for liquidity, a desire to mitigate risk, and/or a preference for immediate payment, rather than waiting for confirmation of a plan, claims reconciliation and distribution. Contrarian has contracted to purchase Notes from several Noteholders.
- 2. However, under the guise of protecting Noteholders and preventing distractions during anticipated plan negotiations, the Debtors have unilaterally imposed a 90-day moratorium

¹ A complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC.

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on the transfer of Notes and reserved the right to invalidate prior or future transfers. As set forth in greater detail below, such unilateral action is highly inappropriate and should not be permitted. Preventing liquidity perversely causes further harm to the same defrauded creditors the Debtors claim to want to protect. Accordingly, Contrarian moves this Court for entry of an order allowing the transfer of Notes underlying the claims Contrarian has purchased.

Jurisdiction and Venue

3. The Court has subject matter jurisdiction to consider and determine this matter pursuant to 28 U.S.C. §§ 1334(b) and 157 and the *Amended Standing Order of Reference* from the United States District Court for the District of Delaware dated as of February 29, 2012. This Motion is a core proceeding within the meaning of 28 U.S.C. §157(b). Venue is proper under 28 U.S.C. §§ 1408 and 1409.

Background

- 4. On December 4, 2017 (the "Petition Date"), Woodbridge Group of Companies, LLC and certain of its affiliated Debtors filed voluntary petitions for relief under chapter 11 of Title 11 of the United States Code (the "Bankruptcy Code"). Thereafter, certain other affiliated Debtors commenced voluntary chapter 11 bankruptcy cases. The Debtors are continuing to manage their financial affairs and property as debtors in possession pursuant to §§ 1107 and 1108 of the Bankruptcy Code. The Debtors bankruptcy cases (collectively, the "Cases") are being jointly administered pursuant to various prior orders of the Court.
- 5. On December 14, 2017, the United States Trustee for the District of Delaware appointed an official committee of unsecured creditors (the "Committee") in the Cases pursuant to §1102 of the Bankruptcy Code [Docket No. 79].

2

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- 6. Prior to the Petition Date, the Debtors were engaged in a retail fundraising operation managed by WMF Management, LLC, which directly owns seven fund entities (the "Funds"). The Funds raised money from thousands of retail investors ("Noteholders") by issuing short-term notes ("Notes") that were secured by a pledge to the Funds of certain promissory notes and related loan and security agreements, deeds of trust, or mortgages ("Collateral Documents") from special purpose vehicle entities that hold real properties (the "PropCos"). Upon information and belief, the Debtors, their in-house salespeople, and their outside broker network touted the Notes to the Noteholders as being secured by first-priority liens upon real property owned by the PropCos. In reality, it appears the Noteholders only had an unperfected security interest in the Collateral Documents; upon information and belief, there was never a collateral agent established for the benefit of the Noteholders to protect the Noteholders' interest in their collateral and no UCC-1 financing statements were filed on behalf of the Noteholders.
- 7. Upon information and belief, the Debtors stopped making payments on the Notes and, by the Petition Date, there were approximately \$750 million Notes outstanding, held by approximately 9,000 Noteholders.
- 8. After the Petition Date, by order entered on January 23, 2018,² this Court approved a settlement (the "Settlement") reached between certain of the Debtors and other

² Order, Pursuant to Sections 105(a) and 1102 of the Bankruptcy Code and Bankruptcy Rule 9019, Approving the Consensual Resolution of (A) Motion of the Ad Hoc Committee of Holders of Promissory Notes of Woodbridge Mortgage Investment Fund Entities and Affiliates Pursuant to Section 1102(a)(2) of the Bankruptcy Code Directing the Appointment of an Official Committee of Noteholders, (B) Emergency Motion of Official Committee of Unsecured Creditors for Entry of an Order Directing the Appointment of a Chapter 11 Trustee Pursuant to 11 U.S.C. § 1104, (C) Motion by the U.S. Securities and Exchange Commission for Order Directing the Appointment of a Chapter 11 Trustee, (D) Joinder of Additional Noteholders to Motion of the Ad Hoc Committee of Holders of Promissory Notes of Woodbridge Mortgage Investment Fund Entities and Affiliates Pursuant to Section1102(a)(2) of The Bankruptcy Code Directing the Appointment of an Official Committee of Noteholders, and (E) Motion of the Ad Hoc

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parties in interest by which, among other things, the Debtors' board of managers was reconstituted and an ad hoc Noteholder group (the "Noteholder Group") and an ad hoc unitholder group (the "Unitholder Group") was authorized and formed.

The Notes Transfer Moratorium Imposed by the Debtors

9. By *Notice Regarding Transfers of Units or Notes* filed with the Court on March 21, 2018 (the "Notice") [Docket No. 799], the Debtors declared a unilaterally imposed moratorium on any further transfer of Notes for ninety (90) days and reserved all rights with respect to the invalidity and ineffectiveness of any prior, current, or future attempts to transfer Notes (the "Moratorium"). In the Notice, the Debtors justified the Moratorium on the basis that the terms of their organizational documents and other Note documents require the Debtors' consent for transfer, and that the Moratorium was imposed after consideration with the Committee, the Noteholder Group, and the Unitholders Group (collectively, the "Committees") in the hope of negotiating a plan that can be effectuated by year-end, avoiding distractions so the Debtor can focus on exiting the chapter 11 process, and the desire to protect Noteholders. Notably, the Debtors seek to enforce the contracts that they themselves fraudulently induced the Noteholders to enter into and have breached and have remained in breach.

10. The Moratorium has no bearing on the plan process, and it does not protect Noteholders. To the contrary, it serves to further exacerbate the Noteholders' financial difficulties by destroying the Notes' liquidity. The Noteholders are the victims of the Debtors' mammoth ponzi-scheme, the investors having been fraudulently induced to invest \$750 million based on the lie that their investments were sound and secured by first-priority liens upon real property. A majority of the Noteholders are individuals who had entrusted the Debtors'

Committee of Unitholders of Woodbridge Mortgage Investment Fund Entities Pursuant to 11 U.S.C. § 1102(a)(2) Directing Appointment of an Official Committee of Unitholders [Docket No. 357].

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fraudulent lending vehicles with substantial assets, and for whom the Debtors' default on the Notes and bankruptcy is causing financial hardship. Restricting the transfer of the Notes only makes matters worse for them. Noteholders face their own individual circumstances; some may need immediate liquidity and/or some may not wish to bear the risk of case outcome and return or the timing of confirmation of a plan and subsequent distribution. Yet, through the Moratorium, without any consideration of individual Noteholder needs, the Debtors adopted a one size fits all approach and eviscerated many Noteholders' hope for immediate liquidity. Unlike other creditors in the Cases, the Moratorium prevents Noteholders from opting out of the bankruptcy process. And despite the Debtors' contentions, if Noteholders are free to assign the Notes without the Debtors' consent it would not adversely impact the Debtors' plan process because (a) the identity of an assignee is no longer relevant to the Debtors given that the Notes are in default and are not being paid now, and (b) the Debtors would not need to waste unnecessary time or focus reviewing every transfer.³ Regardless, avoiding distractions for a debtor simply does not justify preventing creditors from selling their claims.

11. As for protecting the Noteholders, while this is a noble goal, it is inappropriate for the Debtors to unilaterally determine what is best for the thousands of Noteholders that have already been victimized by these Debtors. The Debtors have not considered each Noteholder's liquidity needs or risk tolerance, and for the Debtors to impose their views on a global class of creditors is highly restrictive and patently unfair to the creditors that do want to sell their Notes. Additionally, the Debtors do not know the individual tax considerations of each Noteholder, or the implications their unilateral Moratorium and stated right to invalidate prior or future transfers

³ Each transfer of a Note can simply be recorded by the claims agent retained in the Cases. *Order Appointing Garden City Group, LLC as Claims and Noticing Agent Nunc Pro Tunc to the Petition Date* [Docket No. 46].

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might have on any particular Noteholder. Preventing a creditor who wants to monetize its claims and get out of the Cases to instead wait and bear further value risk (whether due to increased Case expenses, delay, or possible negative information, that impacts the value of the claim and sale price, or due to an individual's tax considerations) is not an outcome that "protects" creditors. There is simply no valid basis for the Moratorium.

Relief Requested and Basis Thereto

- 12. Accordingly, by this Motion, Contrarian seeks entry of an order authorizing the Noteholders to freely assign their Notes (and the related right to payment and distributions thereunder) and for it to acquire all rights, title and interests in the Notes without further order of this Court or obtaining prior consent from the Debtors notwithstanding the Moratorium.
- 13. Although the Notes indicate that they are not assignable by Noteholders without the Debtors' written consent, Contrarian submits that prior approval of the Debtors for an assignment should not be mandated in these circumstances when the Notes were issued as part of a massive ponzi scheme, the Noteholders were fraudulently induced to invest in the Notes and there was a material default so soon after the issuance of the Notes by the Debtors' failure to make payments to the Noteholders.
- 14. It is well-settled law that when a contract is materially breached, the non-breaching party is discharged from the further performance under the contract. *See In re Lavigne,* 114 F.3d 379, 387 (2nd Cir. 1997) ("a breach in a contract which substantially defeats the purpose of that contract can be grounds for rescission. The non-breaching party will be discharged from the further performance of its obligations under the contract when the breach goes to the root of the contract" citing *Dept. of Economic Dev. v. Arthur Andersen & Co., 924 F. Supp. 449, 483 (S.D.N.Y. 1996)*). Here, because the Debtors breached their obligations to the

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Noteholders by failing to pay monthly mandated interest payments (among other breaches), they can no longer enforce the terms of the Notes, including the provision that requires their prior consent to any assignment of the Notes. The Debtors should not be allowed to "cherry pick" which provisions of the Notes they would like to remain in force after they have defaulted. Accordingly, any Noteholder that seeks to assign or otherwise transfer its interests and claims should not be required to obtain the Debtors' written consent.

- 15. Moreover, the consent provisions in the Notes should not be enforced in these Cases because it would inflict a second injury upon the Noteholders who are looking to exit from their investment and need to recoup some of their losses. As noted, a significant number of the Noteholders are individuals who are suffering financial hardships as a result of the Debtors' default on the Notes and bankruptcy Cases, which is only aggravated by the Moratorium. Permitting the transfer of their Notes freely would provide the Noteholders with the ability to monetize their debt immediately and avoid case outcome and timing risks, at no cost to the Debtors.
- 16. It is well held that the automatic stay is a shield and may not be used as a sword. In re Briarpatch Film Corp., 281 B.R. 820, 834 (Bankr. S.D.N.Y. 2002)(citing cases). Because the Noteholders are subject to the automatic stay, they are not able to exercise any remedies available to them under the Notes and related documents based upon the Debtors' default; but, the Noteholders should also not be held hostage by preventing them from assigning their interests in the Notes and attendant claims. Rather, like the general unsecured creditors in the Cases, the Noteholders should be free to assign and transfer their respective interests in the Notes without regard to any consent restrictions.

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17. Also, as a matter of public policy, the consent provisions should not be enforced because the identity of any assignee of the Notes is no longer relevant to the Debtors since any payment on the Notes will only occur under a plan confirmed in these Cases. The assignment of claims is extremely common in bankruptcy cases and promotes greater liquidity. General unsecured creditors may freely trade their claims in the Cases without any restrictions and the Noteholders should be permitted to do so as well. Therefore, the Court should, as a matter of equity, authorize the transfer of Notes without the Debtor's consent in view of the policy favoring assignability of claims. Freely permitting assignments and other transfers of the Notes in these circumstances will also eliminate the burden of having the Noteholders seek and the Debtors having to consider providing written consent, which would appease the Debtors' concern about diverting their focus from the plan process.⁴

18. For the foregoing reason, Contrarian submits that the Notes should be freely assignable and transferable without the Debtors' consent or further order of this Court.

Notice

19. Notice of this Motion has been served upon counsel for the Debtors, counsel for each of the Committees, the United States Trustee for the District of Delaware, all parties who have filed requests for notice in the Cases and filed with the Bankruptcy Court electronically. Contrarian submits that no other or further notice need be provided.

No Prior Request

 Contrarian has not previously sought the relief requested herein from this or any other Court.

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⁴ This is in addition to the fact that, as noted above, the Debtors were in breach of the agreement containing these provisions from the outset.

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WHEREFORE, Contrarian respectfully requests that an order be entered, substantially in the form attached hereto as Exhibit A, authorizing the Noteholders to freely assign all of their right, title and interests in the Notes and grant to Contrarian such other and further relief as is just and proper.

BIELLI & KLAUDER, LLC

Dated: April 3, 2018 Wilmington, Delaware /s/ David M. Klauder
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Counsel to Contrarian Funds, LLC

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

Debtors.	Re: Docket No.
WOODBRIDGE GROUP OF COMPANIES, LLC, et al.,	Case No. 17-12560 (KJC) (Jointly Administered)
In re:	Chapter 11

ORDER GRANTING MOTION OF CONTRARIAN FUNDS, LLC FOR AUTHORITY TO ACQUIRE PROMISSORY NOTES AGAINST THE DEBTORS

Upon the motion (the "Motion") of Contrarian Funds, LLC ("Contrarian") for entry of an order authorizing it to acquire, and the Noteholders¹ to freely assign, all right, title and interests in the Notes against the Debtors without further order of this Court or obtaining prior consent from the Debtors; and a hearing on the Motion having been held on May ___, 2018; and the Court having found that (i) it has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334, (ii) this proceeding is a core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A) and (B), (iii) venue of this proceeding is proper pursuant to 28 U.S.C. §§ 1408 and 1409, and (iv) notice of the Motion was provided to all necessary and appropriate parties; and the Court having determined that the bases set forth in the Motion establish sufficient grounds for the relief granted herein; and due deliberation having been had; and sufficient cause appearing therefor, it is hereby ORDERED that

- 1. The Motion is granted as set forth herein.
- 2. Each and any Noteholder shall be and hereby is authorized to freely assign or otherwise transfer its right, title and interest in the Notes and attendant claims against the Debtors

 $^{^1}$ All capitalized and undefined terms used in this Order shall have the meaning assigned to such terms in the Motion.

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free of any restrictions or requirements set forth in the Notes and any related agreement or

document without further order of this Court; provided that any such assignment or other transfer

shall be subject the applicable requirements of the Federal Rules of Bankruptcy Procedure.

3. The claims under the Notes shall remain subject to all defenses, counterclaims,

and objections of the Debtors related thereto, including the Debtors' right to object to the claim

on any and all grounds.

4. Contrarian and the Debtors are authorized to take all such actions necessary or

appropriate to implement the terms of this order.

5. Notwithstanding Bankruptcy Rule 6004(h), the terms and conditions of this Order

shall be immediately effective and enforceable upon its entry.

6. The Court retains jurisdiction with respect to all matters arising from or related to

the interpretation, implementation, and enforcement of this order.

Dated: May____, 2018

Wilmington, Delaware

KEVIN J. CAREY

UNITED STATES BANKRUPTCY JUDGE

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re: Chapter 11

WOODBRIDGE GROUP OF COMPANIES, LLC, et al.,

S, Case No. 17-12560 (KJC) (Jointly Administered)

Debtors.

Objection Deadline: April 24, 2018 at 4:00 p.m. (EDT) Hearing Date: May 1, 2018 at 11:00 a.m. (EDT)

NOTICE OF MOTION OF CONTRARIAN FUNDS, LLC FOR AUTHORITY TO ACQUIRE PROMISSORY NOTES AGAINST THE DEBTORS

Contrarian Funds, LLC, by and through its undersigned counsel, filed the *Motion of Contrarian Funds*, *LLC for Authority to Acquire Promissory Notes Against the Debtors* (the "Motion").

You are required to file a response to the Motion on or before <u>April 24, 2018 at 4:00</u> p.m. (ET).

At the same time, you must also serve a copy of the response upon the Debtor's attorneys:

David M. Klauder, Esquire BIELLI & KLAUDER, LLC

1204 N. King Street Wilmington, DE 19801 Phone: (302) 803-4600 Fax: (302) 397-2557 dklauder@bk-legal.com Alan D. Halperin, Esq. Debra J. Cohen, Esq.

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A HEARING ON THE MOTION WILL BE HELD ON <u>May 1, 2018 at 11:00 a.m. (ET)</u> before the Honorable Kevin J. Carey at the United States Bankruptcy Court for the District of Delaware, 824 North Market Street, 5th Floor, Wilmington, DE 19801 in Courtroom Number 5.

IF YOU FAIL TO RESPOND IN ACCORDANCE WITH THIS NOTICE, THE COURT MAY GRANT THE RELIEF DEMANDED IN THE MOTION WITHOUT FURTHER NOTICE OR HEARING.

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BIELLI & KLAUDER, LLC

Dated: April 3, 2018 Wilmington, Delaware /s/ David M. Klauder
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Counsel to Contrarian Funds, LLC

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:

Chapter 11

WOODBRIDGE GROUP OF COMPANIES, LLC, et al.,

Case No. 17-12560 (KJC) (Jointly Administered)

Debtors.

Objection Deadline: April 24, 2018 at 4:00 p.m. (EDT) Hearing Date: May 1, 2018 at 11:00 a.m. (EDT)

CERTIFICATE OF SERVICE

I, David M. Klauder, certify that on April 3, 2018, I caused a true and correct copy of the *Motion of Contrarian Funds, LLC for Authority to Acquire Promissory Notes Against the Debtors*, to be served via facsimile, electronic mail, or U.S. First Class Mail, Postage Prepaid as indicated, upon those on the attached service list.

BIELLI & KLAUDER, LLC

Dated: April 3, 2018 Wilmington, Delaware /s/ David M. Klauder
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Counsel to Contrarian Funds, LLC

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:

WOODBRIDGE GROUP OF COMPANIES, LLC, et al., 1

Case No. 17-12560 (KJC)

(Jointly Administered)

Debtors.

Re: Dkt. No. 1586

Chapter 11

DEBTORS': (I) RESPONSE TO MOTION TO SHORTEN NOTICE WITH RESPECT TO MOTION TO QUASH OF CONTRARIAN FUNDS, LLC; AND (II) CROSS-MOTION FOR CONTINUANCE OF HEARING ON MOTION OF CONTRARIAN FUNDS, LLC FOR AUTHORITY TO ACQUIRE PROMISSORY NOTES AGAINST THE DEBTORS

Woodbridge Group of Companies, LLC and its affiliated debtors and debtors in possession (collectively, the "Debtors") in the above-captioned chapter 11 cases (the "Chapter 11 Cases") hereby: (i) respond to the *Motion to Shorten Notice With Respect to Motion to Quash of Contrarian Funds, LLC* [Docket No. 1586] (the "Motion to Shorten"), filed by Contrarian Funds, LLC ("Contrarian"), in respect of the *Motion to Quash of Contrarian Funds, LLC* [Docket No. 1585] (the "Motion to Quash"); and (ii) cross-move for a continuance of the hearing on the *Motion of Contrarian Funds, LLC for Authority to Acquire Promissory Notes Against the Debtors* [Docket No. 890] (the "Note Motion") to June 5, 2018 (the next omnibus hearing date after May 1, 2018). As detailed below, the Debtors support the relief requested in the Motion to Shorten (that is, to have the Motion to Quash heard on May 1, 2018) if and only if the hearing on the Note Motion is continued from May 1, 2018 to June 5, 2018.

The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of such information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

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INTRODUCTION

- 1. Each of the nearly 9,000 prepetition notes issued by the Debtors (the "Notes") contain anti-assignment provisions that are clear and conspicuous:
 - 14. <u>No Assignment.</u> Neither this Note, the Loan Agreement of even date herewith between Borrower and Lender, nor all other instruments executed or to be executed in connection therewith (collectively, the "<u>Collateral Assignment Documents</u>") are assignable by Lender without the Borrower's written consent and any such attempted assignment without such consent shall be null and void.
- 2. In its Note Motion, Contrarian essentially asks the Court to enjoin the Debtors from enforcing these provisions in thousands of Notes with a categorical declaration that "[e]ach and any Noteholder shall be and hereby is authorized to freely assign or otherwise transfer its right, title and interest in the Notes and attendant claims against the Debtors free of any restrictions or requirements set forth in the Notes and any related agreement or document" Note Mot. Ex. A (Proposed Order) ¶ 2. But see FED. R. BANKR. P. 7001(7) (requiring an adversary proceeding "to obtain an injunction or other equitable relief").
- 3. The Note Motion requests sweeping and unprecedented relief that could have profound effects on the Debtors and their creditors. For example, given the contentions of federal and state securities regulators that the Notes are unregistered securities,² it may well be the case that injunctive relief of the type Contrarian seeks will have material securities law consequences. The proposed purchase and sale of securities without a registration statement or valid exemption that is applicable to all holders could expose the Debtors' noteholders to significant risk, and Contrarian conspicuously fails to offer any indemnity or other potentially

² See generally Complaint for Injunctive and Other Relief, SEC v. Shapiro, et al., No. 1:17-cv-24624 (S.D. Fla., filed Dec. 20, 2017) (the "SEC Complaint") (broadly charging the Debtors with federal securities fraud in connection with unregistered sale of Notes); see also id. ¶ 36 ("Five states, Texas, Massachusetts, Arizona, Pennsylvania, and Michigan, have entered temporary or permanent cease and desist orders against one or more of the Corporate Defendants related to their unregistered sale of securities.").

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ameliorative relief with regard to such potential consequences. Contrarian is resisting even limited discovery into key issues such as whether its solicitations are false or misleading (as the Debtors have reason to believe – $see\ infra\ \P\ 5$) or would otherwise potentially violate securities laws. It is telling that neither the Note Motion nor the Motion to Quash cites a single other instance in which relief of this nature – a wholesale voiding of anti-assignment restrictions in thousands and thousands of individual instruments (let alone instruments that federal and state regulators have already charged are unlawfully unregistered securities) – has even been sought, let alone granted, by any bankruptcy court in the country. These are uncharted waters.

4. Given the stakes, it is critical that the Debtors and all parties in interest have a full and fair opportunity to be heard – including with respect to the availability of discovery. The Debtors will demonstrate in their opposition to the Motion to Quash that the Note Motion places Contrarian's good faith and the terms on which Contrarian is attempting to acquire Notes squarely at issue by, *inter alia*, explicitly appealing to equitable considerations as grounds for voiding the anti-assignment provisions. *See* Note Mot. ¶ 17 ("[A]s a matter of public policy, the consent provisions should not be enforced [and] the Court should, as a matter of equity, authorize the transfer of Notes without the Debtor's consent in view of the policy favoring assignability of claims."). Contrarian has thus invited scrutiny of its motives, its conduct, and its "conscience and good faith." *Precision Instrument Mfg. Co. v. Auto. Maint. Mach. Co.*, 324 U.S. 806, 814–15 (1945) (discussing "the equitable maxim that 'he who comes into equity must come with clean hands," which is "far more than a mere banality": "It is a self-imposed ordinance that closes the doors of a court of equity to one tainted with inequitableness or bad faith relative to the matter in which he seeks relief").

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- 5. By way of illustration only, the Debtors are aware of one particular solicitation made by Contrarian purporting to be an "offer of 82 cents per dollar for your Note, which must be recognized and allowed by the Debtor." *See* **Exhibit A** hereto. On information and belief, the actual price Contrarian is offering is in the 20- to 25-cent range; the 82-cent "offer" in the solicitation is conditioned on the Debtors agreeing that the Notes are secured a position the Debtors have disputed since literally the first day in these Chapter 11 Cases. The solicitation as written is materially misleading, and it "has immediate and necessary relation to the equity that [Contrarian] seeks in respect of the matter in litigation." *Keystone Driller Co. v. Gen. Excavator Co.*, 290 U.S. 240, 245 (1933). It is manifestly a proper topic of discovery.
- 6. Critically, the discovery at issue in the Motion to Quash is the same discovery the Debtors seek in order to fully respond to the Note Motion. Thus, if Contrarian's Motion to Shorten is granted but the hearing on Contrarian's Note Motion is not continued, the Debtors' response to the Note Motion will be due at the same time as the Debtors' opposition to the Motion to Quash the very discovery the Debtors seek in order to respond to the Note Motion. Such a sequence makes no sense.
- 7. The Debtors are agreeable to the Motion to Quash being heard on May 1, 2018 (as requested in the Motion to Shorten) *if* the hearing on the Notes Motion is continued to June 5, 2018. At the May 1 hearing, the Debtors will ask the Court to deny the Motion to Quash. If the Court does so, the Court will have determined that the Debtors are entitled to take discovery in connection with the Note Motion which will in turn mean that a hearing on the Note Motion that very same day (May 1, 2018) is premature. And even if the Court were to grant the Motion to Quash on May 1, it would still be appropriate for the Debtors to have the benefit of the Court's ruling in preparing their response to the Note Motion, and for the Note Motion to be heard at the

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same June 5, 2018 hearing as the Debtors' recently-filed *Notice of Debtors'* (*I*) Objection to Proof of Claim No. 1216 Asserted by Putative Transferee Contrarian Funds, LLC Without Prejudice to Right of Putative Transferors Elissa and Joseph Berlinger to Assert Such Claim; and (II) Request for a Limited Waiver of Local Rule 3007-1(f)(iii), to the Extent Such Rule May Apply [Docket No. 1563] (the "Claim Objection"), which rests on the non-enforceability of Notes in the hands of a putative purchaser who acquired the Notes in violation of antiassignment provisions. The Claim Objection is inextricably intertwined with the Note Motion, and the two should be heard together.

8. For these reasons, and as more particularly set out below, the Debtors support the relief requested in the Motion to Shorten (that is, to have the Motion to Quash heard on May 1, 2018) if and only if the hearing on the Note Motion is continued from May 1, 2018 to June 5, 2018, concurrent with the Claim Objection.

RELEVANT BACKGROUND

A. The Bankruptcy Case

- 9. On December 4, 2017, approximately 270 of the Debtors commenced voluntary cases under chapter 11 of the Bankruptcy Code. Thereafter, on February 9, 2018, March 9, 2018, March 23, 2018, and March 27, 2018, additional affiliated Debtors (27 in total) commenced voluntary cases under chapter 11 of the Bankruptcy Code (collectively, the "Petition Dates"). Pursuant to sections 1107(a) and 1108 of the Bankruptcy Code, the Debtors are continuing to manage their financial affairs as debtors in possession.
- 10. The Chapter 11 Cases are being jointly administered pursuant to Bankruptcy Rule 1015(b) and Local Rule 1015-1. As of the date hereof, no trustee has been appointed in the Chapter 11 Cases. An official committee of unsecured creditors (the "Unsecured Creditors")

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Committee") was appointed in the Chapter 11 Cases on December 14, 2017 [Docket No. 79]. On January 23, 2018, the Court approved a settlement providing for the formation of an ad hoc noteholder group (the "Noteholder Group") and an ad hoc unitholder group (the "Unitholder Group" and, collectively with the Unsecured Creditors' Committee and the Noteholder Group, the "Constituencies") [Docket No. 357].

B. Contrarian's Note Motion

- The prepetition Notes issued by the Debtors contain restrictions on assignment. For example, each of the Notes appended to Contrarian's proof of claim (which is itself appended as Exhibit C to the Claim Objection) provides: "Neither this Note, the Loan Agreement of even date herewith between the Borrower and Lender, nor all other instruments executed or to be executed in connection therewith (collectively, the 'Collateral Assignment Documents') are assignable by Lender without the Borrower's written consent and any such attempted assignment without such attempted consent shall be null and void." Note ¶ 14.

 Delaware law holds that such provisions are valid and enforceable, *see*, *e.g.*, *Paul v*. *Chromalytics Corp.*, 343 A.2d 622, 625-26 (Del. Super. Ct. 1975), and Contrarian's Uniform Commercial Code ("UCC") argument to the contrary in the Motion to Quash is without merit.
- 12. On March 21, 2018, the Debtors filed the *Notice Regarding Transfers of Units or Notes* [Docket No. 799] (the "<u>Transfer Notice</u>"), which informed creditors of "a temporary moratorium on consideration of consent to any Transfer of Units or Notes for the next ninety (90) days" in order to, *inter alia*, avoid distractions and focus on exiting the chapter 11 process.

In brief, UCC § 9-408 applies only to security interests in notes, not to sales of notes. The pertinent section of Article 9 is UCC § 9-406(e), which makes clear that anti-assignment provisions in promissory notes may be enforced to prohibit sales of notes. *See, e.g., Day v. White*, No. 2013-0044, 2017 U.S. Dist. LEXIS 90135, at *18-23 (D.V.I. June 12, 2017).

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- 13. On April 3, 2018, Contrarian filed the Note Motion. In it, Contrarian seeks what is in essence an injunction barring the Debtors from enforcing the anti-assignment provisions in the Notes. As grounds for such extraordinary relief, Contrarian makes several assertions of fact, including that Noteholders are being affirmatively harmed, *see* Note Mot. ¶ 2 ("Preventing liquidity perversely causes further harm to the same defrauded creditors the Debtors claim to want to protect."), *id.* ¶ 10 ("Restricting the transfer of the Notes only makes matters worse for [the Noteholders]."), and that the Debtors are acting unfairly vis-à-vis their creditors, *see id.* ¶ 11 ("The Debtors have not considered each Noteholder's liquidity needs or risk tolerance, and for the Debtors to impose their views on a global class of creditors is highly restrictive and patently unfair to the creditors that do want to sell their Notes."). Further, the Note Motion explicitly appeals to public policy and equitable considerations as grounds for voiding the anti-assignment provisions, *see id.* ¶ 17, thus bringing into play considerations of clean hands.
- 14. On April 4, 2018 (the day after the Note Motion was filed), the Debtors sent a letter (attached hereto as **Exhibit B**) to Contrarian's counsel seeking informal discovery with respect to the Note Motion, with a response requested by April 10, 2018. Contrarian's response (attached hereto as **Exhibit C**) declined to provide such discovery. That same day, the Debtors served a deposition notice (Mot. to Quash Ex. A), followed the next day by the document requests (attached hereto as **Exhibit D**) that mirror the informal discovery requests. The Debtors requested that Contrarian respond to the document requests by April 16, 2018, and noticed the deposition for April 18, 2018, in order to gather information necessary to prepare the Debtors' response to the Note Motion by the April 24, 2018 deadline.
- 15. On April 16, 2018, the Debtors filed the Claim Objection, objecting to Claim No.1216 (the "Contrarian Proof of Claim"), which is the sole claim filed to date by Contrarian in

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these Chapter 11 Cases. The Claim Objection is set for hearing on June 5, 2018, and it is inextricably intertwined with the Note Motion. Indeed, the Claim Objection (which rests on Bankruptcy Code section 502(b)(1)) directly undercuts the relief requested in the proposed order that Contrarian seeks in the Note Motion, as that proposed order includes the following carve-out: "The claims under the Notes shall remain subject to all defenses, counterclaims, and objections of the Debtors related thereto, including the Debtors' right to object to the claim on any and all grounds." Note Mot. Ex. A (Proposed Order) ¶ 3. If the Claim Objection is sustained on June 5 (as the Debtors believe it should be), then the order that Contrarian seeks in connection with the Note Motion will have served no purpose.

16. On April 18, 2018, Contrarian filed its Motion to Quash, which seeks an order quashing the Deposition Notice, and the associated Motion to Shorten, which seeks to have the Motion to Quash set for hearing on May 1, 2018 – *i.e.*, the same day the Note Motion is set for hearing.⁴ The Motion to Quash observes that "Contrarian will serve a response and objections to th[e] Document Request[s] in accordance with the Bankruptcy Rules," Mot. to Quash ¶ 15 n.3, which presumably means on May 10, 2018 (*i.e.*, 30 days after the requests were served), rather than by the already-passed April 16, 2018 date requested by the Debtors. If the hearing on the Note Motion stays set for May 1, 2018, it is not clear what good responses to written discovery served nine days later will be.

RELIEF REQUESTED

17. The Debtors are agreeable to the Motion to Quash being heard on May 1, 2018 so long as the hearing on the Notes Motion is continued to June 5, 2018. Accordingly, by this

Contrarian requested, and the Debtors agreed, to give Contrarian a few extra days to file the Motion to Quash and to defer the deposition until that motion's disposition to avoid needless rushed ex parte proceedings.

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response and cross-motion, the Debtors ask the Court to: (i) enter the *Order Approving Motion to Shorten Notice With Respect to Motion to Quash of Contrarian Funds, LLC* that is appended as Exhibit A to Contrarian's Motion to Shorten, such that the Motion to Quash is heard on May 1, 2018, with objections due by April 24, 2018; and (ii) continue the hearing on Contrarian's Note Motion to June 5, 2018, with a corresponding extension of the deadline to respond to the Note Motion such that responses are due May 29, 2018.

BASIS FOR RELIEF

- 18. The Court has broad discretion and authority with respect to scheduling matters for hearing, *see*, *e.g.*, 11 U.S.C. § 105(a), and "to control the disposition of the causes on its docket with economy of time and effort for itself, for counsel, and for litigants." *Landis v. N. Am. Co.*, 299 U.S. 248, 254 (1936). The Debtors respectfully submit that the most efficient way of proceeding is to set the Motion to Quash for hearing on May 1, 2018, and to continue the hearing on the Note Motion to June 5, 2018. No party will be prejudiced by such a schedule least of all Contrarian, which had the option of promptly responding to the Debtors' tailored discovery (first informally, then pursuant to proper notices) in an expeditious manner, which would have allowed the Note Motion to be heard on May 1, 2018. Instead, Contrarian chose to resist all discovery by instead filing the Motion to Quash. Contrarian is within its rights to seek relief by its Motion to Quash, but it will have no cause to complain if its chosen course of action results in the hearing on its Note Motion being continued to the next available omnibus hearing date of June 5, 2018.
- 19. As the Debtors will demonstrate in their opposition to the Motion to Quash, the Note Motion makes numerous assertions that the Debtors are entitled to test through the discovery process, including that enforcement of the anti-assignment provisions "perversely

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causes further harm to the same defrauded creditors the Debtors claim to want to protect," Note Mot. \P 2, "inflict[s] a second injury upon the Noteholders," id. \P 15, and is contrary to sound "public policy" and "equity," id. \P 17. These assertions are material to the Note Motion (otherwise Contrarian would not have made them), and the Debtors have reason to believe that there is evidence to be adduced in discovery that flatly contradicts them. The Debtors should have the opportunity to make their case to the Court for discovery *before* being required to respond on the merits of the Note Motion. That is why a continuance of the Note Motion is necessary and appropriate here.

- 20. Finally, without delving into the merits of Contrarian's substantive arguments (such as they are), several brief points are appropriate in response to the Motion to Shorten, which itself contains extensive merits arguments that go well beyond mere scheduling issues. *See, e.g.*, Mot. to Shorten ¶ 10 (asserting that the information sought by the Debtors in discovery "is not relevant to the Note Motion"); *id.* ¶ 11 ("Bankruptcy Rule 3001(e) severely limits standing to challenge the transfer of claims as a broad policy in favor of the free transfer of claims.... As if that were not enough, state law does not authorize the moratorium the Debtors have sought to impose."); *id.* ¶ 14 ("As discovery should not be used as a lever to restrict legitimate market activity that can benefit these investors, the Court should immediately quash the Deposition Notice."); *id.* ¶ 18 ("Noteholders have the right to transfer the Notes that they own pursuant to the corresponding terms agreed to by Contrarian and the relevant Noteholders.").
 - Federal Rule of Bankruptcy Procedure 3001(e) does not override state law and transform non-assignable instruments into assignable ones. No case so holds, and
 as the Debtors have set out in their Claim Objection there is extensive case

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law to the effect that a claim transferred in violation of an applicable bar to assignment is unenforceable in the hands of the putative transferee and thus objectionable under 11 U.S.C. § 502(b)(1). *See, e.g., In re Gilbreath*, 409 B.R. 84, 121 (Bankr. S.D. Tex. 2009). In other words, the pertinent rule is not Bankruptcy Rule 3001 – it is Bankruptcy Code section 502(b)(1).

- One party's breach (even a material breach) of a contract does not render the contract's anti-assignment provision unenforceable. See, e.g., In re Diamondhead Casino Corp., 2016 Bankr. LEXIS 2450, at *45-46 (Bankr. D. Del. June 7, 2016). If it did, then no debtor could ever enforce any provision in executory contracts and leases if the debtor defaulted prepetition. That is not the law.
- The Note Motion seeks relief that is in the nature of either a mandatory injunction compelling the Debtors to assent to assignments notwithstanding the provisions of the Notes (quoted above in paragraph 1) or a declaratory judgment that the Debtors' consent is unnecessary, such that the Note Motion is procedurally inapt.

 See FED. R. BANKR. P. 7001(7) & (9).
- 21. The brief points adverted to above are by no means exhaustive, but they are indicative of the weakness of the merits arguments made in the Note Motion. In exercising its broad discretion with respect to scheduling and case management, the Court may properly take into account all the facts and circumstances here including the unprecedented nature of the relief being sought, the absence of any on-point authority supporting such relief, the potential impact on the Debtors and these Chapter 11 Cases of permitting unrestricted trading of what several regulatory authorities have asserted are securities, and the unwillingness of the moving

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party to permit any inquiry into non-privileged matters that are directly relevant to that party's asserted entitlement to relief.

22. On April 18, 2018, counsel for the Debtors emailed Contrarian's counsel to inquire whether Contrarian would consent to the Debtors' proposed continuance of the hearing on the Note Motion. *See* **Exhibit E** hereto. Directly prior to the filing of this response, Contrarian's counsel relayed that Contrarian does not consent to the Debtors' request.

CONCLUSION

23. For all of the foregoing reasons, the Debtors respectfully request that the Court:

(i) enter the *Order Approving Motion to Shorten Notice With Respect to Motion to Quash of Contrarian Funds, LLC* that is appended as Exhibit A to Contrarian's Motion to Shorten, such that the Motion to Quash is heard on May 1, 2018, with objections due by April 24, 2018;

(ii) enter an order, in the form attached hereto as **Exhibit F**, continuing the hearing on Contrarian's Note Motion to June 5, 2018, with a corresponding extension of the deadline to respond to the Note Motion such that responses are due May 29, 2018; and (iii) grant such other or further relief as may be necessary or appropriate.

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Dated: April 19, 2018

Wilmington, Delaware

YOUNG CONAWAY STARGATT & TAYLOR, LLP

/s/ Ian J. Bambrick

Sean M. Beach (No. 4070) Edmon L. Morton (No. 3856) Ian J. Bambrick (No. 5455) Allison S. Mielke (No. 5934)

Rodney Square

1000 North King Street Wilmington, Delaware 19801 Tel: (302) 571-6600 Fax: (302) 571-1253

-and-

KLEE, TUCHIN, BOGDANOFF & STERN LLP

Kenneth N. Klee (pro hac vice) Michael L. Tuchin (pro hac vice) David A. Fidler (pro hac vice) Jonathan M. Weiss (pro hac vice) 1999 Avenue of the Stars, 39th Floor Los Angeles, California 90067

Counsel for the Debtors and Debtors in Possession

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Exhibit A

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CAPITAL MANAGEMENT

411 WEST PUTNAM AVENUE, SUITE 425 | GREENWICH, CT 06830

January 24, 2018

Re: Woodbridge Group Companies, LLC

Dear Noteholder:

Contrarian Capital Management, L.L.C. ("Contrarian"), a multi-billion dollar money management firm founded in 1995, would like to purchase your secured promissory note (the "Note") against Woodbridge Group Companies, LLC (the "Debtor") in the United States Bankruptcy Court for the District of Delaware. We encourage you to consider our offer of 82 cents per dollar for your Note, which must be recognized and allowed by the Debtor.

This offer is based upon market conditions, the actual size and type of your Note and your Note being recognized by the Debtor. Notes will be purchased on a first offered, first bought basis, and Contrarian reserves the right to reject any Notes presented. Contrarian's purchase of your Note is subject to the execution and delivery of transfer documentation, the assignment of the Note to Contrarian per the books and records of the Debtor and our due diligence, including a copy of the promissory note, any account statements from the Debtor and all supporting documentation for the Note.

The amount Contrarian is offering for your claim may be more or less than you may receive when a confirmed Plan of Reorganization or Liquidation for the Debtor is completed. We recommend that you familiarize yourself with the public information with respect to these cases. While Contrarian believes this is the highest offer currently in the market for your Note, please contact us if this is not your best offer.

To further discuss the sale of your Note, please contact Rhoda Freeman (Freeman @Contrariancapital.com) or John Bright (Jbright @Contrariancapital.com) at (800) 266-3810 or (203) 862-8232.

Sincerely,

Contrarian Capital Management, L.L.C

TOLUFREE: (800) 266-3810 | PHONE (203) | 2-8232 | FAX: (203) 485-5910 | WWW.CONTRARIANCA | FAL COM

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Exhibit B

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1999 Avenue of the Stars Thirty-Ninth Floor Los Angeles, California 90067 voice: 310-407-4000 fax: 310-407-9090 www.ktbslaw.com

rpfister@ktbslaw.com Direct Dial: 310-407-4065

April 4, 2018

VIA ELECTRONIC MAIL

Alan D. Halperin, Esq.
(ahalperin@halperinlaw.net)
Debra J. Cohen, Esq.
(dcohen@halperinlaw.net)
Halperin Battaglia Benzija, LLP
40 Wall Street, 37th Floor
New York, New York 10005

David M. Klauder, Esq. (dklauder@bk-legal.com) Biellli & Klauder, LLC 1204 North King Street Wilmington, Delaware 19801

Re: Motion of Contrarian Funds, LLC for Authority to Acquire Promissory Notes Against the Debtors [Docket No. 890]

Dear Counsel:

We represent Woodbridge Group of Companies, LLC and its affiliated debtors and debtors-in-possession (collectively, the Debtors). Yesterday you filed the above-referenced motion (the Motion) on behalf of Contrarian Funds, LLC (Contrarian). The Motion states, *inter alia*, that: (i) "Contrarian has contracted to purchase Notes from several Noteholders," Mot. \P 1; (ii) the Debtors' moratorium on consideration of consent to transfers "causes further harm to the same defrauded creditors the Debtors claim to want to protect," *id.* \P 2, "inflict[s] a second injury upon the Noteholders, *id.* \P 15, and is akin to them "be[ing] held hostage," *id.* \P 16; and (iii) "as a matter of public policy" and "a matter of equity," the Court should order that the consent provisions in the notes are not enforceable.

The Debtors have significant concerns with respect to Contrarian's standing to pursue the relief requested in the Motion and the propriety of the procedural vehicle by which such relief is being sought. In addition, Contrarian's framing of the issue in terms of public policy and equity raises numerous ancillary questions. Reserving the right to undertake formal discovery (including a deposition or depositions) of Contrarian if necessary, but in order to deal with the Motion in the most expeditious possible fashion, the Debtors request that Contrarian voluntarily produce the following three categories of documents:

 All offers and solicitations made by or on behalf of Contrarian for the acquisition of any notes or claims against the Debtors. The documents

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David M. Klauder, Esq. Alan D. Halperin, Esq. April 4, 2018 Page 2

should include the price(s) being offered and all terms and conditions of each offer.

- All contracts, assignments, transfers, consents, receipts, bills of sale, remittances, and other documents of any type constituting or concerning the acquisition of any notes or claims against the Debtors. The documents should reflect all terms of the transactions (including price), and should indicate what if any consideration has actually been paid by Contrarian, along with all documents evidencing such payment including, by way only of example, wire transfer advices and cancelled checks.
- All communications between Contrarian (including any agent or person or entity acting for or on behalf of Contrarian) and any creditor of the Debtors (including any agent or person or entity acting for or on behalf of any creditor or group of creditors). The documents should include any negotiations that have taken place and any representations or predictions that have been made.

To be clear, it is essential that all the preceding be complete and unredacted. If you have concerns about public disclosure of all or part of any of these documents, we are prepared to work with you to assure those concerns are addressed.

We would appreciate production of the foregoing on or before Tuesday, April 10, 2018. If that is not possible, please at least advise by that time and state when production will occur.

Very truly yours,

Robert J. Pfister

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Exhibit C

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Kramer Levin



April 10, 2018

BY EMAIL

Robert J. Pfister Klee, Tuchin, Bogdanoff & Stern LLP 1999 Avenue of the Stars Los Angeles, CA 90067

P. Bradley O'Neill
Partner
T 212-715-7583
F 212-715-8000
BOneili@KRAMERLEVIN.com

1177 Avenue of the Americas New York, NY 10036 T 212.715.9100 F 212.715.8000 e: Motion of Contrarian Funds, LLC for Authority to Acquire Promissory Notes Against the Debtors [Docket No.890]

Dear Mr. Pfister:

We are co-counsel to Contrarian Funds, LLC ("Contrarian") in connection with its recent motion for authority to acquire promissory notes [Dkt. No. 890]. I have received your letter, dated April 4, 2018, to our co-counsel seeking certain consensual expedited discovery from Contrarian, which you purport to justify based on concerns about Contrarian's standing and the procedural basis for the motion.

Contrarian has no desire to unnecessarily increase expense or inconvenience for the estate and other parties. But the discovery you seek is simply not appropriate. Concerns about Contrarian's standing do not require discovery. Contrarian has purchased the Debtor's notes and thus is both a creditor in this proceeding, see proof of claim No 1216, and a party in interest, and therefore has the right to appear and be heard. Similarly, your alleged procedural concerns about the form of the motion appear to be legal in nature and do not require discovery.

As importantly, it is not clear what bearing the specifics of Contrarian's transactions with various noteholders have on the merits of Contrarian's motion. The terms of its acquisition of promissory notes do not impact the administration of the estates or plan negotiations. Nor is it clear the Debtors have any basis to question transactions in the market between non-debtors. Bankruptcy Rule

KL2 3065872.2

KRAMER LEVIN NAFTALIS & FRANKEL LLP NEW YORK | SILICON VALLEY | PARIS

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Robert J. Pfister April 9, 2018



3001(e) governs the assignment of claims in bankruptcy and "is designed to permit free assignability with minimal judicial intervention." *In re Preston Trucking Co.*, 332 B.R. 315, 332 (Bankr. D. Md. 2005); accord Fed. R. Bankr. P. 3001, Advisory Committee Note (1991)(stating that the purpose of Rule 3001(e) is to "limit the court's role in the adjudication of disputes regarding transfers of claims."). Indeed, Rule 3001(e) allows only the transferor — and not the Debtor — to object to the transfer of a claim. See *In re Lynn*, 285 B.R. 858, 862 (Bankr. S.D.N.Y. 2002) ("third parties, including the Debtor, do not have standing to object to a claim assignment itself"). Nor does the Debtor appear to have a basis under State law to object to note purchases. The UCC plainly provides that restrictions on transfer of a promissory note are ineffective. See UCC 9-408.

If the Debtors have some basis for their resistance to the motion or the discovery they seek of which I am not aware, please let me know. I am happy to discuss the matter with you further.

Sincerely,

P. Bradley O'Neill

PO:ls

cc: Alan D. Halperin, Esq. David M. Klauder, Esq.

KL2 3065872.2

2

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Exhibit D

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:

Chapter 11

WOODBRIDGE GROUP OF COMPANIES, LLC, et

Case No. 17-12560 (KJC)

 $al.,^1$

(Jointly Administered)

Debtors.

DEBTORS' FIRST SET OF REQUESTS FOR PRODUCTION OF DOCUMENTS

PROPOUNDING PARTY: The Debtors

RECEIVING PARTIES: Contrarian Funds, LLC

DOCUMENT REQUESTS: 1 through 3

Pursuant to Rule 34 of the Federal Rules of Civil Procedure ("FRCP"), made applicable by Rules 7034 and 9014 of the Federal Rules of Bankruptcy Procedure, the debtors and debtors in possession (the "Debtors") in the above-captioned chapter 11 bankruptcy case hereby request that Contrarian Funds, LLC ("Contrarian") "produce and permit [the Debtors] to inspect [or] copy" the documents, electronically stored information and tangible things set out below, FRCP 34(a)(1), by Monday, April 16, 2018 or such other deadline as the Court may specify or the parties may mutually agree.

Definitions

1. Capitalized terms used but not otherwise defined herein shall have the meanings ascribed to them in the Motion (as defined below).

The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of this information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

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- 2. "Contrarian," the "Debtors," and "FRCP" have the meanings set out in the prefatory paragraph above.
- 3. "Affiliate," whether or not capitalized and whether in the singular or plural, has the meaning given to that term by Bankruptcy Code § 101(2).
- 4. "Communication" means the transmittal of information (in the form of facts, ideas, inquiries, or otherwise) whether written or oral and, with respect to oral communications, includes any Document evidencing the date, participants, subject matter, and content of any such oral communication, including transcripts, minutes, notes, recordings, calendar entries, and the like.
- 5. "Concerning" means relating to, referring to, describing, evidencing or constituting.
- 6. "Document(s)" is meant as broadly as possible and includes, without limitation, all "documents or electronically stored information" referenced in FRCP 34(a)(1)(A). A draft or non-identical copy is a separate document within the meaning of this term.
- 7. "Motion" means the Motion of Contrarian Funds, LLC for Authority to Acquire Promissory Notes Against the Debtors [Docket No. 890], filed by Contrarian on April 3, 2018.
- 8. "Person" means any natural person or any legal entity. Reference to any "Person" includes any and all agents, advisors, employees, representatives, attorneys, successors-in-interest, and all other persons or entities acting in his, her, or its behalf or under his, her or its control.
 - 9. "You" and "Your" means Contrarian.

Instructions

 Unless otherwise indicated, the documents requested to be produced include all documents in Your possession, custody, or control or the possession, custody, or control of 01:23088141.1

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anyone acting on Your behalf. If any requested document was, but no longer is, in Your possession, custody, or control, state the disposition of each such document.

- 2. Responsive documents should be produced in accordance with Local Bankruptcy Rule 7026-3(d)-(f) and as they are kept in the usual course of business or organized and labeled to correspond with the categories in the requests. Selection of documents from the files and other sources and the numbering of such documents shall be performed in such a manner as to ensure that the source of each document may be determined, if necessary. Electronic records and computerized information must be produced in their native format with all metadata preserved and intact.
- 3. You are required to produce the original and all non-identical copies, including all drafts, of each document requested. If You are not able to produce the original of any document, please produce the best available copy and all non-identical copies, including drafts. A document with handwritten, typewritten or other recorded notes, editing marks, etc., is not and shall not be deemed identical to one without such modifications, additions, or deletions.
- 10. "All," "any," and "each" shall each be construed as encompassing any and all; the connectives "and" and "or" shall be construed either disjunctively or conjunctively as necessary to bring within the scope of the discovery request all responses that might otherwise be construed to be outside of its scope; and the use of the singular form of any word includes the plural and vice versa.
- 4. If any document is withheld under any claim of privilege, including without limitation attorney-client privilege and/or attorney work product, please provide the following information with respect to such document: (a) the date of the document; (b) the name and title of its author(s) or preparer(s); (c) the name and title of each Person who was sent or furnished

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with, received, or has custody of the document or a copy thereof; (d) the title of the document; (e) the claim of privilege under which it is withheld; and (f) a description of the subject matter of the document in sufficient detail to support Your contention that the document is privileged.

- 5. If an objection is made to any request or part thereof, state your objection and the ground(s) with particularity in your written response.
- 6. These requests are continuing in nature. If, after producing the requested documents, You obtain or become aware of any further documents responsive to this request, You are required to produce such additional documents within thirty (30) days after such documents become known to You.

Document Requests

REQUEST FOR PRODUCTION NO. 1: All contracts, assignments, transfers, consents, receipts, bills of sale, remittances, and other Documents of any type constituting or concerning the acquisition of any Notes or claims against the Debtors. The Documents should reflect all terms of the transactions (including price), and should indicate what, if any, consideration has actually been paid by You or Your Affiliates, along with all Documents evidencing such payment including, without limitation, wire transfer advices and cancelled checks.

REQUEST FOR PRODUCTION NO. 2: All Documents Concerning any offers or solicitations made by or on behalf of You or Your Affiliates for the acquisition of any Notes or claims against the Debtors. The Documents should include the price(s) being offered and all terms and conditions of each offer.

REQUEST FOR PRODUCTION NO. 3: All Communications between You or any of Your Affiliates and any Noteholder or other creditor of the Debtors (including any agent or person or entity acting for or on behalf of any Noteholder or other creditor of the Debtors). The

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Documents should include, without limitation, any negotiations that have taken place and any representations or predictions that have been made.

Dated: April 11, 2018

/s/ Sean M. Beach

Wilmington, Delaware

YOUNG CONAWAY STARGATT & TAYLOR, LLP

Sean M. Beach (No. 4070) Edmon L. Morton (No. 3856) Ian J. Bambrick (No. 5455) Allison S. Mielke (No. 5934)

Rodney Square, 1000 North King Street

Wilmington, Delaware 19801 Tel: (302) 571-6600 Fax: (302) 571-1253

-and-

KLEE, TUCHIN, BOGDANOFF & STERN LLP

Kenneth N. Klee (*pro hac vice*) Michael L. Tuchin (*pro hac vice*) David A. Fidler (*pro hac vice*) Jonathan M. Weiss (*pro hac vice*) 1999 Avenue of the Stars, 39th Floor Los Angeles, California 90067

Counsel to the Debtors and Debtors in Possession

Case 17-12560-KJC Doc 1593-5 Filed 04/19/18 Page 1 of 3

Exhibit E

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From: Robert J. Pfister "O"Neill, P. Bradley" Subject: RE: Woodbridge

Wednesday, April 18, 2018 6:46:19 PM Date:

Brad,

Following up on the voice message I just left on your office line with regard to Contrarian's Motion to Shorten, the Debtors are agreeable to having the Motion to Quash heard at the May 1 omnibus (as requested in your Motion to Shorten) so long as the Note Motion itself is continued to the June 5 omnibus. That way, Judge Carey can hear argument on the discovery issue you raise in the Motion to Quash and rule on that issue, and the Debtors can then prepare an appropriate response to the Note Motion (either incorporating our discovery if Judge Carey allows discovery, or confining the arguments strictly to legal issues if Judge Carey does not allow discovery). In addition, moving the Note Motion to June 5 would have the added benefit of allowing it to be heard at the same time as the Debtors' objection to Contrarian's proof of claim, which is set for June 5 and which raises issues that are inextricably intertwined with the Note Motion.

Please let me know whether Contrarian will agree to the foregoing.

Regards,

Rob

Robert J. Pfister KLEE, TUCHIN, BOGDANOFF & STERN LLP 1999 Avenue of the Stars, 39th Floor Los Angeles, California 90067 Telephone: (310) 407-4000 Fax: (310) 407-9090

Direct: (310) 407-4065

mail: RPfister@ktbslaw.com web: http://www.ktbslaw.com

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From: Robert J. Pfister

Sent: Monday, April 16, 2018 10:07 AM

To: 'O'Neill, P. Bradley' Subject: RE: Woodbridge

Confirmed.

Robert J. Pfister KLEE, TUCHIN, BOGDANOFF & STERN LLP 1999 Avenue of the Stars, 39th Floor Los Angeles, California 90067 Telephone: (310) 407-4000 Fax: (310) 407-9090

Direct: (310) 407-4065

Case 17-12560-KJC Doc 1593-5 Filed 04/19/18 Page 3 of 3

mail: RPfister@ktbslaw.com web: http://www.ktbslaw.com

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From: O'Neill, P. Bradley [mailto:BOneill@KRAMERLEVIN.com]

Sent: Monday, April 16, 2018 6:34 AM

To: Robert J. Pfister **Subject:** Woodbridge

Rob:

This will confirm our conversation on Friday. Contrarian will be moving for a protective order in respect of your discovery. You have agreed that we may file that motion on or before Wednesday of this week and the deposition will not go forward pending the disposition of the motion. Thank you for the courtesy.

Brad

P. Bradley O'Neill

Partner

Kramer Levin Naftalis & Frankel LLP 1177 Avenue of the Americas, New York, New York 10036 T 212.715.7583 M 646.808.7953 F 212.715.8382 boneill@kramerlevin.com

Bio

This communication (including any attachments) is intended solely for the recipient(s) named above and may contain information that is confidential, privileged or legally protected. Any unauthorized use or dissemination of this communication is strictly prohibited. If you have received this communication in error, please immediately notify the sender by return e-mail message and delete all copies of the original communication. Thank you for your cooperation.

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Exhibit F

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

Debtors.	Re: Dkt. No
WOODBRIDGE GROUP OF COMPANIES, LLC, et al., ⁵	(Jointly Administered)
In re:	Case No. 17-12560 (KJC)
In ro	Chapter 11

ORDER GRANTING DEBTORS' CROSS-MOTION FOR CONTINUANCE OF HEARING ON MOTION OF CONTRARIAN FUNDS, LLC FOR AUTHORITY TO ACQUIRE PROMISSORY NOTES AGAINST THE DEBTORS

Upon consideration of the Debtors' cross-motion for the continuance of the hearing on the *Motion of Contrarian Funds, LLC for Authority to Acquire Promissory Notes Against the Debtors* (the "Cross-Motion")⁶ filed by the above-captioned debtors and debtors in possession (collectively, the "Debtors") in these chapter 11 cases (the "Chapter 11 Cases"); and upon consideration of the record of these Chapter 11 Cases; and it appearing that the Court has jurisdiction to consider the Cross-Motion pursuant to 28 U.S.C. §§ 1334 and 157, and the *Amended Standing Order of Reference* from the United States District Court for the District of Delaware dated February 29, 2012; and it appearing that the Cross-Motion is a core matter pursuant to 28 U.S.C. § 157(b)(2) and that the Court may enter a final order consistent with Article III of the United States Constitution; and it appearing that venue of these Chapter 11 Cases and of the Cross-Motion is proper pursuant to 28 U.S.C. §§ 1408 and 1409; and it

The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of such information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

⁶ Capitalized terms used but not defined herein have the meaning assigned to such terms in the Cross-Motion.

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appearing that due and adequate notice of the Cross-Motion has been given under the circumstances, and that no other or further notice need be given; and it appearing that the relief requested in the Cross-Motion is in the best interests of the Debtors' estates, their creditors, and other parties in interest; and after due deliberation, and good and sufficient cause appearing therefor, it is hereby

IT IS HEREBY ORDERED THAT:

- 1. The Cross-Motion is GRANTED as set forth herein.
- 2. The hearing on the Note Motion is continued to June 5, 2018, or, to the extent that the hearing on June 5, 2018, is rescheduled, the next regularly scheduled omnibus hearing in these Chapter 11 Cases.
- 3. The terms and conditions of this Order shall be immediately effective and enforceable upon its entry.
- 4. This Court shall retain jurisdiction and power with respect to all matters arising from or related to the interpretation and implementation of this Order.

Dated:		_, 2018
	Wilmington, Delaware	_

KEVIN J. CAREY UNITED STATES BANKRUPTCY JUDGE

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IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:

WOODBRIDGE GROUP OF COMPANIES, LLC, et al..1

Debtors.

Chapter 11

Case No. 17-12560 (KJC)

(Jointly Administered)

Requested Objection Deadline: April 26,

2018 at 4:00 p.m. (ET)

Requested Hearing Date: May 1, 2018 at

11:00 a.m. (ET)

MOTION TO QUASH OF CONTRARIAN FUNDS, LLC

Contrarian Funds, LLC ("Contrarian"), by and through its undersigned counsel, submits this motion to quash the *Notice of Rule 30(b)(6) Deposition of Contrarian Funds, LLC* (the "Deposition Notice") [Dkt. No. 954] (attached as Exhibit A) filed by the above-captioned debtors and debtors in possession (the "Debtors"), and respectfully states as follows:

Introduction

1. As the Court is aware, certain creditors (the "Noteholders") in this case hold claims under promissory notes issued by the Debtors (the "Notes"). In March 2018, the Debtors filed a notice purporting to establish a 90-day moratorium on the transfer of Notes and to reserve the right to invalidate earlier or later transfers. On April 3, 2018, Contrarian, which had earlier acquired Notes, filed a motion seeking to allow the Noteholders to transfer their Notes free of the limitations the Debtors sought to impose (the "Note Motion") [Dkt. No. 890]. In response, the Debtors served Contrarian with the Deposition Notice seeking to examine a Contrarian witness

The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of this information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

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concerning the terms of Contrarian's Note purchases and, in particular, the prices at which the transactions closed.

- 2. These topics require testimony concerning sensitive, confidential commercial information that any investor would be reluctant to divulge. Not only is this information highly sensitive and confidential, it is not relevant to the Note Motion. Implementing a broad policy in favor of the free transfer of claims, Bankruptcy Rule 3001(e) severely limits standing to challenge the transfer of claims. To remove the Court from the burden of adjudicating claims transfers, only the transferor and not the Debtor may object to the transfer of a claim. As if that were not enough, state law does not authorize the moratorium the Debtors have sought to impose.
- 3. At bottom, the Deposition Notice attempts to achieve indirectly what Bankruptcy Rule 3001(e) bars the Debtors from doing directly preventing the transfer of claims. No discovery from Contrarian is necessary to adjudicate the propriety of that effort. Indeed, the Debtors' attempt to compel discovery of sensitive and confidential commercial information through the Deposition Notice appears to be another attempt to prevent claims trading by imposing additional indirect costs on claims buyers.
- 4. Not only are these efforts inconsistent with the Bankruptcy Rules, but the Debtors should not be attempting to police transactions between non-debtors in the market. If creditors wish to monetize their claims rather than bearing the risk that there may not ultimately be a distribution in these cases, that is their choice, not the Debtors'. It should not matter to the Debtors who holds claims against them, and the Debtors should not be in the business of trying to prevent individual creditors from disposing of their claims as they see fit.

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5. Discovery should not be used as a lever to restrict legitimate market activity that can benefit these investors. The Court should quash the Deposition Notice.

JURISDICTION AND VENUE

6. The Court has subject matter jurisdiction to consider and determine this matter pursuant to 28 U.S.C. §§ 1334(b) and 157 and the *Amended Standing Order of Reference* from the United States District Court for the District of Delaware dated as of February 29, 2012. This Motion is a core proceeding within the meaning of 28 U.S.C. §157(b). Venue is proper under 28 U.S.C. §§ 1408 and 1409.

BACKGROUND

On December 4, 2017 (the "Petition Date"), Woodbridge Group of Companies,
 LLC and certain affiliates filed voluntary petitions for relief under chapter 11 of Title 11 of the
 United States Code (the "Bankruptcy Code").

Case Background

- 8. The primary business of the Debtors was purported to be real estate finance and development. To support this "business," the Debtors conducted retail fundraising operations through WMF Management, LLC, which directly owns seven fund entities (the "Funds"). The Funds raised money from thousands of retail investors ("Noteholders") by issuing short-term notes ("Notes"). The Notes were purportedly secured by a pledge of certain promissory notes and related loan and security agreements, deeds of trust, or mortgages ("Collateral Documents") owned by the Funds. Upon information and belief, the Debtors stopped making payments on the Notes and, by the Petition Date, there were approximately \$750 million Notes outstanding, held by approximately 9,000 Noteholders.
- 9. In September of 2016, the United States Securities and Exchange Commission (the "SEC") began investigating the Debtors. In late December 2017, the SEC filed a sealed

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complaint against the Debtors' principal, Robert H. Shapiro, and several of the Debtors alleging that Mr. Shapiro had used the Debtors and their affiliates to conduct a massive Ponzi scheme.

On December 14, 2017, the United States Trustee appointed a three-member Official Committee of Unsecured Creditors (the "Committee") [Dkt. No. 79]. Two weeks later, the Committee filed an emergency motion seeking to appoint a chapter 11 trustee (the "Trustee Motion") [Dkt. No. 150]. In the Trustee Motion, the Committee alleged that the Debtors' CRO and independent manager were controlled by Mr. Shapiro. The SEC also filed its own motion to appoint a chapter 11 trustee, and various other parties further supported these motions. By order entered January 23, 2018, the Court approved a settlement reached between certain of the Debtors (the "Settlement Order") [Dkt. No. 357], the Committee, the SEC and other parties in interest, which, among other things, reconstituted the Debtors' board and authorized the formation of an ad hoc Noteholder group (the "Noteholder Group") and an ad hoc unitholder group (the "Unitholder Group").

The Moratorium Notice and Contrarian's Response

transferring it without the consent of the Debtors. On March 21, 2018, the Debtors filed a *Notice Regarding Transfers of Units or Notes* (the "Moratorium Notice") [Dkt. No. 799]. In the notice, the Debtors declared a unilateral moratorium on granting their consent to any further transfers of Notes for ninety (90) days and reserved all rights with respect to the invalidity and ineffectiveness of any prior, current, or future attempts to transfer Notes (the "Moratorium"). The Notice stated that the purpose of the Moratorium was to (i) allow "significant progress . . . toward a plan that can be effectuated by year-end with a significant recovery for noteholders and unitholders, (ii) the necessity to avoid distractions and focus on exiting the chapter 11 process, and (iii) the desire to protect noteholders and unitholders." Moratorium Notice at 2.

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- 12. The Notice also stated that the Debtors had discussed the Moratorium with the Committee, the Noteholder Group, and the Unitholder Group, and that all groups had unanimously requested that the Debtors impose the Moratorium. Despite this representation, the Noteholder Group has posted a statement to its website stating that they did not request or consent to the Moratorium.²
- 13. Contrarian is a distressed debt investor established in 1995. Among other things, Contrarian buys claims against companies in bankruptcy providing valuable liquidity to the claims market and options for creditors who do not wish to bear the cost or risk of bankruptcy proceedings. As part of its business, Contrarian has acquired certain Notes. It has also filed one proof of claim against the Debtors. *See* Claim No. 1216.
- 14. Two weeks after the Moratorium Notice, Contrarian filed the Note Motion seeking an order authorizing the Noteholders to freely assign their Notes without further order of the Court or consent of the Debtors. In the Note Motion, Contrarian noted that there was no basis for the unilateral imposition of the Moratorium, that the Debtors were attempting to enforce a contract they had breached, and that it was not in the best interests of the Noteholders to be prevented from assigning their Notes. Note Motion at 6-7.
- 15. In response to the Note Motion, on April 10, 2018, the Debtors filed the Deposition Notice seeking a deposition of Contrarian on April 18, 2018. The Deposition Notice calls for the production of a witness to testify concerning the following topics:
 - (1) The factual allegations contained in the Motion, including, without limitation, the statement that "Contrarian has contracted to purchase Notes from several Noteholders."

See Exhibit B (Notice Regarding Moratorium on Selling/Transferring Notes/Proofs of Claim, http://www.omnimgt.com/sblite/templates/a/dcontent.aspx?clientid=CsgAAncz%2b6YSOuba%2frNA%2bYUOxDUkxoyi8zM3581F06fCuy2ZumFvi0Dlk4FX3Nt4QzVmOWX5nOw%3d&vid=663265 ("Despite statements in the Notice to the contrary, the Noteholder Group did not request nor consent to this moratorium.")).

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- (2) Any contracts, assignments, transfers, consents, receipts, bills of sale, remittances, and other Documents of any type constituting or concerning the acquisition of any Notes or claims against the Debtors, including all terms of such transactions (including price) and the consideration, if any, that Contrarian has paid in connection with such transactions.
- (3) Any offers or solicitations made by Contrarian for the acquisition of any Notes (as defined in the Motion) or claims against the Debtors, including the terms and conditions of any such offers or solicitations.
- (4) Any communications between Contrarian and any Noteholder or other creditor of the Debtors, including any negotiations that have taken place and any representations or predictions that have been made by Contrarian.

The Debtors have also served a document request seeking documents related to the above topics.³

ARGUMENT

16. Under Federal Rule of Civil Procedure 26(b), "[p]arties may obtain discovery regarding any nonprivileged matter that is relevant to any party's claim or defense and proportional to the needs of the case." Fed. R. Civ. P. 26(b)(1). "[T]he party seeking the discovery has the burden of clearly showing the relevancy of the information sought." *Fassett v. Sears Holdings Corp.*, 319 F.R.D. 143, 149 (M.D. Pa. 2017) (quoting *Caver v. City of Trenton*, 192 F.R.D. 154, 159 (D.N.J. 2000)). In determining the scope of discoverable information, courts first look to the pleadings. *Fassett*, 319 F.R.D. at 149. Courts must also determine whether the requests are "overly broad and unduly burdensome." *Id.* (citing *Miller v. Hygrade Food Prods. Corp.*, 89 F. Supp. 2d 643, 657 (E.D. Pa. 2000)).

17. In 2015, Rule 26(b) was amended to include the proportionality requirement as a way to improve the discovery process, which had "become too expensive, time consuming, and contentious." *United States ex rel. Customs Fraud Investigations, LLC. v. Victaulic Co.*, 839

³ Contrarian will serve a response and objections to this Document Request in accordance with the Bankruptcy Rules.

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F.3d 242, 258-59 (3d Cir. 2016). The proportionality requirement in Rule 26(b)(1) requires the consideration of "the importance of the issues at stake in the action, the amount in controversy, the parties' relative access to relevant information, the parties' resources, the importance of the discovery in resolving the issues, and whether the burden or expense of the proposed discovery outweighs its likely benefit." Fed. R. Civ. P. 26(b)(1).

- 18. Courts in the Third Circuit have found that "when the burden of a discovery request is likely to outweigh the benefits, Federal Rule of Civil Procedure 26(b)(2)(C) vests the District Court with the authority to limit a party's pursuit of otherwise discoverable information." *F.T.C. v. Dutchman Enterprises, LLC*, No. 2:09-cv-141 (FSH)(MAS), 2010 WL 3034521, at *2 (D.N.J. Aug. 2, 2010). Under Rule 26(b)(2)(C), a court must limit discovery if "the proposed discovery is outside the scope permitted by Rule 26(b)(1)." Fed. R. Civ. P. 26(b)(2)(C)(iii).
- 19. Rule 26(b)(1) allows parties to take discovery that is "relevant to any party's claim or defense." The matters for examination in the Deposition Notice focus exclusively on the details of Contrarian's purchase of Notes, the economic terms of those transactions, and all communications related to the purchase by Contrarian of any claim against the Debtor. None of these topics bear on the propriety of the Moratorium Notice or the Note Motion.⁴ The details of any transaction between Contrarian and a Noteholder are irrelevant to the issues at hand.
- 20. "Bankruptcy Rule 3001(e) governs the assignment of claims" *In re Lynn*, 285 B.R. 858, 861 (Bankr. S.D.N.Y. 2002). It "is designed to permit free assignability with minimal judicial intervention." *Preston Trucking Co. v. Liquidity Solutions, Inc. (In re Preston Trucking Co.)*, 333 B.R. 315, 332 (Bankr. D. Md. 2005), *aff'd*, 392 B.R. 623 (D. Md. 2008). Historically, the bankruptcy courts policed claims trading. But the 1991 amendment to

The Debtors have not filed any opposition to the Note Motion. As a result, there is not yet a contested matter and no basis for the conduct of discovery under Rule 9014.

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Bankruptcy Rule 3001(e) "was expressly intended to curtail judicial oversight of the claim assignment process by . . . limiting the court's role to determining disputes between assignee and assignor, the only party entitled to notice of the transfer." *Lynn*, 285 B.R. at 861. Bankruptcy Rule 3001(e) "narrows the Court's role in determining the validity of the assignment of claims to ruling upon the filing of a timely objection." *Preston Trucking*, 333 B.R. at 336.

- 21. Under the plain language of Rule 3001(e)(2) "third parties, including the Debtor, do not have standing to object to a claim assignment itself." *Lynn*, 285 B.R. at 862. Rather, only the transferor may file an objection to the assignment of a claim. Fed. R. Bankr. P. 3001(e)(2). If no objection is filed by the transferor, the rule provides that "the transferee **shall** be substituted for the transferor." *Id.* (emphasis added).
- In light of this, the economic terms of a claim transfer are irrelevant to whether the transferee may assert the claim against the estate. In *Viking Associates, L.L.C. v. Drewes (In re Olson)*, a party had acquired a significant number of claims against the estate. 120 F.3d 98, 100 (8th Cir. 1997). The bankruptcy court ordered the Clerk not to transfer the claims because it found that the party "had abused the bankruptcy process by purchasing all of the claims against the estate at a fraction of what they were worth" and also misled claim sellers about the transactions. *Id.* The Eighth Circuit reversed. Under Bankruptcy Rule 3001(e), it held, unless there was an objection by the transferor, there was no "dispute." *Id.* at 102. Because no transferor had objected, "there [was] no longer any role for the court." *Id.*
- 23. Furthermore, not only do the Debtors lack standing to object to claims transfers, but they cannot persuasively argue that assignment of the Notes was invalid under non-bankruptcy law. In the Moratorium Notice, the Debtors state that their "organizational documents" and the documents governing Notes would require the Debtors' consent for any

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transfer or assignment. However, under applicable non-bankruptcy law, such a provision in a promissory note is ineffective to prevent its assignment. Article 9 of the Uniform Commercial Code ("UCC") applies to "a transaction, regardless of its form, that creates a security interest in personal property or fixtures by contract." Del. Code Ann. tit. 6, § 9-109(a)(1). Section 1-201 of the UCC defines "security interest" to include "any interest of . . . a buyer of . . . a promissory note in a transaction that is subject to Article 9." *Id.* § 1-201(35).

- 24. Section 9-408 of the UCC renders ineffective a contractual provision that requires the consent of the maker of a promissory note before the note may be transferred. In particular, it provides that "a term in a promissory note [... that] prohibits, restricts, or requires the consent of the person obligated on the promissory note or the account debtor to, the assignment or transfer of, or creation, attachment, or perfection of a security interest in, the promissory note ... is ineffective to the extent that the term ... would impair the creation, attachment, or perfection of a security interest "Id. § 9-408(a).
- 25. Here, the Debtors seek to enforce a provision in the Notes that purports to require their consent to any transfer of the Note. Because Contrarian's interest, as a buyer of a Note is a security interest under the UCC, and the provision in the Notes would prevent the creation of that security interest absent the consent of the Debtors, it is ineffective under applicable non-bankruptcy law.
- 26. Even if this were not the case, the Debtors cannot be heard to enforce a non-assignment provision under Notes that they have materially breached through non-payment. Under Delaware law, "[a] party is excused from performance under a contract if the other party is in material breach thereof." *BioLife Sols., Inc. v. Endocare, Inc.*, 838 A.2d 268, 278 (Del. Ch. 2003), *as revised* (Oct. 6, 2003). For example, in *Hipcricket, Inc. v. mGage, LLC*, a debtor

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attempted to enforce a restrictive covenant in a contract. No. CV 11135-CB, 2016 WL 3910837, at *1 (Del. Ch. July 15, 2016). The debtor, however, had rejected the contract as part of confirmation, resulting in a breach as of the petition date. *Id.* at *11. Noting that "a party in material breach of a contract may not demand performance from the non-breaching party[,]" the court held that "it would be inequitable here to allow [the breaching party] to enforce a contract that it materially breached." *Id.* at *12-13.

- 27. Here, by failing to pay principal and interest when due, as well as proposing to strip the security interests in the underlying collateral, the Debtors have materially breached the terms of the Notes. Having breached their obligations, the Debtors cannot enforce other terms of the Notes to the detriment of the non-breaching Noteholders.
- 28. Because the Debtors lack standing under the Bankruptcy Rules to object to the transfer of claims, and the non-assignment provision in the Notes cannot be enforced under non-bankruptcy law, discovery of the terms of Contrarian's purchases of Notes is simply not relevant. The Debtor's Moratorium Notice is ineffective as a matter of law, and the sensitive, confidential details of Contrarian's transactions or communications are beside the point. Indeed, the Debtors' attempts to extract such information merely seek to use the discovery process to erect further barriers to claims trading that Bankruptcy Rule 3001(e) was intended to eliminate.
- 29. While the Debtors may claim, as they did in the Moratorium Notice, that they hope to protect Noteholders, it is not for the Debtors to second guess the judgment of those Noteholders who seek to monetize their claims without actually consulting them. The best people to decide what is in the Noteholders' best interests are the Noteholders themselves.

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Although the contract in *Hipcricket* was governed by Washington law, the court noted that "Delaware law follows the same rule." *Hipcricket* 2016 WL 3910837, at *12, n.146.

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30. Rather than paternalistically deciding that they know what is best for the thousands of individuals allegedly defrauded by the Debtors, the Debtors should allow the Noteholders to decide for themselves whether they want to bear the risk of a plan process (and an initial cash distribution estimated to be in the single digits as a percentage of the face amount of the Notes) that, at best, will not be resolved until the end of the year. The Debtors should not be allowed to lock-in creditors who decide not to bear this risk.

LOCAL RULE 7026-1(d) CERTIFICATION

Contrarian hereby certifies that it has made a reasonable effort to reach agreement with the Debtors concerning the issues in this motion, but no agreement was reached.

CONCLUSION

For the foregoing reasons, Contrarian respectfully requests that the Court enter an order quashing the Deposition Notice and granting Contrarian such other and further relief as may be just and proper.

[Remainder of this page intentionally left blank.]

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Dated: April 18, 2018

Wilmington, Delaware

BIELLI & KLAUDER, LLC

/s/ David M. Klauder

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Counsel to Contrarian Funds, LLC

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EXHIBIT A

Cases 4.7-7-225660KKCC DDoo 4.5858-1 Fiffeite 0.40/4/0/8/8.8 Pageg 4.26134

IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re:

WOODBRIDGE GROUP OF COMPANIES, LLC, et al., 1

Debtors.

Chapter 11

Case No. 17-12560 (KJC)

(Jointly Administered)

NOTICE OF RULE 30(b)(6) DEPOSITION OF CONTRARIAN FUNDS, LLC

TO ALL PARTIES AND THEIR ATTORNEYS OF RECORD:

PLEASE TAKE NOTICE that, pursuant to Rule 30(b)(6) of the Federal Rules of Civil Procedure ("FRCP"), made applicable herein by Rules 7030 and 9014 of the Federal Rules of Bankruptcy Procedure, the debtors and debtors in possession (the "Debtors") in the above-captioned chapter 11 bankruptcy case will take a deposition of Contrarian Funds, LLC ("Contrarian") on Wednesday, April 18, 2018, commencing at 10 o'clock a.m., at the law offices of Young Conaway Stargatt & Taylor, LLP, Rockefeller Center, 1270 Avenue of the Americas, Suite 2210, New York, New York 10020, or at such other time or place as the Court may specify or the parties may mutually agree.

PLEASE TAKE FURTHER NOTICE that the deposition will be taken before an officer authorized to administer oaths, all testimony will be recorded by stenographic means, LiveNote may be used, and the deposition may also be recorded by audiovisual means.

01:23088142.1

The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of this information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

COSTS 4.71-71-252506 K-KOC DDoo'd 5553-1 Fille 10 40/4/01/8/8.8 Pagag 2 36 fo 3 4

PLEASE TAKE FURTHER NOTICE that "the matters for examination," FRCP 30(b)(6), concern the matters relevant to the *Motion of Contrarian Funds*, *LLC for Authority to Acquire*Promissory Notes Against the Debtors [Docket No. 890] (the "Motion"), filed by Contrarian on April 3, 2018, specifically including:

- (1) The factual allegations contained in the Motion, including, without limitation, the statement that "Contrarian has contracted to purchase Notes from several Noteholders."
- (2) Any contracts, assignments, transfers, consents, receipts, bills of sale, remittances, and other Documents of any type constituting or concerning the acquisition of any Notes or claims against the Debtors, including all terms of such transactions (including price) and the consideration, if any, that Contrarian has paid in connection with such transactions.
- (3) Any offers or solicitations made by Contrarian for the acquisition of any Notes (as defined in the Motion) or claims against the Debtors, including the terms and conditions of any such offers or solicitations.
- (4) Any communications between Contrarian and any Noteholder or other creditor of the Debtors, including any negotiations that have taken place and any representations or predictions that have been made by Contrarian.

PLEASE TAKE FURTHER NOTICE that, pursuant to FRCP 30(b)(6), Contrarian must "designate one or more officers, directors, or managing agents, or . . . other persons who consent to testify" on behalf of Contrarian regarding "information known or reasonably available to" Contrarian with respect to the preceding matters.

01:23088142.1

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Dated: April 10, 2018

/s/ Sean M. Beach

Wilmington, Delaware

YOUNG CONAWAY STARGATT & TAYLOR, LLP

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-and-

KLEE, TUCHIN, BOGDANOFF & STERN LLP

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Counsel to the Debtors and Debtors in Possession

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EXHIBIT B

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Woodbridge Group of Companies, LLC, et al.

Ad Hoc Noteholder Group Website



Letter to Woodbridge Noteholders

Critical Case Documents

Proof of Claim Form & Instructions

A Note Regarding Letters to the Bankruptcy Court

FAQ

Notice Regarding "Fraud Loss" Tax Deduction

Notice Regarding Moratorium on Selling/Transferring Notes/Proofs of Claim

Notice Regarding Deadline to File Proofs of Claim

Submit an Inquiry





Chapter 11 Case No. 17-12560 U.S. Bankruptcy Court - District of Delaware Hon, Kevin J. Carev

Notice Regarding Moratorium on Selling/Transferring Notes/Proofs of Claim

You may have been or possibly will be contacted by someone asking if you are interested in selling/transferring your Note or the proof of claim you filed for amounts due under the Note. Certain provisions in your loan documents prohibit transfer of a loan document or in the case of a Note, require the Borrower's consent prior to a transfer. On March 21, 2018, the Debtors filed a Notice Regarding Transfers of Units or Notes stating that for the next 90 days they will not consent to any transfers of Notes (this would include a transfer by a Noteholder of its proof of claim) or Units. Despite statements in the Notice to the contrary, the Noteholder Group did not request nor consent to this moratorium and it expects that opportunities to transfer your Note or proof of claim will arise in due course. In addition, the Noteholder Group is in discussions with the Debtors, the Unsecured Creditors Committee and the Unitholder Group for there to be an opportunity for Noteholders to borrow a certain amount against a portion of their expected recoveries in the bankruptcy cases on their Note on a non-recourse basis. The terms and timing of any such loans are not known at this time but we will provide an update when these and other details are available.

Page Top

All Calendar Events

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Making Brands Work Th

Case 17-12560-KJC Doc 1585-3 Filed 04/18/18 Page 1 of 2

IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

inistered)
12560 (KJC)

ORDER GRANTING MOTION TO QUASH OF CONTRARIAN FUNDS, LLC

Upon the motion (the "**Motion**") of Contrarian Funds, LLC ("**Contrarian**") to quash the *Notice of Rule 30(b)(6) Deposition of Contrarian Funds, LLC* (the "**Deposition Notice**") [Dkt. No. 954] filed by the above-captioned debtors and debtors in possession (the "**Debtors**"); and a hearing on the Motion having been held on ______, 2018; and the Court having found that (i) it has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334, (ii) this proceeding is a core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A) and (B), (iii) venue of this proceeding is proper pursuant to 28 U.S.C. §§ 1408 and 1409, and (iv) notice of the Motion was provided to all necessary and appropriate parties; and the Court having determined that the bases set forth in the Motion establish sufficient grounds for the relief granted herein; and due deliberation having been had; and sufficient cause appearing therefor, it is hereby ORDERED that

- 1. The Motion is granted as set forth herein.
- 2. The Debtors' Deposition Notice is hereby quashed.

The last four digits of Woodbridge Group of Companies, LLC's federal tax identification number are 3603. The mailing address for Woodbridge Group of Companies, LLC is 14140 Ventura Boulevard #302, Sherman Oaks, California 91423. Due to the large number of debtors in these cases, which are being jointly administered for procedural purposes only, a complete list of the Debtors, the last four digits of their federal tax identification numbers, and their addresses are not provided herein. A complete list of this information may be obtained on the website of the Debtors' noticing and claims agent at www.gardencitygroup.com/cases/WGC, or by contacting the undersigned counsel for the Debtors.

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3. The Court retains jurisdiction with respect to all matters arising from or related to the interpretation, implementation, and enforcement of this order.

Dated: May ___, 2018 Wilmington, Delaware

KEVIN J. CAREY UNITED STATES BANKRUPTCY JUDGE

https://www.law.com/newyorklawjournal/2018/03/14/litigation-funding-in-bankruptcy-court-anessential-tool-for-maximizing-the-value-of-the-debtors-estate/

Litigation Funding in Bankruptcy Court: An Essential Tool for Maximizing the Value of the Debtor's Estate

Third-party litigation funding promises to become a more regular feature in bankruptcy litigation, just as it has become more prevalent in general civil litigation. To this point, the Bankruptcy Code has proven flexible enough to address this phenomenon.

By Kenneth Epstein and Eric B. Fisher | March 14, 2018 at 02:35 PM

Perhaps now more than ever unsecured creditors face an uphill battle to obtain a meaningful recovery in most corporate bankruptcy cases. The debtor's assets are typically "liened up" well in advance of a bankruptcy filing, leaving little value unencumbered for anyone other than senior lenders. The trend in many commercial bankruptcy cases is towards a quick auction of the debtor's assets, [1] meaning that, after secured lenders are paid from the asset-sale proceeds, the likelihood of unsecured creditors receiving meaningful value under a plan of reorganization or liquidation may be remote.

When there is no available cash to pay them under a plan, unsecured creditors may be assigned the rights of a debtor to bring avoidance actions and other litigation claims against third parties. These litigation assets possess real value only when there are resources available to prosecute the claims aggressively to yield meaningful settlements or judgments for the benefit of unsecured creditors. Without these resources, a debtor may be unable to bring a claim or may be forced to settle a claim for less than full value. It can be a challenge to finance bankruptcy estate litigation when the debtor's remaining resources, after payment of senior creditors, are needed for the bankruptcy estate's wind-down and claims-administration expenses.

Litigation funding is a tool for unlocking the value of a bankruptcy estate's litigation claims when the estate itself lacks the resources to pursue the claims and traditional sources of financing are not available. It can be used by any party pursuing a claim for the benefit of the estate: the debtor, creditors' committee or trustee—and at any stage in the case, both before and after confirmation of a plan of reorganization or liquidation. This article offers an overview of commercial litigation funding in the bankruptcy context.

Overview of Commercial Litigation Funding

As most litigators now know, litigation funding is an investment in the outcome of a litigation made by a third party. Through a litigation funding transaction, a party to a litigation secures capital from a funder based on the anticipated future value of the litigation. When litigation counsel is hired on a contingent fee basis, litigation funding can be used to pay for disbursements, like expert witness and e-discovery costs; and when litigation counsel's fee arrangement is not a pure contingent fee, then litigation funding may be used for counsel's fees as well. Simply put, litigation funding may afford the bankruptcy estate

representative greater flexibility in hiring the lawyers and advisors of their choice.

Litigation funding can be used in the bankruptcy context to fund any type of action that creates an opportunity for significant recoveries for the estate. In addition to the more typical preference and fraudulent transfer claims, litigation funding may also be used to support the prosecution of breach of fiduciary duty claims, malpractice claims, tax claims, commercial tort litigation, insurance claims and any other claim that could yield value for the estate.

If a case financed by a litigation funder is resolved successfully through settlement, award or judgment, the funder is repaid its initial investment and an agreed-upon return. Should the outcome be unfavorable for the litigant, the litigation funder is owed nothing. In the United States, litigation funders do not take control of the cases that they fund. For example, a litigation funder will not control its client's choice of counsel, mandate settlement or direct case strategy. While a litigation funder may have an opinion on each of these matters, ultimately it is left up to the client to decide.

Litigation funding can help level the playing field when an estate representative is up against well-heeled defendants seeking to use their greater resources to drive a settlement unfavorable to the estate. In this circumstance, with money in its coffers, the estate representative can litigate and negotiate from a position of strength.

If the litigation asset is valuable enough, it may be possible for an estate representative to obtain and use funding in ways unrelated to a particular case. For example, excess funds from a litigation funder can be used to pay the administrative costs of the trust, to investigate additional potential sources of recovery to creditors, to pay financial advisors and other professionals who

are unwilling or unable to share risk in the case, or to find assets and enforce judgments against judgment debtors.

It may also be possible to guarantee a minimum recovery to the estate from a particular litigation asset. For example, in *In re Complete Retreats*, No. 06-50245, 2011 WL 1424579 (Bankr. D. Conn. 2011), the liquidating trustee entered into an option agreement with its litigation funder whereby, subject to court approval, the litigation funder paid the trustee an option premium for the right to fund the trustee's fraudulent conveyance action. The option premium ensured a minimum recovery to the estate and also secured funding to prosecute the litigation. The defendants to the fraudulent conveyance action filed an objection to the trustee's motion for approval of the agreement on the grounds the funding agreement was champertous and against public policy. In overruling the defendants' objection, and approving the funding agreement, the court held that securing a minimum recovery to the estate was clearly in the estate's best interest, and that the agreement was not champertous or against public policy. Id. at *3.

Established, reputable litigation funders have broad experience and expertise in evaluating the merits of a litigation claim. Because funders conduct rigorous due diligence in evaluating a claim as a possible investment, they may be more objective in evaluating its value to the estate. In a trust scenario, this independent analysis can help justify the pursuit of claims, and help trustees, receivers and other estate representatives make more informed decisions about the claims they are considering.

The Bankruptcy Context Provides Rigorous Oversight of Funding Arrangements

A recent survey conducted by Law360 found that, while lawyers in general have mixed feelings about litigation financing, lawyers who have actual experience using this type of financing view it favorably. [2] Those reporting negative views gave no specific reasons, but an oft-cited concern is that funders may have motivations that are not fully disclosed and that may incline them towards resolutions that are not necessarily in the best interest of the litigant. While this concern is based on misconceptions about litigation funding, it is particularly the case that the concern is alleviated in the bankruptcy context.

During the pendency of a Chapter 11 case, there is a high degree of transparency required of the debtor, and the debtor's actions are overseen by multiple parties, including the bankruptcy court, the U.S. Trustee's office, creditors (secured and unsecured) and other stakeholders. Non-ordinary course agreements, like litigation funding agreements, entered into by the debtor post-petition, must be disclosed and are subject to approval by the bankruptcy court. The approval process typically involves an opportunity for parties in interest to object to the funding agreement and for the court to rule on that objection. [3] The likelihood that an estate or its professionals would enter into an imprudent agreement are lessened because of this oversight. The bankruptcy process protects not only the estate but also the funders. Funders take comfort in entering into an agreement that has been thoroughly vetted and approved by a court.

Most of the bankruptcy decisions involving litigation funding have arisen postpetition when a party in interest objected to a trustee's motion to approve a litigation funding agreement between the trust and a commercial funder. Though it may depend on the circumstances in the particular bankruptcy case, post-petition litigation funding will typically be reviewed by the bankruptcy

court under a broad standard of reasonableness. *In re Superior National Ins. GR*, 2014 WL 51128, at *3 (U.S. Bankr. Ct. C.D. Cal. Jan. 7, 2014) (business judgment standard applied to review post-confirmation third-party funding of litigation trust). For example, in *Davidson Kempner Capital Mgmt. LP v. Official Committee of Unsecured Creditors of Motors Liquidation Co. (In re Motors Liquidation Co.)*, 2017 WL 3491970, at *8 (S.D.N.Y. Aug. 14, 2017),[4] the district court approved litigation funding provided by U.S. Treasury and Export Development Canada over the objection of a hedge fund that claimed that the financing it had offered to the plaintiff was less expensive than the government funding. Applying a reasonableness standard under Rule 9019 of the Bankruptcy Code, the district court rejected this challenge and affirmed the bankruptcy court's approval of the litigation funding supplied to the estate by the government. See also *In re Tropicana Entertainment*, Case No. 08-10856 (KJC) (U.S. Bankr. Ct. D. Del. Jan. 20, 2017) (approving post-confirmation funding for the litigation trust).

Section 364(c) of the Bankruptcy Code, which concerns court approval of liens granted against the debtor's property, may apply if the funding is secured by estate property. Most third-party funders seek a security interest in the proceeds of the litigation they are funding. Accordingly, it also may be important to insist on a subordination or other inter-creditor agreement between the third-party funder and other secured creditors of the estate to ensure clarity and avoid possible disagreements down the road. Funders will typically require this to protect their investment.

As litigation funding becomes more prevalent, it may be supplied by third parties through structures that are different from a typical loan, if an alternative structure will help to meet the needs of the case. Other sections of the Bankruptcy Code will thus also likely come into play. For example, §363(b)(1)

may be applicable if the funding is essentially a sale of the estate's claim to a third party. As a recent illustration, Gerchen Keller, now part of Burford, purchased an interest in a fraudulent transfer judgment against defendants in the Renco bankruptcy, in a transaction that was approved as a §363 sale under the Bankruptcy Code. This sale structure helped the bankruptcy trustee to ensure a minimum recovery to the estate's creditors while also funding the trustee's continuing litigation of the case on appeal. In addition to the oversight and court approval process, the interests of the estate in litigation are also protected in bankruptcy court by the legal duties imposed on the debtor's estate and its representatives. Bankruptcy trustees and receivers have duties set forth under the bankruptcy code and are obliged to act in the estate's best interest. As a fiduciary, the estate representative must maintain control over the litigation and cannot cede control to the funder. Thus, while some litigation funding arrangements may give greater input and monitoring rights to the funder than other arrangements, in the bankruptcy context, acceptable arrangements will likely be strict about ensuring the estate's complete control over the litigation. See, e.g., In re Land Resource, LLC v. Meininger, 505 B.R. 571, 576 (M.D. Fla. 2014) (approving litigation funding agreement and noting that "Trustee would maintain ultimate control over the prosecution").

Conclusion

Third-party litigation funding promises to become a more regular feature in bankruptcy litigation, just as it has become more prevalent in general civil litigation. To this point, the Bankruptcy Code has proven flexible enough to address this phenomenon. Bankruptcy estate professionals, including lawyers, trustees and receivers, should remain alert to issues concerning

litigation funding, to ensure that they deploy this tool when it can best be used to maximize the value of the debtor's estate.

Endnotes:

- [1] For one of the earliest quantitative studies and discussions of this trend, see Lynn M. LoPucki & Joseph W. Doherty, "Bankruptcy Fire Sales," 106 Mich. L. Rev. 1 (2007).
- [2] Cristina Violante, "What Your Colleagues Think of Litigation Finance," Law 360 (Dec. 11, 2017).
- parties in interest in the Chapter 11 case, defendants also have standing to object to litigation funding. In those circumstances, courts will need to balance the need for transparency against the right of the estate representative to not have to disclose potentially sensitive information to defendants in active litigation. For example, in *In re Superior National Ins. GR*, 2014 WL 51128, at *4 (U.S. Bankr. Ct. C.D. Cal. Jan. 7, 2014), the bankruptcy court required that the estate representative review and approve all requests for litigation funding, but allowed the filing of portions of motions to approve funding under seal, so as to facilitate court review, while not providing the information to the defendants to the fraudulent transfer action.
- [4] Binder & Schwartz serves as counsel to the Motors Liquidation Company Avoidance Action Trust in the underlying litigation of *Motors Liquidation Company Avoidance Action Trust v. JPMorgan Chase Bank, N.A., et al.*, Case No. 09-00504 (MG) (Bankr. S.D.N.Y.).

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736 F.3d 247 United States Court of Appeals, Third Circuit.

In re KB TOYS INC., et al., Debtors.

ASM Capital, L.P.; and ASM Capital II, LLP, Appellants.

No. 13–1197. | Argued Sept. 24, 2013. | Filed: Nov. 15, 2013.

Synopsis

Background: Chapter 11 trustee objected to proofs of claim filed by purchaser of debtors' trade claims on ground that original selling creditors from whom claimant purchased its claims were in possession of avoidable preferences that they had yet to turn over or pay back. The Bankruptcy Court, Kevin J. Carey, J., 470 B.R. 331, disallowed the claims. Purchaser appealed. The United States District Court for the District of Delaware, Richard G. Andrews, J., affirmed. Purchaser appealed.

Holdings: The Court of Appeals, Shwartz, Circuit Judge, held that:

- [1] a trade claim that is subject to disallowance in the hands of the original claimant as a voidable preferential payment or transfer from the debtor's estate is similarly disallowable in the hands of a subsequent transferee and
- [2] purchaser was not entitled to protections of good faith purchaser provision.

Affirmed.

West Headnotes (7)

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[1] Bankruptcy - Conclusions of law;de novo review
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Bankruptcy Discretion

Bankruptcy 🤛 Clear error

- 51 Bankruptcy
- 51XIX Review
- 51XIX(B) Review of Bankruptcy Court
- 51k3782 Conclusions of law; de novo review
- 51 Bankruptcy
- 51XIX Review
- 51XIX(B) Review of Bankruptcy Court
- 51k3784 Discretion
- 51 Bankruptcy
- 51XIX Review

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In re KB Toys Inc., 736 F.3d 247 (2013)
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        51XIX(B) Review of Bankruptcy Court
        51k3785 Findings of Fact
        51k3786 Clear error
```

The Court of Appeals exercises plenary review of a decision of a district court sitting as an appellate court in a bankruptcy proceeding, where the Court of Appeals reviews the bankruptcy court's findings of fact under the clearly erroneous standard, its conclusions of law under a de novo standard, and its exercises of discretion for abuses thereof.

Cases that cite this headnote

[2] **Bankruptcy** Fransfer or assignment

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51 Bankruptcy
51VII Claims
51VII(D) Proof; Filing
51k2904 Transfer or assignment
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A trade claim that is subject to disallowance in the hands of the original claimant as a voidable preferential payment or transfer from the debtor's estate is similarly disallowable in the hands of a subsequent transferee. 11 U.S.C.A. § 502(d).

3 Cases that cite this headnote

Bankruptcy Construction and Operation

Statutes Policy behind or supporting statute

Statutes • Statute as a Whole; Relation of Parts to Whole and to One Another

```
Statutes Plain, literal, or clear meaning; ambiguity
51 Bankruptcy
51I In General
51I(B) Constitutional and Statutory Provisions
51k2021 Construction and Operation
51k2021.1 In general
361 Statutes
361III Construction
361III(A) In General
361k1074 Purpose
361k1077 Policy behind or supporting statute
361 Statutes
361III Construction
361k1151 In general
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361III(E) Statute as a Whole; Relation of Parts to Whole and to One Another

361 Statutes

361III Construction

361III(H) Legislative History

361k1242 Plain, literal, or clear meaning; ambiguity

Courts must be mindful, particularly when examining the Bankruptcy Code, that statutory interpretation is "a holistic endeavor"; consequently, courts must not be guided by a single sentence or member of a sentence, but look to the provisions of the whole law, and to its object and policy, and, if the statutory text is ambiguous, look to the legislative history.

Cases that cite this headnote

In re KB Toys Inc., 736 F.3d 247 (2013)

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[4] Bankruptcy 🕪 Effect of avoidable transfer and surrender thereof

- 51 Bankruptcy
- 51VII Claims
- 51VII(A) In General
- 51k2822 Creditors Entitled to Assert Claims
- 51k2824 Effect of avoidable transfer and surrender thereof

Claims that are disallowable as voidable preferential payments or transfers from the debtor's estate must be disallowed no matter who holds them. 11 U.S.C.A. § 502(d).

4 Cases that cite this headnote

[5] Bankruptcy 🗪 Transfer or assignment

- 51 Bankruptcy
- 51VII Claims
- 51VII(D) Proof; Filing
- 51k2904 Transfer or assignment

The claim purchaser bears the risk that avoidable transfers are not returned, since claim purchasers voluntarily choose to take part in the bankruptcy process and therefore are aware of, or should be aware of, the risks and uncertainties in the bankruptcy process, and claim purchasers are in a position to mitigate disallowance risk, whereas the other creditors are not.

1 Cases that cite this headnote

[6] Bankruptcy • Construction and Operation

- 51 Bankruptcy
- 51I In General
- 51I(B) Constitutional and Statutory Provisions
- 51k2021 Construction and Operation
- 51k2021.1 In general

Courts are reluctant to accept arguments that would interpret the Bankruptcy Code, however vague the particular language under consideration might be, to effect a major change in pre-Code practice that is not the subject of at least some discussion in the legislative history.

Cases that cite this headnote

[7] Bankruptcy 🌦 Avoidance rights and limits thereon, in general

Bankruptcy - Transfer or assignment

- 51 Bankruptcy
- 51V The Estate
- 51V(H) Avoidance Rights
- 51V(H)1 In General
- 51k2701 Avoidance rights and limits thereon, in general
- 51 Bankruptcy
- 51VII Claims
- 51VII(D) Proof; Filing
- 51k2904 Transfer or assignment

Purchaser of debtors' trade claims was not entitled to protections of good faith purchaser provision, since purchaser did not purchase property of estate and purchaser should have known that it was taking on risks and uncertainties attendant to bankruptcy process. 11 U.S.C.A. §§ 502(d), 550(b).

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1 Cases that cite this headnote

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Before: CHAGARES, VANASKIE, and SHWARTZ, Circuit Judges.

Opinion

OPINION OF THE COURT

SHWARTZ, Circuit Judge.

I.

This appeal arises out of the Chapter 11 liquidation of KB Toys Inc. and affiliated entities (the "Debtors"). Pursuant to 11 U.S.C. § 502(d), the Residual Trustee of the KBTI Trust ¹ sought to disallow certain trade claims that ASM Capital, L.P., and ASM Capital II, LLP, (together, "ASM") obtained from some of the creditors. Under § 502(d), a bankruptcy claim can be disallowed if a claimant receives property that is avoidable or recoverable by the bankruptcy estate. *See* 11 U.S.C. § 502(d). The issue here is whether a trade claim that is subject to disallowance under § 502(d) in the hands of the original claimant is similarly disallowable in the hands of a subsequent transferee. For the reasons set forth herein, the answer is yes and thus, we will affirm.

The Debtors' plan of reorganization established the KBTI Trust. The KBTI Trust is authorized to liquidate and collect assets for the benefit of creditors.

II.

A.

Creditors holding claims against an entity who has filed a Chapter 11 petition sometimes face a risky and lengthy bankruptcy process. To avoid this risk and expense, a creditor may look to sell its claim, a practice permitted under the bankruptcy rules. *In re Kreisler*, 546 F.3d 863, 864 (7th Cir.2008) (citing Fed. R. Bankr.P. 3001(e)). By selling its claim, a risk averse creditor can opt out of the bankruptcy process and obtain an immediate, albeit discounted, payment on the debt it is owed. *See id.* Claim purchasers buy these claims and hope to receive a distribution from the debtor's estate in excess of the price paid. *See* Tally M. Wiener & Nicholas B. Malito, *On the Nature of the Transferred Bankruptcy Claim*, 12 U. Pa. J. Bus. L. 35, 36 (2009) ("Some purchasers are simply ... investing with an eye towards receiving a distribution on claims in cash or readily liquidated property in excess of the purchase price."). ²

Other claims purchasers attempt to make a profit in more sophisticated ways. For example, in reorganizations, some purchasers seek to purchase claims from a particular class of claims with a view toward receiving equity interests in the

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reorganized debtor. See Michelle M. Harner, Trends in Distressed Debt Investing: An Empirical Study of Investors' Objectives, 16 Am. Bankr.Inst. L.Rev. 69, 82 (2008) (reporting that many claims purchasers invest in bankruptcy cases to pursue an exchange of debt for equity). This was not ASM's goal.

A trade claim is usually transferred via contract. If a claim is transferred before a proof of claim is filed, Federal Rule of Bankruptcy Procedure 3001(e)(1) allows a transferred to file the proof of claim. See Fed. R. Bankr.P. 3001(e)(1). If a claim is transferred after a proof of claim is filed, Rule 3001(e)(2) requires a claims transferre to file an "evidence of transfer" with the bankruptcy court. See Fed. R. Bankr.P. 3001(e)(2).

B. ³

ASM does not challenge any of the factual findings made by either the Bankruptcy Court or the District Court. ASM Br. at 13 ("[O]nly the legal conclusions—and not any factual findings—of the courts below are challenged.").

The Debtors filed voluntary petitions for relief under Chapter 11 of the Bankruptcy *250 Code on January 14, 2004 (the "Petition Date") to liquidate all of their assets. On March 15, 2004, as required by 11 U.S.C. § 521(a)(1)(B)(iii), each Debtor filed a Statement of Financial Affairs ("SOFA"). Each SOFA required the disclosure of all payments made within the 90 days immediately preceding the Petition Date. Payments made during this 90–day time period are potentially vulnerable to attack as avoidable preferences. See 11 U.S.C. § 547(b)(4)(A).

Between April 7, 2004 and May 22, 2007, ASM, which participates in the sale and purchase of bankruptcy claims nationwide, purchased the nine claims at issue in this appeal (the "Claims") via Assignment Agreements. The Claims were originally held by various trade claimants (the "Original Claimants") to whom the Debtors owed money. The Assignment Agreements underlying the transfers of four of the Claims contained a generic indemnification clause. Five did not. Each Assignment Agreement contained specific restitution provisions that dealt with risks particular to bankruptcy. These provisions shift the risk of disallowance back to the Original Claimant by requiring the Original Claimant to pay restitution to ASM if the Claim is disallowed. ⁴

The restitution provisions took one of two forms. In one set of agreements, the restitution provisions provided: "[i]n the event ... the Claim ... is avoided, disallowed, expunged, reduced or is otherwise subordinated ... in whole or in part, [the Original Claimant] ... agrees to make immediate Restitution." App. 132, 135, 270, 273. In the other set of agreements, the restitution provisions provided: "[the Original Claimant] agrees to make to [ASM] immediate proportional restitution or repayment of the above Purchase Price to the extent the Claim is ... avoided, disallowed, expunged, reduced or subordinated for any reason whatsoever in whole or in part...." App. 117, 120, 123, 126, 129.

Each Original Claimant was listed on a SOFA as receiving a payment within 90 days of the Petition Date. The Trustee brought preference actions ⁵ against the Original Claimants, eventually obtaining a judgment in each case. The judgments against the Original Claimants were uncollectable because the Original Claimants all went out of business. ASM purchased eight of the Claims before the Trustee commenced the preference actions and purchased one after the Trustee obtained a judgment.

To succeed in a preference action, a trustee must show that a transfer: (1) was to or for the benefit of a creditor; (2) was for or on account of an antecedent debt owed by the debtor before such transfer was made; (3) was made while the debtor was insolvent; (4) was on or within 90 days before the filing of the bankruptcy petition; and (5) enabled the creditor to receive more than it would have in a Chapter 7 liquidation. 11 U.S.C. § 547(b). Preference actions, among other things, "facilitate the prime bankruptcy policy of equality of distribution among creditors of the debtor. Any creditor that received a greater payment than others of its class may be required to disgorge the payment so that all may share equally." 5 *Collier on Bankruptcy* ¶ 547.01 (16th ed.2010).

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On July 31, 2009, the Trustee filed an objection with the Bankruptcy Court seeking the disallowance of the Claims pursuant to § 502(d). The Trustee did not allege that ASM itself received an avoidable transfer. Instead, the Trustee contended that the Claims are disallowable under § 502(d) because each Original Claimant received a preference before transferring its Claim to ASM.

After considering the language of § 502(d) and its legislative history, the Bankruptcy Court disallowed the Claims, concluding that a claims purchaser holding *251 a trade claim is subject to the same § 502(d) challenge as the original claimant. Put differently, the Bankruptcy Court held that, under § 502(d), "[d]isabilities attach to and travel with the claim." App. 76. The Bankruptcy Court also observed that ASM is a sophisticated entity, well aware of the bankruptcy process, who had access to both the SOFA and the Original Claimants, and thus, was on "constructive notice" of the potential preference actions and could have discovered the potential for disallowance under § 502(d) with "very little due diligence." App. 88. Accordingly, the Bankruptcy Court held that ASM was not entitled to protection as a "good faith" purchaser.

[1] ASM appealed the decision to the District Court, which affirmed the Bankruptcy Court. The District Court noted that it believed the plain language of § 502(d) was ambiguous but it otherwise adopted the reasoning of the Bankruptcy Court. ASM appealed. ⁶

We exercise plenary review of a decision of a district court sitting as an appellate court in a bankruptcy proceeding. *In re Mintze*, 434 F.3d 222, 227 (3d Cir.2006). We review the Bankruptcy Court's findings of fact under the clearly erroneous standard, its conclusions of law under a de novo standard, and its exercises of discretion for abuses thereof. *Id.* at 227–28. The Bankruptcy Court had jurisdiction pursuant to 28 U.S.C. §§ 157 and 1334. The District Court had appellate jurisdiction under 28 U.S.C. §§ 158(a)(1) and 1334. We have appellate jurisdiction pursuant to 28 U.S.C. §§ 158(d) and 1291.

III.

A.

Section 502(d) of the Bankruptcy Code provides: Notwithstanding subsections (a) and (b) of this section, the court shall disallow *any claim of any entity* from which property is recoverable under section 542, 543, 550, or 553 of this title or that is a transferee of a transfer avoidable under section 522(f), 522(h), 544, 545, 547, 548, 549, or 724(a) of this title, unless such entity or transferee has paid the amount, or turned over any such property, for which such entity or transferee is liable under section 522(i), 542, 543, 550, or 553 of this title.

11 U.S.C. § 502(d) (emphasis added). The issue in this case, which only concerns trade claims, turns on the interpretation of the phrase "any claim of any entity."

[2] [3] The Court's analysis begins with the text of the statute. If the text is clear and unambiguous, this Court must simply apply it. *Roth v. Norfalco L.L.C.*, 651 F.3d 367, 379 (3d Cir.2011) ("When the meaning of statutory text is plain, our inquiry is at an end."). Yet courts must be mindful, particularly when examining the Bankruptcy Code, that statutory interpretation is "a holistic endeavor." *Official Comm. of Unsecured Creditors of Cybergenics Corp. ex rel. Cybergenics Corp. v. Chinery*, 330 F.3d 548, 559 (3d Cir.2003) (en banc) (quotation and citation omitted). Consequently, courts "must not be guided by a single sentence or member of a sentence, but look to the provisions of the whole law, and to its object and policy." *Id.* (quotation and citation omitted). If the statutory text is ambiguous, a court may look to the legislative history. *Blum v. Stenson*, 465 U.S. 886, 896, 104 S.Ct. 1541, 79 L.Ed.2d 891 (1984).

[4] The language of § 502(d) states that "any claim of any entity" who received an avoidable transfer ⁷ shall be disallowed. *252 Thus, the statute operates to render a category of claims disallowable—those that belonged to an entity who had received an avoidable transfer. Further, the statute provides that such claims cannot be allowed until the entity who received the avoidable transfer, or the transferee, returns it to the estate. 11 U.S.C. § 502(d) (stating that

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the trustee shall disallow such claims "unless such entity or transferee has paid the amount, or turned over any such property, for which such entity or transferee is liable ..."). Accordingly, "any claim" falling into this category of claims is disallowable until the avoidable transfer is returned. Because the statute focuses on claims—and not claimants—claims that are disallowable under § 502(d) must be disallowed no matter who holds them.

A transfer of property can be avoided under one of the various avoidance sections. For example, a trustee or a debtor in possession may avoid preferential transfers under 11 U.S.C. § 547 and fraudulent transfers under 11 U.S.C. § 548.

To hold otherwise would contravene the aims of § 502(d), the first of which is to ensure equality of distribution of estate assets. *Enron Corp. v. Springfield Assocs., L.L.C. (In re Enron Corp.) (Enron II)*, 379 B.R. 425, 434 (S.D.N.Y.2007); see also Cybergenics, 330 F.3d at 559 (noting that courts must look to a law's "object and policy" when interpreting the law). If a transferred claim was protected from disallowance, an original claimant who received an avoidable transfer would have an incentive to sell its claim and "wash" the claim of any disability. After all, if the original claimant did not transfer its claim, the claim would be disallowed pursuant to § 502(d). If the original claimant could transfer the claim for value to a transferee, the original claimant would receive value for a claim that would otherwise be disallowed and the transferee, who would receive the claim "washed" of its disability, could then share in the distribution of estate assets. In short, the original claimant would have an incentive to sell its claim—so it could receive some value for an otherwise valueless claim—and the transferee would have an incentive to buy the claim—because once the claim is in its hands, the claim is eligible to receive a distribution.

Allowing such a result would negatively impact the other creditors in two ways. First, because the original claimant has not returned the avoidable transfer, the estate has less money and the other creditors would receive smaller amounts from the estate because it would not include the unreturned preference payment or conveyance. Second, the estate would pay on a claim that would have been otherwise disallowed.

[5] This result would also undermine the second of § 502(d)'s aims, coercing compliance with judicial orders. *Enron II*, 379 B.R. at 434. Section 502(d) can be used to compel an original claimant to comply with a judgment and return the preferential payment as a condition of collecting on its claim. Failure to satisfy this condition provides a basis for the trustee to ask the bankruptcy court to disallow the claim. After the claim is sold, the original claimant no longer has a claim that the trustee can leverage to obtain the disgorgement of the preference payment. To allow the sale to wash the claim entirely of the cloud would deprive the trustee of one of the tools the Bankruptcy Code gives trustees to collect assets—asking the bankruptcy court to disallow problematic claims. Accordingly, interpreting § 502(d) to permit this type of "claim washing" would undermine the twin aims of § 502(d). 8 For all of these reasons, the *253 statute's language is properly interpreted to mean that the potential disallowance runs with the claim.

- At oral argument before our Court and the District Court, an important policy consideration was raised, which further supports this interpretation: who should bear the risk that avoidable transfers are not returned? The answer must be the claim purchaser for two reasons. First, claim purchasers voluntarily choose to take part in the bankruptcy process. Claim purchasers, who are typically sophisticated entities, "are aware of, or should be aware of, the risks and uncertainties" in the bankruptcy process. Enron Corp. v. Avenue Special Situations Fund II, LP (In re Enron Corp.) (Enron I), 340 B.R. 180, 202 (Bankr.S.D.N.Y.2006), vacated and remanded by Enron II, 379 B.R. 425, 434 (S.D.N.Y.2007). Because they choose to voluntarily take part in this risky process, it is only fair to require them to bear the risk that the original claimant will not return an avoidable transfer. Second, claim purchasers are in a position to mitigate disallowance risk, whereas the other creditors are not. A claim purchaser can perform due diligence on the original claimant and estimate the risk of disallowance. The claim purchaser can then account for this risk when determining the price to pay for a claim. Additionally, a claim purchaser may shift the risk of disallowance back to the original claimant through an indemnity clause in the transfer agreement.
- [6] Moreover, the legislative history supports this conclusion. The legislative history provides that § 502(d) is "derived from present law," which, as the Bankruptcy Court noted, was section 57(g) of the Bankruptcy Act of 1898. H.R. Rep. 95–595, at 354 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6310. Section 57(g) provided:

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Even if the legislative history were not so clear, we would still consider section 57(g) because courts are "reluctant to accept arguments that would interpret the [Bankruptcy] Code, however vague the particular language under consideration might be, to effect a major change in pre-Code practice that is not the subject of at least some discussion in the legislative history."

*Dewsnup v. Timm, 502 U.S. 410, 419, 112 S.Ct. 773, 116 L.Ed.2d 903 (1992). Indeed, other courts have recognized that section 57(g) is relevant to the interpretation of § 502(d). See In re LaRoche Indus., Inc., 284 B.R. 406, 409 (Bankr.D.Del.2002)

(examining a case interpreting section 57(g) when faced with an issue arising under § 502(d)); In re America's Shopping Channel, Inc., 110 B.R. 5, 7–8 (Bankr.S.D.Cal.1990) (same); In re Mid Atl. Fund, Inc., 60 B.R. 604, 610 (Bankr.S.D.N.Y.1986) (same).

The claims of creditors who have received or acquired preferences, liens, conveyances, transfers, assignments or encumbrances, void or voidable under this title, shall not be allowed unless such creditors shall surrender such preferences, liens, conveyances, transfers, assignments, or encumbrances.

Katchen v. Landy, 382 U.S. 323, 86 S.Ct. 467, 473 n. 5, 15 L.Ed.2d 391 (1966) (quoting section 57(g)). In Swarts v. Siegel, 117 F. 13 (8th Cir.1902), the Court of Appeals for the Eighth Circuit interpreted section 57(g) as it applied to a claimant who purchased promissory notes from a bank that received a preference. 117 F. at 14. The Swarts court held that the "[t]he disqualification of a claim for allowance created by a preference inheres in and follows every part of the claim, whether retained by the original creditor or transferred to another, until the preference is surrendered."

Id. at 15. Thus, the case law interpreting section 57(g) is consistent with our interpretation of § 502(d).

In an attempt to distinguish *Swarts*, ASM cites to *In re Wood & Locker*, *Inc.*, 1988 U.S. Dist. LEXIS 19501 (W.D. Tex. June 17, 1988). The *Wood & Locker* court held that *Swarts* was only applicable to cases where the original claimant or a transferee received "provable and traceable direct benefits by the payment of the preferences." *Id.* at *8. ASM contends that since it did not receive a provable and traceable direct benefit from the preference payment, it should not be saddled with paying the preference. Appellant Br. at 22. Neither ASM nor the *Wood & Locker* court, however, explain why § 502(d) requires proof of a traceable direct benefit to the entity who possesses the claim. Instead, they both make this assertion without analysis of the statutory text. Once the text is analyzed, it is clear that the plain language of § 502(d) does not require proof of a benefit from the avoidable transfer. Thus, ASM's lack of a benefit from the preferences is irrelevant to the question before the Court.

*254 Finally, because ASM included provisions in the Assignment Agreements that directly deal with risks particular to bankruptcy, it is evident that ASM was aware that disallowance could potentially attach to, and travel with, the Claims. Thus, ASM's conduct when negotiating and entering into the Assignment Agreements is consistent with our interpretation of § 502(d).

In short, because § 502(d) permits the disallowance of a claim that was originally owned by a person or entity who received a voidable preference that remains unreturned, the cloud on the claim continues until the preference payment is returned, regardless of whether the person or entity holding the claim received the preference payment. 11

In addition to the Bankruptcy Court in this case, two other bankruptcy courts have reached the same conclusion: *Enron I*, 340 B.R. at 199 (holding that a claim in the hands of a transferee "should be disallowed to the same extent that such claim would be subject to disallowance in the hands of the transferor"), and *In re Metiom, Inc.*, 301 B.R. 634, 642–43 (Bankr.S.D.N.Y.2003) (holding that because § 502(d) "disallows *the claim* ... [t]he claim and the defense to the claim under [§] 502(d) cannot be altered by the claimant's subsequent assignment of the claim to another entity ... that has not received an avoidable transfer.").

Two district courts have reached opposite conclusions. In *Enron II*, the District Court viewed the language of § 502(d) as focusing "on the claimant as opposed to the claim" and this led it to "conclu[de] that disallowance is a personal disability of a claimant, not an attribute of the claim." 379 B.R. at 443. It then proceeded to rely on state law to determine the impact of this "personal disability" and concluded that whether a claim suffered a disability depended upon how it was conveyed to the transferee. Specifically, the District Court held that disallowance under § 502(d) is a personal disability of particular claimants and not an attribute of a claim, unless the transferee took the claim by assignment, as opposed to by sale. *Enron II*, 379 B.R. at 439–45. The District Court stated that an assignee "stands in the shoes of the assignor" and therefore takes

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the claim with "whatever limitations it had in the hands of the assignor," *id.* at 435–36 (citations and internal quotations omitted), but a purchaser of the same claim is not subject to any personal disabilities of the transferor. *Id.* at 436. *Enron II*'s reliance on this supposed state law distinction may also be problematic for several reasons. First, the state law on which it relies does not provide a distinction between assignments and sales. Second, resort to state law in a bankruptcy case must be done with care. *See Int'l Shoe Co. v. Pinkus*, 278 U.S. 261, 265, 49 S.Ct. 108, 73 L.Ed. 318 (1929) ("The power of Congress to establish uniform laws on the subject of bankruptcies throughout the United States is unrestricted and paramount."); *In re Boston Reg'l Med. Ctr., Inc.*, 291 F.3d 111, 126 (1st Cir.2002) (observing that if a state law dictated a result inconsistent with federal bankruptcy law, then it would be "preempted").

B.

[7] ASM also argues that the claims should not be disallowed because it purchased its claims in "good faith" and is therefore entitled to the protections of a good faith purchaser under 11 U.S.C. § 550(b). Section 550(b) provides:

The trustee may not recover under section (a)(2) of this section from—

- (1) a transferee that takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the voidability of the transfer avoided; or
- (2) any immediate or mediate good faith transferee of such transferee.

11 U.S.C. § 550(b). An application of the plain language of the statute to the facts of this case shows that ASM is not entitled to a defense under § 550(b).

*255 First, § 550(b) is not applicable to ASM. Section 550(b) protects a good faith transferee who purchases property of the estate that is avoidable under the various avoidance sections. 11 U.S.C. § 550(a), (b); see Wasserman v. Bressman, 327 F.3d 229, 235 (3d Cir.2003). ASM did not purchase property of the estate. ASM purchased claims against the Debtors' estates. A claim against an estate is not property of that estate. Enron I, 340 B.R. at 206 ("[A] claim as defined under [§] 101(5), is not, and has never been, considered property of the estate (it is being asserted against) under [§] 541 of the Bankruptcy Code."). Thus, on its face, § 550(b) is inapplicable to ASM.

Second, there is no reason or precedent to extend the "principles" of § 550(b) to protect ASM. Claim purchasers are entities who knowingly and voluntarily enter the bankruptcy process. Thus, a purchaser should know that it is taking on the risks and uncertainties attendant to the bankruptcy process. Indeed, if the bankruptcy process were not risky and uncertain, claimants might be less likely to sell their claims to a claim purchaser. Put differently, a claim purchaser's opportunity to profit is partly created by the risks inherent in bankruptcy. Disallowance of a claim pursuant to § 502(d) is among these risks.

Relatedly, while ASM claims it lacked knowledge of the avoidability of the transfers, ASM could have protected itself from the risk of disallowance by reviewing the Debtors' publicly available SOFAs, which would have put it on notice of the Claims' vulnerability to preference attacks, and performing due diligence on the Original Claimants. At bottom, ASM voluntarily exposed itself to a risk that it had the ability to investigate before acquiring the claims. Conscious of this risk, it included indemnity and restitution provisions in the Assignment Agreements. ASM is in a better position than the estate to protect itself against the Original Claimants going out of business by factoring this possibility in to the price of the claim. Accordingly, in this case, extending § 550(b)'s "principles" beyond the plain statutory language is inappropriate.

IV.

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For all of these reasons, we will affirm.

All Citations

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End of Document

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KeyCite Yellow Flag - Negative Treatment
Distinguished by In re Rexford Properties, LLC, Bankr.C.D.Cal., September 7, 2016
814 F.3d 993
United States Court of Appeals,
Ninth Circuit.

In re THE VILLAGE AT LAKERIDGE, LLC, fka Magnolia Village, LLC, Debtor, U.S. Bank N.A., Trustee, et al., by and through CWCapital Asset Management LLC, solely in its capacity as Special Servicer, Appellant,

 $\mathbf{v}_{\boldsymbol{\cdot}}$

The Village at Lakeridge, LLC, Appellee,
Robert Alan Rabkin, Real Party in Interest.

In re the Village at Lakeridge, LLC, fka Magnolia Village, LLC, Debtor,
U.S. Bank N.A., Trustee, et al., by and through CWCapital Asset
Management LLC, solely in its capacity as Special Servicer, Appellant,

The Village at Lakeridge, LLC, Appellee,
Robert Alan Rabkin, Real Party in Interest.

Nos. 13–60038, 13–60039. | Argued and Submitted Oct. 22, 2015. | Filed Feb. 8, 2016.

Synopsis

Background: In a Chapter 11 bankruptcy proceeding, the trustee moved to designate creditor's claim and disallow creditor's vote to confirm reorganization plan. The United States Bankruptcy Court for the District of Nevada, Bruce T. Beesley, J., granted the motion in part, and denied the motion in part. Parties cross-appealed. The Bankruptcy Appellate Panel (BAP), Kirscher, Pappas, and Taylor, JJ., 2013 WL 1397447, affirmed in part, reversed in part, and vacated in part. Trustee appealed.

Holdings: The Court of Appeals, N.R. Smith, Circuit Judge, held that:

- [1] creditor did not become a statutory insider solely by acquiring a claim from a statutory insider, and
- [2] creditor did not qualify as non-statutory insider.

Affirmed.

Clifton, Circuit Judge, filed opinion, concurring in part and dissenting in part.

In re The Village at Lakeridge, LLC, 814 F.3d 993 (2016)

75 Collier Bankr.Cas.2d 125, 62 Bankr.Ct.Dec. 44, Bankr. L. Rep. P 82,921

West Headnotes (22)

[1] Bankruptcy 🕪 Finality

- 51 Bankruptcy
- 51XIX Review
- 51XIX(B) Review of Bankruptcy Court
- 51k3766 Decisions Reviewable
- 51k3767 Finality

A decision of the Bankruptcy Appellate Panel (BAP) is considered final and appealable where it (1) resolves and seriously affects substantive rights and (2) finally determines the discrete issue to which it is addressed. 28 U.S.C.A. § 158(d).

1 Cases that cite this headnote

[2] Bankruptcy 🧼 Finality

- 51 Bankruptcy
- 51XIX Review
- 51XIX(B) Review of Bankruptcy Court
- 51k3766 Decisions Reviewable
- 51k3767 Finality

When the Bankruptcy Appellate Panel (BAP) affirms or reverses a bankruptcy court's final order, the BAP's order is final and appealable. 28 U.S.C.A. § 158(d).

1 Cases that cite this headnote

[3] Bankruptcy 🕪 Court of Appeals

Bankruptcy 🤛 Finality

- 51 Bankruptcy
- 51XIX Review
- 51XIX(B) Review of Bankruptcy Court
- 51k3762 Jurisdiction
- 51k3765 Court of Appeals
- 51 Bankruptcy
- 51XIX Review
- 51XIX(B) Review of Bankruptcy Court
- 51k3766 Decisions Reviewable
- 51k3767 Finality

If the Bankruptcy Appellate Panel (BAP) remands to the bankruptcy court for factual determinations on a central issue, its order is not final and the Court of Appeals lacks jurisdiction to review the order. 28 U.S.C.A. § 158(d).

2 Cases that cite this headnote

[4] Bankruptcy Scope of review in general

Bankruptcy Review of Appellate Panel

- 51 Bankruptcy
- 51XIX Review

In re The Village at Lakeridge, LLC, 814 F.3d 993 (2016)

75 Collier Bankr.Cas.2d 125, 62 Bankr.Ct.Dec. 44, Bankr. L. Rep. P 82,921

- 51XIX(B) Review of Bankruptcy Court
- 51k3779 Scope of review in general
- 51 Bankruptcy
- 51XIX Review
- 51XIX(C) Review of Appellate Panel
- 51k3811 In general

The Court of Appeals reviews the bankruptcy court's decision independent of the decision of the Bankruptcy Appellate Panel (BAP).

Cases that cite this headnote

[5] Bankruptcy ጮ Conclusions of law; de novo review

- 51 Bankruptcy
- 51XIX Review
- 51XIX(B) Review of Bankruptcy Court
- 51k3782 Conclusions of law; de novo review

Whether an insider's status, as would disallow his vote to confirm Chapter 11 reorganization claim, transfers when he sells or assigns his claim to a third party presents a question of law subject to de novo review. 11 U.S.C.A. §§ 101(31), 1129(a)(10).

Cases that cite this headnote

[6] Bankruptcy - Conclusions of law; de novo review

- 51 Bankruptcy
- 51XIX Review
- 51XIX(B) Review of Bankruptcy Court
- 51k3782 Conclusions of law; de novo review

Establishing the definition of non-statutory insider status, for purpose of determining who may vote to confirm Chapter 11 reorganization plan, is a purely legal inquiry subject to de novo review. 11 U.S.C.A. § 1129(a)(10).

1 Cases that cite this headnote

[7] Bankruptcy Determination

- 51 Bankruptcy
- 51XIV Reorganization
- 51XIV(B) The Plan
- 51k3541 Acceptance
- 51k3547 Determination

Whether a specific person qualifies as a non-statutory insider, for purpose of determining whether or not that person may vote to confirm a Chapter 11 reorganization plan, is a question of fact. 11 U.S.C.A. § 1129(a)(10).

Cases that cite this headnote

[8] Bankruptcy 🖦 Clear error

- 51 Bankruptcy
- 51XIX Review
- 51XIX(B) Review of Bankruptcy Court
- 51k3785 Findings of Fact
- 51k3786 Clear error

In re The Village at Lakeridge, LLC, 814 F.3d 993 (2016)

75 Collier Bankr.Cas.2d 125, 62 Bankr.Ct.Dec. 44, Bankr. L. Rep. P 82,921

The Court of Appeals reviews factual findings in a bankruptcy case for clear error.

Cases that cite this headnote

[9] Bankruptcy • Insiders, acceptance by

- 51 Bankruptcy
- 51XIV Reorganization
- 51XIV(B) The Plan
- 51k3541 Acceptance
- 51k3546 Insiders, acceptance by

An "insider," who is disallowed from voting to confirm Chapter 11 reorganization plan, is one who has a sufficiently close relationship with the debtor that his conduct is made subject to closer scrutiny than those dealing at arms' length with the debtor. 11 U.S.C.A. § 101(31).

1 Cases that cite this headnote

[10] Bankruptcy 🕪 Construction and Operation

- 51 Bankruptcy
- 51I In General
- 51I(B) Constitutional and Statutory Provisions
- 51k2021 Construction and Operation
- 51k2021.1 In general

A "non-statutory insider" is a person who is not explicitly listed as an insider in the bankruptcy code, but who has a sufficiently close relationship with the debtor to fall within the definition. 11 U.S.C.A. § 101(31).

3 Cases that cite this headnote

[11] Bankruptcy 🕪 Insiders, acceptance by

- 51 Bankruptcy
- 51XIV Reorganization
- 51XIV(B) The Plan
- 51k3541 Acceptance
- 51k3546 Insiders, acceptance by

A creditor does not become a statutory insider, who will be disallowed from voting to confirm a Chapter 11 reorganization plan, solely by acquiring a claim from a statutory insider. 11 U.S.C.A. §§ 101(31), 1129(a)(10).

Cases that cite this headnote

[12] Bankruptcy Em Transfer or assignment

- 51 Bankruptcy
- 51VII Claims
- 51VII(D) Proof; Filing
- 51k2904 Transfer or assignment

Because insider status, for bankruptcy purposes, is not a property of a claim, general assignment law, in which an assignee takes a claim subject to any benefits and defects of the claim, does not apply in the context of a bankruptcy proceeding. 11 U.S.C.A. § 101(31).

1 Cases that cite this headnote

In re The Village at Lakeridge, LLC, 814 F.3d 993 (2016)

75 Collier Bankr.Cas.2d 125, 62 Bankr.Ct.Dec. 44, Bankr. L. Rep. P 82,921

[13] Bankruptcy 📂 Construction and Operation

Bankruptcy - Transfer or assignment

- 51 Bankruptcy
- 51I In General
- 51I(B) Constitutional and Statutory Provisions
- 51k2021 Construction and Operation
- 51k2021.1 In general
- 51 Bankruptcy
- 51VII Claims
- 51VII(D) Proof; Filing
- 51k2904 Transfer or assignment

The insider status of a person who acquires a claim from another, in a bankruptcy proceeding, is a question of fact that must be determined after the claim transfer occurs. 11 U.S.C.A. § 101(31).

1 Cases that cite this headnote

[14] Bankruptcy • Insiders, acceptance by

- 51 Bankruptcy
- 51XIV Reorganization
- 51XIV(B) The Plan
- 51k3541 Acceptance
- 51k3546 Insiders, acceptance by

Whether a creditor is an insider, as will disallow his vote to confirm Chapter 11 reorganization plan, is a factual inquiry that must be conducted on a case-by-case basis. 11 U.S.C.A. §§ 101(31), 1129(a)(10).

Cases that cite this headnote

[15] Bankruptcy • Insiders, acceptance by

- 51 Bankruptcy
- 51XIV Reorganization
- 51XIV(B) The Plan
- 51k3541 Acceptance
- 51k3546 Insiders, acceptance by

A court cannot assign non-statutory insider status, as will disallow creditor from voting to confirm Chapter 11 reorganization plan, to a creditor simply because it finds the creditor and debtor share a close relationship. 11 U.S.C.A. §§ 101(31), 1129(a)(10).

1 Cases that cite this headnote

[16] Bankruptcy 🕪 Insiders, acceptance by

- 51 Bankruptcy
- 51XIV Reorganization
- 51XIV(B) The Plan
- 51k3541 Acceptance
- 51k3546 Insiders, acceptance by

A creditor is not a "non-statutory insider," who is disallowed from voting to confirm Chapter 11 reorganization plan, unless (1) the closeness of its relationship with the debtor is comparable to that of the enumerated insider classifications listed in the Bankruptcy Code, and (2) the relevant transaction is negotiated at less than arm's length. 11 U.S.C.A. §§ 101(31), 1129(a)(10).

In re The Village at Lakeridge, LLC, 814 F.3d 993 (2016)

75 Collier Bankr.Cas.2d 125, 62 Bankr.Ct.Dec. 44, Bankr. L. Rep. P 82,921

2 Cases that cite this headnote

[17] Bankruptcy 🕪 Insiders, acceptance by

- 51 Bankruptcy
- 51XIV Reorganization
- 51XIV(B) The Plan
- 51k3541 Acceptance
- 51k3546 Insiders, acceptance by

Having, or being subject to, some degree of control is one of many indications that a creditor may be a non-statutory insider, who is disallowed from voting to confirm Chapter 11 reorganization plan, but actual control is not required to find non-statutory insider status. 11 U.S.C.A. §§ 101(31), 1129(a)(10).

1 Cases that cite this headnote

[18] Bankruptcy 🕪 Insiders, acceptance by

- 51 Bankruptcy
- 51XIV Reorganization
- 51XIV(B) The Plan
- 51k3541 Acceptance
- 51k3546 Insiders, acceptance by

A creditor's access to the debtor's inside information may, but not shall, warrant a finding of non-statutory insider status, for purpose of determining if creditor is disallowed from voting to confirm Chapter 11 reorganization plan. 11 U.S.C.A. §§ 101(31), 1129(a)(10).

1 Cases that cite this headnote

[19] Bankruptcy 🗪 Clear error

- 51 Bankruptcy
- 51XIX Review
- 51XIX(B) Review of Bankruptcy Court
- 51k3785 Findings of Fact
- 51k3786 Clear error

A bankruptcy court's factual finding is "clearly erroneous" when, although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed. Fed.Rules Civ.Proc.Rule 52(a)(6), 28 U.S.C.A.

Cases that cite this headnote

[20] Bankruptcy 🗪 Findings of Fact

- 51 Bankruptcy
- 51XIX Review
- 51XIX(B) Review of Bankruptcy Court
- 51k3785 Findings of Fact
- 51k3785.1 In general

So long as the bankruptcy court's findings of fact are plausible in light of the record viewed in its entirety, the Court of Appeals cannot reverse even if the Court of Appeals would have weighed the evidence differently. Fed.Rules Civ.Proc.Rule 52(a)(6), 28 U.S.C.A.; 28 U.S.C.A. § 158(d).

In re The Village at Lakeridge, LLC, 814 F.3d 993 (2016)

75 Collier Bankr.Cas.2d 125, 62 Bankr.Ct.Dec. 44, Bankr. L. Rep. P 82,921

Cases that cite this headnote

[21] Bankruptcy • Insiders, acceptance by

51 Bankruptcy

51XIV Reorganization

51XIV(B) The Plan

51k3541 Acceptance

51k3546 Insiders, acceptance by

Creditor who purchased unsecured debt from sole owner of limited liability corporation (LLC), the Chapter 11 debtor, did not qualify as "non-statutory insider," and thus, was not disqualified from voting to confirm debtor's reorganization plan; although creditor had close personal relationship with one managing board member of the sole owner of the LLC, and that board member approached the creditor with an offer to sell the owner's unsecured debt, creditor did not know and had no relationship with four other managing board members, creditor had no control over the one managing board member with whom he had a relationship, they had separate finances, lived separately, and conducted business separately, and although creditor understood that debtor LLC was in bankruptcy and the purchase amounted to a risky investment, it was a relatively small investment for him, and creditor did not know about the reorganization plan at the time or that his vote would be required to confirm it. 11 U.S.C.A. §§ 101(31), 1129(a)(10).

1 Cases that cite this headnote

[22] Bankruptcy 🕪 Findings of Fact

51 Bankruptcy

51XIX Review

51XIX(B) Review of Bankruptcy Court

51k3785 Findings of Fact

51k3785.1 In general

The Court of Appeals cannot substitute its judgment for that of the bankruptcy court simply because it is convinced that it would have decided the case differently.

Cases that cite this headnote

Attorneys and Law Firms

*996 Gregory A. Cross, Keith C. Owens (argued), Jennifer L. Nassiri (argued), Venable LLP, Los Angeles, CA, for Appellant.

Alan R. Smith (argued), Holly E. Estes, Law Offices of Alan R. Smith, Reno, NV, for Debtor/Appellee.

Appeal from the Ninth Circuit, Bankruptcy Appellate Panel, Kirscher, Pappas, and Taylor, Bankruptcy Judges, Presiding. BAP No. 12–1456.

Before: RICHARD R. CLIFTON and N. RANDY SMITH, Circuit Judges, and ROBERT S. LASNIK, * Senior District Judge.

* The Honorable Robert S. Lasnik, Senior District Judge for the U.S. District Court for the Western District of Washington, sitting by designation.

In re The Village at Lakeridge, LLC, 814 F.3d 993 (2016)

75 Collier Bankr.Cas.2d 125, 62 Bankr.Ct.Dec. 44, Bankr. L. Rep. P 82,921

Opinion

Opinion by Judge N.R. SMITH; Partial Concurrence and Partial Dissent by Judge CLIFTON.

OPINION

N.R. SMITH, Circuit Judge:

Before a bankruptcy court may confirm a reorganization plan in a Chapter 11 bankruptcy, it must determine if any of the persons voting to accept the plan are insiders. ¹ Insiders are either statutory or non-statutory. To be a "statutory insider," a creditor *must* fall within one of the categories listed in 11 U.S.C. § 101(31). A creditor does not become an insider simply by receiving a claim from a statutory insider. To be a non-statutory insider, the creditor must have a close relationship with the debtor and negotiate the relevant transaction at less than arm's length. Thus, Dr. Robert Rabkin does not qualify as a statutory or non-statutory insider. ²

- 1 II U.S.C. § 1129(a)(10) ("The court shall confirm a plan only if all of the following requirements are met: ... If a class of claims is impaired under the plan, at least one class of claims that is impaired under the plan has accepted the plan, determined without including any acceptance of the plan by any insider.").
- In this opinion, we address only Rabkin's statutory and non-statutory insider status. We resolve the remaining claims in a memorandum disposition filed concurrently with this opinion.

I. Factual Proceedings

A. The Parties

The debtor, Village at Lakeridge, LLC ("Lakeridge"), has only one member: *997 MBP Equity Partners 1, LLC ("MBP"). MBP is managed by a board of five members, one of whom is Kathie Bartlett. ³ Bartlett shares a close business and personal relationship with Rabkin, which is unrelated to Bartlett's position with MBP.

Although Bartlett signed Lakeridge's bankruptcy petition and all related documents on behalf of Lakeridge, she testified that she did not have authority to make decisions for MBP—or Lakeridge—on her own.

U.S. Bank National Association ("U.S. Bank") is successor trustee to Greenwich Financial Products, Inc., the company through which Lakeridge financed a property purchase. At the time Lakeridge filed for bankruptcy, U.S. Bank was one of two creditors holding a claim on Lakeridge's assets. U.S. Bank held a fully secured claim worth about \$10 million, and MBP held an unsecured claim worth \$2.76 million.

B. Bankruptcy Court Proceedings

Lakeridge filed for Chapter 11 relief on June 16, 2011. On September 14, Lakeridge filed a Disclosure Statement and an initial Plan of Reorganization. Shortly thereafter, MBP's board decided to sell MBP's unsecured claim. Bartlett, on behalf of MBP's board, approached Rabkin with an offer to sell the claim. On October 27, Rabkin purchased the claim for \$5,000. In its Disclosure Statement, Lakeridge classified Rabkin's claim as a "Class 3 general unsecured claim."

Bartlett testified that MBP's board decided to sell its claim for two reasons: (1) the claim was useless to MBP because it could not vote the claim in favor of its reorganization plan; and (2) the board believed there "may be a tax advantage in selling [the] claim."

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On June 7, 2012, U.S. Bank deposed Rabkin, questioning him about his relationship with Lakeridge, MBP, and Bartlett. In his testimony, Rabkin indicated he had little knowledge of, and no relationship with, Lakeridge or MBP before he acquired MBP's claim. However, Rabkin testified that he had a close relationship with Bartlett, that he saw her regularly, including the day of the deposition, and that he had attended a meeting with his counsel and Lakeridge's counsel one hour before the deposition. Rabkin testified that he purchased MBP's unsecured claim as a business investment, that he had not known how much his claim was worth before the deposition, and that he knew the claim was a risky investment. Rabkin further testified that, prior to the deposition, he had not known his distribution under the proposed reorganization plan was \$30,000. Rabkin claimed to have no interest in Lakeridge other than receiving a return on his investment.

U.S. Bank, through counsel, offered to purchase Rabkin's claim for \$50,000 at the deposition. Rabkin said he would consider the offer. U.S. Bank, in an attempt to compel an immediate answer, increased its offer to \$60,000. Rabkin again agreed to consider the offer, refusing to provide an answer on the spot. After Rabkin consulted with counsel, he did not respond to the offer. The offer lapsed. At a hearing on August 29, 2012, Rabkin stated he had felt pressured to accept U.S. Bank's cash offer while he was under oath, without having time to review it first. ⁵

The district court judge explained that he "underst[ood] the doctor or many people would have been put off by [U.S. Bank's approach to acquiring Rabkin's claim] and [he didn't] think it[was] at all surprising that [Rabkin] would reject it and not really be interested in dealing with the people who made the offer to him thereafter."

On July 1, 2012, U.S. Bank moved to designate Rabkin's claim and disallow it *998 for plan voting purposes ("Designation Motion"). U.S. Bank contended Rabkin was both a statutory and non-statutory insider, and that the assignment to Rabkin was made in bad faith. The bankruptcy court held an evidentiary hearing on the Designation Motion on August 1, 2012. In its subsequent order ("Designation Order"), the court held Rabkin was not a non-statutory insider, because:

(a) Dr. Rabkin does not exercise control over [Lakeridge;] (b) Dr. Rabkin does not cohabitate with Ms. Bartlett, and does not pay [her] bills or living expenses; (c) Dr. Rabkin has never purchased expensive gifts for Ms. Bartlett; (d) Ms. Bartlett does not exercise control over Dr. Rabkin[;] (e) Ms. Bartlett does not pay [Dr.] Rabkin's bills or living expenses; and (f) Ms. Bartlett has never purchased expensive gifts for Dr. Rabkin.

The court also held that Rabkin did not purchase MBP's claim in bad faith. However, the court designated Rabkin's claim and disallowed it for plan voting, because it determined Rabkin had become a statutory insider by acquiring a claim from MBP. In other words, the bankruptcy court determined that, when a statutory insider sells or assigns a claim to a non-insider, the non-insider becomes a statutory insider as a matter of law.

Lakeridge and Rabkin both timely appealed the Designation Order, challenging the court's finding that Rabkin was a statutory insider for purposes of plan voting. U.S. Bank cross-appealed, challenging the findings that Rabkin was not a non-statutory insider and had not purchased MBP's claim in bad faith.

C. Bankruptcy Appellate Panel

[1] [2] [3] The United States Bankruptcy Appellate Panel for the Ninth Circuit ("BAP") affirmed in part, reversed in part, and vacated in part the Designation Order. The BAP reversed the finding that Rabkin had become a statutory insider as a matter of law by acquiring MBP's claim and affirmed the findings that Rabkin was not a non-statutory insider and that the claim assignment was not made in bad faith. The BAP held that insider status cannot be assigned and must be determined for each individual "on a case-by-case basis, after the consideration of various factors." Finally, the BAP held Rabkin could vote to accept the Lakeridge plan under 11 U.S.C. § 1129(a)(10), because he was an impaired creditor who was not an insider. U.S. Bank appealed. We have jurisdiction under 28 U.S.C. § 158(d), and we affirm.

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75 Collier Bankr.Cas.2d 125, 62 Bankr.Ct.Dec. 44, Bankr. L. Rep. P 82,921

- 6 The question of bad faith is addressed in the memorandum disposition filed concurrently with this opinion and will not be addressed here.
- Under 28 U.S.C. § 158(d), we "have jurisdiction of appeals from all final decisions, judgments, orders, and decrees" of the BAP. A decision is considered "final and ... appealable where it 1) resolves and seriously affects substantive rights and 2) finally determines the discrete issue to which it is addressed." *Dye v. Brown (In re AFI Holding, Inc.)*, 530 F.3d 832, 836 (9th Cir.2008) (quoting *Schulman v. California (In re Lazar)*, 237 F.3d 967, 985 (9th Cir.2001)). When the BAP "affirms or reverses a bankruptcy court's final order," the BAP's order is also final. *Vylene Enters., Inc. v. Naugles, Inc. (In re Vylene Enters., Inc.)*, 968 F.2d 887, 895 (9th Cir.1992). However, if the BAP "remands for factual determinations on a central issue, its order is not final and we lack jurisdiction to review the order." *Id.*

The bankruptcy court issued two orders: (1) the Designation Order (finding that Rabkin was not a non-statutory insider and had not acted in bad faith, but nevertheless designating his claim and disallowing it for plan voting purposes because he had acquired the claim from a statutory insider) and (2) the Discovery Order (denying U.S. Bank's Discovery Motions). Both bankruptcy court orders "finally determine[d]" Rabkin's right to vote on Lakeridge's reorganization plan and were therefore final orders. See In re AFI Holding, Inc., 530 F.3d at 836.

However, the BAP's decision as issued was not final, because, although it affirmed and reversed portions of the bankruptcy court orders, it also remanded for discovery to allow factual determinations central to Rabkin's non-statutory insider status and ability to vote on Lakeridge's reorganization plan.

To make the BAP's decision final, U.S. Bank withdrew its arguments concerning the Discovery Order at oral argument, removing the need for remand. Because U.S. Bank withdrew its appeal concerning the Discovery Order, we will not discuss it in this opinion. Nor may U.S. Bank seek to enforce the BAP's holding on that issue at the bankruptcy court level.

*999 II. Standard of Review

- [4] [5] [6] We review the bankruptcy court's decision independent of the BAP's decision. See Boyajian v. New Falls Corp. (In re Boyajian), 564 F.3d 1088, 1090 (9th Cir.2009). Whether an insider's status transfers when he sells or assigns the claim to a third party presents a question of law. Miller Ave. Prof'l & Promotional Servs., Inc. v. Brady (In re Enter. Acquisition Partners), 319 B.R. 626, 630 (9th Cir. BAP 2004). Establishing the definition of non-statutory insider status is likewise a purely legal inquiry. We review questions of law de novo. Stahl v. Simon (In re Adamson Apparel), 785 F.3d 1285, 1289 (9th Cir.2015).
- [7] [8] Whether a specific person qualifies as a non-statutory insider is a question of fact. Friedman v. Sheila Plotsky Brokers, Inc. (In re Friedman), 126 B.R. 63, 70 (9th Cir. BAP 1991), overruled on other grounds by Zachary v. Cal. Bank & Tr., No. 13–16402, 811 F.3d 1191, 2016 WL 360519 (9th Cir. Jan. 28, 2016). We review factual findings for clear error. In re Adamson Apparel, 785 F.3d at 1289.

III. Discussion

- [9] "An insider is one who has a sufficiently close relationship with the debtor that his conduct is made subject to closer scrutiny than those dealing at arms [sic] length with the debtor." S.Rep. No. 95–989, at 25 (1978), as reprinted in 1978 U.S.C.C.A.N. 5787, 5810; H.R.Rep. No. 95–595, at 312 (1977), as reprinted in 1978 U.S.C.C.A.N. 5963, 6269. We recognize two types of insiders: statutory insiders and non-statutory insiders. Statutory insiders, also known as "per se insiders," are persons explicitly described in 11 U.S.C. § 101(31), such as "person[s] in control of the debtor." § 101(31). As a matter of law, a statutory insider has a sufficiently close relationship with a debtor to warrant special treatment. In re Enter. Acquisition Partners, 319 B.R. at 631. No one suggests Rabkin qualifies as a statutory insider in his own right.
- [10] A non-statutory insider is a person who is not explicitly listed in § 101(31), but who has a sufficiently close relationship with the debtor to fall within the definition. See Schubert v. Lucent Techs. Inc. (In re Winstar Commc'ns, Inc.), 554 F.3d 382, 395 (3d Cir.2009) ("[I]n light of Congress's use of the term 'includes' in § 101(31), courts have identified

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a category of creditors, sometimes called 'non-statutory insiders,' who fall within the definition but outside of any of the enumerated categories."); see also § 101(31) (stating that "[t]he term 'insider' includes" the listed categories (emphasis added)); § 102(3) (explaining that "includes" is "not limiting").

A. Statutory Insider Status

[11] [12] [13] U.S. Bank asserts that Rabkin became a statutory insider when he acquired a claim from MBP. We disagree. A person does not become a statutory insider solely by acquiring a claim from a statutory insider for two reasons. First, bankruptcy law distinguishes between the status of a claim and that of a claimant. *1000 Insider status pertains only to the claimant; it is not a property of a claim. Because insider status is not a property of a claim, general assignment law—in which an assignee takes a claim subject to any benefits and defects of the claim—does not apply. Second, a person's insider status is a question of fact that must be determined after the claim transfer occurs. See Concord Square Apartments of Wood Cty., Ltd. v. Ottawa Props., Inc. (In re Concord Square Apartments), 174 B.R. 71, 75 (Bankr.S.D.Ohio 1994). This determination does not ignore the public policy behind protecting secured creditors' interests in bankruptcy cases, as explained below.

The term "insider," as used in the bankruptcy code, is a noun, referring to a person (as defined at § 101(41)). See, e.g., § 101(31) (defining "insider" as a person with a particular relationship with the debtor); see also § 1129(a)(10) (explaining that a court can cram down a reorganization plan when at least one class of impaired claims has voted to accept the plan, not including "any acceptance of the plan by an insider"). The term "insider" is not, as U.S. Bank argues, an adjective used to describe the property of a claim. §

If U.S. Bank's argument were true, we would expect to find references to "the holder of an insider claim" rather than "an insider" in the bankruptcy code.

[14] Whether a creditor is an insider is a factual inquiry that must be conducted on a case-by-case basis. See, e.g., In re Friedman, 126 B.R. at 67, 70–71 (describing in detail the alleged insiders' relationships with the debtor); Miller v. Schuman (In re Schuman), 81 B.R. 583, 586–87 (9th Cir. BAP 1987) (per curiam) (analyzing facts to determine whether the debtor and alleged insider had a sufficiently close relationship to warrant finding insider status). Courts may not bypass this intensive factual analysis by finding that a third party became an insider as a matter of law when he acquired a claim from an insider. If so, a third-party assignee could be foreclosed from voting a claim acquired from an insider, even if the entire transaction was conducted at arm's length. The bankruptcy code did not intend this result.

Further, if a third party could become an insider as a matter of law by acquiring a claim from an insider, bankruptcy law would contain a procedural inconsistency wherein a claim would *retain* its insider status when assigned from an insider to a non-insider, but would *drop* its non-insider status when assigned from a non-insider to an insider. *See In re Applegate Prop.*, *Ltd.*, 133 B.R. 827, 833 (Bankr.W.D.Tex.1991) (holding that an insider of a Chapter 11 debtor may never vote a claim toward plan confirmation, even if the insider acquired the claim from a non-insider); *In re Holly Knoll P'ship*, 167 B.R. 381, 385 (Bankr.E.D.Pa.1994) (same).

Section 1129 of Title 11 contains a number of safeguards for secured creditors who could be negatively impacted by a debtor's reorganization plan. A court may confirm a plan only if, among other requirements: (1) the plan and plan proponent comply with the bankruptcy code; (2) the plan is proposed in good faith; (3) the plan proponent has disclosed the identity of all insiders and potential insiders; (4) at least one class of impaired claims has accepted the plan (and no insider can vote); and (5) the plan "is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan." § 1129. In addition, a court "may designate any entity whose acceptance or rejection of [a] plan was not in good faith, or was not solicited or procured in good faith." § 1126(e). Therefore, U.S. Bank overstates its argument that, unless we reverse the BAP, debtors will begin assigning their claims to third parties

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in return for votes in favor of plan confirmation. *1001 ⁹ We fail to see how establishing a rule that insider status transfers as a matter of law would better protect the creditors' rights than the current factual inquiry. ¹⁰

- For this assertion, U.S. Bank cites *In re Heights Ban Corp.*, 89 B.R. 795 (Bankr.S.D.Iowa 1988). There, the court concluded insider status must transfer with a claim upon assignment, otherwise "the operation of section 1129(a) would be seriously undermined. Debtors unable to obtain the acceptance of an impaired creditor simply could assign insider claims to third parties, who in turn could vote to accept." *Id.* at 799. Although the language in that case supports U.S. Bank's position, the facts do not. The assignor in *In re Heights Ban Corp.* transferred more than his claim; he and his co-shareholders also transferred their shareholder interests in the debtor to the assignee. *Id.* The court concluded that the assignors' and assignee's interests were "so interlocked ... [as to be] indistinguishable with respect to the debtor for purposes of section 1129(a)(10)." *Id.* Thus, the assignee became an insider by becoming a shareholder of the debtor, not simply by acquiring a claim from a statutory insider.
- U.S. Bank correctly points out that this court previously determined insider status does transfer with a claim under the general law of assignment. See Wake Forest, Inc. v. Transamerica Title Ins. (In re Greer West Inv. Ltd. Pship), No. 94–15670, 1996 WL 134293 (9th Cir. Mar. 25, 1996) (unpublished). However, Ninth Circuit Rule 36–3 prohibits parties from citing "[u]npublished dispositions ... of this Court issued before January 1, 2007 ... to the courts of this circuit." Thus, U.S. Bank should not have relied upon, or cited, In re Greer West in its arguments, and we are not bound by the decision.

In conducting a factual inquiry for insider status, courts should begin with the statute. If the assignee fits within a statutory insider classification on his own, the court's review ends; it need not examine the nature of the statutory insider's relationship to the debtor. See In re Enter. Acquisition Partners, 319 B.R. at 631. Because Rabkin did not become a statutory insider by way of assignment and was not a statutory insider in his own capacity, we must determine whether the bankruptcy court erred in finding that Rabkin was not a non-statutory insider.

B. Non-Statutory Insider Status

[15] [16] Non-statutory insiders are the functional equivalent of statutory insiders and, therefore, must fall within the ambit of § 101(31). See In re Winstar Commc'ns, Inc., 554 F.3d at 395. A creditor is not a non-statutory insider unless: (1) the closeness of its relationship with the debtor is comparable to that of the enumerated insider classifications in § 101(31), and (2) the relevant transaction is negotiated at less than arm's length. 11 See Anstine v. Carl Zeiss Meditec AG (In re U.S. Med., Inc.), 531 F.3d 1272, 1277 (10th Cir.2008). A court cannot assign non-statutory insider status to a creditor simply because it finds the creditor and debtor share a close relationship. See id. at 1277–78.

- An "arm's length transaction" is: "1. A transaction between two unrelated and unaffiliated parties. 2. A transaction between two parties, however closely related they may be, conducted as if the parties were strangers, so that no conflict of interest arises." *Transaction, Black's Law Dictionary* (10th ed.2014). The dissent quotes both definitions, but interprets them to mean that *any* affinity between two parties renders a transaction less than arm's length rather than returning to the definition in § 101(31) for guidance. *See* Dissent at 1005.
- [17] [18] A court must conduct a fact-intensive analysis to determine if a creditor and debtor shared a close relationship and negotiated at less than arm's length. Having—or being subject to—some degree of control is one of many indications that a creditor may be a non-statutory insider, but actual control is not required to find non-statutory insider status.

 See *1002 id. at 1277 n. 5. Likewise, access to the debtor's inside information may—but not shall—warrant a finding of non-statutory insider status. See id. at 1277.
- As noted by the Tenth and Third Circuits, if actual control were required for non-statutory insider status, all non-statutory insiders would also be statutory insiders under 11 U.S.C. § 101(31), § 101(31)(A)(iv) (defining "insider" as a "corporation of which the debtor is a director, officer, or person in control" (emphasis added)); § 101(31)(B)(iii), (C)(v) (defining "insider" as a "person in control of the debtor"); In re Winstar Commc'ns, Inc., 554 F.3d at 396; In re U.S. Med., Inc., 531 F.3d at 1279. Such construction of § 101(31) would render meaningless the language: "the term 'insider' includes."

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[19] [20] U.S. Bank asserts the bankruptcy court erred in holding Rabkin was not a non-statutory insider. We review the bankruptcy court's factual finding for clear error. ¹³ In re Friedman, 126 B.R. at 70; Fed.R.Civ.P. 52(a)(6). "A finding is 'clearly erroneous' when[,] although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." United States v. U.S. Gypsum Co., 333 U.S. 364, 395, 68 S.Ct. 525, 92 L.Ed. 746 (1948). We apply this highly deferential standard to findings of fact, because "[f]indings of fact are made on the basis of evidentiary hearings and usually involve credibility determinations." Rand v. Rowland, 154 F.3d 952, 957 n. 4 (9th Cir.1998) (en banc); see also Fed.R.Civ.P. 52(a)(6) ("[T]he reviewing court must give due regard to the trial court's opportunity to judge the witnesses' credibility."). Therefore, so long as the bankruptcy court's findings are "plausible in light of the record viewed in its entirety," we cannot reverse even if we "would have weighed the evidence differently." Anderson v. City of Bessemer, 470 U.S. 564, 574, 105 S.Ct. 1504, 84 L.Ed.2d 518 (1985).

- The dissent argues that "Rabkin's status [is] a mixed question of law and fact, subject to de novo review." Dissent at 1006. Stating that an issue is a "mixed question" is simply the dissent's backdoor to reassessing the facts. As stated in Section II, we have two distinct issues in question, each with a different standard of review. First, we reviewed de novo the bankruptcy court's definition of non-statutory insider status, which is a purely legal question. Now, we must analyze whether the facts of this case are such that Rabkin met that definition, which is a purely factual inquiry and properly left to clear error review.
- [21] [22] The bankruptcy court's finding that Rabkin does not qualify as a non-statutory insider is not clearly erroneous. ¹⁴ U.S. Bank presents no evidence that Rabkin had a relationship with Lakeridge comparable to those listed in § 103(31). Rather, the evidence shows Rabkin had little knowledge of Lakeridge—or its sole member MBP—prior to acquiring MBP's unsecured claim, much less access to inside information. Rabkin does not control MBP or Lakeridge, nor does Lakeridge or MBP have any control over Rabkin. U.S. Bank has shown that Rabkin had a close personal and business relationship with Bartlett, and that Bartlett approached Rabkin, and only Rabkin, with an offer to sell MBP's claim. However, Bartlett does not control MBP or Lakeridge. Rather, Bartlett was one of MBP's five managing members, all of whom discussed potential buyers and agreed to offer the claim to Rabkin. Rabkin did not know, and had no relationship with, the remaining four managing members of MBP.
- The dissent explains how it would have decided this case had it been sitting as the bankruptcy court judge. However, it was not the bankruptcy court judge. The dissent did not preside over the evidentiary hearing and did not hear the evidence in person. This court cannot substitute its judgment for that of the bankruptcy court "simply because it is convinced that it would have decided the case differently." *Anderson*, 470 U.S. at 573, 105 S.Ct. 1504.
- U.S. Bank has not shown that Rabkin's relationship with Bartlett—who is indisputably *1003 a statutory insider of MBP and Lakeridge—is sufficiently close to compare with any category listed in § 103(31). Rabkin had no control over Bartlett, and Bartlett had no control over Rabkin. Rabkin and Bartlett kept separate finances, lived separately, and conducted business separately. The bankruptcy court properly evaluated these factors to determine whether Rabkin's relationship with Bartlett was close enough to make him an insider who was conducting business at less than arm's length with MBP. ¹⁵ Nothing in § 101(31) or case law indicates it would be improper for a debtor to sell, or even give, a claim to a friend if the friend is acting of his own volition and neither party is engaged in bad faith. *See In re Friedman*, 126 B.R. at 70 ("The case law that has developed ... indicates that not every creditor-debtor relationship attended by a degree of personal interaction between the parties rises to the level of an insider relationship.").
- The dissent asserts that the bankruptcy court applied the wrong legal standard because it did not state the words "arm's length transaction" in its final order. Dissent at 1006. The court's failure to use the words "arm's length transaction" is irrelevant. The court's entire explanation is a description of why the transaction was conducted at arm's length and, hence, why Rabkin was not an insider. The court should not be discredited for listing the specific facts that made the transaction arm's length rather than merely stating a conclusion.

Both Rabkin and Bartlett testified that, although Rabkin knew Lakeridge was in bankruptcy and that purchasing the claim was a risky investment, when Rabkin purchased the claim he did not know about Lakeridge's plan of reorganization or that his vote would be required to confirm it. Although Rabkin did not conduct an extensive inquiry into the claim's

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value prior to purchasing it, Rabkin explained that it was a small investment upon which Bartlett had indicated he could make a profit and "due diligence would have been very expensive." ¹⁶ Although Rabkin allowed U.S. Bank's offer to purchase the claim for \$50,000 to lapse and subsequently voted in favor of Lakeridge's reorganization plan, he did so on the understanding that Lakeridge would amend the reorganization plan to increase his payout to an amount comparable to that offered by U.S. Bank.

The dissent argues that "the only logical explanation for Rabkin's actions" is that "[h]e did a favor for a friend." Dissent at 1005. However, the bankruptcy court's explanation that Rabkin made a speculative investment at a relatively low cost and with the potential for a big payoff is equally logical.

These facts do not leave us with a "definite and firm conviction that a mistake has been committed." *See U.S. Gypsum Co.*, 333 U.S. at 395, 68 S.Ct. 525. Rather, the bankruptcy court's finding that, on the record presented, Rabkin was not a non-statutory insider is entirely plausible, and we cannot reverse even if we may "have weighed the evidence differently." *See Anderson*, 470 U.S. at 574, 105 S.Ct. 1504.

IV. Conclusion

The BAP properly reversed the bankruptcy court's holding as to Rabkin's statutory insider status and affirmed the bankruptcy court's holding as to Rabkin's non-statutory insider status. Because Rabkin is neither a statutory nor non-statutory insider, the BAP properly reversed the portion of the bankruptcy court's order that excluded Rabkin's vote for plan confirmation purposes. Therefore, the judgment of the BAP is **AFFIRMED**.

CLIFTON, Circuit Judge, concurring in part and dissenting in part:

I agree with the legal conclusion that a person does not necessarily become a statutory insider solely by acquiring a claim *1004 from a statutory insider, as discussed in section III.A of the majority opinion. As long as the interest previously owned by a statutory insider was acquired by an independent party, for bona fide reasons, uninfected with the unique motivations of the insider, there is no reason that the insider taint should always be unshakeable. The consideration of whether the insider status should stick to the interest properly depends on the particular circumstances and is appropriately treated as something to be determined based on the facts of the situation. But it is clear to me, based on the facts of this case, that Robert Rabkin should be viewed as a non-statutory insider, and the bankruptcy court should treat his claim as such. I respectfully dissent as to Section III.B.

The majority opinion, at 1001, defines a creditor as a non-statutory insider when "(1) the closeness of its relationship with the debtor is comparable to that of the enumerated insider classifications in § 101(31), and (2) the relevant transaction is negotiated at less than arm's length." I agree.

The facts make it clear that this transaction was negotiated at less than arm's length. Rabkin paid \$5,000 to MBP (the sole member of the debtor, Lakeridge), for an unsecured claim against Lakeridge nominally worth \$2.76 million. MBP did not offer the interest to anyone else. The purchase was not solicited by Rabkin. It was proposed to Rabkin by Kathie Bartlett, a member of the MBP board. There was no evidence of any negotiation over price—Rabkin didn't offer less, and MBP didn't ask for more. Rabkin knew little if anything about Lakeridge (or, for that matter, MBP) before he bought the claim, nor did he conduct any investigation to ascertain the current value of that unsecured claim. Even after he purchased the claim, he did not bother to find out more about what it might be worth. Prior to his deposition Rabkin did not even know what the proposed plan of reorganization would pay him for the claim. After he learned that the payment under the plan would be \$30,000, he was offered as much as \$60,000 for his interest, but he declined that offer. \(\frac{1}{2} \)

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The offer was made in a crude manner at Rabkin's deposition by the attorney for U.S. Bank. The manner in which the offer was presented and the demand for an immediate response weighs against putting much weight on Rabkin's rejection of the offer. Even after reflection and consultation with his counsel, however, Rabkin declined the offer and did nothing to pursue any opportunity to realize more than \$30,000 for his interest. That behavior does not support the view that his motivations were purely economic or that his decision-making was that of a party acting at arm's length without regard for his personal relationship with an insider.

The motives of MBP and Bartlett are clear and not denied. MBP is the sole member of Lakeridge. The Lakeridge reorganization plan cannot be approved unless there is a class of creditors willing to vote to approve it. Without the sale of this claim to Rabkin and his anticipated vote to approve the plan, that plan is dead in the water, Lakeridge will be liquidated, and there will be no hope for MBP to obtain anything for either the unsecured claim or, more importantly, its ownership of Lakeridge. It may have wanted to recover something from its unsecured claim, but it did not look for the best possible price because its Lakeridge ownership was far more important. MBP was primarily motivated to place the unsecured claim in the hands of a friendly creditor who could be counted on to vote in favor of the reorganization plan, opening the door to the possibility of obtaining approval of the proposed plan of reorganization.

Rabkin's motivation is a bit murkier, but it is clear that the transaction cannot be understood as a primarily economic proposition *1005 on his part. There was no evidence that he had a habit of making blind bets, say by helping out Nigerian princes or buying the Brooklyn Bridge. There is an alternative explanation that makes a lot more sense. As the majority opinion acknowledges, at 997, Rabkin had a "close business and personal relationship" with Bartlett, the person who proposed this transaction to him. I don't have to know the precise details of the relationship between Rabkin and Bartlett to conclude that it offers the only logical explanation for Rabkin's actions here. He did a favor for a friend, and if it made some money for himself, so much the better.

Rabkin may not have been setting out to lose money or planning simply to give \$5,000 to Bartlett, but that is not the standard. *Black's Law Dictionary* (10th ed.2014) defines "arm's length transaction" as follows:

1. A transaction between two unrelated and unaffiliated parties. 2. A transaction between two parties, however closely related they may be, conducted as if the parties were strangers, so that no conflict of interest arises.

Rabkin and Bartlett were not "unrelated and unaffiliated parties." The transaction was not conducted "as if the parties were strangers." It was not an arm's length transaction. As a result, under the definition recognized by the majority, Rabkin was a "non-statutory insider" because "the relevant transaction [was] negotiated at less than arm's length."

Rabkin at no point attempted to negotiate the price of his purchase, research the value of the claim that was offered to him, or otherwise behave in a manner that suggests that he took his acquisition seriously as an economic investment. This "compels the conclusion" that Rabkin and Bartlett's relationship was "close enough to gain an advantage attributable simply to affinity rather than to the course of dealings between the parties." *In re Kunz*, 489 F.3d 1072, 1079 (10th Cir.2007) (quoting *In re Enter. Acquisition Partners, Inc.*, 319 B.R. 626, 631 (9th Cir. BAP 2004)); *see also, Matter of Holloway*, 955 F.2d 1008, 1011 (5th Cir.1992).

Moreover, though the majority opinion treats the bankruptcy court's determination that Rabkin was not a non-statutory insider as a factual finding subject to review only for clear error, I do not think that reflects a correct understanding of what the bankruptcy court decided. The specific facts of the episode were not seriously contested. Rather, the majority simply accedes to the bottom-line adjudication that, based on those facts, Rabkin was not an insider.

But that finding turns at least as much on the legal standard that defines a non-statutory insider as it does on the facts. Look at what the bankruptcy court said in explaining its conclusion that Rabkin was not a non-statutory insider, quoted by the majority opinion, at 998:

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(a) Dr. Rabkin does not exercise control over [Lakeridge;](b) Dr. Rabkin does not cohabitate with Ms. Bartlett, and does not pay [her] bills or living expenses; (c) Dr. Rabkin has never purchased expensive gifts for Ms. Bartlett; (d) Ms. Bartlett does not exercise control over Dr. Rabkin[;] (e) Ms. Bartlett does not pay [Dr.] Rabkin's bills or living expenses; and (f) Ms. Bartlett has never purchased expensive gifts for Dr. Rabkin.

This list of facts would support a finding that Rabkin and Bartlett are separate financial entities, but it does not show that this transaction was conducted as if they were strangers. At no point does the bankruptcy court mention or refer to an "arm's length transaction" at all, let alone provide a sufficient basis for a finding that Rabkin and Bartlett were unrelated or *1006 dealt with each other as strangers. That is the standard the majority opinion and I both agree should apply, but it was not the standard actually applied by the bankruptcy court. The majority disagrees, stating, at 1003 n. 15, that the bankruptcy court's order "is a description of why the transaction was conducted at arm's length," but the majority opinion is conspicuously silent in explaining how the facts actually justify any such finding.

That tells me that the problem here is not with the facts as found by the bankruptcy court but with the legal test that the bankruptcy court applied. What standard did the bankruptcy court apply to determine whether this transaction was conducted at arm's length, by parties acting like they were strangers? We don't know, because the bankruptcy court order never discussed the concept. At a minimum, this makes Rabkin's status a mixed question of law and fact, subject to de novo review. See In re Bammer, 131 F.3d 788, 792 (9th Cir.1997) ("Mixed questions presumptively are reviewed by us de novo because they require consideration of legal concepts and the exercise of judgment about the values that animate legal principles.").

I do not need to pursue that question further here, though, because even if the clear error standard applies, the finding that Rabkin was not a non-statutory insider cannot survive scrutiny. The majority opinion states three separate times, at 1002, 1002 n. 14 & 1003, that we cannot reverse under the clear error standard simply because we would have decided the case differently, a telling sign that even the majority recognizes that support for the finding is thin at best. It even suggests, at 1002 n. 14, that this dissent presents nothing more than a statement of how I would have decided the case sitting as a bankruptcy judge. But my dissent is based on far more than a mere alternative view of the evidence. I cannot fathom how anyone could reasonably conclude that this transaction was conducted as if Rabkin and Bartlett were strangers. The clear error standard is not supposed to provide carte blanche approval of whatever the bankruptcy court might have found. That is especially true here, where the bankruptcy court never actually stated a finding that the transaction was at arm's length or that the parties conducted the transaction as if they were strangers. Under the proper definition of "arm's length transaction," Rabkin's acquisition of the claim was a transaction "negotiated at less than arm's length." He was a non-statutory insider, and his claim should be treated as such.

The majority's holding also has the troubling effect of creating a clear path for debtors who want to avoid the limitations the Bankruptcy Act places on reorganization plans. The Act allows courts to confirm bankruptcy plans if each class of claims or interests impaired under the plan votes to accept the plan. 11 U.S.C. § 1129(a)(8). Perhaps recognizing that unanimous agreement on a given bankruptcy plan would sometimes prove impossible, Congress also created an exception to § 1129(a)(8) allowing debtors to "cram down" a bankruptcy plan over the objections of some debtor classes. The cramdown provision allows courts to approve a bankruptcy plan so long as all provisions of § 1129(a) are met except for § 1129(a)(8), and the proposed plan is fair, equitable, and does not discriminate unfairly. 11 U.S.C. § 1129(b)(1). Even in the case of a cramdown, though, "at least one class of claims that is impaired under the plan [must have] accepted the plan, determined without including any acceptance of the plan by any insider." 11 U.S.C. § 1129(a)(10).

The legislative history on § 1129 is sparse and provides little insight into Congress's *1007 motives, ² but in accordance with one of the most basic tenets of statutory interpretation, we must "interpret statutes as a whole, giving effect to each word and making every effort not to interpret a provision in a manner that renders other provisions of the same statute inconsistent, meaningless or superfluous." *Boise Cascade Corp. v. U.S. E.P.A.*, 942 F.2d 1427, 1432 (9th Cir.1991). Here,

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we are obligated to interpret § 1129 as a whole and in a way that gives each of its provisions meaning. A cramdown plan cannot be approved unless it is accepted by at least one class of impaired creditors.

As the Fifth Circuit has noted, "the scant legislative history on § 1129(a)(10) provides virtually no insight as to the provision's intended role." In re Vill. at Camp Bowie I, L.P., 710 F.3d 239, 246 (5th Cir.2013) (citing National Bankruptcy Conference, Reforming the Bankruptcy Code: The National Bankruptcy Conference's Code Review Project 277 (1994) (noting that the legislative history of § 1129(a)(10) "is murky, shedding little light on its intended role"); Scott F. Norberg, Debtor Incentives, Agency Costs, and Voting Theory in Chapter 11, 46 U. Kan. L.Rev. 507, 538 (1998) (noting that "[t]he legislative history ... sheds little light on the rationale for section 1129(a)(10)")).

Yet the majority opinion effectively renders that statutory requirement meaningless. Under the holding here, insiders are free to evade the requirement simply by transferring their interest for a nominal amount (perhaps a few peppercorns) to a friendly third party, who can then cast the vote the insider could not have cast itself.

Contrary to the majority's assurances, the requirement that all votes be cast in good faith is not a check on this behavior. In the memorandum disposition issued alongside this opinion, we conclude that Rabkin's vote for the plan was cast in good faith because Appellants had not proven that he had "ulterior motives" for his vote to approve the plan beyond personal enrichment. By this standard, a savvy debtor can comply with the good faith requirement by following a simple formula: develop a reorganization plan that would provide a payout on the insider claim if approved, and then sell the claim to a friendly third party for a price lower than the payout. This enables the debtor to maneuver the third party into a position where it would be foolish not to vote for approval of the reorganization plan, ensuring a "yes" vote and thereby allowing the debtor to effectively avoid the requirement under § 1129(a)(10) that at least one non-insider must approve the plan.

Congress cannot have intended this outcome. If it had, it would not have required that at least one class of impaired creditors—excluding insiders—vote for a plan before it can be approved. Our holding here effectively negates that part of the statute.

I respectfully dissent.

All Citations

814 F.3d 993, 75 Collier Bankr.Cas.2d 125, 62 Bankr.Ct.Dec. 44, Bankr. L. Rep. P 82,921

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138 S.Ct. 960 Supreme Court of the United States

U.S. BANK NATIONAL ASSOCIATION, Trustee, by and through CWCAPITAL ASSET MANAGEMENT LLC, Petitioner

The VILLAGE AT LAKERIDGE, LLC.

No. 15–1509. | Argued Oct. 31, 2017. | Decided March 5, 2018.

Synopsis

Background: In a Chapter 11 bankruptcy proceeding, the trustee moved to designate creditor's claim and disallow creditor's vote to confirm reorganization plan. The United States Bankruptcy Court for the District of Nevada, Bruce T. Beesley, J., granted the motion in part, and denied the motion in part. Parties cross-appealed. The Bankruptcy Appellate Panel (BAP), Kirscher, Pappas, and Taylor, JJ., 2013 WL 1397447, affirmed in part, reversed in part, and vacated in part. Trustee appealed. The United States Court of Appeals for the Ninth Circuit, N.R. Smith, Circuit Judge, 814 F.3d 993, affirmed, and certiorari was granted.

[Holding:] The Supreme Court, Justice Kagan, held that Bankruptcy Court's determination that creditor did not qualify as a non-statutory insider resolved a mixed question of law and fact subject to review for clear error.

Affirmed.

Justice Kennedy filed a concurring opinion.

Justice Sotomayor filed a concurring opinion in which Justices Kennedy, Thomas, and Gorsuch joined.

West Headnotes (8)

[1] Bankruptcy ← Conclusions of law;de novo review
Bankruptcy ← Particular cases and issues

51 Bankruptcy
51XIX Review
51XIX(B) Review of Bankruptcy Court
51k3782 Conclusions of law;de novo review
51 Bankruptcy
51XIX Review
51XIX(B) Review of Bankruptcy Court
51k3785 Findings of Fact
51k3787 Particular cases and issues

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Clear error, rather than de novo review applies to a court's determination of whether a person is a non-statutory insider, turning on whether that person's transactions with the debtor or another of its insiders were at arm's length. 11 U.S.C.A. § 101(31).

1 Cases that cite this headnote

[2] Bankruptcy - Conclusions of law; de novo review

51 Bankruptcy

51XIX Review

51XIX(B) Review of Bankruptcy Court

51k3782 Conclusions of law; de novo review

An appellate panel reviews bankruptcy court's legal conclusion about the test to determine whether someone is a non-statutory insider without the slightest deference. 11 U.S.C.A. § 101(31).

Cases that cite this headnote

[3] Bankruptcy Particular cases and issues

51 Bankruptcy

51XIX Review

51XIX(B) Review of Bankruptcy Court

51k3785 Findings of Fact

51k3787 Particular cases and issues

In evaluating a creditor's insider status, bankruptcy court's findings of "basic" or "historical" fact, addressing questions of who did what, when or where, how or why, are reviewable only for clear error—in other words, with a serious thumb on the scale for the bankruptcy court. 11 U.S.C.A. § 101(31).

Cases that cite this headnote

[4] Federal Courts 🌦 Questions of Law in General

170B Federal Courts

170BXVII Courts of Appeals

170BXVII(K) Scope and Extent of Review

170BXVII(K)2 Standard of Review

170Bk3566 Questions of Law in General

170Bk3567 In general

When applying the law involves developing auxiliary legal principles of use in other cases, appellate courts should typically review a decision de novo.

1 Cases that cite this headnote

[5] Federal Courts • Mixed questions of law and fact in general

170B Federal Courts

170BXVII Courts of Appeals

170BXVII(K) Scope and Extent of Review

170BXVII(K)2 Standard of Review

170Bk3572 Mixed questions of law and fact in general

When mixed questions of law and fact immerse courts in case-specific factual issues, compelling them to marshal and weigh evidence, make credibility judgments, and otherwise address "multifarious, fleeting, special, narrow facts that utterly resist generalization," appellate courts should usually review a decision with deference.

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Cases that cite this headnote

[6] Federal Courts 👺 Mixed questions of law and fact in general

170B Federal Courts170BXVII Courts of Appeals

170BXVII(K) Scope and Extent of Review

170BXVII(K)2 Standard of Review

170Bk3572 Mixed questions of law and fact in general

(Formerly 170Bk3573)

In the constitutional realm, the role of appellate courts in marking out the limits of a standard through the process of case-by-case adjudication favors de novo review even when answering a mixed question of law and fact primarily involves plunging into a factual record.

5 Cases that cite this headnote

[7] Federal Courts • Mixed questions of law and fact in general

170B Federal Courts

170BXVII Courts of Appeals

170BXVII(K) Scope and Extent of Review

170BXVII(K)2 Standard of Review

170Bk3572 Mixed questions of law and fact in general

The standard of review for a mixed question of law and fact all depends on whether answering it entails primarily legal or factual work.

6 Cases that cite this headnote

[8] Bankruptcy 🕪 Conclusions of law; de novo review

Bankruptcy Particular cases and issues

51 Bankruptcy

51XIX Review

51XIX(B) Review of Bankruptcy Court

51k3782 Conclusions of law; de novo review

51 Bankruptcy

51XIX Review

51XIX(B) Review of Bankruptcy Court

51k3785 Findings of Fact

51k3787 Particular cases and issues

Bankruptcy Court's determination that creditor who purchased claim of Chapter 11 debtor's owner and consented to debtor's reorganization did not qualify as a non-statutory insider because his transaction with the owner was conducted at arm's length resolved a mixed question of law and fact subject to review for clear error, rather than de novo review. 11 U.S.C.A. § 101(31).

4 Cases that cite this headnote

*961 Syllabus

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The syllabus constitutes no part of the opinion of the Court but has been prepared by the Reporter of Decisions for the convenience of the reader. See *United States v. Detroit Timber & Lumber Co.*, 200 U.S. 321, 337, 26 S.Ct. 282, 50 L.Ed. 499 (1906).

Respondent Lakeridge is a corporate entity with a single owner, MBP Equity Partners. When Lakeridge filed for Chapter 11 bankruptcy, it had a pair of substantial debts: It owed petitioner U.S. Bank over \$10 million and MBP another \$2.76 million. Lakeridge submitted a reorganization plan, proposing to impair the interests of both U.S. Bank and MBP. U.S. Bank refused the offer, thus blocking Lakeridge's option for reorganization through a fully consensual plan. See 11 U.S.C. § 1129(a)(8). Lakeridge then turned to the so-called "cramdown" plan option for imposing a plan impairing the interests of a non-consenting class of creditors. See § 1129(b). Among the prerequisites for judicial approval of such a plan is that another impaired class of creditors has consented to it. See § 1129(a)(10). But crucially here, the consent of a creditor who is also an "insider" of the debtor *962 does not count for that purpose. *Ibid.* The Bankruptcy Code's definition of an insider "includes" any director, officer, or "person in control" of the entity. § 101(31)(B)(i)-(iii). Courts have devised tests for identifying other, so-called "non-statutory" insiders, focusing, in whole or in part, on whether a person's transactions with the debtor were at arm's length.

Here, MBP (an insider of Lakeridge) could not provide the partial agreement needed for a cramdown plan, and Lakeridge's reorganization was thus impeded. MBP sought to transfer its claim against Lakeridge to a non-insider who could agree to the cramdown plan. Kathleen Bartlett, an MBP board member and Lakeridge officer, offered MBP's claim to Robert Rabkin, a retired surgeon, for \$5,000. Rabkin purchased the claim and consented to Lakeridge's proposed reorganization. U.S. Bank objected, arguing that Rabkin was a non-statutory insider because he had a "romantic" relationship with Bartlett and the purchase was not an arm's-length transaction. The Bankruptcy Court rejected U.S. Bank's argument. The Ninth Circuit affirmed. Viewing the Bankruptcy Court's decision as one based on a finding that the relevant transaction was conducted at arm's length, the Ninth Circuit held that that finding was entitled to clear-error review, and could not be reversed under that deferential standard.

Held: The Ninth Circuit was right to review the Bankruptcy Court's determination for clear error (rather than de novo). At the heart of this case is a so-called "mixed question" of law and fact—whether the Bankruptcy Court's findings of fact satisfy the legal test chosen for conferring non-statutory insider status. U.S. Bank contends that the Bankruptcy Court's resolution of this mixed question must be reviewed de novo, while Lakeridge (joined by the Federal Government) argues for a clear-error standard.

For all their differences, both parties rightly point to the same query: What is the nature of the mixed question here and which kind of court (bankruptcy or appellate) is better suited to resolve it? Mixed questions are not all alike. Some require courts to expound on the law, and should typically be reviewed *de novo*. Others immerse courts in case-specific factual issues, and should usually be reviewed with deference. In short, the standard of review for a mixed question depends on whether answering it entails primarily legal or factual work.

Here, the Bankruptcy Court confronted the question whether the basic facts it had discovered (concerning Rabkin's relationships, motivations, etc.) were sufficient to make Rabkin a non-statutory insider. Using the transactional prong of the Ninth Circuit's legal test for identifying such insiders (whether the transaction was conducted at arm's length, *i.e.*, as though the two parties were strangers) the mixed question became: Given all the basic facts found, was Rabkin's purchase of MBP's claim conducted as if the two were strangers to each other? That is about as factual sounding as any mixed question gets. Such an inquiry primarily belongs in the court that has presided over the presentation of evidence, that has heard all the witnesses, and that has both the closest and deepest understanding of the record—*i.e.*, the bankruptcy court. One can arrive at the same point by asking how much legal work applying the arm's-length test requires. It is precious little—as shown by judicial opinions applying the familiar legal term without further elaboration. Appellate review of the arm's-length issue—even if conducted *de novo*—will not much clarify legal principles or provide guidance

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to other courts resolving other disputes. The issue is therefore one that primarily rests with a bankruptcy court, *963 subject only to review for clear error. Pp. 965 – 969.

814 F.3d 993, affirmed.

KAGAN, J., delivered the opinion for a unanimous Court. KENNEDY, J., filed a concurring opinion. SOTOMAYOR, J., filed a concurring opinion, in which KENNEDY, THOMAS, and GORSUCH, JJ., joined.

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Opinion

JUSTICE KAGAN delivered the opinion of the Court.

[1] The Bankruptcy Code places various restrictions on anyone who qualifies as an "insider" of a debtor. The statutory definition of that term lists a set of persons related to the debtor in particular ways. See 11 U.S.C. § 101(31). Courts have additionally recognized as insiders some persons not on that list—commonly known as "non-statutory insiders." The conferral of that status often turns on whether the person's transactions with the debtor (or another of its insiders) were at arm's length. In this case, we address how an appellate court should review that kind of determination: *de novo* or for clear error? We hold that a clear-error standard should apply.

т

Chapter 11 of the Bankruptcy Code enables a debtor company to reorganize its business under a court-approved plan governing the distribution of assets to creditors. See 11 U.S.C. § 1101 et seq. The plan divides claims against the debtor into discrete "classes" and specifies the "treatment" each class will receive. § 1123; see § 1122. Usually, a bankruptcy court may approve such a plan only if every affected class of creditors agrees to its terms. See § 1129(a)(8). But in certain circumstances, the court may confirm what is known as a "cramdown" plan—that is, a plan impairing the interests of some non-consenting class. See § 1129(b). Among the prerequisites for judicial approval of a cramdown plan is that another impaired class of creditors has consented to it. See § 1129(a)(10). But crucially for this case, the consent of a creditor who is also an "insider" of the debtor does not count for that purpose. See *ibid*. (requiring "at least one" impaired class to have "accepted the plan, determined with-out including any acceptance of the plan by any insider").

The Code enumerates certain insiders, but courts have added to that number. According to the Code's definitional section, an insider of a corporate debtor "includes" any director, officer, or "person in control" of the entity. §§ 101(31) (B)(i)-(iii). Because of the word "includes" in that section, courts have long viewed its list of insiders as non-exhaustive. See § 102(3) (stating as one of the Code's "[r]ules of construction" that "'includes' and 'including' are not limiting"); 2 A. Resnick & H. Sommer, Collier on Bankruptcy ¶ 101.31, p. 101–142 (16th ed. 2016) (discussing cases). Accordingly, courts have devised tests for identifying other, so-called "non-statutory" insiders. The decisions *964 are not entirely uniform, but many focus, in whole or in part, on whether a person's "transaction of business with the debtor is not at arm's length." *Ibid.* (quoting *In re U.S. Medical, Inc.*, 531 F.3d 1272, 1280 (C.A.10 2008)).

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This case came about because the Code's list of insiders placed an obstacle in the way of respondent Lakeridge's attempt to reorganize under Chapter 11. Lakeridge is a corporate entity which, at all relevant times, had a single owner, MBP Equity Partners, and a pair of substantial debts. The company owed petitioner U.S. Bank over \$10 million for the balance due on a loan. And it owed MBP another \$2.76 million. In 2011, Lakeridge filed for Chapter 11 bankruptcy. The reorganization plan it submitted placed its two creditors in separate classes and proposed to impair both of their interests. U.S. Bank refused that offer, thus taking a fully consensual plan off the table. But likewise, a cramdown plan based only on MBP's consent could not go forward. Recall that an insider cannot provide the partial agreement needed for a cramdown plan. See supra, at 963; § 1129(a)(10). And MBP was the consummate insider: It owned Lakeridge and so was—according to the Code's definition—"in control" of the debtor. § 101(31)(B)(iii). The path to a successful reorganization was thus impeded, and Lakeridge was faced with liquidation. Unless ...

Unless MBP could transfer its claim against Lakeridge to a non-insider who would then agree to the reorganization plan. So that was what MBP attempted. Kathleen Bartlett, a member of MBP's board and an officer of Lakeridge, approached Robert Rabkin, a retired surgeon, and offered to sell him MBP's \$2.76 million claim for \$5,000. Rabkin took the deal. And as the new holder of MBP's old loan, he consented to Lakeridge's proposed reorganization. As long as he was not himself an insider, Rabkin's agreement would satisfy one of the prerequisites for a cramdown plan. See § 1129(a)(10); supra, at 963. That would bring Lakeridge a large step closer to reorganizing its business over U.S. Bank's objection.

Hence commenced this litigation about whether Rabkin, too, was an insider. U.S. Bank argued that he qualified as a non-statutory insider because he had a "romantic" relationship with Bartlett and his purchase of MBP's loan "was not an arm's-length transaction." Motion to Designate Claim of Robert Rabkin as an Insider Claim in No. 11-51994 (Bkrtcy. Ct. Nev.), Doc. 194, p. 11 (Motion). ¹ At an evidentiary hearing, both Rabkin and Bartlett testified that their relationship was indeed "romantic." App. 128, 142-143. But the Bankruptcy Court still rejected U.S. Bank's view that Rabkin was a non-statutory insider. See App. to Pet. for Cert. 66a. The court found that Rabkin purchased the MBP claim as a "speculative investment" for which he did adequate due diligence. Id., at 67a. And it noted that Rabkin and Bartlett, for all their dating, *965 lived in separate homes and managed their finances independently. See id., at 66a.

- U.S. Bank also contended that Rabkin automatically inherited MBP's statutory insider status when he purchased its loan. See Motion, p. 10 ("[A]n entity which acquires a claim steps into the shoes of that claimant" (internal quotation marks omitted)). We did not grant review of that question and therefore do not address it in this opinion.
- Perhaps Bartlett expressed some ambivalence on that score. The transcript of her direct examination reads: "Q. Okay. And I think the term has been a romantic relationship—you have a romantic relationship? A. I guess.
 - Q. Why do you say I guess?
 - A. Well, no—yes." App. 142–143.
 - One hopes Rabkin was not listening.

The Court of Appeals for the Ninth Circuit affirmed by a divided vote. According to the court, a creditor qualifies as a non-statutory insider if two conditions are met: "(1) the closeness of its relationship with the debtor is comparable to that of the enumerated insider classifications in [the Code], and (2) the relevant transaction is negotiated at less than arm's length." In re Village at Lakeridge, LLC, 814 F.3d 993, 1001 (2016). The majority viewed the Bankruptcy Court's decision as based on a finding that the relevant transaction here (Rabkin's purchase of MBP's claim) "was conducted at arm's length." Id., at 1003, n. 15. That finding, the majority held, was entitled to clear-error review, and could not be reversed under that deferential standard. See id., at 1001–1003. Rabkin's consent could therefore support the cramdown plan. See id., at 1003. Judge Clifton dissented. He would have applied de novo review, but in any event thought the Bankruptcy Court committed clear error in declining to classify Rabkin as an insider. See id., at 1006.

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This Court granted certiorari to decide a single question: Whether the Ninth Circuit was right to review for clear error (rather than *de novo*) the Bankruptcy Court's determination that Rabkin does not qualify as a non-statutory insider because he purchased MBP's claim in an arm's-length transaction. 580 U.S.——, 137 S.Ct. 1372, 197 L.Ed.2d 553 (2017).

Π

To decide whether a particular creditor is a non-statutory insider, a bankruptcy judge must tackle three kinds of issues—the first purely legal, the next purely factual, the last a combination of the other two. And to assess the judge's decision, an appellate court must consider all its component parts, each under the appropriate standard of review. In this case, only the standard for the final, mixed question is contested. But to resolve that dispute, we begin by describing the unalloyed legal and factual questions that both kinds of courts have to address along the way, as well as the answers that the courts below provided.

[2] Initially, a bankruptcy court must settle on a legal test to determine whether someone is a non-statutory insider (again, a person who should be treated as an insider even though he is not listed in the Bankruptcy Code). But that choice of standard really resides with the next court: As all parties agree, an appellate panel reviews such a legal conclusion without the slightest deference. See *Highmark, Inc. v. Allcare Health Management System, Inc.*, 572 U.S. —, —, 134 S.Ct. 1744, 1748, 188 L.Ed.2d 829 (2014) ("Traditionally, decisions on questions of law are reviewable *de novo*" (internal quotation marks omitted)); Tr. of Oral Arg. 29–30, 33. The Ninth Circuit here, as noted earlier, endorsed a two-part test for non-statutory insider status, asking whether the person's relationship with the debtor was similar to those of listed insiders and whether the relevant prior transaction was at "less than arm's length." 814 F.3d, at 1001; see *supra*, at 964 – 965. And the Ninth Circuit held that the Bankruptcy Court had used just that standard—more specifically, that it had denied insider status under the test's second, transactional prong. See 814 F.3d, at 1002–1003, and n. 15; *supra*, at 964 – 965. We do not address the correctness of the Ninth Circuit's legal test; indeed, we specifically rejected U.S. Bank's request to include that question in our grant of certiorari. See 580 U.S. —, 137 S.Ct. 1372, 197 L.Ed.2d 553; Pet. for Cert. i. We simply take that test as a given in deciding the *966 standard-of-review issue we chose to resolve.

[3] Along with adopting a legal standard, a bankruptcy court evaluating insider status must make findings of what we have called "basic" or "historical" fact—addressing questions of who did what, when or where, how or why. *Thompson v. Keohane*, 516 U.S. 99, 111, 116 S.Ct. 457, 133 L.Ed.2d 383 (1995). The set of relevant historical facts will of course depend on the legal test used: So under the Ninth Circuit's test, the facts found may relate to the attributes of a particular relationship or the circumstances and terms of a prior transaction. By well-settled rule, such factual findings are reviewable only for clear error—in other words, with a serious thumb on the scale for the bankruptcy court. See Fed. Rule Civ. Proc. 52(a)(6) (clear-error standard); Fed. Rules Bkrtcy. Proc. 7052 and 9014(c) (applying Rule 52 to various bankruptcy proceedings). Accordingly, as all parties again agree, the Ninth Circuit was right to review deferentially the Bankruptcy Court's findings about Rabkin's relationship with Bartlett (e.g., that they did not "cohabitate" or pay each other's "bills or living expenses") and his motives for purchasing MBP's claim (e.g., to make a "speculative investment"). App. to Pet. for Cert. 66a–67a; see Tr. of Oral Arg. 8, 39.

What remains for a bankruptcy court, after all that, is to determine whether the historical facts found satisfy the legal test chosen for conferring non-statutory insider status. We here arrive at the so-called "mixed question" of law and fact at the heart of this case. *Pullman–Standard v. Swint*, 456 U.S. 273, 289, n. 19, 102 S.Ct. 1781, 72 L.Ed.2d 66 (1982) (A mixed question asks whether "the historical facts ... satisfy the statutory standard, or to put it another way, whether the rule of law as applied to the established facts is or is not violated"). As already described, the Bankruptcy Court below had found a set of basic facts about Rabkin; and it had adopted a legal test for non-statutory insider status that requires (as one of its two prongs) a less-than-arm's-length transaction. See *supra*, at 964, 965. As its last move, the court compared the one to the other—and determined that the facts found did not show the kind of preferential transaction necessary to turn a creditor into a non-statutory insider. For that decisive determination, what standard of review should apply?

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The parties, after traveling so far together, part ways at this crucial point. U.S. Bank contends that the Bankruptcy Court's resolution of the mixed question must be reviewed *de novo*. That is because, U.S. Bank claims, application of the Ninth Circuit's "very general" standard to a set of basic facts requires the further elaboration of legal principles—a task primarily for appellate courts. Brief for Petitioner 35; see *id.*, at 53 (The "open-ended nature of the Ninth Circuit's standard" compels courts to "develop the norms and criteria they deem most appropriate" and so should be viewed as "quasi-legal"). By contrast, Lakeridge (joined by the Federal Government as *amicus curiae*) thinks a clear-error standard should apply. In Lakeridge's view, the ultimate law-application question is all "bound up with the case-specific details of the highly factual circumstances below"—and thus falls naturally within the domain of bankruptcy courts. Brief for Respondent 17; see Brief for United States 21 (similarly describing the mixed question as "fact-intensive").

[4] [5] [6] [7] For all their differences, both parties rightly point us to the same query. What is the nature of the mixed question here and which kind of court (bankruptcy or appellate) is better suited to resolve it? *967 See Miller v. Fenton, 474 U.S. 104, 114, 106 S.Ct. 445, 88 L.Ed.2d 405 (1985) (When an "issue falls somewhere between a pristine legal standard and a simple historical fact," the standard of review often reflects which "judicial actor is better positioned" to make the decision). Mixed questions are not all alike. As U.S. Bank suggests, some require courts to expound on the law, particularly by amplifying or elaborating on a broad legal standard. When that is so—when applying the law involves developing auxiliary legal principles of use in other cases—appellate courts should typically review a decision de novo. See Salve Regina College v. Russell, 499 U.S. 225, 231-233, 111 S.Ct. 1217, 113 L.Ed.2d 190 (1991) (discussing appellate courts' "institutional advantages" in giving legal guidance). But as Lakeridge replies, other mixed questions immerse courts in case-specific factual issues—compelling them to marshal and weigh evidence, make credibility judgments, and otherwise address what we have (emphatically if a tad redundantly) called "multifarious, fleeting, special, narrow facts that utterly resist generalization." Pierce v. Underwood, 487 U.S. 552, 561-562, 108 S.Ct. 2541, 101 L.Ed.2d 490 (1988) (internal quotation marks omitted). And when that is so, appellate courts should usually review a decision with deference. See Anderson v. Bessemer City, 470 U.S. 564, 574-576, 105 S.Ct. 1504, 84 L.Ed.2d 518 (1985) (discussing trial courts' "superiority" in resolving such issues). 4 In short, the standard of review for a mixed question all depends—on whether answering it entails primarily legal or factual work.

- In selecting standards of review, our decisions have also asked whether a "long history of appellate practice" supplies the answer. *Pierce v. Underwood*, 487 U.S. 552, 558, 108 S.Ct. 2541, 101 L.Ed.2d 490 (1988). But we cannot find anything resembling a "historical tradition" to provide a standard for reviewing the mixed question here. *Ibid*.
- Usually but not always: In the constitutional realm, for example, the calculus changes. There, we have often held that the role of appellate courts "in marking out the limits of [a] standard through the process of case-by-case adjudication" favors *de novo* review even when answering a mixed question primarily involves plunging into a factual record. *Bose Corp. v. Consumers Union of United States, Inc.*, 466 U.S. 485, 503, 104 S.Ct. 1949, 80 L.Ed.2d 502 (1984); see *Ornelas v. United States*, 517 U.S. 690, 697, 116 S.Ct. 1657, 134 L.Ed.2d 911 (1996) (reasonable suspicion and probable cause under the Fourth Amendment); *Hurley v. Irish–American Gay, Lesbian and Bisexual Group of Boston, Inc.*, 515 U.S. 557, 567, 115 S.Ct. 2338, 132 L.Ed.2d 487 (1995) (expression under the First Amendment); *Miller v. Fenton*, 474 U.S. 104, 115–116, 106 S.Ct. 445, 88 L.Ed.2d 405 (1985) (voluntariness of confession under the Fourteenth Amendment's Due Process Clause).
- [8] Now again, recall the mixed question the Bankruptcy Court confronted in this case. See *supra*, at 966. At a high level of generality, the court needed to determine whether the basic facts it had discovered (concerning Rabkin's relationships, motivations, and so on) were sufficient to make Rabkin a non-statutory insider. But the court's use of the Ninth Circuit's legal test for identifying such insiders reduced that question to a more particular one: whether the facts found showed an arm's-length transaction between Rabkin and MBP. See *ibid*. And still, we can further delineate that issue just by plugging in the widely (universally?) *968 understood definition of an arm's-length transaction: a transaction conducted as though the two parties were strangers. See, *e.g.*, Black's Law Dictionary 1726 (10th ed. 2014). Thus the mixed question becomes: Given all the basic facts found, was Rabkin's purchase of MBP's claim conducted as if the two were strangers to each other?

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A bankruptcy court applying the Ninth Circuit's test might, in another case, reach its separate, non-transactional prong: whether "the closeness of [a person's] relationship with the debtor is comparable to that of the enumerated insider classifications" in the Code. *In re Village at Lakeridge, LLC,* 814 F.3d 993, 1001 (2016); see *supra,* at 964. We express no opinion on how an appellate court should review a bankruptcy court's application of that differently framed standard to a set of established facts.

That is about as factual sounding as any mixed question gets. Indeed, application of the Ninth Circuit's arm's-length legal standard really requires what we have previously described as a "factual inference[] from undisputed basic facts." *Commissioner v. Duberstein, 363 U.S. 278, 291, 80 S.Ct. 1190, 4 L.Ed.2d 1218 (1960)* (holding that clear-error review applied to a decision that a particular transfer was a statutory "gift"). The court takes a raft of case-specific historical facts, ⁶ considers them as a whole, balances them one against another—all to make a determination that when two particular persons entered into a particular transaction, they were (or were not) acting like strangers. Just to describe that inquiry is to indicate where it (primarily) belongs: in the court that has presided over the presentation of evidence, that has heard all the witnesses, and that has both the closest and the deepest understanding of the record—*i.e.*, the bankruptcy court.

Or, to use the more abundant description we quoted above, "multifarious, fleeting, special, narrow facts that utterly resist generalization." *Pierce*, 487 U.S., at 561–562, 108 S.Ct. 2541 (internal quotation marks omitted); see *supra*, at 967.

And we can arrive at the same point from the opposite direction—by asking how much legal work applying the arm's-length test requires. Precious little, in our view—as shown by judicial opinions addressing that concept. Our own decisions, arising in a range of contexts, have never tried to elaborate on the established idea of a transaction conducted as between strangers; nor, to our knowledge, have lower courts. See, e.g., Jones v. Harris Associates L. P., 559 U.S. 335, 346, 130 S.Ct. 1418, 176 L.Ed.2d 265 (2010); Commissioner v. Wemyss, 324 U.S. 303, 307, 65 S.Ct. 652, 89 L.Ed. 958 (1945); Pepper v. Litton, 308 U.S. 295, 306–307, 60 S.Ct. 238, 84 L.Ed. 281 (1939). The stock judicial method is merely to state the requirement of such a transaction and then to do the fact-intensive job of exploring whether, in a particular case, it occurred. See, e.g., Wemyss, 324 U.S., at 307, 65 S.Ct. 652. Contrary to U.S. Bank's view, there is no apparent need to further develop "norms and criteria," or to devise a supplemental multi-part test, in order to apply the familiar term. Brief for Petitioner 53; see Tr. of Oral Arg. 18; supra, at 966. So appellate review of the arm's-length issue—even if conducted de novo—will not much clarify legal principles or provide guidance to other courts resolving other disputes. And that means the issue is not of the kind that appellate courts should take over. ⁷

That conclusion still leaves some role for appellate courts in this area. They of course must decide whether a bankruptcy court committed clear error in finding that a transaction was arm's length (or not). (We express no view of that aspect of the Ninth Circuit's decision because we did not grant certiorari on the question. See *supra*, at 965.) In addition, an appellate court must correct any legal error infecting a bankruptcy court's decision. So if the bankruptcy court somehow misunderstood the nature of the arm's-length query—or if it devised some novel multi-factor test for addressing that issue—an appellate court should apply *de novo* review. And finally, if an appellate court someday finds that further refinement of the arm's-length standard is necessary to maintain uniformity among bankruptcy courts, it may step in to perform that legal function. By contrast, what it may *not* do is review independently a garden-variety decision, as here, that the various facts found amount to an arm's-length (or a non-arm's-length) transaction and so do not (or do) confer insider status.

*969 The Court of Appeals therefore applied the appropriate standard in reviewing the Bankruptcy Court's determination that Rabkin did not qualify as an insider because his transaction with MBP was conducted at arm's length. A conclusion of that kind primarily rests with a bankruptcy court, subject only to review for clear error. We accordingly affirm the judgment below.

It is so ordered.

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Justice KENNEDY, concurring.

I join the opinion for the Court and the concurring opinion by Justice SOTOMAYOR. In doing so, it seems appropriate to add these further comments.

As the Court's opinion makes clear, courts of appeals may continue to elaborate in more detail the legal standards that will govern whether a person or entity is a non-statutory insider under the Bankruptcy Code. *Ante*, at 965, 968 – 969, n. 7. At this stage of the doctrine's evolution, this ongoing elaboration of the principles that underlie non-statutory insider status seems necessary to ensure uniform and accurate adjudications in this area.

In particular, courts should consider the relevance and meaning of the phrase "arms-length transaction" in this bankruptcy context. See *ibid*. As courts of appeals address these issues and make more specific rulings based on the facts and circumstances of individual cases, it may be that instructive, more specifically defined rules will develop.

This leads to an additional point. Under the test that the Court of Appeals applied here, there is some room for doubt that the Bankruptcy Judge was correct in concluding that Rabkin was not an insider, especially without further inquiry into whether the offer Bartlett made to Rabkin could and should have been made to other parties who might have paid a higher price. See *In re Village at Lakeridge, LLC*, 814 F.3d 993, 1006 (C.A.9 2016) (Clifton, J., concurring in part and dissenting in part) ("[E]ven if the clear error standard applies, the finding that Rabkin was not a non-statutory insider cannot survive scrutiny"). MBP's failure to offer its claim more widely could be a strong indication that the transaction was not conducted at arm's length. As the Court is careful and correct to note, however, certiorari was not granted on this question. See *ante*, at 968 – 969, n. 7. As a result, whether the test for non-statutory insider status as formulated and used by courts in the Ninth Circuit is sufficient is not before us; and whether on these facts it was clear error to find that Rabkin was not an insider is also not before us.

The Court's holding should not be read as indicating that the non-statutory insider test as formulated by the Court of Appeals is the proper or complete standard to use in determining insider status. Today's opinion for the Court properly limits its decision to the question whether the Court of Appeals applied the correct standard of review, and its opinion should not be read as indicating that a transaction is arm's length if the transaction was negotiated simply with a close friend, without broader solicitation of other possible buyers.

Justice SOTOMAYOR, with whom Justice KENNEDY, Justice THOMAS, and Justice GORSUCH join, concurring. The Court granted certiorari to decide "[w]hether the appropriate standard of review for determining non-statutory insider status" under the Bankruptcy Code is *de novo* or clear error. Pet. for Cert. i. To answer that question, the Court "take[s] *970 ... as a given" the two-prong test that the Court of Appeals for the Ninth Circuit has adopted for determining whether a person or entity is an insider. *Ante*, at 965. I join the Court's opinion in full because, within that context, I agree with the Court's analysis that a determination whether a particular transaction was conducted at arm's length is a mixed question of law and fact that should be reviewed for clear error. See *ante*, at 968 – 969.

I write separately, however, because I am concerned that our holding eludes the more fundamental question whether the Ninth Circuit's underlying test is correct. If that test is not the right one, our holding regarding the standard of review may be for naught. That is because the appropriate standard of review is deeply intertwined with the test being applied. As the Court puts it, "the standard of review for a mixed question all depends—on whether answering it entails primarily legal or factual work." *Ante*, at 967.

Here, the Court identifies the Ninth Circuit as having affirmed on the basis of the second prong of its test, pursuant to which the Ninth Circuit concluded that the relevant transaction between Robert Rabkin and MBP Equity Partners was conducted at arm's length. *Ante*, at 965. Because that analysis is primarily factual in nature, the Court rightly concludes

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that appellate review of the Bankruptcy Court's decision is for clear error. *Ante*, at 968 – 969. However, if the proper inquiry did not turn solely on an arm's-length analysis but rather involved a different balance of legal and factual work, the Court may have come to a different conclusion on the standard of review.

The Court's discussion of the standard of review thus begs the question of what the appropriate test for determining non-statutory insider status is. I do not seek to answer that question, as the Court expressly declined to grant certiorari on it. I have some concerns with the Ninth Circuit's test, however, that would benefit from additional consideration by the lower courts.

As the Ninth Circuit interpreted the Code, "[a] creditor is not a non-statutory insider unless: (1) the closeness of its relationship with the debtor is comparable to that of the enumerated insider classifications in [11 U.S.C.] § 101(31), and (2) the relevant transaction is negotiated at less than arm's length." In re Village at Lakeridge, LLC, 814 F.3d 993, 1001 (2016) (emphasis added). Under this test, because prongs one and two are conjunctive, a court's conclusion that the relevant transaction was conducted at arm's length necessarily defeats a finding of non-statutory insider status, regardless of how close a person's relationship with the debtor is or whether he is otherwise comparable to a statutorily enumerated insider. ¹

Other Circuits have developed analogous rules. See, e.g., Matter of Holloway, 955 F.2d 1008, 1011 (C.A.5 1992); In re U.S. Medical, Inc., 531 F.3d 1272, 1277–1278 (C.A.10 2008); In re Winstar Communications, Inc., 554 F.3d 382, 396–397 (C.A.3 2009). But see In re Longview Aluminum, LLC, 657 F.3d 507, 510 (C.A.7 2011).

It is not clear to me, however, that the Ninth Circuit has explained how this two-prong test is consistent with the plain meaning of the term "insider" as it appears in the Code. The concept of "insider" generally rests on the presumption that a person or entity alleged to be an insider is so connected with the debtor that any business conducted between them necessarily cannot be conducted at arm's length. See Black's Law Dictionary 915 (10th ed. 2014) (defining "insider" as "[a]n entity or person who is so closely related to a debtor that any deal between them will not be *971 considered an arm's-length transaction and will be subject to close scrutiny"). Title 11 U.S.C. § 101(31) defines "insider" by identifying certain individuals or entities who are considered insiders merely on the basis of their status, without regard to whether any relevant transaction is conducted at arm's length. Such an individual is not under any circumstance able to vote for a reorganization plan. See § 1129(a)(10).

In contrast, under prong two of the Ninth Circuit's test, an individual who is similar to, but does not fall precisely within, one of the categories of insiders listed in § 101(31) will not be considered an insider and will be able to vote under § 1129(a)(10) so long as the transaction relevant to the bankruptcy proceeding is determined to have been conducted at arm's length. This would include, for example, a romantic partner of an insider, even one who in all or most respects acts like a spouse.

Given that courts have interpreted "non-statutory insiders" as deriving from the same statutory definition as the enumerated insiders in § 101(31), the basis for the disparate treatment of two similar individuals is not immediately apparent. Lower courts have concluded that the Code's use of the term "includes" in the definition of "insider" in § 101(31) signals that Congress contemplated that certain other persons or entities in addition to those listed would qualify as insiders. See *ante*, at 970. Notably, this Court has never addressed that issue directly, although the Court has held in other contexts that "the term 'including' is not one of all-embracing definition, but connotes simply an illustrative application of the general principle." *Federal Land Bank of St. Paul v. Bismarck Lumber Co.*, 314 U.S. 95, 100, 62 S.Ct. 1, 86 L.Ed. 65 (1941).

Assuming § 101(31) encompasses such "non-statutory insiders," the only clue we have as to which persons or entities fall within that category is the list of enumerated insiders and the presumption of lack of arm's length that follows from that label. Because each of those persons or entities are considered insiders regardless of whether a particular transaction appears to have been conducted at arm's length, it is not clear why the same should not be true of non-statutory insiders.

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That is, an enumerated "insider" does not cease being an insider just because a court finds that a relevant transaction was conducted at arm's length. Then why should a finding that a transaction was conducted at arm's length, without more, conclusively foreclose a finding that a person or entity is a "non-statutory insider"?

Of course, courts must develop some principled method of determining what other individuals or entities fall within the term "insider" other than those expressly provided. I can conceive of at least two possible legal standards that are consistent with the understanding that insider status inherently presumes that transactions are not conducted at arm's length. First, it could be that the inquiry should focus solely on a comparison between the characteristics of the alleged non-statutory insider and the enumerated insiders, and if they share sufficient commonalities, the alleged person or entity should be deemed an insider regardless of the apparent arm's-length nature of any transaction. Cf. *In re Longview Aluminum*, *LLC*, 657 F.3d 507, 510–511 (C.A.7 2011) (considering only whether a manager of a debtor corporation was comparable to the enumerated insiders, regardless of whether any transaction was conducted at less-than-arm's length).

Second, it could be that the test should focus on a broader comparison that includes consideration of the circumstances *972 surrounding any relevant transaction. If a transaction is determined to have been conducted at less-than-arm's length, it may provide strong evidence in the context of the relationship as a whole that the alleged non-statutory insider should indeed be considered an insider. Relatedly, if the transaction does appear to have been undertaken at arm's length, that may be evidence, considered together with other aspects of the parties' relationship, that the alleged non-statutory insider should not, in fact, be deemed an insider.

Neither of these conceptions reflects the Ninth Circuit's test. Rather, the Ninth Circuit considered separately whether Rabkin was comparable to an enumerated insider and whether the transaction between Rabkin and MBP was conducted at arm's length. See 814 F.3d, at 1002–1003. Because the Ninth Circuit concluded that the transaction was undertaken at arm's length, that finding was dispositive of non-statutory insider status under their test, leading this Court, in turn, to consider the standard of review only with respect to that prong.

It is conceivable, however, that if the appropriate test were different from the one articulated by the Ninth Circuit, such as the two examples I outlined above, the applicable standard of review would be different as well. See *ante*, at 965, 967, n. 5. To make more concrete how this may play out in practice, I briefly walk through how I might apply my two proposed tests to the facts of this case.

If a comparative analysis were the right test, and assuming, *arguendo*, that it involves more legal than factual work thus resulting in *de novo* review, certain aspects of Rabkin's relationship with Kathleen Bartlett, an undisputed insider of the debtor, strike me as suggesting that Rabkin should have been designated as a non-statutory insider. Rabkin purchased the claim from MBP, but Bartlett, a member of MBP's board, facilitated the transaction. Even though Rabkin and Bartlett kept separate finances and lived separately, they shared a "romantic" relationship, see *ante*, at 964; Rabkin knew that the debtor was in bankruptcy, 814 F.3d, at 1003; and Bartlett approached only Rabkin with the offer to sell MBP's claim, *id.*, at 1002. In a strict comparative analysis, Rabkin's interactions with Bartlett and MBP suggest that he may have been acting comparable to an enumerated insider, for example, like a relative of an officer of an insider. See § 101(31)(B)(vi).

Even if the comparative analysis included a broader consideration of features of the transaction that suggest it was conducted at arm's length, and assuming, *arguendo*, that *de novo* review would apply, it is not obvious that those features would outweigh the aspects of the relationship that are concerning. Even though Rabkin purportedly lacked knowledge of the cramdown plan prior to his purchase and considered the purchase a "small investment" not warranting due diligence, 814 F.3d, at 1003, there was no evidence of negotiation over the price, *id.*, at 1004 (Clifton, J., dissenting), or any concrete evidence that MBP obtained real value in the deal aside from the prospect of Rabkin's vote in the cramdown. ²

Outside the context of a determination of insider status, it is possible that the nature of a transaction is relevant to assessing the integrity of bankruptcy proceedings in other ways; for example, in assessing whether a vote in a reorganization plan was "not

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in good faith, or was not solicited or procured in good faith." § 1126(e). It troubles me here that neither the Bankruptcy Court nor the Ninth Circuit considered whether Rabkin's purchase of MBP's claim for \$5,000 was for value. See App. to Pet. for Cert. 67a (bankruptcy order); *In re Village at Lakeridge, LLC*, 634 Fed.Appx. 619, 621 (2016). Cf. *In re DBSD North Am., Inc.*, 634 F.3d 79, 104 (C.A.2 2011) (stating that a transferee's overpayment for claims was relevant to a good-faith determination under § 1126(e)); § 548(c) (providing that a transfer will not be considered constructively fraudulent, and will not be voidable under § 548(a), where "a transferee ... takes for value and in good faith"). Indeed, we have no concrete information about what benefit MBP received from the transaction aside from the prospect of Rabkin's vote in the cramdown. Of course, the Ninth Circuit's decision with respect to § 1126(e) is not before this Court, but it again prompts a concern with how the courts below considered the nature of the transaction.

*973 Even if the proper test for insider status called for clear error review, it is possible that the facts of this case when considered through the lens of that test, as opposed to one focused solely on arm's length, may have warranted a finding that Rabkin was a non-statutory insider.

This is all to say that I hope that courts will continue to grapple with the role that an arm's-length inquiry should play in a determination of insider status. In the event that the appropriate test for determining non-statutory insider status is different from the one that the Ninth Circuit applied, and involves a different balance of legal and factual work than the Court addresses here, it is possible I would view the applicable standard of review differently. Because I do not read the Court's opinion as foreclosing that result, I join it in full.

All Citations

138 S.Ct. 960, 86 USLW 4121, 65 Bankr.Ct.Dec. 91, 18 Cal. Daily Op. Serv. 2082, 2018 Daily Journal D.A.R. 2037, 27 Fla. L. Weekly Fed. S 108

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683 Fed.Appx. 131

This case was not selected for publication in West's Federal Reporter.

See Fed. Rule of Appellate Procedure 32.1 generally governing citation of judicial decisions issued on or after Jan. 1, 2007. See also U.S.Ct. of Appeals 3rd Cir. App. I, IOP 5.1, 5.3, and 5.7.

United States Court of Appeals,

Third Circuit.

IN RE: ASHINC CORPORATION, et al., Debtors
ASHINC Corporation

v.

AMMC VII, Limited; Avenue Capital Group; BDCM Opportunity Fund II, L.P.; Black Diamond CLO 2005-1 Ltd.; Del Mar Distressed Opportunities Master Fund; MJX Asset Management, LLC; Par-Four Investment Management; Spectrum Investment Partners L.P.; Teak Hill—Credit Capital Investments, LLC; The CIT Group/Business Credit, Inc.; The Official Committee of Unsecured Creditors; Yucaipa American Alliance Fund II, L.P.; Yucaipa American Alliance (Parallel) Fund II, L.P.; Bennett Management Yucaipa American Alliance Fund I, L.P.; Yucaipa American Alliance (Parallel) Fund II, L.P., Appellants

No. 16-2206 | Argued December 5, 2016 | (Filed: March 23, 2017)

Synopsis

Background: Corporate debtor brought adversary proceeding for determination, inter alia, as to identity of "requisite lenders" under first lien credit agreement executed in connection with extension of post-bankruptcy financing to it upon completion of its earlier Chapter 11 case. The United States Bankruptcy Court for the District of Delaware made such a determination, and appeal was taken. The District Court, Sue L. Robinson, J., 556 B.R. 581, affirmed. Debtor's controlling shareholder, which had not been found to be a "requisite lender" despite holding first lien debt, appealed.

Holdings: The Court of Appeals, Michael J. Melloy, Senior Circuit Judge, sitting by designation, held that:

- [1] third amendment to credit agreement required consent of "requisite lenders," and not unanimous consent of all lenders that extended or acquired interest in post-bankruptcy credit facility, and so third amendment was validly enacted;
- [2] the district court did not err in holding that controlling shareholder could not serve as "requisite lender";
- [3] none of the first lien debt held by controlling shareholder could be included in the "requisite lender" calculation; and
- [4] the credit agreement and its related amendments were not ambiguous under New York law.

Affirmed.

In re ASHINC Corporation, 683 Fed.Appx. 131 (2017)

West Headnotes (4)

[1] Bankruptcy • Credit with priority or security

51 Bankruptcy

51IX Administration

51IX(A) In General

51k3035 Obtaining Credit

51k3036 Credit with priority or security

Third amendment to first lien credit agreement executed in connection with extension of post-bankruptcy financing to corporate debtor upon completion of its earlier Chapter 11 case required consent of "requisite lenders," and not unanimous consent of all lenders that extended or acquired interest in post-bankruptcy credit facility, and so third amendment was validly enacted; pursuant to express terms of credit agreement, unanimous consent of all lenders "affected thereby" was required only for any modification of credit agreement that altered definition of who was "requisite lender" or of "pro rata share," and though change made by third amendment affected calculations done before "requisite lender" calculation was made, amendment did not amend definition of "requisite lender" or "pro rata share," nor did amendment affect all lenders, but only debtor's controlling shareholder

Cases that cite this headnote

[2] Bankruptcy • Credit with priority or security

51 Bankruptcy

51IX Administration

51IX(A) In General

51k3035 Obtaining Credit

51k3036 Credit with priority or security

District court did not err when it determined that, under first lien credit agreement executed in connection with extension of post-bankruptcy financing to corporate debtor upon completion of its earlier Chapter 11 case, debtor's controlling shareholder could not serve as "requisite lender"; based on credit agreement's definition of "lender," controlling shareholder could not be a lender because it was not an original signatory to the agreement, nor could it become a party to the credit agreement pursuant to an assignment agreement because it was not an "eligible assignee," and, under third amendment to credit agreement, controlling shareholder could never be "requisite lender" due to restrictions on amount of debt that it could hold.

1 Cases that cite this headnote

[3] Bankruptcy Experience Credit with priority or security

51 Bankruptcy

51IX Administration

51IX(A) In General

51k3035 Obtaining Credit

51k3036 Credit with priority or security

Pursuant to first lien credit agreement executed in connection with extension of post-bankruptcy financing to corporate debtor upon completion of its earlier Chapter 11 case, none of the first lien debt held by debtor's controlling shareholder, including letter of credit commitments that controlling shareholder improperly acquired, could be included in agreement's "requisite lender" calculation, notwithstanding credit agreement's silence as to the commitments; third amendment to credit agreement excluded term loans from the subject

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calculation, and because controlling shareholder was prohibited from holding letter of credit commitments to begin with, there was no need for agreement or amendment to expressly exclude them from the "requisite lender" calculation.

1 Cases that cite this headnote

[4] Bankruptcy • Credit with priority or security

51 Bankruptcy

51IX Administration

51IX(A) In General

51k3035 Obtaining Credit

51k3036 Credit with priority or security

First lien credit agreement executed in connection with extension of post-bankruptcy financing to corporate debtor upon completion of its earlier Chapter 11 case, and agreement's related amendments, were not ambiguous under New York law with respect to whether term loans acquired by debtor's controlling shareholder were properly excluded from "requisite lender" calculation; third amendment to credit agreement unambiguously excluded controlling shareholder's term loans from the determination of "term loan exposure," "term loan exposure" was part of the "requisite lender" calculation, and so it was unambiguous that controlling shareholder's term loans were to be excluded from the "requisite lender" calculation.

Cases that cite this headnote

*133 On Appeal from the United States District Court for the District of Delaware (D. Del. No. 1-13-cv-01583), District Judge: Honorable Sue L. Robinson

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Before: FISHER, *KRAUSE and MELLOY, ** Circuit Judges.

- Honorable D. Michael Fisher, United States Circuit Judge for the Third Circuit, assumed senior status on February 1, 2017.
- ** Honorable Michael J. Melloy, Senior Circuit Judge, United States Court of Appeals for the Eighth Circuit, sitting by designation.

OPINION ***

This disposition is not an opinion of the full Court and pursuant to I.O.P. 5.7 does not constitute binding precedent.

MELLOY, Circuit Judge.

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Appellants Yucaipa American Alliance Fund I, L.P., Yucaipa American Alliance (Parallel) Fund I, L.P., Yucaipa American *134 Alliance Fund II, L.P., and Yucaipa American Alliance (Parallel) Fund II, L.P. (together, "Yucaipa") appeal the District Court's order affirming the Bankruptcy Court's order granting summary judgment for BDCM Opportunity Fund II, LP, Black Diamond CLO 2005–1 Ltd., and Spectrum Investment Partners (collectively, "BD/S"), Appellees. We will affirm.

I.

Allied Systems Holdings, Inc. ("Allied") declared bankruptcy in 2005. ¹ Allied emerged from that bankruptcy in 2007. Allied financed its emergence from bankruptcy by entering into various loan agreements. In 2012, Allied defaulted on one of those agreements, and a group of creditors filed an involuntary petition for bankruptcy against Allied in bankruptcy court. This appeal arises from that involuntary bankruptcy and involves questions of contract interpretation regarding the rights of lenders under the loan agreement.

Allied refers to Allied Systems Holdings, Inc., as well as its subsidiaries. Allied is now known as ASHINC Corporation. Allied was a transportation-services provider for the automotive industry, specializing in delivering new vehicles from manufacturing plants to dealerships.

When Allied emerged from bankruptcy in 2007, Yucaipa became Allied's majority shareholder with control over Allied's board of directors. To finance Allied's emergence from bankruptcy, Allied entered into the First Lien Credit Agreement ("Credit Agreement"). Pursuant to the Credit Agreement, Allied borrowed \$265 million of First Lien Debt from numerous lenders. The First Lien Debt was comprised of: (1) \$180 million of Term Loans; (2) a revolving credit facility of \$35 million ("Revolving Loans"); and (3) a synthetic letter of credit facility of \$50 million ("LC Commitments"). BD/S acquired First Lien Debt pursuant to the Credit Agreement. At the time of the motion for summary judgment in the Bankruptcy Court in the instant case, the outstanding First Lien Debt was \$244,047,530.

Under the Credit Agreement, amendments required either the consent of the Requisite Lenders or the consent of all affected Lenders. Credit Agreement § 10.5. Consent of all affected Lenders was required only in certain situations listed in § 10.5(b), including if the amendment had the effect of "amend[ing] the definition of 'Requisite Lenders' or 'Pro Rata Share.' "Id. § 10.5(b)(ix). The Credit Agreement defined "Requisite Lenders" as "one or more Lenders having or holding Term Loan Exposure, LC Exposure and/or Revolving Exposure and representing more than 50% of the sum of (i) the aggregate Term Loan Exposure of all Lenders, (ii) the aggregate LC Exposure of all Lenders and (iii) the aggregate Revolving Exposure of all Lenders." Credit Agreement § 1.1. "Pro Rata Share" means "(i) with respect to all payments, computations and other matters relating to the Term Loan of any Lender, the percentage obtained by dividing (a) the Term Loan Exposure of that Lender by (b) the aggregate Term Loan Exposure of all Lenders." Id. Additionally, "Term Loan Exposure" means, "with respect to any Lender, as of any date of determination, the outstanding principal amount of the Term Loans of such Lender..." Id.

Under the Credit Agreement, before it was amended, Yucaipa was prohibited from being assigned any debt. See id. (defining "Eligible Assignee" and expressly excluding the Sponsor, Yucaipa). Further, only original Lender signatories to the Credit Agreement and Eligible Assignees that subsequently become Lenders pursuant *135 to an Assignment Agreement could act as Requisite Lenders. Id.

In April 2008, a majority of Lenders approved the Third Amendment ² to the Credit Agreement, which allowed Yucaipa to acquire a limited amount of Term Loans. Specifically, the Third Amendment made Yucaipa a "Restricted Sponsor Affiliate" and amended the definition of "Eligible Assignee" to provide that "no Restricted Sponsor Affiliate may be an Eligible Assignee with respect to a sale, assignment or transfer of Commitments, Revolving Loans or LC Deposits."

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Third Amendment § 2.1(c). Thus, Yucaipa was effectively prohibited from acquiring any First Lien Debt other than Term Loans. Further, as the District Court summarized, Yucaipa was:

[P]rohibited from acquiring Term Loans exceeding the lesser of (i) 25% of the outstanding Term Loan Exposure or (ii) \$50 million in principal amount of Term Loans ([Third Amendment] §\$ 2.7(e), 2.7(e)); required to make a capital contribution to Allied of no less than 50% of the aggregate principal amount of any Term Loans that Yucaipa obtained within 10 days of the date of acquisition (id. § 2.7(e)); prohibited from exercising any and all voting rights it would otherwise have as a Lender 'for all purposes' (id. §§ 2.1(e), 2.7(a), 2.7(b), 2.7(e)); and subject to a broadly worded covenant not to sue (id. § 2.7).

J.A. 6. The Third Amendment also amended the definition of "Term Loan Exposure," providing that "with respect to any provisions of this Agreement relating to the voting rights of Lenders ... the aggregate outstanding principal amount of the Term Loans of all Restricted Sponsor Affiliates shall be disregarded for purposes of this definition of 'Term Loan Exposure.' "Third Amendment § 2.1(e). Yucaipa did not acquire any First Lien Debt following the execution of the Third Amendment.

The first two amendments are not at issue in the instant appeal.

In February 2009, ComVest Investment Partners III, L.P. ("ComVest") purchased approximately 55% of the First Lien Debt and became the Requisite Lender. In August 2009, Allied and ComVest entered into the Fourth Amendment, which changed the definition of "Term Loan Exposure" back to the original definition included in the Credit Agreement, removed the restrictions on the amount and type of debt Yucaipa could acquire, allowed Yucaipa's debt to be counted in the Requisite Lender calculation, and allowed Yucaipa's debt to have voting rights. ComVest was the only Lender that consented to the Fourth Amendment. Contemporaneously with the execution of the Fourth Amendment, ComVest and Yucaipa executed an Assignment Agreement whereby Yucaipa purchased all of ComVest's First Lien Debt. Following this transaction, Yucaipa declared itself the Requisite Lender. Currently, Yucaipa holds \$134,835,690 of First Lien Debt, including \$114,712,087 of Term Loans and \$20,123,602 of LC Commitments.

In January 2012, BD/S filed suit in New York state court, seeking a declaration that the Fourth Amendment was void and that Yucaipa was not the Requisite Lender. The court granted summary judgment in favor of BD/S, finding that the Fourth Amendment was invalid because § 10.5 of the Credit Agreement required unanimous consent from all Lenders, which was not given. See BDCM Opportunity Fund II, LP v. Yucaipa Am. Alliance Fund I, LP, No. 650150/2012, 2013 WL 1290394 at *5, 2013 N.Y. Misc. LEXIS 1993 at *14 (N.Y. Sup. Ct. Mar. 8, 2013). Thus, the court held, given that the Fourth Amendment *136 was invalid, Yucaipa was not the Requisite Lender. See id. at *6, 2013 N.Y. Misc. LEXIS 1993 at *16. The First Department of the New York Supreme Court's Appellate Division affirmed the lower court's finding that the Fourth Amendment was void and that Yucaipa was not the Requisite Lender. BDCM Opportunity Fund II, LP v. Yucaipa Am. Alliance Fund I, LP, 112 A.D.3d 509, 509–11, 978 N.Y.S.2d 10 (App. Div. 2013).

The New York Court of Appeals denied further review. BDCM Opportunity Fund II, LP v. Yucaipa Am. Alliance Fund I, LP, 22 N.Y.3d 1171, 985 N.Y.S.2d 472, 8 N.E.3d 849, 849 (2014).

In May 2012, while the New York litigation was pending, BD/S filed an involuntary petition for bankruptcy against Allied in bankruptcy court. In October 2012, Allied initiated an adversary proceeding in bankruptcy court seeking a declaration as to the identity of the Requisite Lender and the validity of the Third and Fourth Amendments. BD/S moved for summary judgment seeking a declaration that BD/S is the Requisite Lender under the Credit Agreement.

On July 30, 2013, the Bankruptcy Court granted the motion for summary judgment, finding that BD/S is the Requisite Lender. In its oral ruling, the Bankruptcy Court concluded Yucaipa was collaterally estopped from arguing the Fourth Amendment was valid due to the New York ruling. J.A. 1101:1–2. Further, the Bankruptcy Court found that the Credit

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Agreement and Third Amendment "are not ambiguous in any way, and the Court can ... make its determination based on the four corners of the document." J.A. 1099:15–18. The Bankruptcy Court also found that the Third Amendment "affected no lender." J.A. 1103:11–15. Specifically, the Bankruptcy Court found that the Third Amendment affected only Yucaipa's rights and was, therefore, validly enacted with majority Lender consent. J.A. 1103:16–18. Thus, "[u]pon acquiring the debt, Yucaipa subjected itself to the [Credit Agreement] and all of the amendments, including the [T]hird [A]mendment." J.A. 1104:13–15.

Regarding the Requisite Lender determination, the Bankruptcy Court found that under § 2.1(e) of the Third Amendment, "all of the Yucaipa debt cannot be used in determining who the requisite lender is...." J.A. 1103:19–25. Further, the Bankruptcy Court found that the Third Amendment "prohibited Yucaipa from acquiring any revolving loans, and letters of credit, which would [exclude] those to the extent they exist from the denominator in figuring out the requisite lender." J.A. 1104:3–6. The Bankruptcy Court also found that "the document as a whole[] remove[s] Yucaipa from being able to act as the requisite lender." J.A. 1104:7–12. Finally, the Bankruptcy Court found that "even under the first amendment alone ... Yucaipa cannot be the requisite lender because it's not a lender as an implied term, as it's not an original lender or [Eligible Assignee]." J.A. 1104:15–20.

As a result, the Bankruptcy Court held that when the New York court invalidated the Fourth Amendment, BD/S became the Requisite Lender. J.A. 1105:7–12. Removing Yucaipa-held debt from the denominator of the Requisite Lender calculation reduced the denominator from approximately \$244 million to approximately \$109 million. The Bankruptcy Court concluded that BD/S held 51.7% of the First Lien Debt.

On appeal, the District Court affirmed the Bankruptcy Court's grant of summary judgment in favor of BD/S. The District Court held: (1) the Credit Agreement and the Third Amendment are unambiguous; *137 (2) the Third Amendment is valid; (3) Yucaipa cannot act as the Requisite Lender under the Credit Agreement; (4) any First Lien Debt Yucaipa holds under the Credit Agreement should be excluded from the Requisite Lender determination; and (5) BD/S is the Requisite Lender. Yucaipa timely appealed.

II.

The District Court had jurisdiction over Yucaipa's appeal from the Bankruptcy Court's order granting summary judgment under 28 U.S.C. § 158(a). We have jurisdiction under 28 U.S.C. §§ 158(d) and 1291. "On appeal from a District Court's decision in its bankruptcy appellate capacity, we exercise the same standard of review as the District Court; we review the Bankruptcy Court's legal determinations de novo and its factual determinations for clear error." *Schwab v. PennSummit Tubular, LLC (In re Old Summit Mfg., LLC)*, 523 F.3d 134, 137 (3d Cir. 2008). Specifically, we review "whether there is a genuine issue of material fact and, if not, whether the moving party is entitled to judgment as a matter of law." *Saldana v. Kmart Corp.*, 260 F.3d 228, 232 (3d Cir. 2001) (citation omitted). Our analysis of the Credit Agreement, and the rights and obligations of the parties to the Credit Agreement, is governed by New York law. Credit Agreement § 10.14.

III.

Yucaipa raises three primary arguments on appeal. First, Yucaipa argues that the Third Amendment was not validly enacted because it required unanimous Lender consent, which was not obtained. Second, Yucaipa contends that even if the Third Amendment was validly enacted, Yucaipa's \$20 million in LC Commitments were improperly excluded from the Requisite Lender determination and that the Credit Agreement did not prohibit Yucaipa from being the Requisite Lender. As a corollary to that argument, Yucaipa asserts that BD/S is not the Requisite Lender. Third, Yucaipa argues that the Credit Agreement and its related amendments are ambiguous.

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A.

[1] Under the Credit Agreement, amendments required either the consent of the Requisite Lender(s), majority Lender consent, or the consent of all affected Lenders. Credit Agreement § 10.5. The Third Amendment was adopted pursuant to the consent of a majority of, but not all, Lenders. Yucaipa argues that because the Third Amendment changed the definition of "Term Loan Exposure," it "necessarily and effectively amended the definitions of Requisite Lenders and Pro Rata Share." Brief for Appellants at 35. Thus, Yucaipa argues, the Third Amendment required unanimous affected Lender consent to be valid.

First, Yucaipa contends that because the definitions of Requisite Lender and Pro Rata Share incorporated Term Loan Exposure, the Third Amendment amended those terms, requiring the consent of all affected Lenders. Yucaipa argues that under the Credit Agreement, Requisite Lender is expressed as an equation: (A Lender's or Lenders' First Lien Debt)/ (Total First Lien Debt). Yucaipa contends that the Third Amendment changed the denominator of the equation to ((Total First Lien Debt)—(Yucaipa-Held Debt)). However, the Third Amendment did not change the equation in this manner. Rather, the denominator remains "the sum of (i) the aggregate Term Loan Exposure of all Lenders, (ii) the aggregate LC Exposure of all Lenders and (iii) the aggregate Revolving Exposure of all Lenders." Credit Agreement § 1.1. The change *138 made by the Third Amendment affects calculations done before the Requisite Lender calculation is made. Under the Third Amendment, Yucaipa's debt was excluded from Term Loan Exposure such that the definition of Requisite Lender remained exactly the same. The only difference resulting from the Third Amendment was the number used for Term Loan Exposure in the Requisite Lender calculation. As a result, the Third Amendment did not amend the definition of Requisite Lender and, thus, did not require the consent of all affected Lenders. The same analysis applies to the alleged changed definition of Pro Rata Share.

Second, Yucaipa argues the Third Amendment's change to the definition of Term Loan Exposure affected all Lenders because it made the amount of First Lien Debt smaller for purposes of determining Requisite Lenders and Pro Rata Share. Yucaipa argues that "[d]ecreasing the total size of that pie affected *all* Lenders because it *increased* the percentage of first lien debt each Lender owned and thereby allowed a small minority lender or group of lenders to become Requisite Lender and make decisions affecting all lenders without holding 50% or more of the first lien debt." Brief for Appellants at 44.

However, as the District Court held, the Third Amendment affected no Lender. In so holding, the District Court explained that, under the Third Amendment, only Yucaipa's rights were affected, not the rights of other Lenders. Further, the District Court stated that "the Third Amendment's provision that Term Loans acquired by Yucaipa were expressly disregarded for purposes of Term Loan Exposure and could not be counted in the Requisite Lender calculation affected Yucaipa only." J.A. 21.

The District Court's holding is correct. The Third Amendment did not affect all Lenders. Rather, the Third Amendment impacted and limited Yucaipa's rights only, granting Yucaipa the ability to acquire a limited amount of Term Loans and stripping that debt of any voting rights. Under the original Credit Agreement, Yucaipa could never become the Requisite Lender because it was not a Lender and was not an Eligible Assignee such that it might become a Lender. Thus, the Third Amendment's restrictions on Yucaipa and the exclusion of Yucaipa's debt from Term Loan Exposure was consistent with the original Credit Agreement. No Lender was affected because Yucaipa remained unable to become the Requisite Lender.

Finally, Yucaipa argues the Third Amendment is invalid because the changes it made to "Term Loan Exposure" were similar to the changes made in the Purported Fourth Amendment, which was invalidated in New York state court for lack of unanimous consent. However, the New York court held that the Purported Fourth Amendment required unanimous

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consent because, under that Amendment, for the first time, Yucaipa could become the Requisite Lender. As discussed above, the Third Amendment made no such change. 4

On appeal, the New York Appellate Division explained that "given the no-waiver clause of the credit agreement, the lenders' failure to insist on unanimous consent for the third amendment does not prevent plaintiffs from insisting on unanimous lender consent for the fourth amendment." BDCM Opportunity Fund II, 112 A.D.3d at 511, 978 N.Y.S.2d 10. Thus, Yucaipa's argument that if the Purported Fourth Amendment is invalid for lack of unanimous consent, the Third Amendment is invalid too, fails if the Lenders that did not consent have waived the lack of consent. As BD/S explains, "none of the Lenders that Yucaipa claims were 'affected' by the Third Amendment ever complained that their consent was not obtained." Brief for Appellees at 26. Further, subsequent actions by the Lenders were consistent with the existence of the Third Amendment. Neither party addressed a possible waiver or ratification issue in its brief, but it may be relevant to the applicability of the Third Amendment.

*139 Based on the foregoing discussion, the Third Amendment was validly enacted. The Third Amendment did not amend the definition of Requisite Lenders or Pro Rata Share. Furthermore, no Lender was affected by the Third Amendment. As a result, unanimous Lender consent was not required to approve the Third Amendment and the Third Amendment is valid.

B.

i.

[2] Based on its belief that the Third Amendment is invalid, Yucaipa argues the District Court erred when it held that Yucaipa could not serve as the Requisite Lender under the original Credit Agreement and that BD/S is the Requisite Lender. In so arguing, Yucaipa asserts that while the Credit Agreement prohibited Yucaipa from being an Eligible Assignee, it did not prohibit Yucaipa from being a Lender. Further, Yucaipa argues that the fact that Yucaipa was not an Eligible Assignee did not prohibit Yucaipa from acquiring debt. Rather, it gives rise to a claim against the Lender that makes an assignment of debt to Yucaipa. Thus, Yucaipa claims "[a]ny Person can obtain first lien debt. Any restrictions in the definition of Eligible Assignee can apply only to Lenders seeking to assign their debt to Non-Eligible Assignees." Brief for Appellants at 58.

The Credit Agreement defined "Lender" as "each financial institution listed on the signature pages hereto as a Lender, and any other Person that becomes a party hereto pursuant to an Assignment Agreement." Credit Agreement § 1.1. Based on this definition, Yucaipa could not be a Lender because it was not an original signatory. Further, Yucaipa could not become a party to the Credit Agreement pursuant to an Assignment Agreement because it was not an Eligible Assignee. For an Assignment Agreement to become effective, the assignee was required to "represent[] and warrant[] as of the Closing Date or as of the Assignment Effective Date that (i) it is an Eligible Assignee." Credit Agreement § 10.6(e). The Credit Agreement further stated that an assignee becomes a Lender "subject to the terms and conditions of this Section 10.6." *Id.* § 10.6(f). Yucaipa could not represent and warrant that it was an Eligible Assignee.

This analysis is consistent with the New York court's findings regarding the validity of the Purported Fourth Amendment. There, the court noted, "There is no credible dispute that under the terms of the Credit Agreement as initially drafted and executed, [Yucaipa], as the 'Sponsors' and controlling shareholders of [Allied], were absolutely prohibited from being a Lender to Allied, or an Eligible Assignee of a Lender...." BDCM Opportunity Fund II, 2013 WL 1290394 at *3-4, 2013 N.Y. Misc. LEXIS 1993, at *9.

Further, under the Third Amendment, Yucaipa could never be the Requisite Lender. This is because restrictions in the Third Amendment specifically limited the amount of debt Yucaipa could validly hold. Yucaipa could not hold Term

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Loans that exceeded the lesser of (i) 25% of the outstanding Term Loan Exposure or (ii) \$50 million in principal amount of Term Loans. Third Amendment §§ 2.7(c), 2.7(e). Further, the Third Amendment restricted Yucaipa to acquiring Term Loans only; Yucaipa could not acquire Revolving Loans or LC Commitments. See id. Finally, any Term Loans Yucaipa holds were stripped *140 of voting rights and are specifically excluded from the calculation of Term Loan Exposure. Id. §§ 2.1(e), 2.7(a), 2.7(b), 2.7(e). As a result of these prohibitions and restrictions, Yucaipa could never hold enough of the First Lien Debt to become the Requisite Lender.

ii.

[3] Because of the prohibitions and restrictions imposed in the Third Amendment, none of the First Lien Debt that Yucaipa holds can be included in the Requisite Lender calculation. Yucaipa argues that there is no basis to exclude Yucaipa's LC Commitments from the Requisite Lender calculation. Yucaipa contends that the Third Amendment excluded only Term Loans from the calculation but is silent regarding LC Commitments. However, the Third Amendment was silent regarding the inclusion of Yucaipa-held LC Commitments in the Requisite Lender calculation because Yucaipa was prohibited from holding LC Commitments. Thus, there was no need to expressly exclude them from the Requisite Lender calculation. As the District Court held, "if Yucaipa cannot vote what it was permitted to own, it certainly cannot vote what it was forbidden from owning." J.A. 32.

Yucaipa argues that regardless of how it acquired the First Lien Debt it was prohibited from holding, it should be able to vote that debt because the Credit Agreement is silent. However, "contractual language must be read in context." LightSquared LP v. SP Special Opportunities LLC (In re Lightsquared Inc.), 511 B.R. 253, 335 (Bankr. S.D.N.Y. 2014). In LightSquared, the court focused on the spirit of the credit agreement, holding that the party that "found a loophole in the express terms of the Credit Agreement and exploited it," id. at 336–37, "must be held accountable," id. at 339. It would be inequitable to allow Yucaipa "to achieve an 'end run' around the substance of the Eligible Assignee restrictions in the Credit Agreement and undercut what [Yucaipa] certainly knew the restrictions were designed to prevent." Id. at 339.

It is clear Yucaipa knew that it was prohibited from acquiring LC Commitments and that the Third Amendment restricted Yucaipa's rights as a Lender. Yucaipa's argument that the express language in the Third Amendment does not exclude LC Commitments is an attempted "end run" around the intent to limit Yucaipa's holdings and prevent Yucaipa from becoming the Requisite Lender. Yucaipa should not benefit from the fact that the Third Amendment was silent on whether LC Commitments are part of the Requisite Lender calculation because Yucaipa was prohibited from holding that debt to begin with.

iii.

As a result of the foregoing discussion, the Requisite Lender calculation should be made after excluding the entire amount of First Lien Debt owned by Yucaipa from the Total First Lien Debt. Yucaipa's Term Loans should be excluded based on the language of the Third Amendment and Yucaipa's LC Commitments should be excluded because to include them would be an inequitable "end run" around the clear intent of the Third Amendment. Yucaipa holds approximately \$115 million in Term Loans and \$20 million in LC Commitments, totaling \$135 million of the total First Lien Debt. The total outstanding First Lien Debt is approximately \$244 million. Thus, the denominator in the Requisite Lender calculation is \$109 million. BD/S holds approximately \$56.5 million of First Lien Debt. The Requisite Lender equation, then, becomes \$56.5 million/ \$109 million, which equals 51.7%. To be Requisite *141 Lenders, Lenders must own more than 50% of the First Lien Debt. At 51.7%, BD/S as a collective satisfies that requirement, and the District Court correctly held that BD/S is the Requisite Lender.

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C.

[4] Notwithstanding the foregoing, Yucaipa contends the Credit Agreement and Third Amendment are ambiguous, and, thus, Yucaipa should have been allowed to present extrinsic evidence to clarify the parties' intent. Specifically, Yucaipa seeks to present evidence of an earlier draft of the Third Amendment. We conclude the Credit Agreement and Third Amendment are unambiguous, and the District Court correctly declined to consider Yucaipa's extrinsic evidence.

Under New York law, a contract's intent and whether or not a contract is ambiguous are largely related. As a threshold matter, "[i]n interpreting a contract, the intent of the parties governs." *Am. Express Bank Ltd. v. Uniroyal, Inc.*, 164 A.D.2d 275, 277, 562 N.Y.S.2d 613 (App. Div. 1990). Courts look to the plain language of the agreement as a whole to find the parties' intent. *See id.* Further, we must avoid "interpretations that render contract provisions meaningless or superfluous." *Manley v. AmBase Corp.*, 337 F.3d 237, 250 (2d Cir. 2003). Finally, if reasonable minds could find that the language of a contract has only one meaning, the contract is unambiguous. *See State v. Home Indem. Co.*, 66 N.Y.2d 669, 495 N.Y.S.2d 969, 486 N.E.2d 827, 829 (1985).

"Whether or not a writing is ambiguous is a question of law to be resolved by the courts." W.W.W. Assocs., Inc. v. Giancontieri, 77 N.Y.2d 157, 565 N.Y.S.2d 440, 566 N.E.2d 639, 642 (1990). Like intent, ambiguity is determined based on the contract as a whole. See id. Finally, "[i]t is well settled that 'extrinsic and parol evidence is not admissible to create an ambiguity in a written agreement which is complete and clear and unambiguous on its face.' "Id. (quoting Intercontinental Planning, Ltd. v. Daystrom, Inc., 24 N.Y.2d 372, 300 N.Y.S.2d 817, 248 N.E.2d 576, 580 (1969)).

Yucaipa argues that the Credit Agreement was unclear whether it was proper to exclude Yucaipa's Term Loans from the Requisite Lender calculation. Yucaipa claims it was not clear that the Third Amendment's provision stripping the voting rights of Yucaipa-held debt related to the Requisite Lender calculation. However, the Third Amendment unambiguously excluded Yucaipa's Term Loans from the determination of Term Loan Exposure. Term Loan Exposure is a part of the Requisite Lender calculation. Thus, it is unambiguous that Yucaipa's Term Loans should be excluded from the Requisite Lender calculation.

Further, Requisite Lenders exercise their rights through voting but the Third Amendment stripped Yucaipa of voting rights. Yucaipa alleges that because the Third Amendment was adopted without language that was included in an earlier draft that "expressly excluded Yucaipa's debt holdings in the definition of Requisite Lenders," the parties' intent to exclude Yucaipa's debt holdings was ambiguous. Brief for Appellants at 62. However, the plain language of the Third Amendment and the Credit Agreement was unambiguous; it would be improper to consider this extrinsic evidence because it creates an ambiguity. See W.W.W. Assocs., 565 N.Y.S.2d 440, 566 N.E.2d at 642. It is clear that because Yucaipa is stripped of voting rights, and the Requisite Lender acts by voting, Yucaipa cannot be the Requisite Lender.

Finally, Yucaipa argues that the Credit Agreement was ambiguous regarding the *142 parties' intent to prohibit Yucaipa from ever becoming the Requisite Lender. Yucaipa contends that it was improper for the court to look at the parties' intent to interpret the Credit Agreement and that intent could not be drawn from the four corners of the contract. However, as discussed above, courts regularly look to the plain language of a contract to determine intent. In this case, both the Bankruptcy Court and the District Court relied on contract provisions to support the conclusion that such an intent existed. The Courts did not resolve competing inferences, as Yucaipa claims. Rather, they construed the definitions in the Credit Agreement for "Requisite Lender," "Eligible Assignee," and "Lender" in a manner that was consistent with the Credit Agreement as a whole. As discussed above, those provisions made clear that the parties' intent was to prohibit Yucaipa from ever becoming the Requisite Lender. Thus, the District Court did not err by holding that the Credit Agreement and the Third Amendment are unambiguous.

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IV.
For the foregoing reasons, we will affirm the judgment of the District Court.
All Citations
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In re LightSquared Inc., 511 B.R. 253 (2014)

KeyCite Yellow Flag - Negative Treatment
Distinguished by In re BH Sutton Mezz LLC, Bankr.S.D.N.Y., December 1, 2016
511 B.R. 253
United States Bankruptcy Court, S.D. New York.

In re: LightSquared Inc., et al., Debtors.
LightSquared LP, LightSquared Inc., LightSquared Investors Holdings Inc., TMI
Communications Delaware, Limited Partnership, LightSquared GP Inc., ATC Technologies,
LLC, LightSquared Corp., LightSquared Inc. of Virginia, LightSquared Subsidiary LLC,
SkyTerra Holdings (Canada) Inc., and SkyTerra (Canada) Inc., Plaintiff—Intervenors,

SP Special Opportunities LLC, DISH Network Corporation, EchoStar Corporation, and Charles W. Ergen, Defendants.

Case No. 12–12080 (SCC) Jointly Administered

|
Adv. Pro. No. 13–01390 (SCC)

|
Signed June 10, 2014

Synopsis

Background: Chapter 11 debtor filed complaint seeking determination that special purpose entity (SPE) through which principal of one of debtor's competitors acquired its debt was not an eligible assignee, as well as entry of order disallowing, or equitably subordinating, proof of claim filed by SPE.

Holdings: The Bankruptcy Court, Shelley C. Chapman, J., held that:

- [1] language in credit agreement that prohibited any assignment of limited partnership debt to businesses which were in competition with partnership or their subsidiaries was not technically violated when principal of one of limited partnership's competitors formed SPE to purchase partnership debt;
- [2] debt purchase, while not technically a violation of language of credit agreement prohibiting sale of partnership debt to limited partnership's competitors or their "subsidiaries," was violative of implied covenant of good faith and fair dealing;
- [3] even assuming that restrictions on assignment were breached, this breach did not provide basis for disallowance of the SPE's claim; but
- [4] SPE's conduct was such as to warrant equitable subordination of its claim in amount to be determined after further proceedings.

So ordered.

In re LightSquared Inc., 511 B.R. 253 (2014)

West Headnotes (35)

[1] Assignments - Consent of debtor

- 38 Assignments
- 38II Mode and Sufficiency of Assignment
- 38k58 Consent of debtor

Language in credit agreement that prohibited any assignment of limited partnership debt to businesses which were in competition with partnership or their subsidiaries, in order to prevent such competitors from gaining access to substantial non-public information about limited partnership's business and ongoing operations, and that also excluded from universe of eligible assignees any natural persons, was not technically violated when principal of one of limited partnership's competitors formed special purpose entity (SPE) to purchase partnership debt; while the SPE may have been "affiliate" of one of limited partnership's competitors, credit agreement did not prohibit "affiliates," but only "subsidiaries," of competitors from purchasing partnership debt, and SPE, as entity wholly owned by competitor's principal rather than by competitor itself, was not an ineligible "subsidiary."

Cases that cite this headnote

[2] Assignments - Consent of debtor

Bankruptcy 🗪 Transfer or assignment

- 38 Assignments
- 38II Mode and Sufficiency of Assignment
- 38k58 Consent of debtor
- 51 Bankruptcy
- 51VII Claims
- 51VII(D) Proof; Filing
- 51k2904 Transfer or assignment

Purchase of debt of limited partnership by special purpose entity (SPE) created by principal of one of limited partnership's competitors, while not technically a violation of language of credit agreement prohibiting sale of partnership debt to limited partnership's competitors or their "subsidiaries," was in nature of end-run around restrictions on debt assignments, which were designed to ensure that no competitor gained access to non-public information about limited partnership's business and ongoing operations, and deprived limited partnership of fruits of credit agreement in manner violative of implied covenant of good faith and fair dealing; that SPE was formed to deliberately circumvent restrictions on assignment, rather than to make personal investments on behalf of competitor's principal, was amply demonstrated by evidence in record, including evidence that the SPE continued to make substantial purchases of partnership debt at rates approaching a dollar-for-dollar purchase price in order to acquire blocking position in limited partnership's Chapter 11 case and to facilitate acquisition of partnership assets by competitor.

1 Cases that cite this headnote

[3] Bankruptcy Proceedings

- 51 Bankruptcy
- 51IX Administration
- 51IX(C) Debtor's Contracts and Leases
- 51k3117 Proceedings

In re LightSquared Inc., 511 B.R. 253 (2014)

Under New York law, while party is precluded from recovering on claim both for breach of contract and for breach of the implied covenant of good faith and fair dealing, when meaning of contact is in doubt, party may plead breach of implied covenant of good faith and fair dealing as an alternative theory to its breach of contract claim.

Cases that cite this headnote

[4] Contracts 🕪 Terms implied as part of contract

- 95 Contracts
- 95II Construction and Operation
- 95II(A) General Rules of Construction
- 95k168 Terms implied as part of contract

Under New York law, every contract contains implied covenant of good faith and fair dealing in course of performance.

Cases that cite this headnote

[5] Contracts 🕪 Terms implied as part of contract

- 95 Contracts
- 95II Construction and Operation
- 95II(A) General Rules of Construction
- 95k168 Terms implied as part of contract

Under New York law, implied covenant of good faith and fair dealing is, in spirit, a pledge that neither party shall do anything which will have effect of destroying or injuring the right of the other party to receive fruits of contract.

Cases that cite this headnote

[6] Contracts 🌬 Acts or Omissions Constituting Breach in General

- 95 Contracts
- 95V Performance or Breach
- 95k312 Acts or Omissions Constituting Breach in General
- 95k312(1) In general

Under New York law, conduct that is technically permissible under credit agreement may nevertheless give rise to breach of implied covenant of good faith and fair dealing if it is intended to achieve result which is prohibited by agreement and which would do away with fruits of contract.

Cases that cite this headnote

[7] Bankruptcy E Claims allowable; what constitutes 'claim.'

Bankruptcy 🗪 Transfer or assignment

- 51 Bankruptcy
- 51VII Claims
- 51VII(A) In General
- 51k2825 Claims allowable; what constitutes 'claim.'
- 51 Bankruptcy
- 51VII Claims
- 51VII(D) Proof; Filing
- 51k2904 Transfer or assignment

In re LightSquared Inc., 511 B.R. 253 (2014)

Even assuming that acquisition of bankrupt limited partnership's debt by special purpose entity (SPE) created by principal of one of the partnership's competitors violated restrictions imposed by credit agreement on assignment of partnership debt, and was not just breach of implied covenant of good faith and fair dealing, this would not provide basis for disallowance of proof of claim filed by the SPE, where credit agreement did not contain clear language voiding assignment to party that was not an eligible assignee or invalidating claim by such a party, and in fact provided that any breach of restrictions on assignment would not relieve debtorborrower of obligation to perform; claim could not be disallowed as "unenforceable under any agreement or applicable law." 11 U.S.C.A. § 502(b)(1).

1 Cases that cite this headnote

[8] Bankruptcy Emitations and time to sue; computation

Bankruptcy - Transfer or assignment

51 Bankruptcy

51II Courts; Proceedings in General

51II(B) Actions and Proceedings in General

51k2157 Limitations and time to sue; computation

51 Bankruptcy

51VII Claims

51VII(D) Proof; Filing

51k2904 Transfer or assignment

Delay by bankrupt limited partnership in seeking to enforce restrictions imposed by credit agreement on assignment of its debt, in not taking steps through any of the multiple avenues available to it, such as Rule 2004 examination, to confirm that person behind the debt purchases was principal of one of its competitors, despite fact that there was considerable speculation in media to that effect, and in not filing motion to enforce restrictions on assignment or pursuing injunctive relief in bankruptcy court, prevented partnership from belatedly seeking damages award based on violations of these restrictions on assignment, which were designed to ensure that its debt was not purchased by or on behalf of competitor, and that competitor did not have access to substantial non-public information regarding partnership's ongoing business and operations; partnership's inaction, while perhaps not satisfying each of elements of equitable doctrine of laches, manifested a deliberate indifference as to whether competitor was the entity behind debt purchases and the significant increase in price of its debt, that was inconsistent with subsequent request for award of damages.

Cases that cite this headnote

[9] Equity • Nature and elements in general

150 Equity

150II Laches and Stale Demands

150k67 Nature and elements in general

Equitable doctrine of laches requires: (1) conduct giving rise to the situation complained of, (2) delay by plaintiff in asserting a claim despite the opportunity to do so, (3) lack of knowledge on defendant's part that claim would be asserted, and (4) injury or prejudice to defendant if relief is granted to plaintiff.

Cases that cite this headnote

[10] Estoppel 🗪 Essential elements

156 Estoppel

156III Equitable Estoppel

156III(A) Nature and Essentials in General

In re LightSquared Inc., 511 B.R. 253 (2014)

156k52.15 Essential elements

To equitably estop plaintiff from asserting its claims, defendant must demonstrate that plaintiff: (1) made a false representation or concealed material facts, (2) intended that such conduct would be acted upon by defendant, and (3) had knowledge of the true facts.

Cases that cite this headnote

[11] Bankruptcy 🕪 Equitable powers and principles

- 51 Bankruptcy
- 51II Courts; Proceedings in General
- 51II(A) In General
- 51k2124 Power and Authority
- 51k2125 Equitable powers and principles

Bankruptcy courts have broad equitable powers and have ability to invoke equitable principles to achieve fairness and justice in reorganization process.

1 Cases that cite this headnote

[12] Bankruptcy 🗪 Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

Equitable subordination doctrine empowers bankruptcy court to consider whether, notwithstanding the apparent legal validity of particular claim, conduct of claimant in relation to other creditors is or was such that it would be unjust or unfair to permit claimant to share pro rata with other claimants of equal status. 11 U.S.C.A. § 510(c).

Cases that cite this headnote

[13] Bankruptcy 🕪 Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

Doctrine of equitable subordination empowers court to look beyond the apparent facial validity of claim and evaluate the conduct giving rise to the claim. 11 U.S.C.A. § 510(c).

Cases that cite this headnote

[14] Bankruptcy 🕪 Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

In re LightSquared Inc., 511 B.R. 253 (2014)

Three conditions must be satisfied in order for bankruptcy court to equitably subordinate a claim: (1) claimant must have engaged in some type of inequitable conduct; (2) that misconduct must have resulted in injury to creditors of debtor and conferred an unfair advantage on claimant; and (3) equitable subordination of claim must not be inconsistent with provisions of the Bankruptcy Code. 11 U.S.C.A. § 510(c).

3 Cases that cite this headnote

[15] Bankruptcy 🕪 Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

Inequitable conduct directed against debtor or its creditors may be sufficient to warrant the equitable subordination of claim, irrespective of whether that conduct was related to the acquisition or assertion of claim. 11 U.S.C.A. § 510(c).

1 Cases that cite this headnote

[16] Bankruptcy 🗪 Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

Claim should be equitably subordinated to the extent, and only to the extent, necessary to offset the harm which debtor and its creditors suffered on account of claimant's inequitable conduct. 11 U.S.C.A. § 510(c).

Cases that cite this headnote

[17] Bankruptcy • Objections generally; time, form, and sufficiency; pleading

- 51 Bankruptcy
- 51VII Claims
- 51VII(E) Determination
- 51k2923 Objections generally; time, form, and sufficiency; pleading

Objection to claim that rests on equitable grounds must contain some substantial factual basis to support its allegation of impropriety.

Cases that cite this headnote

[18] Bankruptcy 🕪 Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

"Inequitable conduct," such as may warrant equitable subordination of claim, is not limited to fraud or breach of contract; rather, it includes even lawful conduct that shocks one's good conscience. 11 U.S.C.A. § 510(c).

In re LightSquared Inc., 511 B.R. 253 (2014)

Cases that cite this headnote

[19] Bankruptcy 🕪 Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

"Inequitable conduct," such as may warrant equitable subordination of claim, includes secret or open fraud, lack of faith or guardianship by fiduciary, and unjust enrichment. 11 U.S.C.A. § 510(c).

Cases that cite this headnote

[20] Bankruptcy 🕪 Inequitable conduct

Bankruptcy • Insiders, stockholders, fiduciaries, and dominant persons

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct
- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2968 Insiders, stockholders, fiduciaries, and dominant persons

Doctrine of equitable subordination applies to general, non-inside creditors as well as insiders, though the circumstances warranting equitable subordination of non-insider's claim arise less frequently because the opportunities for abuses triggering equitable subordination tend to be more readily available to insiders. 11 U.S.C.A. § 510(c).

2 Cases that cite this headnote

[21] Bankruptcy 🕪 Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

While there may be fewer traditional grounds available for equitable subordination of non-insider's claim, inasmuch as neither undercapitalization nor breach of fiduciary duty applies to conduct of non-insider, bankruptcy court does not apply a different or heightened standard in deciding whether to equitably subordinate a non-insider's claim. 11 U.S.C.A. § 510(c).

1 Cases that cite this headnote

[22] Bankruptcy 🥟 Inequitable conduct

- 51 Bankruptcy
- 51VII Claims

In re LightSquared Inc., 511 B.R. 253 (2014)

```
51VII(F) Priorities
51k2967 Subordination
51k2967.5 Inequitable conduct
```

Unless the non-insider has dominated or controlled debtor to gain an unfair advantage, type of "inequitable conduct" that justifies subordination of non-insider's claim is breach of an existing, legally recognized duty arising under contract, tort or other area of the law. 11 U.S.C.A. § 510(c).

3 Cases that cite this headnote

[23] Bankruptcy 🗪 Inequitable conduct

```
51 Bankruptcy
51VII Claims
51VII(F) Priorities
51k2967 Subordination
```

51k2967.5 Inequitable conduct

In absence of a contractual breach, party seeking to equitably subordinate a non-insider's claim must demonstrate fraud, misrepresentation, estoppel or similar conduct that justifies the intervention of equity. 11 U.S.C.A. § 510(c).

1 Cases that cite this headnote

[24] Bankruptcy 🕪 Inequitable conduct

```
51 Bankruptcy
51VII Claims
51VII(F) Priorities
51k2967 Subordination
51k2967.5 Inequitable conduct
```

Violation of implied covenant of good faith and fair dealing may provide grounds for equitable subordination of non-insider's claim. 11 U.S.C.A. § 510(c).

3 Cases that cite this headnote

[25] Bankruptcy 🤛 Inequitable conduct

```
51 Bankruptcy
51VII Claims
51VII(F) Priorities
51k2967 Subordination
51k2967.5 Inequitable conduct
```

Creditor misconduct in connection with Chapter 11 process itself, irrespective of applicable non-bankruptcy law, provides an appropriate predicate for equitable subordination of non-insider's claim. 11 U.S.C.A. § 510(c).

Cases that cite this headnote

[26] Bankruptcy 🗪 Inequitable conduct

```
51 Bankruptcy
51VII Claims
51VII(F) Priorities
51k2967 Subordination
51k2967.5 Inequitable conduct
```

In re LightSquared Inc., 511 B.R. 253 (2014)

For equitable subordination to be warranted, any benefit, or unfair advantage, to claimant as result of its inequitable conduct must have resulted in injury to debtor or its creditors; without injury, there is no reason to equitably subordinate a claim. 11 U.S.C.A. § 510(c).

2 Cases that cite this headnote

[27] Bankruptcy 🗪 Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

Equitable subordination of claim requires the proponent of equitable subordination to prove unfair advantage and injury to creditors, because subordination is a remedial measure designed to offset the harm resulting from claimant's inequitable conduct; it is not penal in nature. 11 U.S.C.A. § 510(c).

2 Cases that cite this headnote

[28] Bankruptcy - Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

In calculating extent to which claim should be equitably subordinated, bankruptcy court should attempt to identify the nature and extent of the harm it intends to compensate in a manner that will permit judgment to be made regarding the proportionality of the remedy to the injury that has been suffered by those who will benefit from the subordination. 11 U.S.C.A. § 510(c).

1 Cases that cite this headnote

[29] Bankruptcy 🗪 Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

Remedy of equitable subordination should remain flexible to deal with the inequitable conduct at issue. 11 U.S.C.A. § 510(c).

Cases that cite this headnote

[30] Bankruptcy - Inequitable conduct

- 51 Bankruptcy
- 51VII Claims
- 51VII(F) Priorities
- 51k2967 Subordination
- 51k2967.5 Inequitable conduct

In re LightSquared Inc., 511 B.R. 253 (2014)

Because equitable subordination is remedial rather than punitive in nature, extent of equitable subordination of claim is not related to the amount paid for claim by the offending claimant. 11 U.S.C.A. § 510(c).

Cases that cite this headnote

[31] Bankruptcy 🕪 Inequitable conduct

51 Bankruptcy

51VII Claims

51VII(F) Priorities

51k2967 Subordination

51k2967.5 Inequitable conduct

Purpose of equitable subordination is to protect creditors against unfairness and to restore creditors to position that they would have been in if claimant's misconduct had not occurred. 11 U.S.C.A. § 510(c).

Cases that cite this headnote

[32] Bankruptcy 🕪 Subordination

51 Bankruptcy

51VII Claims

51VII(F) Priorities

51k2967 Subordination

51k2967.1 In general

Bankruptcy Code does not provide for the subordination of a claim to an equity interest, but only authorizes the subordination of claims to other claims or interests to other interests. 11 U.S.C.A. § 510(c).

Cases that cite this headnote

[33] Bankruptcy 🕪 Inequitable conduct

51 Bankruptcy

51VII Claims

51VII(F) Priorities

51k2967 Subordination

51k2967.5 Inequitable conduct

There is no justification for linking equitable subordination of claim to amount that creditor paid for the claim or to the profit that creditor received or may receive from such purchase; if injury sustained by estate and other creditors is greater than amount paid for claim or the resulting profit from purchase, then equitable subordination should be greater, while if injury to creditors is less than the profit realized by offending creditor, then the extent of equitable subordination should be less. 11 U.S.C.A. § 510(c).

Cases that cite this headnote

[34] Bankruptcy 🕪 Equitable powers and principles

Bankruptcy 🤛 Inequitable conduct

51 Bankruptcy

51II Courts; Proceedings in General

51II(A) In General

51k2124 Power and Authority

51k2125 Equitable powers and principles

51 Bankruptcy

In re LightSquared Inc., 511 B.R. 253 (2014)

51VII Claims

51VII(F) Priorities

51k2967 Subordination

51k2967.5 Inequitable conduct

While bankruptcy court can apply doctrine of equitable subordination at its discretion, its power to subordinate an allowed claim is not boundless, and court cannot use equitable principles to disregard unambiguous statutory language of the Bankruptcy Code. 11 U.S.C.A. § 510(c).

3 Cases that cite this headnote

[35] Bankruptcy - Inequitable conduct

51 Bankruptcy

51 VII Claims

51VII(F) Priorities

51k2967 Subordination

51k2967.5 Inequitable conduct

Conduct of special purpose entity (SPE) through which principal of competitor of Chapter 11 debtor circumvented prohibition on sale of debtor's debt to any competitor or subsidiary of competitor, in deliberately disguising fact that its debt purchases were on behalf of competitor while continuing to purchase debtor's debt and ultimately acquiring a blocking position in reorganization case, and in then using that blocking position to control conduct of Chapter 11 case itself and, by deliberately delaying the closings on its debt purchases and obfuscating identities of holders of debtor's debt, in interfering with debtor's ability to negotiate a consensual plan, subverting purpose of court-approved exclusivity period, and preventing court from directing and having visibility into events unfolding in the case, was such as to warrant equitable subordination of SPE's claim, though bankruptcy court could not determine, based on present record, precise amount of injury caused to creditors and estate by the SPE's conduct and could not determine extent to which the SPE's claim had to be subordinated. 11 U.S.C.A. § 510(c).

1 Cases that cite this headnote

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In re LightSquared Inc., 511 B.R. 253 (2014)

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Chapter 11

POST-TRIAL FINDINGS OF FACT AND CONCLUSIONS OF LAW

SHELLEY C. CHAPMAN, UNITED STATES BANKRUPTCY JUDGE

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Between April 13, 2012 and April 26, 2013, Charles Ergen, through an entity *261 named SPSO, purchased approximately \$844 million of the senior secured debt of LightSquared LP, a debtor in these chapter 11 cases. Mr. Ergen—the founder, chairman of the board of directors, and controlling shareholder of DISH Network—bought the debt, he says, without any strategic intent to benefit DISH. Rather, he was interested in acquiring LightSquared debt personally

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because he "liked the investment" and because he had been advised that DISH itself was not eligible to purchase the debt due to restrictions in the LightSquared LP Credit Agreement. The "diligence" on the purchaser eligibility issue, such as it was, was conducted by Mr. Ergen's longtime friend Jason Kiser, the Treasurer of DISH, who from time to time worked on personal matters for Mr. Ergen. Mr. Kiser also arranged the trades on behalf of Mr. Ergen, on "his own time" while at work at DISH. Promptly after Mr. Ergen's initial debt purchase in the face amount of \$5 million on April 13, 2012, and particularly after his significant debt purchase in the face amount of \$247 million on May 4, 2012, the press began to speculate about the identity of the SPSO purchaser, publishing stories with headlines such as "LightSquared [Term Loan] Trades North of 70 as Ergen Enters the Picture" and "Ergen Builds Cash Pile Amidst LightSquared Restructuring Talks." The trades and the press reports did not go unnoticed by LightSquared, especially after the news that it was Carl Icahn who had sold his nearly quarter billion dollar position in the debt to SPSO. Philip Falcone, the founder and principal owner of Harbinger Capital Partners, which is the principal shareholder of LightSquared, reacted to the news swiftly and strategically, writing in an email message: "Well I'm working on giving him a nice surprise," referring to Mr. Ergen and to LightSquared's May 9, 2012 modification of its Credit Agreement's Disqualified Companies list to include DISH.

The game was afoot. Almost two years of moves and counter moves have ensued, with LightSquared's other stakeholders sometimes watching from the sidelines and sometimes entering the fray—all under the watchful gaze of the Federal Communications Commission, which to this day has not taken definitive action to clarify the status of LightSquared's valuable spectrum assets. The questions before the Court, among others, are whether SPSO's debt purchases violated the LightSquared LP Credit Agreement and whether its now approximately \$1 billion claim (inclusive of interest) should therefore be disallowed, or, alternatively, whether SPSO's claim should be equitably subordinated by virtue of its conduct in connection with the debt purchases and/or in connection with these chapter 11 cases. The Court's analysis is as follows. \(\) 1

This Decision supersedes this Court's bench decision read into the record on May 8, 2014.

THE PARTIES

Plaintiffs LightSquared LP, LightSquared Inc., LightSquared Investors Holdings Inc., TMI Communications Delaware Limited Partnership, LightSquared GP Inc., ATC Technologies, LLC, LightSquared Corp., LightSquared Inc. of Virginia, LightSquared Subsidiary LLC, SkyTerra Holdings (Canada) Inc., and SkyTerra (Canada) Inc., as debtors and debtors in possession (collectively, with certain of their affiliated debtors and debtors in possession, "LightSquared" or the "Debtors") provide wholesale mobile satellite communications and broadband services throughout North America. Through its ownership of several satellites and licenses to use mobile satellite service spectrum issued by the Federal Communications Commission (the "FCC"), LightSquared *262 delivers voice and data services to mobile devices used by the military, first responders and other safety professionals, and individuals throughout North America. (See Declaration of Marc R. Montagner [Bankr. Docket No. 3] ¶ [18–3 1.)²

Citations to "Adv. Docket No. __" refer to docket entries in this adversary proceeding, Adv. Pro. 13–1390–scc (Bankr. S.D.N.Y.) (the "Adversary Proceeding") and citations to "Bankr. Docket No. __" refer to docket entries in the Debtors' bankruptcy case, In re LightSquared Inc., Case No. 12–12080–scc (Bankr. S.D.N.Y.).

Plaintiffs Harbinger Capital Partners LLC, HGW U.S. Holding Company LP, Blue Line DZM Corp., and Harbinger Capital Partners SP, Inc. (collectively, "*Harbinger*") own in excess of 82 percent of the common equity of LightSquared and assert a general unsecured claim against LightSquared LP and claims against LightSquared Inc. (*See* Adv. Docket No. 1 ¶ 17.)

Defendant DISH Network Corporation ("DISH") is a public corporation organized and existing under the laws of the state of Nevada with its principal place of business in Englewood, Colorado. DISH provides broadband and satellite television services and aims to expand its broadband offerings, including by building a terrestrial broadband network.

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(PX0781 ¶¶ 30, 43.) In addition to its satellite broadcast business, DISH owns significant spectrum assets, including mobile satellite spectrum. (*Id.*) DISH is a direct competitor of LightSquared. (*Id.* ¶ 30; Jan. 13 Tr. (Ergen) 14:13–18; Jan. 10 Tr. (Kiser) 70:24–71:1; PX0013 at 10; Montagner Dep. 72:13–74:7; PX0159 at L2AP0007578.) ³

Citations to the trial transcripts of the Adversary Proceeding, dated January 9 through January 17, 2014 and March 17, 2014, will be referenced as "Jan. __Tr. (witness) [page:line]" or "Mar. __Tr. (counsel) [page:line]." Citations to deposition testimony from the Adversary Proceeding will be referenced as "Witness Dep. [page:line]."

Defendant EchoStar Corporation ("*EchoStar*") is a public corporation organized and existing under the laws of the State of Nevada with its principal place of business in Englewood, Colorado. EchoStar is a satellite communications company that currently operates, leases, or manages a number of satellites, including the satellites that provide services to DISH. EchoStar is a direct competitor of LightSquared. (PX0781 ¶31; Jan. 10 Tr. (Kiser) 15:15–21; Jan. 13 Tr. (Ergen) 15:8–12.)

Defendant SP Special Opportunities LLC ("SPSO") is a limited liability company organized and existing under the laws of the State of Delaware with its principal place of business nominally in New York, New York. SPSO's sole member and managing member is Special Opportunities Holdings LLC ("SO Holdings"). SO Holdings is a Delaware limited liability company whose sole member and managing member is Defendant Charles W. Ergen ("Ergen").

Defendant Charles W. Ergen, a natural person, is the founder, chairman of the boards of directors, and majority owner of both DISH and EchoStar. Mr. Ergen—personally and through his family trusts—beneficially owns and controls over 88 percent of DISH's voting shares and over 80 percent of EchoStar's voting shares. Mr. Ergen owns approximately 53 percent of DISH. Mr. Ergen also wholly owns and controls SO Holdings and SPSO. (PX0700 ¶ 1–2; Jan. 13 Tr. (Ergen) 94:19–95:2, 208:18–211:20; Howard Dep. 37:25–38:16; PX0372 at 2, 5; PX0371 at 2.)

PROCEDURAL HISTORY

On May 14, 2012 (the "Petition Date"), LightSquared commenced a voluntary bankruptcy case pursuant to chapter 11 of title 11 of the United States Code (the *263 "Bankruptcy Code") in the United States Bankruptcy Court for the Southern District of New York. ([Bankr. Docket No. 1].)

On August 6, 2013, Harbinger commenced the Adversary Proceeding against Mr. Ergen, DISH, EchoStar, L–Band Acquisition, LLC ("LBAC"), SPSO, SO Holdings, Sound Point Capital Management LP ("Sound Point"), and Mr. Stephen Ketchum, alleging inequitable conduct, fraud, aiding and abetting fraud, tortious interference with prospective economic advantage, tortious interference with contractual relationship, unfair competition, and civil conspiracy; and seeking equitable disallowance of claims, compensatory and punitive damages, costs and fees, interest, and other appropriate relief. (See Adv. Docket No. 1.)

On August 22, 2013, LightSquared intervened in the Adversary Proceeding on limited grounds. (Adv. Docket No. 15.) U.S. Bank National Association ("U.S. Bank"), Mast Capital Management LLC ("Mast"), and the Ad Hoc Secured Group of LightSquared LP Lenders (the "Ad Hoc Secured Group") also intervened on the same day. (Adv. Docket Nos. 12, 14.)

On September 9, 2013, motions to dismiss were filed by each of the defendants in the Adversary Proceeding. (Adv. Docket Nos. 29, 30, 32, 33, 34, 35.) On September 30, 2013, Harbinger amended its complaint as of right (the "*Harbinger Amended Complaint*"). (Adv. Docket No. 43.) Between October 3 and October 5, 2013, each of the defendants filed a motion to dismiss the Harbinger Amended Complaint. (Adv. Docket Nos. 44, 45, 46.) After the filing of additional oppositions and replies, this Court held a hearing on October 29, 2013.

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The motions to dismiss filed in the Adversary Proceeding on September 9, 2013 were subsequently amended. See Adv. Docket Nos. 37, 38, 39.

By Order dated November 14, 2013 (the "November Order"), this Court granted Defendants' motions to dismiss the Harbinger Amended Complaint. (PX0770.) The Court also granted Harbinger leave to file a second amended complaint that did not assert claims on Harbinger's own behalf, but that merely set forth an objection, pursuant to section 502 of the Bankruptcy Code, to SPSO's claim. (Id.) The Court also authorized LightSquared to file a complaint setting forth the basis for its intervention. (Id.) On November 21, 2013, the Court issued its Memorandum Decision Granting Motions to Dismiss Complaint ("Decision on the Motions to Dismiss"), which set forth the bases for the November Order. (Adv. Docket No. 68; Harbinger Capital Partners LLC v. Ergen (In re LightSquared Inc.), 504 B.R. 321 (Bankr.S.D.N.Y.2013).)

On November 15, 2013, LightSquared filed a Complaint–in–Intervention (the "LightSquared Complaint") against SPSO, DISH, EchoStar, and Mr. Ergen (collectively, the "Defendants") seeking: (i) a declaration that SPSO is not an "Eligible Assignee" under LightSquared's October 10, 2010 Credit Agreement, as amended, modified, and restated (the "Credit Agreement") (PX0004), (ii) disallowance of SPSO's claim under 11 U.S.C. § 502(b), and (iii) equitable disallowance of SPSO's claim. (PX0771.) The LightSquared Complaint further alleges breach of contract against SPSO, as well as tortious interference with contractual relations against all Defendants. (Id.) The LightSquared Complaint also seeks equitable subordination as a remedy. (Id.)

On December 2, 2013, Harbinger filed a Second Amended Complaint (the "Harbinger Second Amended Complaint," and, together with the LightSquared Complaint, *264 the "Complaints"), seeking (i) a declaration that SPSO is not an "Eligible Assignee" under the Credit Agreement, (ii) disallowance of SPSO's claim under 11 U.S.C. § 502(b), (iii) equitable disallowance of SPSO's claim, and (iv) equitable subordination of SPSO's claim under 11 U.S.C. § 510. The Harbinger Second Amended Complaint further alleges breach of contract against SPSO. (PX0781.)

On November 25 and November 26, 2013, the Defendants filed motions to dismiss the LightSquared Complaint, ⁵ and, on December 5, 2013, SPSO filed a motion to dismiss the Harbinger Second Amended Complaint. (Adv. Docket No. 84.) After the filing of oppositions and replies, the Court held a hearing on December 10, 2013.

5 Adv. Docket Nos. 69, 70, 72, 73.

By Order dated December 12, 2013 (the "December Order"), the Court granted in part and denied in part Defendants' motions to dismiss the Complaints. (PX0784.) The December Order dismissed all of the claims asserted in the Harbinger Second Amended Complaint, except for Harbinger's claim seeking disallowance of SPSO's claim under 11 U.S.C. § 502(b). (Id. ¶3.) With respect to the LightSquared Complaint, the Court granted Defendants' motions only as to LightSquared's equitable disallowance claim against SPSO and its tortious interference claim against SPSO. (Id. ¶2.) The Court retained jurisdiction to hear and determine all matters arising from the interpretation, implementation, and enforcement of the December Order. (Id. ¶4.) Answers to the remaining counts of the LightSquared Complaint and the Harbinger Second Amended Complaint were filed on December 24, 2013. (Adv. Docket Nos. 102, 103, 104.) Pretrial briefs were filed by the parties on January 7 and January 8, 2013. (Adv. Docket Nos. 113, 115, 119, 121.)

On January 9, 2014, the Court commenced a trial ⁶ in the Adversary Proceeding and heard live testimony from eight witnesses: (a) Charles Ergen; (b) Thomas Cullen; (c) Stephen Ketchum; (d) Jason Kiser; (e) Philip Falcone; (f) Douglas Smith; (g) William Q. Derrough; and (h) Mark S. Hootnick.

At the request of the parties, the Court bifurcated the Adversary Proceeding trial into two phases: liability and damages. The liability phase of the trial, which was held between January 9 and 17, 2014, and on March 17, 2014, will be referred to herein

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as the "Trial." The second phase of the trial, in which the extent of equitable subordination to be imposed on SPSO will be determined, has not yet been scheduled by the Court.

The parties also submitted additional evidence consisting of (i) over 800 exhibits and (ii) excerpts from the deposition transcripts of six witnesses in lieu of live testimony. Deposition designations were submitted from the deposition transcripts of: (a) Steven Goodbarn; (b) Gary Howard; (c) Marc Montagner; (d) Robert Olson; (e) David Rayner; and (f) Joseph Roddy.

The Court requested that proposed findings of fact and post-trial briefs be submitted by LightSquared and Harbinger (together, "*Plaintiffs*") on February 24, 2014, and by Defendants on March 10, 2014. Those dates were subsequently modified by the Court. On February 24, 2014 and March 10, 2014, respectively, Plaintiffs submitted their (i) post-trial brief and proposed findings of fact and (ii) supplemental post-trial brief and supplemental proposed findings of fact. (Adv. Docket Nos. 132, 133, 137, 138.) On March 14, 2014, Defendants submitted proposed findings of fact and post-trial briefs, together with a response to Plaintiffs' supplemental posttrial brief. (Adv. Docket Nos. 140, 141, 142, 143, 144.) Closing arguments were held on March 17, 2014.

*265 In addition, a flurry of sanctions motions and replies has been filed by the parties, each of which remains *sub judice*. (See Adv. Docket Nos. 145, 146, 148, 151, 152, 154, 158.)

This is an adversary proceeding pursuant to Rule 7001 of the Federal Rules of Bankruptcy Procedure. Pursuant to 28 U.S.C. §§ 157 and 1334(b), the Court has jurisdiction to consider this matter a "core" proceeding. Venue is proper before this Court pursuant to 28 U.S.C. §§ 1408 and 1409.

FINDINGS OF FACT

The following constitute this Court's findings of fact and conclusions of law pursuant to Rule 7052 of the Federal Rules of Bankruptcy Procedure. Having considered the voluminous evidence, testimonial and documentary, including all exhibits admitted into evidence, as well as Plaintiffs' and Defendants' post-trial proposed findings of fact and briefs, and mindful that a court should not blindly accept findings of fact and conclusions of law proffered by the parties (see St. Clare's Hosp. and Health Ctr. v. Ins. Co. of North Am. (In re St. Clare's Hosp. and Health Ctr.), 934 F.2d 15 (2d Cir.1991) (citing United States v. El Paso Natural Gas Co., 376 U.S. 651, 656, 84 S.Ct. 1044, 12 L.Ed.2d 12 (1964))), and having conducted an independent analysis of the law and the facts, the Court makes the following Findings of Fact and Conclusions of Law:

The findings of fact and conclusions of law herein shall constitute the Court's findings of fact and conclusions of law pursuant to Bankruptcy Rule 7052, made applicable to this proceeding pursuant to Bankruptcy Rule 9014. To the extent any finding of fact later shall be determined to be a conclusion of law, it shall be so deemed, and to the extent any conclusion of law later shall be determined to be a finding of fact, it shall be so deemed.

I. The Parties and Certain Relevant Third Parties

- 1. In 1980, Mr. Ergen founded EchoSphere LLC ("*EchoSphere*") with James DeFranco and Mr. Ergen's wife, Cantey Ergen. (Jan. 13 Tr. (Ergen) 11:24–12:7, 12:21–13:11.) EchoSphere became EchoStar, which later split into EchoStar and DISH. (Jan. 13 Tr. (Ergen) 14:19–24.) Today, EchoStar is a technology company that manufactures set-top boxes and builds and operates satellites. (Rayner Dep. 27:10–18; Jan. 13 Tr. (Ergen) 14:25–15:7.)
- 2. DISH sells satellite television services. (Jan. 13 Tr. (Ergen) 14:13–18.) EchoStar is a supplier to DISH, but they are separate companies. (Jan. 13 Tr. (Ergen) 15:8–12.)
- 3. DISH's board of directors has ten members, four of whom are independent under NASDAQ rules. (Jan. 13 Tr. (Ergen) 15:13–21; see also 3/22/13 DISH Network Corp. Schedule 14A at 2–3; 9/17/13 DISH Network Corp. Form 8–K at 1; 11/5/13 DISH Network Form 8–K at 1; 2/21/14 DISH Network Corp. Form 10–K at 99.) The DISH Board of Directors

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has four regularly-scheduled meetings a year, but on average, the DISH Board will meet between eight and ten times a year. (Jan. 13 Tr. (Ergen) 16:11–14.) Discussions at the DISH board level cover many subjects, including potential acquisitions, the raising of capital, the strategic direction of the company, and personnel issues within the company. (Jan. 13 Tr. (Ergen) 16:21–25.)

- 4. Neither DISH nor EchoStar has an interest in SPSO. (PX0767 (Goodbarn Nevada Dep.) 32:24–33:2, 90:10–23; Olson Dep. 14:6–15:14, 26:7–27:11; Jan. 13 Tr. (Ergen) 36:7–9.)
- 5. Mr. Ergen, as the holder of a majority share of voting rights (approximately *266 88 percent and 79.4 percent of the total voting power in DISH and EchoStar, respectively), has the ability to elect a majority of the directors for both companies and control all other matters requiring the approval of their stockholders. (Jan. 13 Tr. (Ergen) 94:19–95:2, 208:18–211:20; Howard Dep. 37:25–38:16; PX0372 at 2, 5; PX0371 at 2.) Mr. Ergen voted for each of the current DISH Board members, and he testified that he does not know whether it is possible for someone to be a director of DISH without his vote. (Ergen Dep. 18:5–16, 26:19–25; Jan. 13 Tr. (Ergen) 95:3–5.) As a result of Mr. Ergen's dominance, both DISH and EchoStar are "controlled compan [ies] as defined in the Nasdaq listing rules." (PX0349 at 39–40; PX0350 at 34.)
- 6. Mr. Thomas Cullen ("Cullen") is the Executive Vice President of Corporate Development at DISH, a position he has held since June 2011. (Jan. 17 Tr. (Cullen) 98:19–20, 101:3–5.)
- 7. Mr. Jason Kiser ("Kiser") is the Treasurer of DISH and Vice President of Corporate Development at DISH and EchoStar, and, together with Messrs. Ergen and Cullen, is part of the corporate development team at DISH and EchoStar. (Jan. 10 Tr. (Kiser) 15:25–16:6, 68:24–69:2, 69:20–22.) Mr. Kiser arranged SPSO's trades in the secured debt of LightSquared LP ("LP Debt") pursuant to direction from Mr. Ergen by placing the orders for the amount and pricing of the debt and arranging to provide the funds to close the trades. (Jan. 10 Tr. (Kiser) 25:6–8.)
- 8. Mr. Stephen Ketchum ("*Ketchum*") is the founder and sole managing partner of Sound Point. (Jan. 15 Tr. (Ketchum) 13:13–19.) Sound Point is an investment management and advisory firm that served as trading manager and investment advisor for SPSO and executed SPSO's purchases of LP Debt. (Jan. 15 Tr. (Ketchum) 20:14–17.) Messrs. Kiser and Ketchum had a twenty-year long relationship that involved work related to both EchoStar and DISH. Mr. Ketchum served as the point of contact between Sound Point and Messrs. Kiser and Ergen. (Jan. 15 Tr. (Ketchum) 14:19–22, 93:23–94:3; Jan. 10 Tr. (Kiser) 24:10–25:8.)
- 9. SPSO was formed by Sound Point for the exclusive purpose of serving as the investment vehicle through which Mr. Ergen made trades in LP Debt (PX0162; PX0171; PX0183; PX0224; Jan. 10 Tr. (Kiser) 30:16–21, 31:20–32:14; PX0700 ¶¶ 1–2), without those purchases being traceable to Mr. Ergen (see Jan. 10 Tr. (Kiser) 30:16–21, 31:20–22, 32:2–14, 90:6–12, 90:25–91:20; Jan. 13 Tr. (Ergen) 36:13–37:4, 49:20–50:25; PX0117; PX0290 at LSQSPCD–000006771; PX0298).
- 10. Mr. Steven R. Goodbarn ("Goodbarn") is a member of the DISH Board of Directors and was a member of the special committee of independent directors of DISH that was formed to evaluate and make recommendations regarding a possible bid by DISH for LightSquared's assets (the "Special Committee"). (PX0768 ¶ 2.)
- 11. Mr. Gary S. Howard ("Howard") is a former member of the DISH Board of Directors and was a member of the Special Committee. (PX0768 ¶ 2, 53.)
- 12. Harbinger began acquiring the securities of LightSquared's predecessor, SkyTerra Communications, Inc. ("SkyTerra"), in 2006 and eventually took control of the company in early 2010, renaming it LightSquared LP. (Jan. 16 Tr. (Falcone) 14:23–16:11.)

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- 13. Harbinger currently owns about 80 to 85 percent of the stock of LightSquared. (Jan. 16 Tr. (Falcone) 18:8–12.) About 30 to 40 percent of Harbinger's assets are invested in LightSquared, and Harbinger *267 has invested approximately \$1.8 to \$2 billion in LightSquared. (Jan. 16 Tr. (Falcone) 81:3–19.)
- 14. Mr. Philip Falcone ("Falcone") is the portfolio manager of Harbinger Capital Partners LLC. (Jan. 16 Tr. (Falcone) 12:3–13.) Mr. Falcone has been trading high yield distressed debt for over 20 years. (Jan. 16 Tr. (Falcone) 13:13–18.) Mr. Falcone has between \$500 and \$700 million invested in Harbinger, which is a majority of his net worth. (Jan. 16 Tr. (Falcone) 80:6–20.)
- 15. Mr. Falcone is a member of LightSquared's board of directors, having joined the Board in early 2012. (Jan. 16 Tr. (Falcone) 17:25–18:1; 82:1–3.) A majority of the LightSquared Board of Directors is controlled by Harbinger. (Jan. 16 Tr. (Falcone) 81:23–25.)

II. The LightSquared LP Credit Agreement and the Restrictions on the Transfer of LP Debt

16. In 2010, LightSquared obtained authorization from the FCC to build an ancillary terrestrial network ("ATC Network") that would integrate its satellite service with terrestrial satellite ground stations to provide fourth generation long term evolution (4G–LTE) broadband mobile services throughout the United States. (DX054 ¶ 5–7, 29–30, 33.) To finance the buildout of its ATC Network, on October 1, 2010, LightSquared LP and certain of its affiliates entered into the Credit Agreement with UBS AG, Stamford Branch ("UBS"), as Administrative Agent, and entities that were, or would serve as, lenders under the Credit Agreement (collectively, the "Lenders"). (Id. ¶37.) The Credit Agreement is governed by New York law. (PX0004 at HARBAP00004158, § 10.09(a).)

17. The Credit Agreement restricts transfers of the LP Debt. Section 10.04(a) of the Credit Agreement provides, in pertinent part:

[N]o Lender may assign or otherwise transfer any of its rights or obligations hereunder except (i) to an Eligible Assignee in accordance with the provisions of paragraph (b) of this Section 10.04, (ii) by way of participation in accordance with the provisions of paragraph (d) of this Section 10.04 or (iii) by way of pledge or assignment of a security interest subject to the restrictions of paragraph (f) of this Section (and any other attempted assignment or transfer by Borrower shall be null and void).

(PX0004 at HARBAP00004153.)

- 18. Section 10.04(b) states that assignments of LP Debt are permitted to Eligible Assignees: "Subject to the conditions set forth in paragraph (b)(ii) below, any Lender may at any time assign to one or more Eligible Assignees all or a portion of its rights and obligations under this Agreement...." (PX0004 at HARBAP00004154.)
- 19. The term "Eligible Assignee" is defined in Section 1.01 of the Credit Agreement as follows: "[A]ny person to whom it is permitted to assign Loans and Commitments pursuant to Section 10.04(b)(i); provided that 'Eligible Assignee' shall not include Borrower or any of its Affiliates or Subsidiaries, any natural person or any Disqualified Company." (Id. at HARBAP0004058 (emphasis in original).)
- 20. The term "Eligible Assignee" also excludes "any natural person." (PX0004 at HARBAP0004058, § 1.01.) Thus, pursuant to Section 10.04(b)(i), a natural person may not take an assignment of LP Debt ("Subject to the conditions set forth in paragraph (b)(ii) below, any Lender may at any time assign to one or more Eligible Assignees all or a portion of its rights and obligations under this Agreement ..."). (PX0004 at HARBAP00004154.) Pursuant *268 to Section 10.04(d), a natural person also may not receive a Participation in LP Debt ("Any Lender may at any time, without the consent of, or notice to, Borrower or the Administrative Agent sell participations to any person (other than a natural person, *269 Borrower or any of its Affiliates or any Disqualified Company ...")). (Id. at HARBAP00004155.)

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- 21. Mr. Ergen, as a natural person, is not an Eligible Assignee and is not permitted to own the LP Debt.
- 22. "Disqualified Company" is defined in Section 1.01 as follows:

[A]ny operating company which is a direct competitor of the Borrower identified to the Administrative Agent in writing prior to the Closing Date and set forth on $Schedule\ 1.01(a)$, and thereafter, upon the consent of the Administrative Agent ... such additional bona fide operating companies which are direct competitors of the Borrower as may be identified to the Administrative Agent from time to time and notified to the Lenders. A Disqualified Company will include any known subsidiary thereof.

(PX0004 at HARBAP0004057–58.) The Credit Agreement thus prohibits assignment or other transfer of the LP Debt to a LightSquared competitor named on Schedule 1.01(a) or a known subsidiary of such a competitor.

- 23. The word "Subsidiary" in the definition section of the Credit Agreement is defined, "with respect to any person (the 'parent')," as including, "any other person that is otherwise Controlled by the parent...." (PX0004 at HARBAP0004073, § 1.01.) "Controlled" is defined to mean "the possession, directly or indirectly, of the power to direct or cause the direction of the management or policies of a person, whether through the ownership of voting securities, by contract or otherwise...." (*Id.* at HARBAP0004056, § 1.01.)
- 24. SPSO, SO Holdings, and Mr. Ergen were not initially included on Schedule 1.01(a) of the Credit Agreement, which, as of the inception of the Credit Agreement on October 1, 2010, did include EchoStar. (PX0004 at HARBAP00004166.)
- 25. On May 9, 2012, LightSquared amended the Disqualified Company list, Schedule 1.01(a) of the Credit Agreement, to add additional LightSquared competitors, including, among others, DISH. (PX0142.) On May 12, 2012, LightSquared again amended the Disqualified Company list to add Cablevision. (Jan. 16 Tr. (Falcone) 49:17–19; PX0901 at HARBAP00011331; see also PX0190.) Each of DISH and EchoStar is a Disqualified Company under the Credit Agreement. SPSO is not a "known subsidiary" of any company identified as a Disqualified Company.
- 26. According to its CEO, LightSquared amended the Disqualified Company list on May 9 and 12, 2012, immediately prior to the Petition Date, "to make sure that the list of disqualified companies included all of [LightSquared's] competitors, because we didn't want competitors involved in the capital structure. We thought it was important as we were entering bankruptcy to make these updates." (Jan. 9 Tr. (Smith) 126:22–127:24; PX0161.)
- 27. The Credit Agreement defines the term "Affiliate" as "when used with respect to a specified person, another person that directly, or indirectly through one or more intermediaries, Controls or is Controlled by or is under common Control with the person specified." (PX0004 at HARBAP00004050–4051.)
- 28. On September 18, 2010, UBS proposed a draft of the Credit Agreement which did not include the concept of a Disqualified Company, but rather stated that an Eligible Assignee "shall not include Borrower or any of its Affiliates or Subsidiaries, any natural person or any person listed on Schedule 1.01(a)." (PX0001 at L2AP0009323.) UBS's draft did not restrict transfers to affiliates or "Affiliates" of companies or persons listed on Schedule 1.01(a); it only restricted transfers to companies or persons listed in Schedule 1.01(a). (PX0001 at L2AP0009323.)
- 29. On September 19, 2010, counsel for LightSquared proposed comments to UBS's draft. LightSquared's draft restricted transfers of LP Debt to any "Affiliate" of a company or person listed on Schedule 1.01(a). (PX0003.) Specifically, the draft stated that an Eligible Assignee "shall not include Borrower or any of its Affiliates or Subsidiaries, any natural person or any Competitor." (PX0003 at L2AP0011786 (emphasis added).) It further stated, "Competitor' shall mean (i) any person listed on Schedule 1.01(a), (ii) any other competitor of the Borrower that is designated as such in writing

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to the Administrative Agent by the Borrower from time to time and (iii) any Affiliate of any such person." (PX0003 at L2AP0011784.) Therefore, in this draft, transfers were restricted to any person or company listed on Schedule 1.01(a) as well as their "Affiliates."

- 30. On September 21, 2010, counsel for UBS proposed revisions to LightSquared's September 19, 2010 draft. (PX0002.) Those revisions removed the transfer restriction on any Affiliate of a company listed on Schedule 1.01(a) and, instead, restricted transfers to any Disqualified Company and "any known subsidiary thereof." (PX0002 at L2AP0011532.) The language from this draft defining Eligible Assignee and Disqualified Company is what appears in the final, executed Credit Agreement. (PX0002 at L2AP0011532; PX0004 at HARBAP00004057–4058.)
- 31. LightSquared Inc.'s Fourth Amended and Restated Stockholders' Agreement includes the defined term "Affiliates" and prohibits the transfer of any equity securities to "any of the entities set forth in Schedule 2.1(a)(ii) or any of their respective Affiliates." (PX0007 at HARBAP00010483.) LightSquared did not include a similar restriction on the transfer of its bank debt under the Credit Agreement.
- 32. Persons holding LP Debt are entitled to receive substantial non-public information about LightSquared and are granted access to LightSquared's officers and employees for information regarding LightSquared's ongoing business and operations. Prior to initial funding, LightSquared provided to the Lenders, among other things, multiple years of financial statements, plus current forecasts of anticipated financial performance (PX0004 at HARBAP00004092–93, § 3.04); a listing of all interests in real property owned or leased by Borrower, together with representations regarding title, etc. (*id.* at HARBAP00004093–94, § 3.05); a listing of all copyrights, patents, and trademarks owned or licensed by Borrower, together with representations regarding same (*id.* at HARBAP00004094, § 3.06); and copies of all material agreements relating to the business operated by the Borrower (*id.* at HARBAP00004095–96, § 3.09.) Under the Credit Agreement, these disclosures must be updated regularly by the Borrower.
- 33. To meet this obligation, the Borrower must furnish to Lenders the type of information that would be included in annual and quarterly reports on SEC Forms 10–K and 10–Q (PX0004 at HARBAP00004108–9, §§ 5.01(a)-(b)), annual and quarterly budgets (*id.* at HARBAP00004110, § 5.01(h)), and "such other information regarding the operations, business *270 affairs and financial condition of [Borrower, its parents and its subsidiaries] ... as ... any Lender may reasonably request, including, without limitation, updates on the Network buildout." (*Id.* at HARBAP00004110, § 5.01(j).) Each Lender also has the right to inspect and make copies of Borrower's financial records; to inspect Borrower's properties; and to "discuss the affairs, finances, accounts and condition of [Borrower, its parents and its affiliates] with the officers and employees thereof and advisors therefor (including independent accountants)." (*Id.* at HARBAP00004113–14, § 5.07(a).)
- 34. The Credit Agreement also provides that each Lender must "designate at least one individual to receive Private Side Communications [i.e., communications containing material non-public information] on its behalf ... and identify such designee (including such designee's contact information) on such Lender's Administrative Questionnaire." (PX0004 at HARBAP00004149, § 10.01(d).) A Lender may elect not to receive material non-public information, but must, if so electing, waive "any and all claims based on or arising out of, not having access to Private Side Communications." (Id.)
- 35. SPSO did not waive its right to receive confidential information about LightSquared. To the contrary, SPSO specifically identified in the several Lender Questionnaires it provided to the Administrative Agent one or more persons to whom such information was to be delivered. (PX0198; PX0227; PX0282; PX0317; PX0362; PX0363; PX0365; PX0367; PX0411; PX0563; PX0618; PX0638; PX0658; PX0672; PX0728; PX0733; PX0849; PX0851.) Those individuals had access to information on LightSquared. (*See, e.g.*, PX0919–922.)

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36. Under the express terms of the Credit Agreement, LightSquared's rights under the Credit Agreement cannot be waived. Section 10.02(b) explicitly requires written consent by the parties before a party may be found to have waived the terms of the Credit Agreement:

Required Consents. Subject to Sections 10.02(c) and (d), neither this Agreement nor any other Loan Document nor any provision hereof or thereof may be waived, amended, supplemented or modified except, in the case of this Agreement, pursuant to an agreement or agreements in writing entered into by Borrower and the Administrative Agent or, in the case of any other Loan Document, pursuant to an agreement or agreements in writing entered into by the Administrative Agent, the Collateral Trustee (in the Case of any Security Document) and the Loan Party or Loan Parties that are party thereto, in each case with the written consent of the Required Lenders....

(PX0004 at HARBAP00004149-50.)

37. Section 10.04(a) of the Credit Agreement states that only those transferees permitted under the terms of the Credit Agreement receive any rights, remedies, or claims thereunder:

Nothing in this Agreement, expressed or implied, shall be construed to confer upon any person (other than the parties hereto, their respective successors and assigns permitted hereby, Participants to the extent provided in paragraph (d) of this Section and, to the extent expressly contemplated hereby, the other Indemnitees) any legal or equitable right, remedy or claim under or by reason of this Agreement.

(PX0004 at HARBAP0004153-54.)

- 38. Section 10.04(b) provides that "[a]ny assignment or transfer by a Lender of rights or obligations under this Agreement that does not comply with this paragraph *271 [relating to assignments] shall be treated for purposes of this Agreement as a sale by such Lender of a participation in such rights and obligations in accordance with Section 10.04(d)." (PX0004 ¶ 10.04(b).)
- 39. Section 10.04(d) provides that LightSquared "agrees that any breach by any Lender or participant or sub-participant of the restrictions on assignment hereunder (including, without limitation, to Disqualified Companies) shall not excuse, in any respect, performance by the Borrower under the Loan Documents." (PX0004 ¶ 10.04(d).)
- 40. Section 10.16 of the Credit Agreement states that "all obligations of the Loan Parties [the Borrower and Guarantors] hereunder shall be absolute and unconditional irrespective of ... any lack of validity or enforceability of any Loan Document or any other ... circumstance which might otherwise constitute a defense available to, or a discharge of, the Loan Parties." (PX0004 ¶ 10.16.)

III. Background Regarding SPSO's Purchases of LP Debt

A. Messrs. Ergen and Kiser Investigate Whether DISH and EchoStar Can Purchase LP Debt

- 41. In the fall of 2011, Mr. Ergen believed the spectrum and satellites of LightSquared might be an attractive investment opportunity for DISH and therefore began looking into acquiring LightSquared's LP Debt. (Jan. 13 Tr. (Ergen) 109:3–9; Jan. 10 Tr. (Kiser) 27:12–18.)
- 42. Mr. Ergen asked Mr. Kiser, the Treasurer of DISH and a Vice President of Corporate Development at DISH and EchoStar, to provide him with information concerning a potential purchase by DISH of LightSquared's LP Debt. (Jan. 10 Tr. (Kiser) 27:19–28:5, 32:25–33:11, 77:7–18; Jan. 13 Tr. (Ergen) 25:4–18, 32:15–33:14, 112:10–113:23, 129:21–130:24.) Mr. Ergen stated that, when Mr. Kiser was first asked to check whether DISH could own the LP Debt, Mr. Kiser was acting in his capacity as Treasurer of DISH. (Jan. 13 Tr. (Ergen) 112:10–113:13; PX0832 at 88–89.) Mr. Kiser testified

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that when he initially inquired into who could purchase the LP Debt—and until it was clear that the companies could not purchase the debt—the LightSquared investment was considered a corporate opportunity for DISH and EchoStar. (Jan. 10 Tr. (Kiser) 32:25–34:7.)

- 43. Indeed, at the time when Messrs. Ergen and Kiser investigated purchasing the LP Debt, their roles and responsibilities at DISH and EchoStar included identifying potential investments and acquisitions for both companies. (Jan. 10 Tr. (Kiser) 68:24–69:9; Jan. 13 Tr. (Ergen) 95:6–24.)
- 44. After Mr. Ergen's initial request to determine whether DISH could purchase LP Debt, Mr. Kiser compiled information on LightSquared's spectrum and capital structure, which he shared with Mr. Ergen. (Jan. 10 Tr. (Kiser) 28:6–17.)
- 45. After providing this information to and discussing this information with Mr. Ergen, Mr. Kiser continued his examination into whether DISH and EchoStar could buy the LP Debt. (Jan. 10 Tr. (Kiser) 28:18–21.) To that end, Mr. Kiser sought and obtained Mr. Ergen's permission to retain Sound Point to facilitate purchases of the LP Debt and asked Sound Point's founder, Mr. Ketchum—a longtime investment banker for EchoStar who had worked with Mr. Kiser for over twenty years on EchoStar and DISH-related transactions—if DISH was permitted to purchase the LP Debt. (Jan. 15 Tr. (Ketchum) 14:19–22; PX0116 at LSQ- *272 SPCD-000000904; Jan. 13 Tr. (Ergen) 32:15–25; Jan. 10 Tr. (Kiser) 25:19–22.)
- 46. Mr. Ketchum acknowledged that the LightSquared transactions were the first time in twenty years of working with Mr. Kiser on behalf of DISH and EchoStar that he was asked to handle a personal investment for Mr. Ergen. (Jan. 15 Tr. (Ketchum) 13:22–25, 14:19–22, 94:4–7.)
- 47. At Mr. Kiser's request, Mr. Ketchum reviewed the Credit Agreement and determined that neither EchoStar nor DISH was eligible to purchase the LP Debt. (Jan. 10 Tr. (Kiser) 28:18–29:9, 78:18–79:1; Jan. 13 Tr. (Ergen) 32:22–25; Jan. 15 Tr. (Ketchum) 49:23–50:19, 95:10–14.)
- 48. Subsequently, Mr. Kiser consulted with Sullivan and Cromwell LLP ("Sullivan & Cromwell"), outside counsel to DISH and EchoStar, to determine whether DISH could purchase the LP Debt, providing Sullivan & Cromwell with excerpts from the Credit Agreement. (Jan. 10 Tr. (Kiser) 29:10–30:3, 118:14–18, 120:2–4; Jan. 13 Tr. (Ergen) 32:15–33:5.) No counsel other than Sullivan & Cromwell, including in-house counsel for DISH, in-house counsel for EchoStar, or counsel for Mr. Ergen and SPSO, were consulted on this issue. (Jan. 13 Tr. (Ergen) 32:15–33:3, 114:17–23, 180:23–181:2, 198:17–21; Jan. 10 Tr. (Kiser) 28:18–29:19, 78:24–79:22.)
- 49. After reviewing the Credit Agreement and consulting with Sound Point and Sullivan & Cromwell, Mr. Kiser determined that both DISH and EchoStar were restricted from buying the LP Debt, and communicated this to Mr. Ergen. (Jan. 10 Tr. (Kiser) 29:10–15, 30:4–9, 78:24–80:3, 121:8–22.)
- 50. In the fall of 2011, when Mr. Kiser, Mr. Ketchum, and Sullivan & Cromwell initially determined that both DISH and EchoStar were prohibited from purchasing the LP Debt under the terms of the Credit Agreement, only EchoStar—but not DISH—was listed as a Disqualified Company on Schedule 1.01(a) of the Credit Agreement. (PX0004 at HARBAP00004166; PX0144; PX0151; Jan. 15 Tr. (Ketchum) 50:9–51:2.) DISH was subsequently added to the list of Disqualified Companies in May 2012. (PX0142.)

B. Messrs. Ergen and Kiser Create the Bal Harbour Entities, and Then SPSO, to Purchase LP Debt

51. After learning that DISH was prohibited under the Credit Agreement from purchasing the LP Debt, Mr. Kiser nonetheless asked Sound Point to monitor the prices and volume of the LP Debt. (Jan. 10 Tr. (Kiser) 30:4–9.)

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- 52. In January, February, and March 2012, Mr. Ergen was seeking to acquire LP Debt for 40 cents on the dollar or less. (Jan. 10 Tr. (Kiser) 41:6–15; Jan. 13 Tr. (Ergen) 39:24–40:3; DX011; DX016; DX018; DX019; DX022; PX0021.) During that time, Mr. Kiser was monitoring the price of the debt for Mr. Ergen, but the debt was not yet trading at a price at which Mr. Ergen wanted to buy. (Jan. 10 Tr. (Kiser) 39:18–41:1, 42:24–43:15; DX011; DX016; DX018; DX019; DX022; PX0021; PX0032.)
- 53. On or after May 9, 2012, Messrs. Ergen, Kiser, and Ketchum were aware that the Credit Agreement prohibited competitors DISH and EchoStar from purchasing the LP Debt. In a May 9, 2012 email, Mr. Ketchum reported to Mr. Kiser that "[a]n amendment was just created whereby DISH Network Corp., DBSD, Clearwire, DirecTV, XM Satellite Radio Inc. were named as disqualified buyers." Mr. Ketchum specifically pointed out that "Charlie is not named." (PX0144.) The following day, Mr. Ketchum sent Mr. Kiser *273 the original list of Disqualified Companies, as well as the exact language of the amendment. (PX0151; PX0155; cf. PX0190.) The copy of the amendment that Mr. Ketchum sent to Mr. Kiser included a handwritten note circling the term "Disqualified Company," explaining that this term "includes any known subsidiary thereof." (PX0155 at SPSO-00001608.) Mr. Ketchum understood the term "subsidiary" to include any corporate entity controlled by a designated Disqualified Company. (Jan. 15 Tr. (Ketchum) 52:18–53:16; PX0155.)
- 54. Mr. Kiser further inquired of Sullivan & Cromwell in 2011 whether there were other ways for DISH or EchoStar to take advantage of "the LightSquared opportunity." (Jan. 10 Tr. (Kiser) 81:18–82:5.) Mr. Kiser discussed with Sullivan & Cromwell whether an investment vehicle could buy the LP Debt. (Jan. 10 Tr. (Kiser) 30:10–12.) Mr. Ergen testified that "[w]hen I talk to lawyers it's ... more about, you know, how can I do this, as opposed to what the law says." (PX0866; Jan. 13 Tr. (Ergen) 199:4–7.)
- 55. No evidence was submitted demonstrating any exploration of the possibility of DISH or EchoStar purchasing the LP Debt through an "affiliate," nor any analysis of the possible corporate opportunity involved with such a structure.
- 56. Given the transfer restrictions in the Credit Agreement, if DISH and EchoStar could not buy LP Debt, then Mr. Ergen determined that he had an interest in "personally" purchasing the debt. (Jan. 10 Tr. (Kiser) 33:9–15, 77:11–18.) Accordingly, Mr. Kiser consulted with Sullivan & Cromwell to determine whether Mr. Ergen could buy the LP Debt, after which he understood that this would not work either, because the Credit Agreement barred Mr. Ergen and all other "natural persons" from buying the LP Debt. This led him to set up an investment vehicle. (Jan. 10 Tr. (Kiser) 30:16–21, 80:4–6, 120:20–24.)
- 57. Mr. Kiser structured the LP Debt purchases through a special purpose vehicle ("SPV"), initially directing the creation of two companies, Bal Harbour Capital Management LLC ("Bal Harbour Capital") and Bal Harbour Holdings, LLC (together with Bal Harbour Capital, the "Bal Harbour Entities"). (Jan. 10 Tr. (Kiser) 30:16–31:4, 87:3–8.) The Bal Harbour Entities were incorporated in December 2011. (DX046; see also Delaware Department of State, Division of Corporations website (http://corp.delaware.gov/).)
- 58. After the Bal Harbour Entities had been formed, Mr. Kiser realized that a Littleton, Colorado address had been used in its formation documents. Mr. Ergen resides in Littleton, which is near Englewood, Colorado, where DISH and EchoStar are headquartered. (Jan. 10 Tr. (Kiser) 32:2–14, 35:21–24; Jan. 13 Tr. (Ergen) 36:13–20.) Concerned that the Colorado address would compromise Mr. Ergen's anonymity, Mr. Kiser directed Sound Point to create new SPVs to replace the Bal Harbour Entities. (Jan. 10 Tr. (Kiser) 32:2–14, 90:6–12, 91:12–20; Jan. 13 Tr. (Ergen) 35:24–36:6, 36:21–37:4, 49:20–50:25; PX0117.)
- 59. Mr. Ketchum suggested to Mr. Kiser that the new entity's name be SP Special Opportunities, LLC—a name suggesting Sound Point ownership. (PX0165.) Following Mr. Ketchum's suggestion, Mr. Kiser directed Sound Point to set up SPSO and SO Holdings on May 16, 2012. (PX0221; PX0183; Jan. 10 Tr. (Kiser) 31:10–32:1, 91:9–11.)

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- The capital structure of SPSO and SO Holdings was set up to mirror that of the Bal Harbour Entities. (PX0224; PX0221; PX0058.)
- *274 60. Rather than listing a Colorado address, the SO Holdings and SPSO formation documents listed a Delaware address. (PX0183 at SPSO-00000512, SPSO-00000514.) As Mr. Kiser testified, SPSO's address was specifically chosen to deflect any possible connection between Mr. Ergen and Sound Point's purchases of the LP Debt. (Jan. 10 Tr. (Kiser) 32:2-14.)
- 61. It was important to Messrs. Ergen and Kiser that the public not know they were behind Sound Point's purchases. (Jan. 10 Tr. (Kiser) 30:16–21, 31:20–22, 32:2–14, 90:25–91:20; Jan. 13 Tr. (Ergen) 36:13–20; PX0171; PX0183; PX0224; PX0290 at LSQ–SPCD–000006771; PX0298.)
- 62. SPSO's first trade in LightSquared debt was made on April 13, 2012, at a price of 48.75 cents on the dollar. (Jan. 10 Tr. (Kiser) 35:25–36:13; Jan. 13 Tr. (Ergen) 42:16–18; PX0859.) The second trade was executed on May 3, 2012, at 59 cents on the dollar. (PX0859.)
- 63. On May 4, 2012, SPSO entered into a trade for a \$247 million block of LP Debt, paying approximately \$149 million. (PX0859.) Between April 13 and May 4, 2012 (prior to LightSquared's Petition Date on May 14, 2012), SPSO purchased a total of approximately \$287 million in face amount of LP Debt. These initial purchases were made at prices between 48.75 cents and 60.25 cents on the dollar and cost Mr. Ergen a total of approximately \$172 million. (PX0859.)
- 64. Following SPSO's purchase of the \$247 million piece of debt, news reports speculated that Mr. Ergen was the purchaser of the debt. (Jan. 10 Tr. (Kiser) 37:5–13.) On May 7, 2012, a *Reuters* story on the trade mentioned that Mr. Steven Ketchum of Sound Point previously counted Mr. Ergen as one of his investment banker clients and that DISH owned wireless airwaves "similar to LightSquared." (PX0121.) On May 9, 2012, an *LCD News* story carried the headline, "LightSquared TL trades north of 70 as Ergen enters the picture." (DX045.) On May 10, 2012, a *Wall Street Journal* blog, "Deal Journal," published an entry titled "Ergen Builds Cash Pile Amid LightSquared Restructuring Talks." (DX396.) Following the publication of those articles, the price of LightSquared's debt increased. (PX0859; DX047.)
- 65. Mr. Ergen testified that when he started buying LightSquared debt, he did not have an idea of how much debt SPSO would eventually buy, and he was not interested in achieving a "blocking position" in the debt. (Jan. 13 Tr. (Ergen) 43:17–44:8.)
- 66. Even after creating the Bal Harbour Entities and SPSO and purchasing large quantities of LP Debt, Messrs. Ergen and Kiser continued to check whether DISH or EchoStar could purchase the LP Debt directly. (PX0243.) On October 4, 2012, Mr. Kiser wrote to Mr. Ergen, "I still can't get confirmation the restricted list [LightSquared] had in place that prevented the company from buying them has fallen away due to the BK." (*Id.*) The same day, Mr. Ergen responded, "[i]f we can't be sure the company can buy them, then I am interested to increase my position at the 75 level at least up to a 33% ownership level of the class." (*Id.*)
- 67. Mr. Ergen and Mr. Kiser checked the restrictions again in order to understand whether LightSquared's bankruptcy filing had altered any of the restrictions, such that DISH could now purchase LP Debt. (Jan. 13 Tr. (Ergen) 240:23–241:14.) Nevertheless, Mr. Ergen believed that it was not worth contacting the banks and undermining his anonymity to determine whether the transfer restriction had in fact *275 fallen away. (Jan. 13 Tr. (Ergen) 49:14–50:13.)

C. SPSO and Mr. Ketchum Did Not Reveal that Mr. Ergen Was Behind the LP Debt Purchases

68. Sound Point endeavored not to disclose SPSO's connection to Mr. Ergen. For example, on May 2, 2012, Mr. Ketchum advised a Sound Point employee that "EchoStar wants up to \$50mm LightSquared," and asked him to reach out to

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Seaport, a middleman, but directed that "we can't tip our hand." The employee replied, "Yeah, i haven't indicated anything to anyone." (PX0088.) The following day, the employee reported that he spoke with Seaport and noted that Kevin Gerlitz, another Sound Point employee, was concerned that the trade would show Bal Harbour Capital as the buyer in the documentation. The employee asked, "Will this create problems?" Mr. Ketchum responded, "Possibly. Sh*t." (PX0089.) Indeed, Sound Point was not even willing to disclose the identity of the buyer to Jefferies as the middleman, even if Jefferies created an ethical wall. (PX0100.)

69. A few days later, on May 5, 2012, Mr. Ketchum sent an email to Mr. Kiser describing a voicemail he received from a *Wall Street Journal* reporter regarding Sound Point, stating he was "obviously" not going to call the reporter back, even though he "clearly didn't understand what Sound Point is." (PX0119.) Mr. Ketchum further noted that the reporter "did not mention Charlie or EchoStar" in his voicemail. (*Id.*) Mr. Kiser forwarded Mr. Ketchum's email to Mr. Ergen, explaining that Mr. Kiser had spoken to Mr. Ketchum about the issue and that "[t]here might just be a lot of people fishing all over the place based on speculation (they're [sic] weren't a lot of other logical buyers)." (*Id.*)

70. Similarly, on May 7, 2012, after receiving a press inquiry, Mr. Ketchum reached out to Mr. Kiser and asked whether they should "employ a more strenuous strategy" around denying to the press that Mr. Ergen was behind SPSO. (PX0124.) Additionally, email exchanges demonstrate Messrs. Ketchum and Kiser making light of the fact that there were rumors in the press indicating that Carlos Slim ("*Slim*") was behind Sound Point's purchases of the LP Debt, noting that Mr. Ketchum would "continue to get looks" because he's "Carlos Slim's main man" and that a news report suggesting it was Slim and not Ergen was "[m]aybe [] right." 9 (See PX0271; PX0216; Jan. 15 Tr. (Ketchum) 91:20–92:3.)

Garlos Slim is the principal of the Mexican telecommunications companies Telmex Internacional and America Movil (PX0895 (Cellular News, *America Movil, Telmex to Invest \$880 Mn in Peru Through 2012,* (Apr. 18, 2010), available at http://www.cellular-news.com/story/42891.php (last visited Feb. 24, 2014)).)

IV. SPSO is Solely a Front for Mr. Ergen

71. Further evidencing that Sound Point viewed SPSO as being identical to Mr. Ergen, Sound Point entered into a Trading Management Agreement with SPSO on April 15, 2012—a month before SPSO and SO Holdings were even formed. ¹⁰ (PX0055 at LSQ–SPCD– *276 00000750; Jan. 15 Tr. (Ketchum) 18:22–25, 99:9–19; PX0221.) Mr. Ketchum could not recall another instance where he entered into a Trading Management Agreement with an entity that had not yet been formed. (Jan. 15 Tr. (Ketchum) 19:5–10; PX0049; PX0083; PX0084; PX0087; PX0088; PX0224.) Mr. Ketchum knew he was dealing with Mr. Ergen and had no doubt that Mr. Ergen had the financial wherewithal to fund the trades.

On April 5, 2012, Bal Harbour Capital entered into a trading management agreement with Sound Point, granting Sound Point non-discretionary authority to execute trades on its behalf. (PX0131 at LSQ-SPCD000011949; Jan. 15 Tr. (Ketchum) 15:5–14.) Bal Harbour Capital was initially capitalized with one dollar (\$1.00) and itself had no right to secure additional funding. (Jan. 15 Tr. (Ketchum) 19:18–25; PX0058 at LSQ-SPCD000012134; PX0147 at SPSO-00001602; Ergen Dep. 120:2–10.) Under Bal Harbour Capital's Limited Liability Company Agreement, Mr. Ergen had no obligation to make further capital contributions beyond the initial one dollar capital contribution (PX0058 at LSQ-SPCD-000012127 ("[T]he Managing Member shall have no right or obligation to make any further capital contributions in the Company.").)

A. SPSO was Undercapitalized and Funded Solely at Mr. Ergen's Discretion

72. SPSO is wholly owned by its one Managing Member, SO Holdings, and Mr. Ergen wholly owns and is the sole Managing Member of SO Holdings. ¹¹ (PX0221 at LSQSPCD-000005552, 5557, 5560, 5565; Jan. 10 Tr. (Kiser) 31:15–19.)

The Bal Harbour Entities also were solely owned by Mr. Ergen. (PX0058 at LSQ-SPCD-000012124; PX0059 at SPSO-00000396.)

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- 73. SPSO—the vehicle on behalf of which most of the LP Debt trades were initiated and all of the trades closed—was formed with a *de minimis* amount of funding. (Jan. 10 Tr. (Kiser) 56:22–57:6; Jan. 13 Tr. (Ergen) 127:20–25; PX0529; PX0530; PX0560; PX0859.) The operating agreements for both SPSO and SO Holdings require that the Managing Member—Mr. Ergen—make an initial capital contribution of ten dollars (\$10.00) for each entity. (PX0221 at LSQ—SPCD–000005553, 5558, 5561, 5566; Jan. 15 Tr. (Ketchum) 18:5–21.) Mr. Ergen testified that this initial contribution to SPSO "wasn't very much," (Jan. 10 Tr. (Ergen) 127:18–25), and Mr. Kiser ignored Mr. Ketchum's recommendation, based on advice from Sound Point's CFO, that Mr. Ergen's other SPV, Bal Harbour Capital, be capitalized initially with \$500,000. (Jan. 10 Tr. (Kiser) 87:24–88:3.)
- 74. Neither the SPSO operating agreement nor SO Holdings operating agreement requires additional capital contributions from Mr. Ergen as Managing Member. (PX0221 at LSQ-SPCD-000005553, 5561 ("[t]he Managing Member is entitled, but not required, to make additional contributions to the capital of the Company").)
- 75. Bear Creek Asset Management LLC ("Bear Creek") is a registered investment advisor that manages fixed-income instruments for high-net-worth individuals and corporations. (Roddy Dep. 17:8–11.) Bear Creek manages DISH's and EchoStar's corporate cash in short-term investment accounts. (Jan. 10 Tr. (Kiser) 22:1–9; Jan. 13 Tr. (Ergen) 24:14–15; Roddy Dep. 43:3–14.) Bear Creek also manages a substantial amount of Mr. Ergen's personal assets. (Jan. 10 Tr. (Kiser) 22:9–13; Jan. 13 Tr. (Ergen) 24:11–13.)
- 76. Mr. Ergen was the only person who could make the decision to transfer funds from his account at Bear Creek to Bal Harbour Capital or SPSO for settlement of the LightSquared trades. (Jan. 10 Tr. (Kiser) 57:7–58:12, 87:13–19; Jan. 15 Tr. (Ketchum) 99:9–19; PX0046; PX0055; PX0116 at LSQ–SPCD–000000905 (Mr. Ergen had "full discretion over the investment decisions" in his accounts at Sound Point); Jan. 10 Tr. (Kiser) *277 24:6–9 (Mr. Ergen "makes his own decision" with respect to his investments).)
- 77. The initial capital contribution amounts for SPSO and SO Holdings were insufficient to buy a significant amount of LP Debt. (Jan. 15 Tr. (Ketchum) 18:8–21, 20:4–13.)
- 78. Although Mr. Ketchum knew that the Bal Harbour Entities and SPSO did not have sufficient funds in their accounts to cover the purchases of LP Debt prior to the closing of the trades, Mr. Ketchum did not perform a credit check with respect to SPSO and did not have an understanding of SPSO's financial resources or wherewithal. (Jan. 15 Tr. (Ketchum) 20:18–25; PX0062; PX0066; PX0070.)
- 79. Sound Point nevertheless traded on behalf of Mr. Ergen's minimally-funded entities because Mr. Ketchum understood that the entities were backstopped by Mr. Ergen. (PX0052; PX0056; PX0058; PX0059; PX0074.) For instance, on April 13, 2012, Sound Point initiated a \$5 million LP Debt trade for Bal Harbour Capital, even though at that time the Bal Harbour account had not yet been funded. (PX0859; PX0066; PX0049; PX0050; PX0062; PX0070.) On April 17, 2012, Mr. Ketchum wrote to Kiser that, "[w]e need to get the Citi account open for BH Holdings and get \$500,000 in the account before we do any more LightSquared trades." (PX0066.)
- 80. Mr. Ketchum testified that Sound Point was "comfortable" that Mr. Ergen would pay for SPSO's LightSquared debt purchases because "[i]t was implicit that if we executed a trade, SPSO would pay to settle the trade." Sound Point understood that this money would come from Mr. Ergen, and Mr. Ketchum stated that Sound Point was satisfied that the trades would be settled based on Mr. Ergen's credit rather than SPSO's credit. (Jan. 15 Tr. (Ketchum) 21:1–22:8, 120:13–16; Jan. 10 Tr. (Kiser) 57:7–59:5, 61:5–9, 74:11–19; DX229; PX0041; PX0052 at LSQSPCD–000005238 (documentation for Bal Harbour BNP Paribas account stated that Mr. Ergen had "\$100 million +" of liquid net worth); PX0091; PX0116 at LSQ–SPCD–00000904.)

B. SPSO Votes Against Extension of LightSquared's Negotiations with Lenders

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81. In early 2012, both Messrs. Ergen and Kiser knew that there was a strong possibility that LightSquared would file for bankruptcy. (See, e.g., PX0033 (February 20, 2012 email from Mr. Cullen to Messrs. Ergen and Kiser enclosing article on LightSquared's default on \$56 million payment to Inmarsat); PX0075 (April 27, 2012 email from Mr. Cullen to Mr. Kiser enclosing Wall Street Journal article discussing bankruptcy as an imminent possibility); PX0078 (April 30, 2012 email from Mr. Kiser to Mr. Ergen enclosing Wall Street Journal article discussing Mr. Falcone's attempt to get a one week "extension on default"); PX0121 (May 7, 2012 email from Mr. Cullen to Messrs. Ergen and Kiser enclosing Reuters story noting LightSquared's "uncertain future" and the possibility of a default); PX0163 (May 11, 2012 email from Mr. Kiser to Mr. Ergen enclosing Debtwire article suggesting LightSquared could file for bankruptcy).)

82. Throughout early 2012, Mr. Ketchum kept Mr. Kiser apprised as he monitored LightSquared's situation. (PX0031; PX0039; PX0044; PX0064; PX0074.) On May 4, 2012—prior to LightSquared's bankruptcy filing—SPSO was notified that, in connection with the \$247 million in LP Debt that SPSO had agreed to purchase but had not yet closed on, it had the right to vote on a proposed amendment to the Credit Agreement that would give LightSquared more time to attempt to *278 reach an agreement with the LP Lenders and avoid bankruptcy. In an email on Friday, May 4, 2012, Mr. Kiser wrote to Mr. Ergen, in part, that "[t]he seller is inclined to vote to approve this one week extension of time to continue negotiations, and so if the buyer does not direct the seller to the contrary, that is how the seller will vote." (Jan. 10 Tr. (Kiser) 111:13–112:5; PX0111.) The amendment was due several days later, on Monday, but responses were sought before the weekend if possible. (PX0097.) Mr. Ergen replied to Mr. Kiser's email, "I would have them vote no." (Jan. 10 Tr. (Kiser) 113:13–15, 113:23–25; Jan. 13 Tr. (Ergen) 166:1–167:16; PX0111.) Following Mr. Ergen's direction, Mr. Kiser directed Sound Point to vote "no" on the amendment. (Jan. 10 Tr. (Kiser) 116:18–117:21; PX0097; PX0109.) A Sound Point employee relayed these instructions to Mr. Ketchum, commenting "[n]o extension, so they want it to file bankruptcy." Mr. Ketchum replied, "[n]o surprise there." (PX0096.)

83. While Mr. Ergen testified that he determined to vote "no" because he did not have the documents necessary to decide how to vote (Jan. 13 Tr. (Ergen) 166:1–167:16, 261:13–263:8), the record reflects that the amendment documents likely could have been obtained by Sound Point, had Messrs. Ergen and/or Kiser indicated an interest in reviewing them over the weekend. When a Sound Point employee told Mr. Kiser that "I might have figured out a way to get the docs ... please stand by," Mr. Kiser simply responded "[w]e'll vote no." (PX0097; PX0096.) Mr. Kiser also conceded that, before voting no, he made no effort to discuss with any of the LP Lenders why they wanted to extend the default deadline. (Jan. 10 Tr. (Kiser) 118:10–13; PX0097.) After seeing the email exchanges between Messrs. Kiser and Ketchum concerning the availability of the amendment documents, Mr. Ergen testified, "I'm disappointed that [Kiser] answered no.... That's not the way I would have done it...." (Jan. 13 Tr. (Ergen) 262:13–263:8.)

C. SPSO's LP Debt Purchases

84. Mr. Ergen funded SPSO's debt purchases from his personal account at Bear Creek. None of the money used to fund SPSO's purchases of LightSquared debt came from DISH or EchoStar. (Jan. 13 Tr. (Ergen) 59:11–12; Jan. 10 Tr. (Kiser) 57:18–23; Rayner Dep. 23:14–24:2, 24:13–23; Olson Dep. 14:6–15:14.)

85. Mr. Robert Olson, DISH's Chief Financial Officer ("Olson"), testified that if DISH money had been used to fund the trades, he would have known because DISH's controller, Paul Orban, would need to approve the transactions. (Olson Dep. 14:10–15:14.)

86. Mr. Ergen's Bear Creek account that was used to fund SPSO's trades in LightSquared debt is titled the "Lindsey Revocable Trust" account (Jan. 10 Tr. (Kiser) 58:13–17; Roddy Dep. 17:24–18:8; DX326), and was set up in 2000 for estate planning purposes. (Jan. 13 Tr. (Ergen) 61:17–23, 62:7–8.) Mr. Ergen is its sole beneficiary and is authorized to make investments for the trust, and his wife, Cantey Ergen, is a co-trustee. (Jan. 13 Tr. (Ergen) 61:17–23, 62:7–8, 252:18–20.) Bear Creek understood that the Lindsey Revocable Trust was a personal trust account for Mr. Ergen. (Roddy Dep. 17:24–18:8.)

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87. Mr. Ergen does not have an agreement or understanding with DISH regarding SPSO's investment in LightSquared debt, and he understands that the money he personally invested in LightSquared debt is at risk. (Jan. 13 Tr. (Ergen) 233:6–16.) Thus, if SPSO's claim in *279 LightSquared receives an impaired recovery, Mr. Ergen bears the sole risk. (Jan. 13 Tr. (Ergen) 233:6–16.) In addition, there is no agreement pursuant to which DISH or EchoStar will share in any gains from SPSO's investments. Mr. Olson confirmed that there are no agreements between Mr. Ergen and DISH related to Mr. Ergen's purchases of LightSquared debt. (Olson Dep. 26:7–27:11.)

88. Between April 13, 2012 and April 26, 2013, SPSO contracted to purchase over \$1 billion in face amount of LP Debt, of which it actually closed trades for \$844,323,097.83 in face amount. When a trade was scheduled to close, Mr. Kiser would contact Bear Creek and tell it how much money was needed to close the trade. (Jan. 10 Tr. (Kiser) 21:23–22:13; 57:7–17.) Mr. Ergen would then authorize the wire transfer and Bear Creek would liquidate investments to fund the transfer. (Jan. 10 Tr. (Kiser) 21:23–22:13, 57:7–17.)

89. The following chart sets forth SPSO's trades in LP Debt, including the trade and closing dates, par amount, purchase price, cost, broker, and settlement status:

Trade Date	Closing Date	Par	Price	Cost	Counterparty	Status
04/13/12	09/06/12	5,000,000.00	48.750	2,437,500	UBS	Settled
05/03/12	07/23/12	4,545,500.00	59.00	2,681,845	Jefferies	Settled
05/03/12	07/26/12	20,000,000.00	59.250	11,850,000	Seaport	Settled
05/03/12	09/06/12	3,000,000.00	58.750	1,762,500	UBS	Settled
05/03/12	09/06/12	2,000,000.00	58.500	1,170,000	UBS	Settled
05/03/12	07/23/12	5,000,000.00	59.000	2,950,000	Jefferies	Settled
05/04/12	05/31/12	247,259,046.62	60.250	148,973,576	Jefferies	Settled
10/04/12	11/30/12	19,417,287.99	78.500	15,242,571	Jefferies	Settled
10/23/12	02/06/13	3,000,000.00	83.750	2,512,500	UBS	Settled
11/15/12	01/08/13	7,997,057.00	81.750	6,537,594	Jefferies	Settled
12/12/12	6/11/13	2,000,000.00	84.000	1,680,000	Goldman Sachs	Settled
12/13/12	03/12/13	7,000,000.00	86.000	6,020,000	Jefferies	Settled
12/20/12	04/09/13	14,782,302.32	85.500	12,934,515	UBS	Settled
12/28/12	03/13/13	15,000,000.00	88,500	13,275,000	Jefferies	Settled
01/02/13	03/07/13	20,000,000.00	89.125	17,825,000	Jefferies	Settled
01/02/13	04/05/13	6,000,000.00	89.125	5,347,500	Jefferies	Settled
01/03/13	03/07/13	17,999,999.97	89.250	16,065,000	Jefferies	Settled
01/07/13	05/24/13	7,000,000.00	89.500	6,265,000	Jefferies	Settled
01/14/13	05/24/13	9,410,420.00	91.500	8,610,534	Jefferies	Settled

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(02/01/13	07/23/13	20,000,000.00	91.875	18,375,000	JPM	Settled
(03/25/13	05/24/13	88,262,536.00	93.375	84,180,394	Jefferies	Settled
(03/28/13	-	168,759,227.85	96.000	162,008,859	Jefferies	Unsettled
(04/01/13	6/25/13	5,500,000.00	96.000	5,280,000	Seaport	Settled
(04/19/13	6/14/13	122,250,172.79	96.000	117,360,166	Jefferies	Settled
(04/26/13	6/18/13	145,712,408.57	96.000	139,883,912	Jefferies	Settled
(04/26/13	6/18/13	46,186,366.57	96.00	44,338,912	Jefferies	Settled
Tota	l Purchased		1,013,082,326.30	84.45	855,567,877		
То	tal Settled		844,323,097.83		693,559,018		Settled
Tota	al Unsettled		168,759,227.85				Unsettled

^{*280 (}See PX0859 at 4.)

D. Mr. Ergen's Desire to Obtain a Blocking Position in LP Debt

- 90. Mr. Ergen's strategy in acquiring LP Debt included the acquisition of a blocking position that would enable SPSO to enforce "certain rights" during the bankruptcy proceeding. (Jan. 10 Tr. (Kiser) 47:22–48:10, 56:11–14; Jan. 13 Tr. (Ergen) 172:10–174:2; DX047.)
- 91. Mr. Ergen understood that creditors could be treated differently as a result of his investments in Loral, which went through a bankruptcy process. Mr. Ergen ended up with equity while other investors ended up with cash. (Jan. 13 Tr. (Ergen) 52:6–11.) Based on that experience, Mr. Ergen believed that 33 percent was a "meaningful percentage in bankruptcy," and that with that percentage, he "couldn't get jammed with a different kind of currency than somebody else in that class might get." ¹² (Jan. 13 Tr. (Ergen) 51:12–18, 172:25–173:3.) Mr. Ergen had a sizeable enough position in LightSquared to protect that he decided to acquire a blocking position; he stated that he "knew there were ways that [he] might be able to protect [his] investment if [he] got a third that [he] wouldn't have if [he had] half of that." (Jan. 13 Tr. (Ergen) 51:12–24.)
- Mr. Kiser understood that a blocking position is desirable and protects one's investment by preventing others from unilaterally changing one's rights. (Jan. 10 Tr. (Kiser) 54:11–17.)
- 92. At Mr. Ergen's direction, Mr. Kiser (through Sound Point) regularly monitored how close SPSO was to reaching a blocking position and kept a close eye on developments in the bankruptcy itself. (*See* PX0244; PX0264; PX0276; PX0288; PX0289; PX0375; PX0379; PX0306; Jan. 15 Tr. (Ketchum) 102:7–12; *see also* PX0064; PX0096; PX0413; PX0239; PX0344; PX0262.) ¹³
- Although Mr. Ketchum initially testified that he did not recall discussing acquiring a blocking position with Mr. Kiser, he later admitted that Mr. Kiser told him that "he was very interested in tracking whether or not SPSO had a blocking position with respect to LightSquared." (Jan. 15 Tr. (Ketchum) 102:7–12.)
- 93. After Mr. Ergen decided to acquire a 33 percent stake in the LP Debt, Mr. Kiser asked Mr. Ketchum to track whether SPSO had a blocking position and to supply Mr. Kiser with the information about the calculation of a blocking position.

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(Jan. 15 Tr. (Ketchum) 102:7–16; 25:11–26:18, 48:19–25, 102:7–12, 104:16–21; PX0244; PX0144.) Notwithstanding such request, Mr. Kiser did not share SPSO's investment strategy with Mr. Ketchum. (Jan. 15 Tr. (Ketchum) 102:7–16.)

94. On March 28, 2013—the date on which Messrs. Ergen and Kiser believed they had achieved their goal of obtaining a blocking position—Mr. Ketchum sent an email to Mr. Kiser, stating "You just bought a spectrum company." Later in that same email chain, Mr. Ketchum observed to one of his colleagues that "we now control the company." (PX0385.)

V. Mr. Ergen Acted, at Least in Part, for the Benefit of DISH in Acquiring LP Debt Through SPSO

95. In the course of amassing a substantial position in LP Debt, Mr. Ergen used DISH's employees, resources, facilities, and counsel. Members of the DISH and EchoStar boards and DISH's management also were made aware of Mr. Ergen's purchases; there was no evidence presented reflecting any action or investigation by the DISH Board with respect to SPSO's LP Debt trades.

*281 96. It is within the scope of Mr. Ergen's broad authority to lead strategic acquisitions of spectrum assets for DISH and EchoStar. (Jan. 10 Tr. (Kiser) 69:3–6, 69:23–70:9; Jan. 13 Tr. (Ergen) 95:6–16, 96:15–24; Howard Dep. 33:25–34:12; see also PX0010.) Mr. Ergen, as the Chairman of the Boards of DISH and EchoStar, is an officer and a full-time, salaried employee of DISH and EchoStar. (Jan. 13 Tr. (Ergen) 11:13–14, 94:4–18, 94:8–18; PX0349 at 20, 31; PX0350 at 17, 34.) In that capacity, Mr. Ergen "focus[es] on [the] strategic direction of the company" which includes acquisitions and strategic investments. (Jan. 13 Tr. (Ergen) 95:6–16; Jan. 10 Tr. (Kiser) 69:3–9; Howard Dep. 33:25–34:11; see also PX0010.) His responsibilities include the strategic pursuit of spectrum assets, which Mr. Ergen sees as necessary to compete with the large wireless carriers, to further DISH's strategic goal of diversifying away from its core Pay–TV business. (Jan. 10 Tr. (Kiser) 70:10–19; Jan. 13 Tr. (Ergen) 96:15–24, 100:25–101:4; Howard Dep. 30:15–31:13, 33:10–35:13; PX349 at ii.)

97. Mr. Ergen's role in managing the strategic direction of DISH and EchoStar includes the companies' attempts to acquire, or merge with, numerous spectrum-owning companies. (Jan. 13 Tr. (Ergen) 101:5–103:5.) Mr. Ergen is "responsible for what DISH does in connection with the LightSquared bankruptcy" and he "leads bids of this nature" as part of his responsibilities for DISH. (PX0767 (Goodbarn Nevada Dep.) at 186:25–96, 232:12–17.)

98. Mr. Kiser testified that Mr. Ergen "typically" is involved in strategic investments, and Mr. Kiser could not point to a single strategic investment made by DISH and EchoStar that Mr. Ergen had opposed. (Jan. 10 Tr. (Kiser) 69:23–70:9.) Further, Mr. Ergen, who achieves board consensus before bringing issues to vote, has not voted against a single board resolution in the past five years. (Jan. 13 Tr. (Ergen) 236:3–8.)

99. DISH has two policies governing investments made on behalf of the company. (Jan. 10 Tr. (Kiser) 23:10–11.) One policy governs the company's cash management projects and outlines how Bear Creek may invest the company's money. (Jan. 10 Tr. (Kiser) 23:11–21.) The second policy governs the company's strategic investments and states that "[a]ny investment not otherwise permitted by the Corporation's cash management policy shall not exceed \$125 million in any single transaction or series of related transactions without approval of the Board of Directors; and investments not otherwise permitted by the Corporation's cash management policy shall not exceed \$200 million in aggregate in any calendar quarter without approval of the Board of Directors." (DX331; Jan. 10 Tr. (Kiser) 23:10–24:5; Olson Dep. 12:15–23, 20:7–23.)

A. Mr. Kiser's Role in SPSO's LP Debt Purchases

100. Mr. Kiser has been employed by DISH and its predecessor companies for 27 years. (Jan. 10 Tr. (Kiser) 14:4–9, 15:25–16:1, 69:10–22; Jan. 13 Tr. (Ergen) 21:12–14.) As DISH's Treasurer, he focuses on corporate development, including capital-raising, investor relations, strategic acquisitions and investments, and the purchase of marketable securities. (Jan. 10 Tr. (Kiser) 16:2–6, 108:16–20, 140:6–18; Jan. 17 Tr. (Cullen) 139:18–140:5.) Mr. Kiser also performs corporate

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development services for EchoStar pursuant to a management services agreement between DISH and EchoStar. (Jan. 10 Tr. (Kiser) 69:10–22.)

- 101. As Treasurer of DISH, Mr. Kiser reports directly to Mr. Ergen. Under DISH's bylaws, Mr. Kiser must "perform *282 all duties commonly incident to his office and such other duties as may, from time to time, be assigned to him by ... the Chairman of the Board of Directors." (PX0821 at § 5.2(f).) Accordingly, Mr. Kiser receives authorization from Mr. Ergen in making strategic investments for DISH's portfolio. (Jan. 10 Tr. (Kiser) 69:3–9.)
- 102. In the course of his duties, Mr. Kiser likewise has been involved in numerous proposed or actual transactions on behalf of DISH or EchoStar, including transactions involving Clearwire, Sprint, Blockbuster Inc., DBSD, and TerreStar. (Jan. 17 Tr. (Cullen) 139:16–140:9; Kiser Dep. 117:23–118:6, 173:18–21.) Mr. Ergen testified that "Kiser, in his role at DISH over the years, had been involved in a number of transactions and was familiar with looking at capital structures and interpreting those capital structures and determining things such as who could buy debt or if—and if there were any restrictions." (Jan. 13 Tr. (Ergen) 162:9–16.)
- 103. The scope of Mr. Kiser's employment and authority extends to transacting and monitoring trades on behalf of DISH, including purchases of other companies' debt and interacting with Bear Creek. (Jan. 10 Tr. (Kiser) 21:23–22:18.)
- 104. For example, when DISH made a decision sometime in early 2012 to make a strategic investment in LodgeNet, a company that provides pay-per-view movie services to hotel rooms, Mr. Ergen authorized Mr. Kiser to acquire LodgeNet debt on behalf of DISH, and Mr. Kiser—without authorization from the DISH Board—worked with Sound Point to execute the trades. (Jan. 13 Tr. (Ergen) 128:12–129:20; Jan. 15 Tr. (Ketchum) 14:11–18.) Similarly, when DISH acquired DBSD, Mr. Kiser checked for restrictions on competitors purchasing debt and then executed the trades of distressed debt. (Jan. 10 Tr. (Kiser) 106:21–107:16, 108:8–15.)
- 105. Mr. Kiser acted on direction from Mr. Ergen when he purchased the LP Debt, interacted with Bear Creek, and oversaw and monitored the LP Debt trades—precisely the same functions Mr. Kiser performs for DISH and EchoStar. (*See, e.g.,* Jan. 10 Tr. (Kiser) 84:13–22, 86:18–87:23; PX0031; PX0037; PX0064; PX0068; PX0078; PX0096; PX0136; PX0239; PX0344; PX0422; PX0295; PX0331; PX0390.)
- 106. Even after Mr. Ergen began purchasing the LP Debt, there were times when it was unclear to Mr. Kiser whether he was working for Mr. Ergen personally or for DISH. When he investigated whether the restrictions on DISH purchases had fallen away in the bankruptcy, he "asked a question for the company ... I think I've also got an obligation to the company just as he does. I'm a fiduciary for the company." (Jan. 10 Tr. (Kiser) 83:19–84:24.) Further illustrating these overlapping and conflicting roles, Mr. Kiser testified that "I think I took one hat off and put the other hat on." (Jan. 10 Tr. (Kiser) 84:23–24.)

B. Mr. Ergen Uses DISH Employees, Resources, and Legal Counsel to Facilitate the LP Debt Purchases

- 107. Prior to and throughout the period in which Messrs. Ergen and Kiser were amassing LP Debt, other DISH employees, including Mr. Cullen—another member of DISH's corporate development group—closely monitored news relating to LightSquared and reported on those events to Messrs. Ergen and Kiser. (PX0018; PX0033; PX0075; PX0187; PX0223; PX0195; PX0393; PX0407; PX0408; PX0438.)
- 108. Mr. Kiser transacted business on *283 behalf of SPSO from his DISH office, ¹⁴ using DISH's computers, phone lines, and email and outside investment bankers during general business hours. ¹⁵ (Jan. 10 Tr. (Kiser) 42:4–8; PX0042.) Although the purchases were purportedly done on Mr. Ergen's behalf, Kiser received no compensation apart from his salary at DISH for directing nearly \$1 billion in LP Debt trades. Compensation was allegedly unnecessary because Kiser (a 27–year veteran of DISH/EchoStar) performed the trades "for the experience" and because, as Mr. Ergen testified,

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"he gets to spend time with me and I think he likes that." (Jan. 10 Tr. (Kiser) 26:13–19, 74:25–75:7; Jan. 13 Tr. (Ergen) 23:15–24:1, 133:7–10.)

- Mr. Ergen also used his assistant at DISH to assist with SPSO matters. (PX0560; PX0059.)
- Mr. Kiser kept no log of the amount of time he spent working for Mr. Ergen personally compared to how much time he was working for DISH. (Jan. 10 Tr. (Kiser) 103:9–17.)

109. Mr. Ergen has a family office, a personal asset manager (Bear Creek), and stock brokers that he uses regularly. (Jan. 13 Tr. (Ergen) 23:3–4, 26:15–17, 126:15–21, 127:2–3; Jan. 10 Tr. (Kiser) 21:6–12.) He has also made personal investments through a hedge fund, GSO. (Jan. 13 Tr. (Ergen) 126:22–127:3.) Yet, Mr. Ergen used DISH employees and facilities to acquire the LP Debt. (Jan. 13 Tr. (Ergen) 127:4–13.)

110. Mr. Kiser consulted DISH's outside counsel at Sullivan & Cromwell (whom Mr. Ergen never retained as personal counsel) to determine initially whether DISH and, later, Mr. Ergen, was prohibited from purchasing the LP Debt. (Jan. 10 Tr. (Kiser) 29:10–30:9, 33:9–34:7, 77:11–18, 80:4–6, 119:16–120:4, 120:11–24; PX0144.) Mr. Ergen relied on this advice for months, and did not retain personal counsel until the spring of 2013, after SPSO gained its blocking position. (Jan. 13 Tr. (Ergen) 67:1–11.)

C. DISH Board Members and Management Take No Action Upon Learning of Mr. Ergen's LP Debt Acquisition

111. In May 2012, news reports began speculating that Mr. Ergen was behind Sound Point's purchases of LP Debt. (PX0121; PX0898.) Mr. Ergen testified that no DISH or EchoStar Board member asked him about his purchases prior to his May 2, 2013 presentation to the DISH Board. (Jan. 13 Tr. (Ergen) 119:20–120:3; Jan. 10 Tr. (Kiser) 37:10–24.) In response to questioning from the Court, Mr. Ergen testified that once he learned that he could purchase the LP Debt personally, he did not apprise the DISH Board, its general counsel, or Mr. Cullen that he was acquiring the LP Debt because he did not believe that he had a fiduciary obligation to do so once he confirmed it was not a corporate opportunity for DISH or EchoStar. (Jan. 13 Tr. (Ergen) 37:17–38:9.)

112. On May 10, 2012, *The Denver Post* reported that Charlie Ergen "has snatched up \$350 million worth of debt in LightSquared." (PX0898.) A DISH spokesman declined to comment on the article. After reading the *Denver Post* article, DISH board member Gary Howard sent an email that same day to Stanton Dodge, DISH's General Counsel ("*Dodge*"), Tom Ortolf, a member of the Boards of Directors of DISH and EchoStar, and Mr. Goodbarn, a member of the Board of Directors of DISH, asking if the article was accurate. (DX397.)

113. In response to Mr. Howard's email, Mr. Dodge sent an email on May 16, 2012 to the entire DISH Board, including *284 Mr. Ergen and DISH's associate counsel, Brandon Ehrhart, stating:

further to [G]ary's email below and since another board member inquired about the recent press reports regarding LightSquared bonds, [I] wanted to send a brief note to the full board. [T]he company did not buy any LightSquared bonds.

(DX397.) What follows in the email is redacted.

114. Mr. Dodge's email did not answer the Board members' pointed question whether Ergen was buying the LP Debt. When Mr. Dodge asked Mr. Ergen about the news report, Mr. Ergen responded that there "might be some truth" to the report. (Jan. 13 Tr. (Ergen) 116:3–22, 118:23–119:19.) There is no evidence in the record that (i) Mr. Dodge made further inquiry or (ii) Mr. Ergen ever told Mr. Dodge that, in the fall of 2011, Mr. Kiser had investigated whether DISH could purchase LP Debt and had consulted on that topic with Sullivan & Crowmwell. There is also no evidence that Mr. Dodge, who has fiduciary obligations to DISH, informed the DISH Board whether a corporate opportunity was implicated by Mr. Ergen's LP Debt purchases.

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115. Shortly thereafter, on July 23, 2012, Mr. Ehrhart attended a call with DISH's outside counsel, Scott Miller, of Sullivan & Cromwell, to discuss "LightSquared debt." (PX0892.) Mr. Miller previously handled DISH's mergers and acquisition work, including with respect to Sling Media, Sirius, and TerreStar. (PX0918.)

116. Carl Vogel, a DISH Board member, asked Mr. Kiser, as well as others, if the news reports about Mr. Ergen's purchases were true. Mr. Kiser testified that he never responded to Mr. Vogel's email because Mr. Vogel's question was addressed to multiple people and because "it was Charlie's personal business." (Jan. 10 Tr. (Kiser) 37:16–38:9.) When Mr. Vogel received an email on August 9, 2012 from Jim Millstein, of Millstein & Co., L.P., a restructuring firm, inquiring whether DISH was purchasing LightSquared's debt, he did not deny DISH's involvement. Rather, he forwarded the email to Mr. Cullen and advised Mr. Millstein to "contact Tom Cullen or Charlie to discuss." (PX0232.) Similarly, Mr. Ehrhart received an email from Brendan O'Neill of Canadian law firm Goodmans LLP, stating, "[n]ot sure if DISH is involved at all from the press, but thought I might just reach out in case any assistance was required from us." Like Mr. Vogel, Mr. Ehrhart did not deny DISH's involvement, only replying "[h]ope you are well too Brendan." (PX0420.)

117. In April 2013, DISH spokesman Bob Toevs ("*Toevs*"), head of Corporate Communications, also sent several emails to Mr. Ergen and several senior officers, including Messrs. Cullen, Dodge, Clayton, and Jeff Blum (a Senior Vice President and Deputy General Counsel), about a news article discussing DISH amassing LightSquared debt through Sound Point, and noting that Mr. Toevs "has not commented." (PX0393; PX0407; PX0408.) Mr. Toevs' April 2, 2013 email referred to past coverage on the very same issue and had links to news stories dating back to May 2012. (PX0393; PX0408.) None of these top DISH executives responded to the e-mail to inquire whether Mr. Ergen in fact was buying the LP Debt, and Mr. Ergen testified that, apart from Messrs. Kiser, Cullen, and Dodge, he did not speak to anyone regarding his LP Debt purchases until the May 2, 2013 board presentation. (Jan. 13 Tr. (Ergen) 116:3–22, 119:20–24.)

118. Mr. Cullen, a Federal Rule of Civil Procedure 30(b)(6) representative for DISH, testified that Mr. Kiser was the *285 only person at DISH who knew about Mr. Ergen's LP Debt purchases prior to May 2013. (Jan. 17 Tr. (Cullen) 121:21–122:9.) Mr. Cullen testified that he reached this conclusion without speaking to any DISH board members or senior management, other than Mr. Olson, DISH's Chief Financial Officer, and Mr. Kiser. (*Id*: 12–123:4.)

119. Mr. Cullen works closely with Mr. Ergen in the corporate development group, is considered to be "Ergen's closest confidante on all things wireless," and leads DISH's strategic acquisitions. (PX0890 (May 3, 2013 *Reuters* article.)) When news stories surfaced in the second quarter of 2012 about Mr. Ergen buying LightSquared debt and Mr. Cullen asked Mr. Ergen about these reports, Mr. Ergen confirmed to Mr. Cullen that there either "is" or "might be" "some truth" to the reports and said nothing else. (Jan. 17 Tr. (Cullen) 117:8–18; Jan. 13 Tr. (Ergen) 116:3–22.)

120. Mr. Cullen acknowledged that he, Mr. Ergen, and Mr. Kiser discussed LightSquared, among other several other "MSS ¹⁶ players," "continuously," throughout 2012. (Jan. 17 Tr. (Cullen) 134:9–18.) While Mr. Cullen testified that he did not know that Mr. Kiser was assisting Mr. Ergen with his LP Debt acquisitions, he confirmed that he repeatedly sent emails to Messrs. Ergen and Kiser about LightSquared during the period in which the purchases were made. (Jan. 17 Tr. (Cullen) 110:22–111:7, 112:2–13, 119:12–120:12, 133:7–134:8; PX0075; PX0195; PX0223; PX0393.) Although Mr. Cullen testified that it was routine practice for him to send updates about MSS companies to the corporate development group, he generally did not include any of the other group members on the emails concerning LightSquared. (Jan. 17 Tr. (Cullen) 134:4–135:8; PX0075; PX0195; PX0393; PX0438.) In fact, when Mr. Toevs forwarded an article regarding an inquiry from *The Wall Street Journal* regarding the Sound Point purchases to Mr. Cullen, Mr. Cullen forwarded that email only to Mr. Kiser. (PX0393.)

"MSS" stands for Mobile Satellite Services.

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- 121. Mr. Cullen acknowledged that, as an executive, he owed fiduciary obligations to DISH. Nevertheless, he testified that when he learned that Mr. Ergen was buying the LP Debt: (i) he did not ask Mr. Ergen why DISH was not buying the debt, (ii) he did not ask in-house counsel whether there was an issue with Mr. Ergen making a personal investment in the debt, and (iii) he did not take any steps to determine whether Mr. Ergen's purchases were a corporate opportunity. (Jan. 17 Tr. (Cullen) 143:1–20.)
- 122. Further, when Mr. Cullen learned through news reports in May 2013 that Mr. Ergen's entity, LBAC, made a bid for LightSquared's spectrum assets (see ¶ 13 6–3 8, *infra*) he did not ask Mr. Ergen if he was usurping a corporate opportunity. (Jan. 17 Tr. (Cullen) 143:25–145:16.) Indeed, Mr. Cullen, who typically is involved in DISH's acquisition process, stated that he did not know for over two months that LBAC's bid had been presented to DISH on May 2, 2013 as an opportunity. (Jan. 17 Tr. (Cullen) 144:3–146:19; PX0890.)

D. Mr. Ergen Controls the Boards of DISH and EchoStar

- 123. Mr. Ergen, as the holder of a majority share of voting rights (approximately 88 percent and 79.4 percent of the total voting power in DISH and EchoStar, respectively), has the ability to elect a majority of the directors for the companies and control all other matters requiring the approval of their stockholders.
- *286 124. When asked if "[i]t was [his] view that nobody else could act in an independent way of Charlie," DISH's independent director, Mr. Goodbarn, responded, "[t]hat is correct." (PX0767 (Goodbarn Nevada Dep.) at 233:25–234:3.)
- 125. DISH and EchoStar, in public filings, state that their "future success will depend to a significant extent upon the performance of Charles W. Ergen," the loss of whom "could have a material adverse effect [on the companies'] business, financial condition and results of operation," and "place substantial weight on Mr. Ergen's recommendations in light of his role as Chairman and as co-founder and controlling shareholder of DISH Network." (PX0349 at 32; PX0350 at 27; PX0372 at 24; PX0371 at 21.)

E. Soon After Acquiring a Blocking Position, Mr. Ergen Makes a Presentation to the DISH Board that Contemplates a DISH Bid

126. As noted, by March 28, 2013, Mr. Ergen achieved a blocking position, having contracted to purchase \$168 million in LP Debt on that date. ¹⁷ (Jan. 13 Tr. (Ergen) 174:20–178:3; PX0379; PX0859.)

- On March 28, 2013, believing it could buy LP Preferred Interests, SPSO entered into a bundled trade of LP Debt and LP Preferred Interests. (PX0859; DX136.) The March 28, 2013 bundled trade remained open for several months afterwards but never closed, and Mr. Ergen does not own the LP Debt that was the subject of this trade. Regardless, Mr. Ergen's subsequent purchases of LP Debt in April 2013 brought him to a "blocking position." (PX0859.)
- 127. Mr. Ergen testified that, in April 2013, he began to contemplate making a "personal" acquisition of LightSquared because of changes in the wireless industry and at the FCC. (Jan. 13 Tr. (Ergen) 65:4–9; Jan. 10 Tr. (Kiser) 65:12–16.) At that time, the wireless industry was going through a "seismic shift," including the consolidation of several companies and an increasing transmission of data. (Jan. 13 Tr. (Ergen) 65:10–19.) As Mr. Kiser explained,

[T]here were a lot of pieces in the wireless industry that were moving around; a lot of the industry was consolidating at a pace that's probably unlike any other. So, you know, the company had been in discussions, and we're still in discussions with other wireless companies, companies that had spectrum and were complimentary to the portfolio assets that DISH had. And as the pieces on the chessboard were starting to move and avenues were—people were getting lined up, companies like MetroPCS had been acquired, you know, Sprint and ClearWire were on the block, and, you know,

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DISH was making attempts to purchase them, I think as Charlie saw those pieces start to move, it started to look more interesting to potentially own the asset.

(Jan. 10 Tr. (Kiser) 65:17-66:8.)

128. Mr. Ergen also testified that he believed in April 2013 that if he wanted to make a bid for LightSquared, he would have to do so by July 15, 2013—the date on which the Debtors' exclusive periods would terminate pursuant to the Exclusivity Stipulation. ¹⁸ (Jan. 13 Tr. (Ergen) *287 66:9–15.) Given the risk that a consensual plan of reorganization might be negotiated before exclusivity expired, Mr. Ergen understood that he had to act quickly if he wanted to try to acquire LightSquared's assets and provide "the opportunity for DISH and EchoStar to participate if they chose to do so." (Jan. 13 Tr. (Ergen) 66:9–15; 67:5–11; 77:8–20.)

On January 17, 2013, the Debtors filed a motion to further extend their exclusive periods to file a chapter plan to July 20, 2013. ([Bankr. Docket Nos. 485–88]; DX352.) After a contested hearing on January 31, 2013, LightSquared negotiated the Stipulation Between Parties in Interest Regarding Entry of Order Pursuant to 11 U.S.C. § 1121(d) Further Extending LightSquared's Exclusive Periods To File a Plan of Reorganization and Solicit Acceptances Thereof (the "Exclusivity Stipulation"). On February 13, 2013, this Court entered an order incorporating the terms of the Exclusivity Stipulation. ([Bankr. Docket No. 522]; PX0852.) The Exclusivity Stipulation extended the Debtors' exclusive periods to July 15, 2013, and it required the parties to engage in good faith negotiations regarding the terms of a consensual chapter 11 plan. (PX0852 at 3–4; Jan. 13 Tr. (Ergen) 77:3–20.) If a consensual plan was not reached by July 15, a sales process of LightSquared's assets would begin. (PX0852 at Ex. A ¶ 6.)

129. Once he became interested in LightSquared as an acquisition target, Mr. Ergen asked Mr. Kiser to retain bankruptcy counsel. (Jan. 13 Tr. (Ergen) 67:1–11; Jan. 10 Tr. (Kiser) 66:9–19.) In April 2013, Mr. Ergen hired Willkie Farr & Gallagher LLP ("Willkie Farr"), who had represented DISH in the TerreStar bankruptcy, to serve as his bankruptcy counsel. (Jan. 13 Tr. (Ergen) 180:23–181:10.)

130. By early May 2013, Mr. Ergen had concluded that he was interested in a potential acquisition of LightSquared. (Jan. 13 Tr. (Ergen) 77:3–78:2.) At that time, DISH was consumed with a potential acquisition of Sprint, and if DISH acquired Sprint, DISH would not have enough capital to acquire LightSquared also. (Jan. 13 Tr. (Ergen) 67:21–68:2; PX0767 (Goodbarn Nevada Dep.) 32:11–23.) DISH also was considering a potential acquisition of Clearwire at that time. (PX0767 (Goodbarn Nevada Dep.) 30:15–25; Jan. 13 Tr. (Ergen) 20:17–21.)

131. On May 1 and 2, 2013—just over a month after obtaining a blocking position—Mr. Ergen made presentations to the Boards of EchoStar and DISH, respectively, informing them about his acquisition of LightSquared debt and his proposal for DISH and/or EchoStar to acquire LightSquared's assets for \$2 to \$2.1 billion (the "*Ergen Presentation*"). (PX0867; PX0767 (Goodbarn Nevada Dep.) at 21:1–18; Howard Dep. 55:3–15, 56:24–57:13, 87:11–88:3, 141:13–20; Jan. 13 Tr. (Ergen) 77:3–7, 77:21–78:2, 78:17–79:9, 80:11–13; PX0480; PX0492.)

132. The Ergen Presentation informed the Boards that Mr. Ergen's blocking position in the LP Debt could help facilitate any bid for LightSquared's assets:

[Ergen's] substantial interests in L2 debt and preferred stock compliment [sic] any acquisition strategy and could have significant influence in L2's chapter 11 cases.

(PX0867; Jan. 13 Tr. (Ergen) 182:11-183:11.)

133. The Ergen Presentation proposed a course of action, stating: "[s]ubmit offer now, subject to minimal conditions, and require prompt acceptance (e.g., by May 15) before marketing process gets underway." (PX0867 at SPSO-00011828.) If, however, LightSquared did not accept the proposal, the presentation continued: "NewCo will have the ability to see results of marketing process and, if process is unsuccessful, revert with different bid later." The Ergen Presentation also

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described the chapter 11 timing considerations: "L2 has the exclusive right to file a chapter 11 plan until July 15. L2 likely to begin exploring strategic alternatives in early June if no restructuring or sale strategy emerges." (PX0867 at SPSO–00011828.) The presentation contained an "Illustrative Transaction Timeline" that outlined a schedule of events related to a potential transaction, including the execution *288 of a purchase agreement by May 31, 2013. (PX867.)

134. At the time of the Ergen Presentation, Mr. Ergen understood that the DISH Board ¹⁹ had not performed any analysis of LightSquared. (Jan. 13 Tr. (Ergen) 207:15–17.) ²⁰ Mr. Ergen understood that the DISH Board had not authorized a DISH bid in May 2013, and it had not passed a resolution authorizing him to make a bid personally. (Jan. 13 Tr. (Ergen) 208:4–13.)

- On May 31, 2013, after a "long series of discussions," a committee of the EchoStar Board rejected the opportunity to participate in the LBAC bid because it involved more speculative risk than the company wanted to take on given its financial resources at the time, and participation in the bid would limit EchoStar's ability with respect to other potential strategic investments. (Rayner Dep. 25:17–26:3; 26:18–27:9.)
- As both Mr. Goodbarn and Mr. Howard testified, at that time, DISH was consumed with a potential acquisition of Sprint and Clearwire, and the DISH Board could not focus on a potential acquisition of LightSquared, which was a far lower priority than the other two potential acquisitions. (PX0767 (Goodbarn Nevada Dep.) 32:4–23, 88:5–10, 88:14–20, 95:20–24, 104:9–12, 123:13–20; Howard Dep. 176:11–177:2, 177:25–178:10; Jan. 17 Tr. (Cullen) 102:8–103:4, 121:15–20.)

VI. DISH Contemplates and Makes a Bid for LightSquared at Mr. Ergen's Behest

A. DISH Forms a Special Committee to Evaluate a DISH Bid and the Propriety of Mr. Ergen's LP Debt Purchases

135. Shortly after Mr. Ergen made his May 2, 2013 presentation to the DISH Board regarding a potential acquisition of LightSquared's assets, on May 8, 2013, the Board formed a special committee consisting of directors independent of Mr. Ergen—Messrs. Goodbarn and Howard—to examine the propriety of Mr. Ergen's purchases of the LP Debt and the prospect of a DISH bid for LightSquared's assets. Pursuant to resolutions recorded in the May 8, 2013 minutes of the DISH Board, the Special Committee was vested with the power and authority to: (i) review and evaluate a potential bid (including any potential conflicts of interest) and engage in discussions and/or negotiations; (ii) negotiate definitive agreements with the parties concerning the terms and conditions of the potential bid; and (iii) determine whether such terms and conditions are fair to DISH. (PX0768 (Howard Nevada Affidavit) ¶ 8–10; PX0491 at DISH_NY000000002–4.) The Board formally resolved that the Special Committee's authority would expire *only* upon the Special Committee's "determination, in its sole and absolute discretion, as set forth in its written notice to the Chairman of the Board of Directors" as long as a bid for LightSquared remained viable. (PX0491 at DISH_NY000000005.)

B. Mr. Ergen Makes a "Personal" Bid That Sets the Floor and Ensures He Will Be Repaid in Full

136. Without consulting the newly-formed Special Committee, on May 15, 2013, Mr. Ergen submitted an unsolicited bid for LightSquared LP's spectrum assets for \$2 billion (the "*LBAC Bid*"). (PX0768 (Howard Nevada Affidavit) ¶ 14; PX0504; PX0513; Jan. 13 Tr. (Ergen) 80:11–19.) LBAC did not exist at the time the offer was made and was not formed until two weeks later, on May 28, 2013. (PX0837–838; Jan. 13 Tr. (Ergen) 191:8–192:25.) ²¹

At the time LightSquared received the bid, it had not been formally disclosed that Mr. Ergen was behind the SPSO LP Debt purchases. (Jan. 16 Tr. (Falcone) 69:22–25, 71:24–72:2.)

*289 137. The LBAC Bid expressly stated the buyer of the LightSquared assets would be "owned by one or more of Charles Ergen, affiliated companies and/or other third parties." (PX0504 at GH_L2_00450.) As detailed in the Ergen Presentation, Mr. Ergen priced the bid at \$2 billion, approximately the total amount of the outstanding LP Debt, in what he characterized as an effort to induce serious consideration by LightSquared's LP Debt creditors. (PX0504; PX0867.)

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138. A key feature of the LBAC Bid, which was non-binding and expired on May 31, 2013, was LBAC's apparent "willingness to fund the Purchase Prices, on a non-refundable basis," prior to receipt of FCC and Industry Canada approvals and authorizations. (Jan. 13 Tr. (Ergen) 80:20–81:7; PX0504.) The \$2 billion bid would have enabled Mr. Ergen to be paid in full on his LP Debt investment and receive \$140 million in profit as well as "significant" interest. (Jan. 13 Tr. (Ergen) 132:20–133:6, 134:6–15, 233:20–234:7.)

139. When asked what would have happened if the DISH Board had wished to offer a lower price than Mr. Ergen's, Mr. Ergen stated that "[a]ll they needed to say was, Charlie, don't do it." (Jan. 13 Tr. (Ergen) 207:18–20.)

140. Mr. Ergen's testimony that he was prepared to proceed with the LBAC Bid as a "personal investment" was not credible. (Jan. 13 Tr. (Ergen) 245:17–247:9.) At the time of the LBAC Bid, Mr. Ergen did not have any financing agreements lined up with investors and had not even received a term sheet related to a possible financing of the "acquisition." He did not receive as much as a draft term sheet until July 18, 2013—two months *after* his bid would have expired. (Jan. 13 Tr. (Ergen) 185:20–186:7, 193:15–25, 195:23–196:13; DX285.) Even then, under the term sheet, Mr. Ergen would have had to provide over a billion dollars in cash. (Jan. 13 Tr. (Ergen) 87:3–88:20.) To obtain that amount of cash, Mr. Ergen testified that he would have used \$300–\$500 million of his personal liquid cash and borrowed the rest against his EchoStar stock. (Jan. 13 Tr. (Ergen) 88:21–89:1.)

C. The DISH Special Committee

141. On or about May 17, 2013, the Special Committee set out to engage independent counsel and independent financial advisors, as authorized by the resolutions of the DISH Board. (PX0910; PX0534; PX0491 at DISH_NY000000004; PX0768 (Howard Nevada Affidavit) ¶ 11.) When Mr. Ergen learned that the Special Committee wished to engage counsel, he was opposed to the idea, emailing "[w]hy would we have special committee counsel. You are way ahead of your skis here." (DX188.) As a result, the Special Committee, following Mr. Ergen's direction, delayed the engagement of independent advisors. (PX0768 (Howard Nevada Affidavit) ¶¶ 22, 25, 26.) At a May 31, 2013 meeting, Mr. Ergen suggested that the Special Committee should delay engaging its financial advisor, as, in Mr. Ergen's view, there would "be little activity, if any, in the coming weeks" regarding a LightSquared transaction. (PX0768 (Howard Nevada Affidavit) ¶ 25.) Perella Weinberg ("PWP"), the financial advisor to the Special Committee, was ultimately retained on June 28, 2013, after the Sprint and Clearwire deals had failed to proceed. (See DX0224 (email from Gary Howard to DISH Board); PX0768 (Howard Nevada Affidavit) ¶ 33.) 22

- In addition to PWP, the Special Committee also retained Cadwalader, Wickersham & Taft LLP as counsel. (Jan. 13 Tr. (Ergen) 82:1–8; 85:9–21; Howard Dep. 190:8–13; DX224; DX255.)
- *290 142. After delaying the retention of its professionals and keeping the committee in what Mr. Howard later described as a "holding pattern," Mr. Ergen suddenly reversed course in early July, urging the Special Committee to complete its evaluation quickly and make a recommendation to the DISH Board. (PX0768 at ¶ 34.)
- 143. According to its members, the Special Committee did not have documents detailing Mr. Ergen's ownership of LightSquared debt and preferred stock other than what Mr. Ergen presented to the Board in May. (Howard Dep. 76:8–15.) Following that meeting, the Special Committee requested that Mr. Ergen provide the Committee with information regarding SPSO's trades. (PX0767 (Goodbarn Nevada Dep.) 92:23–93:1; Jan. 13 Tr. (Ergen) 82:18–83:13.) The Special Committee made repeated requests for such information from Mr. Ergen.
- 144. On June 2, 2013, the Special Committee again requested information regarding further details of the bank debt and preferred stock purchases Mr. Ergen made through SPSO. (DX213; Howard Dep. 143:15–144:24.) As of June 5, 2013, the Committee still had not received the schedule of Mr. Ergen's trades. (DX219; PX0767 (Goodbarn Nevada Dep.) 128:25–129:12.)

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145. The June 17, 2013 meeting minutes make it clear that the Special Committee was still looking for information relating to Mr. Ergen's trades: "The Committee discussed the need for additional information from Mr. Ergen regarding his acquisition of LightSquared debt and/or preferred stock, as well as regarding the rationale and business case for an acquisition by the Corporation of LightSquared's L–Band Mobile Satellite Service Spectrum." (DX238.)

146. Following the June 17 meeting, the Special Committee sent Mr. Ergen a letter requesting information regarding his trades in LightSquared debt. (DX244; DX238; Jan. 13 Tr. (Ergen) 83:14–85:8.) The letter stated that "[w]e would also appreciate further detail regarding your relationship with Sound Point Capital Management and its affiliate SP Special Opportunities, LLC ... as it relates to the LightSquared opportunity and your acquisition, whether directly or indirectly, of any interests in any claims, loan obligations or preferred equity securities of LightSquared." (DX244 at GH_L2_000111.)

147. On July 6, 2013, Mr. Howard informed the DISH Board that the Special Committee had "no further insight into the bond purchases made by Charlie's entity." (DX224; Goodbarn Nevada Dep. 165:3–10, 165:16–21.) As of July 21, 2013, the Special Committee still had not received the information it requested regarding Mr. Ergen's trades in LightSquared debt. (PX0767 (Goodbarn Nevada Dep.) 208:5–12.)

148. Mr. Howard testified that the Special Committee was interested in determining whether there was a way that DISH could have bought LP Debt notwithstanding the transfer restrictions. (Howard Dep. 204:14–205:15.) Mr. Ergen never provided the Special Committee with the requested information on his trades. (PX0767 (Goodbarn Nevada Dep.) at 92:10–93:15, 128:16–129:12, 129:21–130:5; PX0768 (Howard Nevada Affidavit) ¶ 27, 28, 30; PX0605; PX0663; DX224; PX0654.) Mr. Goodbarn testified that Mr. Ergen did not share information regarding his trades with the Special Committee as a ploy to insulate himself from this adversary *291 proceeding. (PX0767 (Goodbarn Nevada Dep.) at 104:23–105:6.)

149. Upon learning of the LBAC Bid from news alerts on May 20 and 21, 2013, ²³ Mr. Howard stated that he was surprised, as it "was [his] expectation that Mr. Ergen would not make any LightSquared bid without first discussing it with the DISH Board and the Special Committee in order to get their approval, since any such bid could impact DISH's own strategy vis-à -vis LightSquared." ²⁴

- Mr. Howard stated that he was not aware that Mr. Ergen had made a personal bid to purchase LightSquared's assets until Mr. Goodbarn forwarded to him an updated Charles Schwab news alert on May 21, 2013. (See PX0768 (Howard Nevada Affidavit) at ¶ 15.) He confirmed that the Special Committee had not been advised of and had not approved of the LBAC Bid. (Id. at ¶ 20.) He was concerned that, by making the bid, "Mr. Ergen was narrowing the scope and ability of the Special Committee to fully explore alternative strategies for DISH to pursue with respect to LightSquared, as well as to define and/or negotiate Mr. Ergen's role with respect to DISH's strategy." (Id. at ¶ 21.)
- 24 Id. at ¶ 15.

150. When asked whether the Special Committee considered proposing that DISH make a bid for LightSquared's spectrum in an amount below that of the LBAC Bid, Mr. Goodbarn stated that the LBAC Bid "made it difficult socially to do that ... [b]ecause [Ergen's] put a line in the sand on a bid and we're part of a, you know, a DISH board and he owns a majority of the company." (PX0767 (Goodbarn Nevada Dep.) at 100:7–21.) Pressed further on why it would be difficult for DISH to make a bid lower than Mr. Ergen's bid, Mr. Goodbarn explained that if Mr. Ergen had committed to a \$2 billion bid with no other bidder present, and the Special Committee then bid \$1.5 billion, Mr. Ergen may take "a big loss" on his debt investment and "that does not make a very happy chairman." (PX0767 (Goodbarn Nevada Dep.) at 100:22–101:5.)

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- 151. On July 3, 2013, Mr. Ergen sent to Messrs. Goodbarn, Howard, and David Moskowitz, an in-house attorney and a Senior Vice President for DISH and EchoStar, via email (the "*Ergen Transmittal Email*"), a presentation for the Special Committee and the DISH Board. (PX0927.)
- 152. In the Ergen Transmittal Email, Mr. Ergen states, "This is just a high level view of lightsquared and its potential relation to dish. Please feel free to share with the board or advisors. Also, not on here would be the possibility of freeing up at least two of the existing dbsd/terrestar satellites that could possibly be monetized." (*Id.* at DISH_PLAN000003150.)
- 153. The six-page presentation, attached to the Ergen Transmittal Email, was dated July 8, 2013 and was entitled "Strategic Investment Opportunity—L–Band Acquisition, LLC" (the "Ergen July 8 Presentation"). (PX0928.) The Ergen July 8 Presentation was delivered to the Special Committee and PWP, among other recipients, at a special meeting of the DISH Board on July 8, 2013.
- 154. The Ergen July 8 Presentation provided, for discussion purposes in the context of considering whether DISH would participate in the LBAC Bid, certain valuation information relating to LightSquared's spectrum as of that date.
- 155. Under a line item entitled "Implied Net Primary Asset Value," the Ergen July 8 Presentation lists a range of values of between \$3.341 billion and \$5.213 billion, with a midpoint of \$4.277 billion, referring to Mr. Ergen's estimate of the value of 20 MHz of LightSquared's spectrum *292 assets and its satellites, excluding its 10MHz of lower downlink spectrum.
- 156. Under the heading "Implied Supplemental Asset Value," the Ergen July 8 Presentation lists a range of values of between \$1.833 billion and \$3.783 billion, with a midpoint of \$2.308 billion, for what it identifies as the total of (i) 5.0 MHz of "Reclaimed Unuseable [sic] AWS-4," (ii) 5.0 MHz of "Reclaimed Impaired AWS-4," and (iii) "L-Band Downlink Spectrum." Id. at 5 (DISH_PLAN000003114). The Implied Supplemental Asset Value was Mr. Ergen's estimate of (a) the increase in value of DISH's existing spectrum that would flow from DISH's acquisition of LightSquared's spectrum, which would permit unusable and impaired uplink AWS-4 spectrum to be converted to downlink and (b) his range of values for 20 MHz of LightSquared's downlink spectrum. In other words, the supplemental value of LightSquared's assets to DISH was estimated by Mr. Ergen to be between \$1.833 billion and \$3.783 billion.
- 157. Combined with the Implied Net Primary Asset Value of \$3.341 billion to \$5.213 billion, the total value of LightSquared's assets in DISH's hands (the "Combined Implied Net Primary and Supplemental Asset Value") was estimated by Mr. Ergen to be between \$5.174 billion and \$8.996 billion, with a midpoint of \$7.085 billion.
- 158. On or about July 21, 2013, PWP provided two reports to the DISH Board—a nine-page presentation entitled "Project Discus Summary Conclusions," dated July 21, 2013 and a 69–page PWP document, dated July 2013, entitled "Project Discus Discussion Materials" (the "PWP Report"). (PX0929; PX0930.) In a section captioned "Illustrative Value of DISH's Use Cases Related to LightSquared," the PWP Report concludes, "The cumulative value of the illustrative use cases that leverage the LightSquared LP acquisition is estimated to be \$4.4–\$13.3bn." (Id. at 39 (DISH_PLAN135).) The PWP Report also recites that "In June 2013, [SPSO] joined the Ad Hoc Secured Group to prevent termination of LightSquared LP's obligations of the Exclusivity stipulation." (PX930 at 66 (DISHSC_PLAN00000162).)
- 159. On July 21, 2013, the Special Committee presented its conclusions to the DISH Board, recommending that DISH pursue the LBAC Bid for \$2.2 billion, subject to five express conditions, four of which implicated further review and decision making by the Special Committee:
 - (i) that any material changes to the terms of the bid and/or APA would be subject to the review and approval of the Committee;
 - (ii) that DISH would acquire one hundred percent of LBAC, to the exclusion of EchoStar;

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- (iii) that the Committee and its legal and financial advisors would remain involved in all negotiations regarding the proposed transaction going forward;
- (iv) that the Committee would review and approve the terms of the acquisition by DISH of Mr. Ergen's interest in LBAC; and
- (v) that the Committee expressly reserved the right to obtain all of the requested information regarding Mr. Ergen's acquisition of debt and/or other securities issued by LightSquared as well as the right to evaluate potential corporate opportunity issues.

(PX0716 at GH_L2_000973-74; PX0768 at ¶ 47.)

- 160. Immediately after the Special Committee delivered its conditional approval of the LBAC Bid, the DISH Board disbanded the Special Committee without *293 giving any advance notice to the Special Committee. Other than Messrs. Howard and Goodbarn, who abstained, the Board's vote was unanimous (PX0768 (Howard Nevada Affidavit) ¶ 49–52; DX400), notwithstanding that (i) the conditions set forth in the Special Committee's conditional approval had not been satisfied (PX0736) and (ii) the resolutions creating the Special Committee allowed disbandment only upon the Special Committee's decision, with the bid remaining viable. (PX0491 at DISH_NY0000000005.)
- 161. After the Special Committee was disbanded, on July 22, 2013, DISH agreed to buy LBAC from Mr. Ergen for a dollar, without the Special Committee reviewing the terms of the acquisition agreement. (Howard Dep. 315:10–316:3; Jan. 13 Tr. (Ergen) 195:6–8.)
- 162. On July 23, 2013, DISH announced its intention to bid through LBAC for LightSquared's spectrum for \$2.2 billion (the "DISH/LBAC Bid"). Mr. Howard learned of the bid through the "wires" and did not even know whether the bid was submitted by DISH or by Mr. Ergen. (PX0725.) On July 24, 2013, the Special Committee wrote a letter to the DISH Board expressing its surprise at its disbandment and noting that the five conditions remained unsatisfied. (PX0736.) On July 25, 2013, Mr. Howard resigned from the DISH Board, an action taken so suddenly that DISH risked delisting from the NASDAQ. (PX0746; see also PX0741; DX313.)
- 163. On July 23, 2013, DISH announced that it had executed a Plan Support Agreement (the "PSA"), pursuant to which LBAC would act as the stalking horse bidder for the Ad Hoc Secured Group's plan of reorganization (the "Ad Hoc Secured Group Plan"). (Jan. 13 Tr. (Ergen) 195:6–12; PX0730.) There was no document submitted into evidence reflecting the involvement of the Special Committee in (i) the negotiation and documentation of DISH's purchase of LBAC from Mr. Ergen or (ii) the negotiation of documents that were critical to the LightSquared acquisition—the PSA and the Asset Purchase Agreement (the "APA"). Mr. Howard stated that neither the Special Committee nor its advisors were ever asked to participate in negotiations with the Ad Hoc Secured Group, and neither the Special Committee nor its counsel had been involved in negotiating the APA. (PX0768 (Howard Nevada Affidavit) at ¶¶ 42, 46.)
- 164. The APA, incorporated by reference into the PSA, contained a broad release for all claims against Mr. Ergen, DISH, EchoStar, and SPSO (an entity which purportedly has no ties or relationship with DISH). (PX0823 § 7.6; PX0841 at 11, n.9, 70, 88; 17 C.F.R. § 240.12b-2.)

VII. LightSquared as a Strategic Investment for DISH

A. DISH and EchoStar's Prior Acquisitions of Spectrum Assets

165. DISH's strategic goals include participation in the wireless space and contemplate the need for a great deal of spectrum. (Jan. 13 Tr. (Ergen) 26:18–20, 96:18–98:22, 100:25–101:4.) Mr. Ergen testified that spectrum is a limited resource that currently suffers from a shortage, with the amount of data flowing over available spectrum doubling every

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year. (Jan. 13 Tr. (Ergen) 47:3–48:10, 96:5–14; PX0747 at SPSO–00012492.) Mr. Falcone concurred with Mr. Ergen's view of spectrum, referring to wireless spectrum as "beachfront property." (Jan. 16 Tr. (Falcone) 15:17–16:1).

166. DISH and EchoStar have for years been attempting to acquire, or merge with, numerous spectrum-owning *294 companies, including actual and potential transactions involving DBSD, TerreStar Networks ("*TerreStar*"), Sirius XM Holdings, Inc., Clearwire Corp., Sprint Corp., and Inmarsat plc. (Jan. 13 Tr. (Ergen) 95:6–96:4, 101:5–103:5, 105:11–108:10.)

167. DISH and EchoStar have a history of purchasing distressed or discounted debt of their targets as a step toward an eventual acquisition, including acquiring a blocking position in distressed satellite companies in bankruptcy, such as DBSD and TerreStar, enabling them to acquire the companies' spectrum assets at a discount. (Jan. 13 Tr. (Ergen) 100:25–103:9; Jan. 10 Tr. (Kiser) 108:21–109:6, 106:24–107:3; Howard Dep. 285:15–24.)

168. In DISH's acquisition of TerreStar through bankruptcy, Mr. Ergen and DISH employed a three-step strategy. First, EchoStar became the largest secured creditor of TerreStar and the second-biggest shareholder in the parent, TerreStar Corp. (PX0012 (EchoStar 10–Q Jun. 30, 2011 at 14).) Second, DISH became the ultimate purchaser of TerreStar as a stalking horse bidder, repaying EchoStar in full. (DX008 (DISH 8–K Jun. 16, 2011 at 2).) Third, DISH entered into a purchase agreement with TerreStar whereby both the debt-buyer (EchoStar) and the acquirer (DISH) obtained broad releases that ensured EchoStar's claims would be paid in full. (Jan. 13 Tr. (Ergen) 105:14–17; PX0011 at 1, 5, 9 n.4, 61.)

169. DISH's acquisition of DBSD through the bankruptcy process, in which Mr. Ergen was also intimately involved, employed a similar strategy. (Jan. 13 Tr. (Ergen) 106:7–10.) DISH acquired a blocking position in DBSD's first lien debt and attempted to acquire a blocking position in DBSD's second lien debt to facilitate its acquisition. (Jan. 13 Tr. (Ergen) 104:4–10, 105:11–13, 106:2–10; PX0831) (*In re DBSD North America, Inc.*, 634 F.3d 79, 104 (2d Cir.2011) ("DISH purchased the claims as votes it could use as levers to bend the bankruptcy process toward its own strategic objective of acquiring DBSD's spectrum rights, not protecting its claim")); PX0864 (*In re DBSD North America, Inc.*, 421 B.R. 133, 136 (Bankr.S.D.N.Y.2009) (quoting DISH document stating that DISH "believe[d] there is a strategic opportunity to obtain a blocking position in the 2nd Priority Convertible Notes and control the bankruptcy process for this potentially strategic asset.").) Despite the bankruptcy court's designating DISH's votes, DISH ultimately acquired DBSD's spectrum assets and was repaid in full on its debt holdings. (PX0864, 421 B.R. at 143 (designating DISH's votes).)

170. In March 2012, DISH gained control of DBSD and TerreStar's spectrum, now known as AWS-4 spectrum, which, as of at least January 17, 2014, DISH had still not deployed. (Jan. 13 Tr. (Ergen) 101:5-14, 147:22-25; Jan. 17 Tr. (Cullen) 111:21-24; DX024; Jan. 10 Tr. (Kiser) 109:7-9; Jan. 17 Tr. (Cullen) 139:2-9.)

B. Mr. Ergen's Consideration of LightSquared's Spectrum Assets

171. Mr. Ergen testified that in 2011, he considered, for at least a second time, a DISH investment in LightSquared. ²⁵ (Jan. 13 Tr. (Ergen) 109:3–9.) Mr. Ergen believed that LightSquared was "very similar" to DBSD and TerreStar—companies DISH had recently acquired—and that its spectrum "could fit with the existing spectrum [that DISH owns] in the long- *295 term." ²⁶ (Jan. 13 Tr. (Ergen) 109:10–16, 111:5–16; PX747.)

- Many years earlier, EchoStar had been interested in LightSquared's predecessor company, SkyTerra, prior to Harbinger's own investment. (Jan. 13 Tr. (Ergen) 111:23–112:9; Jan. 16 Tr. (Falcone) 15:12–16:11.)
- Mr. Ergen recognized the value in LightSquared's spectrum, testifying that it is "great collateral." (Jan. 13 Tr. (Ergen) 214:25–215:9.) Had DISH been able to directly purchase the LP Debt, which constituted discounted notes supported by oversecured collateral, it would have realized the same economic benefits as Mr. Ergen. (Id.:13–17, 215:25–216:8; see also PX0587.)

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- 172. In order for DISH to operate a terrestrial wireless network, it needs uplink spectrum to pair with its downlink spectrum; because LightSquared has clean uplink spectrum, ²⁷ this creates a natural synergy. (Jan. 9 Tr. (Smith) 125:4–21.) LightSquared's L–Band spectrum is a "natural pairing" for DISH, given that LightSquared's uplink spectrum is "safe to use as uplink spectrum." (Jan. 9 Tr. (Smith) 114:22–126:2.) LightSquared's spectrum could be repurposed as uplink-only spectrum and paired with the spectrum DISH acquired with TerreStar and DBSD, which can be converted to downlink ²⁸—thereby avoiding known interference problems with the uplink portion of that spectrum. (PX0154; PX0195; Jan. 13 Tr. (Ergen) 151:18–25.)
- 27 The interference issues raised before the FCC relate primarily to LightSquared's downlink spectrum.
- After DISH acquired 40 MHz of AWS—4 spectrum from DBSD and TerreStar, it applied for a waiver of the ATC requirement, which would allow DISH to build out a terrestrial-only wireless network. In December of 2012, the FCC issued a decision that authorized DISH to use its AWS—4 spectrum on a standalone terrestrial basis. However, the FCC's authorization came with a restriction: because DISH's AWS—4 uplink spectrum is immediately adjacent to downlink H-block spectrum—and the presence of uplink and downlink spectrum immediately adjacent to one another results in interference between the bands—there was a need for a "guard band" or transition zone, in between the two spectrum bands. Accordingly, the FCC imposed strict power limitations of 5mW EIRP on mobile transmissions at 2000–2005Mhz and a requirement that DISH accept all interference flowing from the H-block into this 5 MHz of DISH's AWS—4 spectrum. This requirement meant that 5 MHz of DISH's acquired spectrum became largely unusable, and DISH only has 35 MHz usable spectrum of the 40 MHz that it acquired from DBSD and TerreStar. To maximize the full value of the 40MHz of its newly acquired AWS—4 spectrum, DISH would have to convert all of the AWS—4 spectrum to downlink spectrum (which it requested in September 2013 and obtained approval for in December 2013) and find uplink spectrum elsewhere. (DX411 (October 21, 2013 DISH letter summarizing meetings requesting waiver from FCC); DX339 (December 20, 2013 FCC order granting waiver).)
- 173. LightSquared has significant blocks of usable uplink spectrum. Indeed, LightSquared is presently, and has been for some time, the only significant source of available uplink spectrum to acquire. (See PX0195 ("one potentially logical technical solution that could combine LightSquared's spectrum (as uplinks) with the TerreStar and DBSD spectrum (if that was all converted to downlinks)").)
- 174. Mr. Ergen testified that had he acquired LightSquared, his plan would entail "two or three years to clean up LightSquared['s spectrum]," *i.e.*, obtain the necessary FCC approvals, and that he believed "at the end of the process, there would be ... twenty megahertz of uplink spectrum." (Jan. 13 Tr. (Ergen) 245:17–246:21.)
- 175. The DISH Special Committee concluded in June 2013 that the purchase of LightSquared's spectrum assets "would be an attractive opportunity for the Corporation's shareholders, given that such an acquisition could enhance the value of the spectrum already owned by the Corporation." (PX0716 at GH_L2_000972.) DISH and Mr. Ergen were aware of the inherent value in LightSquared's spectrum *296 and its actual and potential synergies with DISH's spectrum.
- 176. As set forth in paragraphs 153–57 *supra*, the Ergen July 8 Presentation was delivered to the DISH Special Committee and PWP, financial advisor to the DISH Special Committee, among other recipients, at a special meeting of the DISH Board on July 8, 2013. The Combined Implied Net Primary and Supplemental Asset Value listed in the presentation —*i.e.*, the estimated total value of LightSquared's assets in DISH's hands—was estimated by Mr. Ergen to be between \$5.174 billion and \$8.996 billion, with a midpoint of \$7.085 billion.
- 177. Mr. Ergen acknowledged during a DISH earnings call on August 6, 2013 that LightSquared's spectrum would be beneficial to DISH: LightSquared is "interesting to [DISH]" because the spectrum "potentially could fit with the existing spectrum that [DISH has] in long term.... So putting all that spectrum together at the same time maintaining the ability to use the satellite for voice and data ... makes a lot of sense." (PX0747 at SPSO–00012486.)

C. DISH'S Pursuit of Sprint and Clearwire

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178. At the same time that DISH was ostensibly pursuing the Sprint and Clearwire transactions, ²⁹ Mr. Ergen was simultaneously pursuing LightSquared's assets to preserve optionality for DISH in case DISH's bids for Sprint and Clearwire fell through. Mr. Ergen has stated publicly that: "I like, strategically, to have a lot of optionality and it's easier to make good choices when you have options." (PX0839 at 7.) Thus, he pursued LightSquared as an alternative for DISH if the Sprint and Clearwire acquisitions fell through-as they ultimately did. (PX0832 (Ergen Nevada Dep.) at 135:23-136:3 (a DISH bid for LightSquared could be a "Plan B" if potential deal with Sprint did not work out), 140:22-141:23 (Mr. Ergen made the bid for LightSquared's spectrum to preserve DISH and EchoStar's "optionality" to participate); Jan. 13 Tr. (Ergen) 186:25-187:20 (the bid "opened up the optionality for DISH to the extent they lost Sprint"); PX0908 at 10 ("we realize [SoftBank is] a formidable competitor and we have to be prepared to win and we have to be prepared to lose").)

On January 8, 2013, DISH made an unsolicited and non-binding bid for Clearwire, (DX106; PX0315). DISH ultimately withdrew its tender offer on June 26, 2013. (DX257.) On April 15, 2013, DISH made a bid for Sprint (DX153) but abandoned its bid for Sprint on June 21, 2013. (DX250.)

VIII. Mr. Ergen's Assertion That He Was Making a Personal Investment Is Belied by the Evidence

179. Mr. Ergen's substantial purchases of LP Debt are not consistent with his historical personal investments. Mr. Ergen has a history of investing in low-risk, diversified, liquid assets—not investing substantially all of his liquid assets in the distressed debt of a single company. Moreover, while Mr. Ergen's willingness to pay near par for the distressed LP Debt is consistent with a plan to obtain a blocking position—and indeed, a majority position—in order to acquire the underlying company, such purchases are somewhat inconsistent with a personal investment by a typical creditor seeking to make a profit on distressed debt by buying low and selling high.

A. SPSO's Purchases of LP Debt Were Inconsistent with Mr. Ergen's Personal Past Investment Strategy

180. Bear Creek manages investments for Mr. Ergen in a trust account known as *297 the Lindsey Revocable Trust (the "Trust"). (Roddy Dep. 18:3–8.) Ordinarily, the Trust—in the names of both Mr. Ergen and his wife, as co-trustees contains "almost all of [Mr. Ergen's] assets." (Jan. 13 Tr. (Ergen) 61:13-21.) The Trust account is conservatively managed, with most securities rated "A" or better, and diversified across "[m]unicipal taxable securities, [and] commercial paper." (Roddy Dep. 57:9-58:3, 58:20-22, 59:6-12; Jan. 13 Tr. (Ergen) 168:4-14.)

181. Mr. Ergen has never directed Bear Creek to invest in distressed debt, and Bear Creek has never invested more than 50 percent of Mr. Ergen's funds in the stock of a single issuer. (Roddy Dep. 60:20-61:5.) Indeed, no more than ten percent of Mr. Ergen's funds could be invested in any single issuer, and the only distressed debt investment that Mr. Kiser could recall Mr. Ergen investing in was an indirect investment through the portfolio of a hedge fund, GSO. (Roddy Dep. 74:5-13.) Moreover, prior to investing in the LP Debt, Mr. Ergen had never invested his personal funds in a competitor of DISH or a company he considered to be a strategic opportunity for DISH, nor had he previously invested in spectrum assets or bought distressed debt in a company that owned spectrum assets. (Jan. 10 Tr. (Kiser) 100:2–21; Jan. 13 Tr. (Ergen) 122:18–123:4, 154:16–155:12, 156:11–14.)

182. When it came to LightSquared, however, Mr. Ergen deviated from his past investment practices, and invested nearly all of his non-DISH/EchoStar assets—approximately \$700 million—to acquire the LP Debt. (Jan. 13 Tr. (Ergen) 170:20-172:9; PX0832 (Ergen Nevada Dep.) 105:19-106:10; PX0859.) Aside from his ownership in DISH and EchoStar, Mr. Ergen's investment in LightSquared is by far his largest personal investment. (Jan. 10 Tr. (Kiser) 102:2–14; Jan. 13 Tr. (Ergen) 153:17–21.) Bear Creek's managing director testified that Mr. Ergen transferred "probably" over \$700 million from the Trust to the Bal Harbour Entities and SPSO, and that Bear Creek had never seen Mr. Ergen pull out that much money in a period of 13 months for the benefit of the same beneficiary or beneficiaries. (Roddy Dep. 95:16–96:6; see also

PX0814 at BC001351-68; PX0811 at BC00428-497; PX0809; Jan. 13 Tr. (Ergen) 169:4-170:19.) 30

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Around that time, Bear Creek managed between \$626 million and likely \$750 million dollars for Ergen. (Roddy Dep. 71:11–18.) Today, it manages under \$100 million. (Roddy Dep. 72:22–73:5.)

183. According to Mr. Ergen, if the Ad Hoc Secured Group Plan had been confirmed per the proposed schedule, he would not only have been repaid in full, but he would have received approximately \$150 million in profit plus a "significant" amount in interest. (Jan. 13 Tr. (Ergen) 132:22–133:6, 134:6–15, 233:20–234:7.)

184. Mr. Ergen testified that although he withdrew \$700 million from a family trust, he never informed his wife—a cotrustee of the Trust—that he had used the money to invest in the LP Debt. (Jan. 13 Tr. (Ergen) 120:8–21, 252:8–20.) Indeed, although Mr. Ergen's wife is a DISH board member (and a co-founder of DISH and EchoStar), she purportedly never asked him whether he was purchasing the LP Debt prior to the May 2, 2013 board meeting. (Jan. 10 Tr. (Kiser) 15:5–21; Jan. 13 Tr. (Ergen) 119:20–120:7; PX0302 at 20.) Notably, Mrs. Ergen was among the recipients of the May 2012 email DISH's general counsel sent stating, in response to a question over whether "charlie had bought \$350 million light squared *298 bonds," that "the company did not buy any LightSquared bonds." (DX397.)

185. Mr. Ergen testified that he was interested in purchasing the LightSquared assets personally if DISH declined to bid, but he had not made critical decisions essential to the acquisition of a company, such as who would run the business, where key employees would be officed, or how he would resolve the conflict of interest inherent in owning a DISH competitor. (Jan. 13 Tr. (Ergen) 244:11–245:12.)

B. The Price at Which Mr. Ergen Attempted to Purchase the LP Debt and Offered for the LP Preferred Interests Is Inconsistent with the "Great Investment" Premise

186. SPSO paid 96 cents on the dollar for approximately \$320 million of LP Debt, prices which are consistent with DISH's past practices of paying at or close to par for strategic purposes. (PX0864 (*In re DBSD North America, Inc.*, 421 B.R. at 140) (discussing DISH paying par for debt); Jan. 13 Tr. (Ergen) 106:2–17.) Mr. Ergen stated that, in 2013, he felt the LP Debt was even more valuable because of changes in the industry and at the FCC, so he raised his limit up to nearly par—96 cents on the dollar—and bought whatever people would sell at that level. (Jan. 13 Tr. (Ergen) 66:16–25.)

187. As discussed *supra*, in October 2012, Mr. Ergen instructed Mr. Kiser to increase his position in the LP Debt up to a level that would establish a blocking position. (PX0243.) By March 25, 2013, Mr. Ergen needed to purchase another \$112 million in the debt to reach that goal. (Jan. 13 Tr. (Ergen) 175:7–176:14; PX0379.) On March 28, 2013, Mr. Ergen initiated a trade for \$168 million in LP Debt at 96 cents on the dollar—which was 50 percent more than he initially paid in April 2012. (Jan. 13 Tr. (Ergen) 176:17–178:3; PX0859.) Mr. Ergen also sought to purchase the Preferred Stock of LightSquared LP ("*LP Preferred Interests*") that was bundled with that 96 cents on the dollar LP Debt and offered to pay between 92 and 95 cents on the dollar for the LP Preferred Interests—approximately \$122 million—just so, as Mr. Kiser testified, he could have the privilege of obtaining the LP Debt with which it was bundled. (Jan. 10 Tr. (Kiser) 136:7–14.) Mr. Ketchum testified that SPSO had been offered LP Preferred Interests numerous times in the past, but only pursued the offer when it was bundled with the \$168 million in LP Debt. (Jan. 15 Tr. (Ketchum) 108:12–22; *see also* PX0412 (April 4, 2013 e-mail from Kiser telling Ketchum "We're only interested in the term loan.").) Mr. Ergen denied the fact that he was willing to pay that price because he wanted to get a blocking position. (Jan. 13 Tr. (Ergen) 174:3–18.) Mr. Ergen's testimony is inconsistent with Mr. Ketchum's testimony that Sound Point, Mr. Ergen, and Mr. Kiser shared the goal of obtaining a blocking position. (Jan. 15 Tr. (Ketchum) 54:19–22; PX0305.)

IX. LightSquared and Harbinger Were Aware or at Least Had a Strong Suspicion that Mr. Ergen Was Acquiring LightSquared Debt

A. Although Public Information Provided No Certainty as to Who Was Behind Sound Point's Purchases, There Was Ample Reason to Believe It Was Mr. Ergen

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188. Starting in 2011, and continuing into 2013, Harbinger and LightSquared closely monitored the sales and transfers of LightSquared's bank debt. (Jan. 16 Tr. (Falcone) 18:19–22; Montagner Dep. 85:18–86:21; DX108; DX139; DX156; DX159; DX164; DX173; DX211; DX391; *299 DX392; PX0141; PX0324; PX0358; PX0373; PX0403.) Around May 2012, when LightSquared filed for bankruptcy, LightSquared was updating, several times a week, a list of the "proforma" holders of LightSquared debt, which contained information on open and settled trades. (PX0141; Montagner Dep. 65:23–68:5.)

189. Ten days before LightSquared filed for bankruptcy protection, Mr. Falcone learned that SoundPoint was buying LightSquared debt. (Jan. 16 Tr. (Falcone) 20:17–20.) However, given that Sound Point reportedly only had approximately \$178 million in assets under management but was "purchasing" over \$200 million of LP Debt, it prompted suspicion that Sound Point was not the identity of the ultimate purchaser. (Jan. 17 Tr. (Hootnick) 17:21–18:6; PX0122.)

190. The identity of the purchaser behind Sound Point was the subject of widespread speculation in the media. News reports and blogs at various times connected Mr. Ketchum and Sound Point to Mr. Ergen, Carlos Slim, and the Dolan family (which controlled Cablevision). (See e.g., PX0095; PX0121; PX0122; PX0154; PX0195; DX144.)

191. On April 30, 2012, Paul Voigt of Jefferies privately told Mr. Falcone that he was going to trade \$250 million of LightSquared debt the following day. (DX447.) Around this time, Mr. Falcone had heard rumors that Carl Icahn was looking to sell his \$250 million of LP Debt. (Jan. 16 Tr. (Falcone) 94:20–95:15.) Mr. Falcone responded, "To?" (DX447.) Several days later, on May 4, 2012, Mr. Falcone answered his own question, and in an email to Mr. Voigt referring to the \$250 million trade, wrote, "You sold to Ergen." ³¹ (DX033; Jan. 16 Tr. (Falcone) 30:11–31:15.) Mr. Falcone testified that he sent the email because "[he] believed, at that time, that Ergen was involved and that they may have sold to Ergen." (Jan. 16 Tr. (Falcone) 31:12–15.)

Following SPSO's purchase of the \$250 million piece of debt, news reports speculated that Mr. Ergen was buying the debt. (Jan. 10 Tr. (Kiser) 37:5–13.) On May 7, 2012, a *Reuters* story on the trade mentioned that Mr. Steven Ketchum of Sound Point previously counted Mr. Ergen as one of his investment banker clients and that DISH owned wireless airwaves "similar to LightSquared." (PX0121.) On May 9, 2012, an *LCD News* story carried the headline "LightSquared TL trades north of 70 as Ergen enters the picture." (DX045.) On May 10, 2012, a *Wall Street Journal* blog, "Deal Journal," published an entry titled "Ergen Builds Cash Pile Amid LightSquared Restructuring Talks." (DX396.)

192. On May 4, 2012, Ian Estus, an analyst-trader at Harbinger Capital, investigated Sound Point and forwarded a November 2, 2011 article to Mr. Falcone noting that Mr. Ketchum had a relationship with the Dolan family. Mr. Estus noted, "This is the guy running Sound Point. An old article, but looks like the guy has close ties with the Dolan family." (PX0095.)

193. On May 5, 2012, Mr. Falcone responded to an email regarding Mr. Ergen from Mr. Cohen of Knighthead, and wrote, "Maybe we shouldn't file if he is circling the wagons. Though I think is [sic] a positive. May bring in another strategic." (Jan. 16 Tr. (Falcone) 33:8–12; DX035.) Mr. Falcone testified that he intended to convey that to "have a strategic kind of kicking the tires on your company ... validate[s] the asset and it may bring in—it may prompt other strategics to get involved." (Jan. 16 Tr. (Falcone) 35:3–10, 96:8–12.)

194. On May 6, 2012, Mr. Falcone emailed Matthew Goldstein of *Reuters* and wrote that Mr. Ergen bought LightSquared debt from Carl Icahn, and that Mr. *300 Ergen's purchase would "prompt more strategics to step in." (DX036; DX037; Jan. 16 Tr. (Falcone) 36:17–22.) Later in the day, Mr. Goldstein told Mr. Falcone that he heard the buyer was Sound Point, and Mr. Falcone responded, "Fronting for [E]rgen." (DX037.) Mr. Falcone never indicated to Mr. Goldstein that he was speculating. (Jan. 16 Tr. (Falcone) 105:23–106:4.) When Mr. Falcone sent these emails to Mr. Goldstein, he believed Mr. Ergen was purchasing LightSquared's debt. (Jan. 16 Tr. (Falcone) 38:6–15, 102:3–7.)

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195. On May 7, 2012, Mr. Falcone sent an email to Thomas Cullen of DISH and wrote, "Good purchase." (DX378; Jan. 16 Tr. (Falcone) 39:21–40:1.) Mr. Falcone testified that Mr. Cullen later called Mr. Falcone, but Mr. Falcone never called him back ³² (Jan. 16 Tr. (Falcone) 40:2–7.)

On December 18, 2012, Mr. Falcone again sent an email to Mr. Cullen and wrote, "We should talk. I know you guys are buying the bonds through Sound Point. One of his guys has been talking." (DX097.)

196. On May 7, 2012, Reuters published an article about the recent trade to Mr. Ketchum of a position formerly held by Carl Icahn, noting that Mr. Ketchum had previously worked as an investment banker and "one of his clients was Charlie Ergen's satellite company." (PX0121; see also PX0122.) Similarly, on May 10, 2012, a Wall Street Journal blog noted that the counterparty on the Icahn trade was a "small hedge fund with ties to Ergen" and speculated that DISH's then-recent sale of \$1.9 billion worth of high yield bonds could be used to buy the LP Debt. However, the article, with the aid of DISH, refuted its own claim stating that "[t]he official line out of Dish is that the proceeds from the bond sale will go to pay down debt maturing in 2013 and 2014." (DX396.)

197. On May 8, 2012, Mr. Falcone emailed Gil Ha, a banker at Greenhill & Co. who had a relationship with AT & T, and wrote, "Ergen now involved in LS." (DX043.) Mr. Falcone testified that he sent this email because he thought that if AT & T knew Mr. Ergen was involved in LightSquared, AT & T might be more likely to invest in LightSquared. (Jan. 16 Tr. (Falcone) 41:20–22, 118:15–119:14.)

198. On May 8, 2012, Mr. Falcone emailed Ara Cohen of Knighthead, a senior creditor of LightSquared, and wrote, "I can understand why u guys balked; Charlie will definitely give u guys 25% and an independent board and your full claim." (DX382.)

199. On May 10, 2012, a Harbinger Capital employee advised Mr. Falcone that he had "heard from a couple of people that [E]rgen may not be the guy behind [K]etchum. Some rumors are that it might be the [D]olans, who like [E]rgen are close to [K]etchum." Mr. Falcone did not believe the employee was referring to the Dolans personally, but rather to Cablevision, which the Dolans control. (Jan. 16 Tr. (Falcone) 45:18–46:20; PX0149.)

200. On May 16, 2012, Mr. Falcone sent an email to Greg Bensinger, a reporter at *The Wall Street Journal*, saying that Mr. Ergen and Carlos Slim were involved in buying LightSquared's debt. (DX386.) Mr. Falcone also offered Mr. Bensinger an "exclusive" if he would write a story, stating, "Let me know before I tell someone else if u are going to write anything." (DX386.) Mr. Falcone understood that Mr. Bensinger may write an article based on the information Mr. Falcone had provided. (Jan. 16 Tr. (Falcone) 54:15–22, 108:25–109:4.)

201. On July 9, 2012, *Forbes* indicated that, while speculation following the Icahn *301 trade had focused on Mr. Ergen, "holes have appeared in the thesis that Ergen is backing Sound Point" and "people involved have begun to speculate it might be Carlos Slim or others behind the purchase. Sources have speculated that Cablevision, owned by the Dolan family and one of the country's largest telecom and media company [sic], could be a potential suitor as well." (PX0304 at KCM0013841; see also PX0195 (Tim Farrar, *How many billionaires does it take to screw in a LightSquared?*).)

202. On October 10, 2012, Mr. Falcone was told by an employee at Jefferies, who said he was "very close to [Ergen's] right hand guy," that he would be "shocked if he is lying" about Mr. Ergen not being behind Sound Point's purchases of LP Debt. (PX0254.)

203. New reports continued to indicate throughout 2012 and into 2013 that Mr. Ergen and DISH may be behind Sound Point's LP Debt acquisitions, but no press article definitively confirmed Mr. Ergen's involvement. An April 4, 2013 Wall Street Journal article noted, "[i]t is unclear whether Mr. Ergen or his company, satellite-television operator Dish Network Corp.... has played a role in Sound Point's trading. Mr. Ergen hasn't addressed the trades, and the company

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declined to comment." (DX144.) The same day, an individual working in the telecommunications industry forwarded Mr. Falcone the article, telling him that Carlos Slim was "with Charlie on the debt." The individual explained that he "was in Mexico and was told by [Slim's] investment guy ... that Carlos and Charlie are very tight and Carlos owns Dish Mexico." (PX0409.)

204. Although representatives of LightSquared had, at times in the spring of 2012, speculated that Mr. Ergen, Mr. Slim, Cablevision, Telephonica, or SK Telecom were purchasing LightSquared debt through SPSO, as Mr. Montagner testified, "[i]t was all speculation at the time. No one knew." (Montagner Dep. 64:20–65:10.) Similarly, depending on the day and the information he received or the rumors that were circulating, Mr. Falcone suspected that anyone from Mr. Ergen on behalf of DISH or EchoStar; Sprint; James Dolan on behalf of Cablevision; Carlos Slim; AT & T; or one of the "big PE shops" was behind Sound Point's purchases. (Jan. 16 Tr. (Falcone) 23:24–24:10, 48:21–49:19, 51:2–21, 62:16–63:24, 72:25–74:9; see also PX0095; PX0167; PX0158; PX0312; PX0537; PX0540; PX0356.)

205. On October 4, 2012, Mr. Falcone sent an email to Omar Jaffrey, a banker who has worked in the telecommunications space (and now is the principal of Melody Capital, a plan sponsor), and wrote, "You may want to circle up w[ith] your contact at AT & T and let him know Ergen continues to buy bonds." (DX388; Jan. 16 Tr. (Falcone) 56:3–8.) When Mr. Falcone sent this email, he believed Mr. Ergen was the buyer of the debt. (Jan. 16 Tr. (Falcone) 123:14–18, 124:7–9.) Mr. Falcone also testified that he sent the email in the hope that Mr. Jaffrey would corroborate his belief that Mr. Ergen was buying debt and get AT & T interested in LightSquared. (Jan. 16 Tr. (Falcone) 56:9–57:5.)

206. Even as late as March 28, 2013, Drew McKnight of Fortress Investment Group, LLC ("Fortress") and Mr. Falcone both expressed in an email exchange that it was beneficial that a potential strategic investor, Mr. Ergen, was buying Fortress' LightSquared preferred stock. (DX395; Jan. 16 Tr. (Falcone) 140:24–142:4.)

207. Mr. Falcone testified that he also "suspected" Carlos Slim or Cablevision might have been acquiring LightSquared debt. (Jan. 16 Tr. (Falcone) 23:24–24:10.) He also repeatedly characterized his emails that stated that Mr. Ergen was *302 buying debt as "fishing expedition[s]" for information. (Jan. 16 Tr. (Falcone) 39:3–10, 41:20–42:9, 56:13–20, 124:20–125:7.)

208. In the spring of 2013, Harbinger and LightSquared were monitoring SPSO's open and closed trades particularly closely to determine whether SPSO's holdings would exceed the holdings of the Ad Hoc Secured Group, which would trigger the invalidation of certain provisions of the Exclusivity Stipulation, including the obligation to conduct a formal sale process for LightSquared's assets after the exclusivity period terminated: "[W]e were monitoring the holdings throughout the entire case. But at this point in time it was particularly relevant given a threshold in the exclusivity stip." (Jan. 17 Tr. (Hootnick) 74:8–15.)

209. Mr. Falcone testified that, at least as of March 2013, he wanted to "blow up" the Ad Hoc Secured Group because he did not want LightSquared to have to market or sell its assets. (Jan. 16 Tr. (Falcone) 142:20–143:17.)

B. Harbinger and LightSquared Add DISH to the List of Disqualified Companies Because They Believe Mr. Ergen Is Buying LP Debt

210. On May 6, 2012, in response to an email from Mr. Cohen of Knighthead regarding Mr. Ergen, Mr. Falcone wrote, "Well I'm working on giving him a nice surprise." (DX038.)

211. Three days later, on May 9, 2012, LightSquared amended its list of Disqualified Companies (see ¶ 25–26, *supra*), and Mr. Falcone sent a list of additional Disqualified Companies under the Credit Agreement to Paul Voigt of Jefferies. (DX443; DX383; Jan. 16 Tr. (Falcone) 112:14–114:25.)

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- 212. Two of the companies on the May 9 amendment to the list of Disqualified Companies, DISH and DBSD North America, Inc., are affiliated with Mr. Ergen, but none is affiliated with Mr. Slim. (Jan. 16 Tr. (Falcone) 115:6–16; DX443.) Mr. Falcone testified that he sent this email to Mr. Voigt because he thought Mr. Ergen or DISH was buying LightSquared debt through Sound Point. (Jan. 16 Tr. (Falcone) 114:16–25, 117:22–118:5.) Indeed, after DISH was added to the list of Disqualified Companies under the Credit Agreement, Mr. Falcone told Mr. Voigt that "DISH or soundpoint [sic] can no longer buy." ³³ (DX384.)
- Based on this and other emails, it is clear that Jefferies, the market maker in LightSquared debt, was aware of the connection between Mr. Ergen and SPSO, and that Jefferies was talking to Mr. Falcone about SPSO's trades before they closed. (DX033 (May 4, 2012 Falcone email to Voigt: "You sold to Ergen"); DX377 (May 7, 2012 Falcone email to Voigt forwarding a list of Disqualified Companies including EchoStar: "not sure how Charlie gets around this one"); DX443 (May 9, 2012 Falcone email to Voigt attaching Notice to Administrative Agent: "not sure I would want to trade these anymore and get stuck"); DX055 (May 17, 2012 Falcone email to Voigt: "Ergen and Carlos Slim"); DX089 (November 16, 2012 Falcone email to Voigt: "[W]hat was the date the first block traded out of [I]cahn into [E]rgen[?]").)

C. Neither Harbinger Nor LightSquared Attempted to Use a Rule 2004 Subpoena to Determine Who Was Buying LightSquared Debt Through Sound Point

- 213. Had they been confused about the identity of the purchaser behind SPSO, Harbinger or LightSquared could have sought discovery under Bankruptcy Rule 2004. When asked about this option at trial, Mr. Falcone attempted to deny that he knew what a Rule 2004 subpoena was, initially testifying that he first heard of it a week before the Trial at his deposition on January 8, 2014 (Jan. 16 Tr. (Falcone) *303 129:8–130:8) and then backtracking, minutes later, when confronted with a May 16, 2013 email in which he wrote, "We should also put the '2004' item up as well." (Jan. 16 Tr. (Falcone) 131:22–132:10; DX405.)
- 214. Mr. Falcone then testified that, in fact, before Mr. Ergen publicly disclosed his interest in SPSO, he had discussions with his legal team regarding issuing a Rule 2004 subpoena. (Jan. 16 Tr. (Falcone) 131:24–132:22.)
- 215. Mr. Montagner testified that he understood LightSquared could have served a subpoena on the holders of its secured debt to identify who was behind SPSO. (Montagner Dep. 57:5–9.) Mr. Hootnick, a Managing Director at Moelis & Company ("Moelis"), LightSquared's financial advisor, also testified that he was involved in discussions with LightSquared regarding the use of discovery to find out who was purchasing LightSquared debt through Sound Point, but LightSquared decided not to pursue such discovery. (Jan. 17 Tr. (Hootnick) 67:10–22.)
- 216. Ultimately, neither Harbinger nor LightSquared ever tried to use a Bankruptcy Rule 2004 subpoena to find out who was behind SPSO's purchases of LP Debt. (Jan. 16 Tr. (Falcone) 131:10–132:22.)

D. LightSquared and Moelis Representatives Also Suspect Mr. Ergen Is Buying Debt Through Sound Point

- 217. Mr. Hootnick testified that it was "our view" that Mr. Ergen was purchasing LightSquared debt through Sound Point. ³⁴ (Jan. 17 Tr. (Hootnick) 62:3–6; *see also id*:13–23.) He further testified that Moelis "never really believed" that Mr. Slim was behind Sound Point. (Jan. 17 Tr. (Hootnick) 87:12–19.)
- Mr. Hootnick's belief did not change with the passage of time. He testified that he understood, at least as of April 3, 2013, that The Wall Street Journal had very good sources saying that Mr. Ergen was behind Sound Point's purchases of LightSquared debt. (DX140; Jan. 17 Tr. (Hootnick) 63:11–21.)
- 218. Mr. Montagner held the same beliefs. On May 7, 2012, after seeing news reports that Sound Point had purchased LightSquared debt, Mr. Montagner emailed Stan Holtz of Moelis and wrote, "Ketchum, with his 175 MM fund, bought 350 of the debt on Friday[.] He is probably a front for Charlie Ergen." (DX040; Montagner Dep. 60:21–61:15.)

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219. Mr. Montagner testified that he was not aware of anyone at LightSquared doing anything to try to stop Sound Point's debt purchases. (Montagner Dep. 64:20–65:19, 104:19–25, 105:6–17.)

E. LightSquared and Harbinger Make Inquiries to Determine Who Is Behind Sound Point's LP Debt Purchases but Fail to Take Action Based on Their Suspicions

220. LightSquared and Harbinger made efforts before and after LightSquared's bankruptcy filing to uncover the identity of the party behind Sound Point's purchases. (Jan. 16 Tr. (Falcone) 23:12–15, 24:20–24.) In early May 2012, Mr. Icahn, a substantial holder of the LP Debt, sold a large block of LP Debt to Sound Point, spawning press speculation. (Jan. 9 Tr. (Smith) 127:25–128:18; Jan. 17 Tr. (Hootnick) 19:8–11; PX0121).

- 221. Upon learning of Sound Point's purchase, Mr. Smith, having never heard of Sound Point, asked Messrs. Montagner and Hootnick to find out who was behind Sound Point's purchases. (Jan. 9 Tr. (Smith) 127:16–129:3.) Similarly, Harbinger instructed Barry Ridings of Lazard Freres & Co LLC to reach out to Mr. Ergen. (PX0899.) Despite trying "a *304 number of times," they "could never verify who was behind Sound Point." (Jan. 9. Tr. (Smith) 129:4–13; *see also* Jan. 16 Tr. (Falcone) 47:4–9.) As Mr. Hootnick testified, "[t]here were a lot of suspicions that that was the case, but we could not get confirmation on that topic." (Jan. 17 Tr. (Hootnick) 54:18–55:10.)
- 222. Mr. Montagner also asked Kurt Haufler, Treasurer of LightSquared, to reach out to UBS to obtain information regarding LightSquared's debt trading activity. Mr. Haufler was not able to confirm through UBS who was behind Sound Point. (Montagner Dep. 49:9–50:17, 51:6–17.)
- 223. Further, both Messrs. Montagner and Holtz reached out directly to Mr. Ketchum to inquire who was behind SPSO. (Jan. 17 Tr. (Hootnick) 17:16–18:13, 59:14–60:20.) Mr. Ketchum intentionally rebuffed their inquiries. (*See Jan.* 15. Tr. (Ketchum) 88:22–89:22.)
- 224. Mr. Montagner left multiple voicemails for Mr. Ketchum in May 2012, around the time press reports surfaced connecting Mr. Ergen to the LP Debt purchases. Mr. Ketchum returned one call "late one night" and left a voicemail. That voicemail was the only direct communication Mr. Montagner had with Mr. Ketchum. (Jan. 15 Tr. (Ketchum) 88:22–89:14.) As Mr. Ketchum admitted, he understood that Mr. Montagner had contacted him seeking information about Sound Point and SPSO, but Mr. Ketchum intentionally avoided speaking with Mr. Montagner, only returning one call at an "odd hour" because he did not want to speak to him. (Jan. 15 Tr. (Ketchum) 88:22–89:14.)
- 225. Mr. Montagner also asked Mr. Holtz to schedule a meeting with Mr. Ketchum. Mr. Holtz told Mr. Montagner that Mr. Ketchum did not want to meet with LightSquared at that time. Mr. Holtz did not get any further information. (Montagner Dep. 53:25–54:21.) Mr. Ketchum admitted to receiving Mr. Holtz's inquiries, but did not give him information about Sound Point's LP Debt purchases. (Jan. 15 Tr. (Ketchum) 89:15–22.)
- 226. LightSquared's investigation continued in 2013. As reflected in the minutes of LightSquared's board of directors meeting on April 18, 2013, Moelis and Sound Point had a meeting, but Sound Point would not disclose its investors or beneficial owners. (Jan. 9 Tr. (Smith) 154:25–155:15; PX0443.)
- 227. Moelis persisted in its efforts, calling "Mr. Ketchum regularly and meet [ing] with him regularly, and ... continu[ing] during that period [i.e., spring 2013] to try and find out who Sound Point-if they were representing somebody and what their intention was." Mr. Ketchum continued to refuse to identify Sound Point's investors or intentions. (Jan. 17 Tr. (Hootnick) 23:13–24; Jan. 15 Tr. (Ketchum) 88:22–89:22; PX0443.)
- 228. Further, Mr. Hootnick directly "ask[ed] Mr. Ketchum if he was working with Mr. Ergen ... but [Ketchum] refused to answer any of those questions." (Jan. 17. Tr. (Hootnick) 19:8–20; Jan. 15 Tr. (Ketchum) 88:22–89:14; 89:18–22.) Mr. Hootnick also reached out to Rachel Strickland of Willkie Farr, who had represented Mr. Ergen in the TerreStar

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bankruptcy, to see whether she would shed light on whether Mr. Ergen was involved in SPSO's LP Debt purchases. (Jan. 17 Tr. (Hootnick) 19:21–21:3, 64:3–9.) Despite more than six phone calls and "a couple" of lunch meetings, Ms. Strickland would not confirm whether Mr. Ergen was involved. (Jan. 17 Tr. (Hootnick) 20:22–21:3.)

229. Aside from relying on LightSquared and its financial advisor to determine for whom Sound Point was purchasing the LP Debt, Mr. Falcone undertook his own extensive efforts to ascertain who *305 was behind SPSO, "turn[ing] over every rock," including enlisting the help of LightSquared management and reaching out to "people on the street," reporters, Mr. Cullen of DISH, and representatives of AT & T and Sprint. (Jan. 16 Tr. (Falcone) 22:1–11.) Mr. Falcone further utilized Harbinger employees and advisors, as well as colleagues and acquaintances, to gather information. (Jan. 16 Tr. (Falcone) 36:17–37:15, 38:6–22, 39:3–10, 39:18–40:7, 40:8–12, 41:8–19, 43:23–44:2, 44:21–45:17, 47:4–9, 53:11–54:22, 55:14–56:1, 56:3–57:8, 59:11–20, 59:21–60:22; DX037; DX097; PX0142; DX358; DX378; DX386.) Neither Harbinger nor LightSquared took any legal action to determine the identity of the party behind SPSO.

F. On May 21, 2013, LightSquared and Harbinger Definitively Learn that Mr. Ergen is Behind SPSO

230. On May 21, 2013, counsel for Mr. Ergen disclosed to counsel for LightSquared that Mr. Ergen was the sole investor in SPSO. (PX0539; Jan. 9 Tr. (Smith) 129:14–18; Jan. 16 Tr. (Falcone) 24:11–19; Jan. 17 Tr. (Hootnick) 15:25–16:12.)

231. Hours before receiving confirmation, Mr. Falcone advised representatives and advisors for Harbinger and LightSquared that "[i]f I were a betting man I would say that Sound Point is Slim." (Jan. 16 Tr. (Falcone) 72:25–73:18; PX0540.) Upon receipt of counsel's email confirming that Mr. Ergen was in fact the ultimate purchaser of Sound Point's LP Debt, Mr. Falcone responded "[f]ortunately, I'm not a betting man." (Jan. 16 Tr. (Falcone) 73:19–74:9; PX0537.)

X. SPSO Delays Closing Hundreds of Millions of Dollars in LP Debt Trades for Several Months During a Critical Time in LightSquared's Bankruptcy Case

232. Messrs. Ergen and Kiser testified that there were "economic" reasons for leaving the LP Debt trades open for as long as possible, that they were prepared to close "as soon as the upstreams paperwork" was done, and that they never intended to delay the settlement of the trades. (Jan. 10 Tr. (Kiser) 64:5–25, 128:20–23; Jan. 13 Tr. (Ergen) 63:7–9.) The documentary evidence is to the contrary. Efforts were undertaken to delay the closing of SPSO's LP Debt trades in that, among other things: (i) Mr. Ergen was insistent on holding onto his money for as long as possible; (ii) Mr. Ketchum—at Mr. Kiser's direction—gave false excuses to SPSO's counterparties to delay the closing of the trades; (iii) Mr. Ergen had no incentive to close the LP Debt trades because he could direct the vote on the trades even before they settled; (iv) there is no evidence in the record that a decision to settle the LP Debt trades was driven by a return Mr. Ergen received on his assets held at Bear Creek; (v) a delay in settling the LP Debt trades was not due to liquidity concerns because hundreds of millions of dollars of Mr. Ergen's Bear Creek investments were liquidated and held in Mr. Ergen's account and additional investments could have been liquidated in a matter of days; and (vi) inconsistent and contradictory testimony was given regarding the reasons why settlement was delayed, including the need to complete "upstreams paperwork." (See, e.g., PX0204; PX0481; PX0466; PX0498; PX0495; Jan. 10 Tr. (Kiser) 64:5–25, 95:20–23, 128:24–131:23; Roddy Dep. 66:7–25, 85:17–86:4, 87:9–16.)

A. Mr. Kiser, with Sound Point's Assistance, Delays the Closing of LP Debt Trades

233. Mr. Kiser testified that Mr. Ergen delayed closing hundreds of millions of dollars in LP Debt trades because Mr. Ergen was insistent on holding onto his *306 capital for as long as possible and would only fund trades when they needed to close. (Jan. 10 Tr. (Kiser) 57:4–6; Jan. 13 Tr. (Ergen) 59:13–22.) Thus, when Sound Point entered into a trade for LP Debt, Mr. Kiser would have to create the liquidity necessary to fund the purchases and wire the funds to the accounts set up for SPSO. (Jan. 10 Tr. (Kiser) 87:13–23.) Prior to closing a trade, Messrs. Kiser and Ergen provided Bear Creek—the financial manager for DISH, EchoStar, and Mr. Ergen—with a wire transfer authorization and Bear

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Creek would liquidate assets to fund the trades. (Jan. 10 Tr. (Kiser) 21:23–22:18, 57:7–58:12; Jan. 10 Tr. (Ergen) 57:7–15; Roddy Dep. 42:18–43:14, 45:3–19.)

- 234. Of the 25 trades entered into by SPSO for purchases of LP Debt, eighteen of them took over two months to settle, and, of those eighteen trades, six took over four months to settle. (PX0859.) By May 20, 2013, SPSO had contracted for, but had failed to settle, approximately \$593,757,000 in face amount of LP Debt trades (and approximately \$610,000,000 counting trades held by brokers on that date)—more than 33 percent of the total outstanding LP Debt obligations—and had kept open a number of trades that it had entered into as far back as December 12, 2012. *Id.*
- 235. SPSO's counterparties to the hundreds of millions of dollars in open LP Debt trades repeatedly reached out to Sound Point to settle the trades and were paper-work ready to do so. (Jan. 15 Tr. (Ketchum) 80:23–81:6, 85:15–25, 105:4–16, 109:8–111:12; PX0279; PX0495 at SPSO–00003025; PX0859; PX0204; PX0209; PX0270; PX0308; PX0319; PX0328; PX0339.) Messrs. Kiser and Ergen, contrary to their testimony, delayed closing even when they knew counterparties were anxious to close. To assuage the concerns of SPSO's counterparties, Sound Point offered various excuses to counterparties. Mr. Ketchum testified that he did not know specifically why SPSO was unable to close the LP Debt trades timely and only knew Mr. Kiser wanted to delay. (Jan. 15 Tr. (Ketchum) 69:3–16; *see*, *e.g.*, PX0204 (Sound Point employee emailing Mr. Ketchum on June 4, 2012 regarding a LightSquared trade entered into on May 3, 2012 and stating, "Jefferies is looking to settle the other two trades. Do you want to? Or delay?"); PX0481; PX0523.)
- 236. For example, on January 14, 2013, UBS sought to close a trade with SPSO that had been pending for months. Mr. Ketchum, in an email to his colleague, said he "forwarded this to EchoStar." Three days later, the colleague asked Mr. Ketchum, "would you mind following up with EchoStar [because] UBS has asked to close again." By January 24, 2013, UBS again was pressuring Sound Point to close the trades, "emailing to close daily," and Sound Point continued to delay. "Try and hold them off for another day," another Sound Point employee responded. (PX0348; see also PX0319 (Sound Point on January 14, 2013, replying "[s]orry but we are not able to settle that one right now" in response to weekly inquiries from UBS); PX0328 (Sound Point internally discussing following up with "Echostar" regarding UBS trade); PX0364 (March 7, 2013 Sound Point email stating it would be able to settle "next week" in response to repeated inquiries since February 2013 regarding a December 2012 trade).)
- 237. On February 19, 2013, a Sound Point employee asked Mr. Ketchum to follow up with Mr. Kiser regarding ongoing email and telephone requests from Jefferies to close multiple trades, with trade dates going back as early as October 23, 2012. (PX0347; PX0859.) The employee reminded Mr. Ketchum that "[w]e have *307 been pushing Jefferies off for nearly 3 weeks." (PX0347.)
- 238. Then, on April 23, 2013, Mr. Ketchum wrote to Mr. Kiser, "Kevin [of Sound Point] thinks we can hold [Jefferies] off on any payments until at least May 15" in connection with over \$289 million in LP Debt that had not settled. (PX0458; PX0441; PX0859.) Jefferies followed up with Sound Point on April 25, 2013, seeking to close \$88 million of the open LP Debt purchases. (PX0466.) Mr. Ketchum inquired internally as to whether he could blame SPSO's delay on the "upstreams," *i.e.*, the work required to trace back the chain of ownership to original lenders, but he was told by Sound Point personnel that such work had already been completed. (PX0466; Jan. 15 Tr. (Ketchum) 76:9–77:8.)
- 239. When a Sound Point employee asked Mr. Ketchum for a "reason and an eta" to give Jefferies, another employee suggested telling Jefferies "we are waiting on funding from our investor." Mr. Ketchum rejected that idea, and proposed a different excuse: "Let's not say that. Let's just say we are in the process of exiting some other large positions we have to pay for this and that I have spoken with Steve Sander (head of sales) [at Jefferies] about this." (PX0466; see also PX0468 (Mr. Ketchum stating that they should tell Sound Point that "our LP wants time to dispose of other assets"); PX0308 (Jefferies repeatedly inquiring whether funds are available); PX0341 (Sound Point writing to Jefferies that they are "still waiting on the funds"); Jan. 10 Tr. (Kiser) 63:15–20.)

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240. On May 9, 2013, Jefferies emailed Sound Point again, imploring Mr. Ketchum to address the open trades. (PX0498.) As of that date, SPSO had seven open trades with Jefferies, totaling approximately \$588 million in LP Debt from trades dating back as far as January 2013. (PX0859.) Mr. Sanders of Jefferies pleaded in an email to Mr. Ketchum: "this is a big problem for me. I would like to come down and talk to you this afternoon around 4 or 5pm mano a mano [.] Is this possible?" Mr. Ketchum replied, offering the party line established the day before—that he was waiting for other "trades to settle." Mr. Ketchum went on to state that he had "already pushed extremely hard to get to where we are now in terms of closing." (PX0498.) Notwithstanding the pressure from Jefferies, none of the open trades closed for another several weeks. (PX0859.)

241. Knowing Jefferies was anxious to close the open trades and aware that the volume of unsettled LP Debt trades was substantial, Sound Point prepared a schedule of "Proposed Settlement Dates" to send to Mr. Kiser—selecting proposed dates up to four months or more after the initiation of the trade as illustrated by the following chart included in an email exchanged between Messrs. Ketchum and Kiser on May 8, 2013:

Proposed Settlement Dates

Trade Date	Cost	Type	Desk	Settlement Date	Cumulative
01/07/13		TLB	JEFF	05/17/13	
01/14/13		TLB	JEFF	05/17/13	
12/12/12		TLB	GS	06/01/13	
03/25/13		TLB	JEFF	06/01/13	
02/01/13		TLB	JPM	07/01/13	
03/28/13		TLB	JEFF	07/01/13	
04/01/13		TLB	SEAPORT	07/01/13	
03/28/13		Pref	JEFF	07/15/13	
04/19/13		TLB	JEFF	08/01/13	
04/26/13		TLB	JEFF	08/15/13	

(PX0495 at SPSO-00003025; *see also* PX0460; PX0461; PX0474; PX0497; PX0454 (April 22, 2013 internal Sound Point email noting that the amount of unsettled trades had "jumped to almost \$404 [million]"); Jan. 15 Tr. (Ketchum) 109:1- *308 111:12.) Sound Point provided the proposed settlement dates to Jefferies to give assurance (even though there was none) that the LP Debt trades would close. (Jan. 15 Tr. (Ketchum) 123:12-124:1.) Mr. Ketchum stated that the "proposed settlement dates" in the schedule he emailed to Mr. Kiser on May 8 were suggested by Mr. Ketchum as a "compromise solution" in order to get the open Jefferies trades settled, and he proposed the schedule to Mr. Kiser before conveying such dates to Jefferies in order to see if a schedule of this kind was capable of execution by SPSO. (Jan. 15 Tr. (Ketchum) 124:12-17.) 35 Mr. Ketchum's testimony that these dates were "projections" of the dates upon which he thought the open trades would close was not credible; rather, these dates reflect a gameplan for delaying the closings. 36

See also Jan. 15 Tr. (Ketchum) 132:8–15 ("my job was to find a date, propose a date to SPSO that I thought was reasonable in the context of closing distressed trades, obtain permission from SPSO, and in particular, Jason, to go back and offer those dates to Jefferies so that they could be mollified and feel that there was some sort of definition around when the trades would be closed.").

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Mr. Kiser testified that he instructed Mr. Ketchum to prepare a schedule for him showing unsettled trades and expected settlement dates so that he could have the money available on those dates, in order to avoid the "back-and-forth" with counterparties who may not have been ready to close when the funds were made available. (Jan. 10 Tr. (Kiser) 63:25–64:14) ("And it got to a point where I told Steve, hey, look, get me a list and tell me when these things will trade so that we can have the money available for them rather than doing this back-and-forth type of thing."). This testimony was also not credible.

242. Sound Point also performed an internal analysis on May 8, 2013 which showed that, to settle the LP Debt trades with Jefferies, SPSO took an average of 69 days after the trade date and 38 days after the "contractual settlement date" of "T+20," or twenty days after the trade date. (PX0493.) There is no reason for Sound Point to have performed such an analysis other than to provide support for its proposed further delays. Indeed, trade counterparties were keenly aware of SPSO's failure to adhere to the industry norms for the timing of settlements. For example, Jefferies emailed Sound Point, "[w]e are past the T+20 date and would really like to get this off our books." (PX0205; see also PX0209; PX0270; PX0234.)

243. Frustrated with the unprecedented delay in closing the trades, Jefferies complained internally that "[w]hat the buyer has done is not market protocol" and separately to its immediate counterparty that "we remain beholden to [Sound Point] as far as continuing to make progress." (PX0538; PX0880.)

B. There was No True Economic Benefit for Messrs. Ergen and Kiser to Keep the LP Debt Trades Open

244. Messrs. Kiser and Ergen consistently testified that they were "in no rush to close" because it was to Mr. Ergen's economic benefit to wait as long as possible before closing on the trades. (Jan. 10 Tr. (Kiser) 97:23–99:14; Jan. 13 Tr. (Ergen) 157:16–158:6.) As Mr. Kiser testified, Mr. Ergen "was getting a return on his capital and his investments. So if he didn't have to pay for it and he can make money on another end where his money was invested, that seemed like a smart move." (Jan. 10 Tr. (Kiser) 98:3–6.) However, Bear Creek account statements reflect that Mr. Ergen earned a relatively low rate of interest on the funds in his trust accounts. (PX0796–818.)

245. On July 9, 2013, SPSO filed with the Court a joinder; annexed as Exhibit A to the joinder was an amended stipulation (the "SPSO Stipulation") stating that "the timing of closing of each of SPSO's acquisitions of Prepetition LP Obligations was primarily driven by the sellers of such claims." (PX0699 \P 16.) This was not true. A prior July 3, 2013 stipulation, which was modified and amended by the *309 SPSO Stipulation, had stated that "SPSO's trade counterparties did not request that SPSO settle or close the trades for several months" and that "SPSO and Ergen took no action to delay" the closing of any of the trades. (PX0699; PX0858.) Each of these statements by SPSO's counsel was contradicted by Messrs. Ergen, Kiser, and Ketchum.

246. Mr. Ergen understood that he did not need to "rush" to close the trades because he could direct the vote of the LP Debt he had purchased without settling on the trade, as it was common practice for the seller of the LP Debt to give the buyer the option to vote on matters relating to the LP Debt. (Jan. 13 Tr. (Ergen) 163:1–10; Jan. 10 Tr. (Kiser) 64:17, 97:25, 129:7–13; PX0111.)

247. There were economic costs associated with leaving the LP Debt trades open for extended periods of time that were not taken into account, despite the parties' awareness of such costs. If SPSO failed to close certain LP Debt trades by the closing date specified in the purchase agreement, it was charged a penalty "cost of carry fee" and in some instances had to forgo receiving a share of Adequate Protection Payments ³⁷ for the unsettled trade. (See Agreed Final Order (A) Authorizing Debtors to Use Cash Collateral, (B) Granting Adequate Protection to Prepetition Secured Parties, and (C) Modifying Automatic Stay [Bankr. Docket No. 136] at 18 (granting adequate protection for Lenders); Jan. 15 Tr. (Ketchum) 81:1–82:3; PX0493; see, e.g., DX104 at LSQ–SPCD–000000176 (imposing "AP Payment" and "cost of carry" fees from T+20 to settlement date); DX109 at LSQ–SPCD–000000285; PX0851 at SPSO–00000072; PX0650 at LSQ–SPCD–000000073.) Despite these economic costs, Sound Point only closed one LP Debt trade—the May 4, 2012

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purchase of \$247 million in LP Debt from Carl Icahn's company Icahn Enterprises LP—within the contractual settlement period. (Jan. 15 Tr. (Ketchum) 82:7–15; PX0493; PX0859.)

- "Adequate Protection Payments" refer to the payments of \$6,250,000, made on the first business day of each month, and distributed as interest payments to holders of LP Debt after the payment of nonprofessional and professional fees pursuant to the Agreed Final Order (A) Authorizing Debtors to Use Cash Collateral, (B) Granting Adequate Protection to Prepetition Secured Parties, and (C) Modifying Automatic Stay (Bankr. Docket No. 136 at 18), and the Amended Final Order Authorizing Debtors to Use Cash Collateral, (B) Granting Adequate Protection to Prepetition Secured Parties, and (C) Modifying Automatic Stay. (Bankr. Docket No. 136 at 18–19; Bankr. Docket No. 544 at 18–19.)
- 248. Neither Mr. Kiser nor Mr. Ergen monitored the interest earned on the specific assets of the Trust selected for liquidation, and they had no involvement in the selection of those assets. (Jan. 10 Tr. (Kiser) 128:24–131:23.)
- 249. Bear Creek, in its sole discretion, decided which assets to liquidate from the Trust, and Messrs. Ergen and Kiser both testified that they had no knowledge of how the assets were liquidated. (Jan. 13 Tr. (Ergen) 159:20–24.) Bear Creek's corporate representative testified that he selected assets for liquidation based on "which ones are the easiest to liquidate closest to the market value," and generally selected assets with low interest rates, consistent with the overall conservative nature of the Trust. (Roddy Dep. 57:9–58:3, 58:20–22, 59:6–12, 69:7–11.) The Bear Creek representative was not aware that SPSO may have to pay cost of carry fees and forego Adequate Protection Payments if the LP Debt trades were not closed by a certain date and, therefore, this had no impact on assets selected for liquidation. (Roddy Dep. 67:15–69:22, 86:5–87:3.) Only Messrs. Ergen and Kiser, and not the *310 Bear Creek representatives, were aware that SPSO was accruing (and possibly missing out on) Adequate Protection Payments by delaying the closing of trades. (PX0258; PX0256; PX0259.)

C. LP Debt Trades Were Not Left Open Due to Liquidity Constraints

- 250. Messrs. Ergen, Kiser, and Ketchum offered two main explanations to account for the lengthy delays between the trade and settlement dates: (1) Mr. Ergen did not have immediate liquid funds available (Jan. 10 Tr. (Kiser) 129:23–131:18; Jan. 15 Tr. (Ketchum) 69:3–25); and (2) the necessary paperwork or "upstreams" were not complete. (Jan. 10 Tr. (Kiser) 62:1–17, 128:24–129:22.) Neither explanation is credible.
- 251. Mr. Kiser gave inconsistent testimony as to the role of liquidity in the settlement delays. At Trial, he denied that liquidity caused any delays. (Jan. 10 Tr. (Kiser) 128:24–129:13.) When reminded that he had stated otherwise at his deposition, Mr. Kiser conceded that he "gave that as an example of one thing" that caused delays. (Jan. 10 Tr. (Kiser) 129:23–130:1.)
- 252. Contrary to the testimony of Mr. Kiser and Mr. Ketchum (Jan. 10 Tr. (Kiser) 129:23–131:18; Jan. 15 Tr. (Ketchum) 84:10–14), a lack of available liquidity does not explain the significant delays in closing. SPSO's LP Debt purchases were funded by Mr. Ergen's assets held in the Trust. When SPSO was ready to close a trade, Mr. Ergen would authorize a wire transfer from the Trust, which Bear Creek made available for transfer within several days. (Roddy Dep. 66:12–25, 85:17–86:4, 87:9–16; PX0091; PX0273; PX0353; PX0519.) Mr. Ergen testified: "As far as I know, I don't believe, other than several days, or perhaps a Friday where it didn't make economic sense to wire money, that there was [sic] any delays because of that reason." (Jan. 13 Tr. (Ergen) 159:13–19.)
- 253. Neither Mr. Kiser nor Mr. Ergen could identify a single instance in which liquidating assets to free up funds for SPSO took longer than a few days. (Jan. 10 Tr. (Kiser) 132:10–20; Jan. 13 Tr. (Ergen) 158:7–159:19.) In at least one case, liquid funds were readily available, but Mr. Kiser instructed Bear Creek to hold off on wiring funds. (See PX0530 (Kiser instructs Bear Creek on May 20, 2013 to "[w]ait for the green light from me prior [to] sending. Obviously it's not going today so just check with me each morning.").) The account statements produced by Bear Creek reflect that, as of April

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30, 2013, some \$461 million held in the Trust account had been liquidated, and, as of May 31, 2013, approximately \$207 million in liquid funds still remained in the Trust account. (PX0810; PX0812.)

254. Despite acknowledging that he had testified at his deposition that liquidity issues were the sole cause for delay, Mr. Kiser testified at Trial that delays were primarily caused by the amount of time it took to complete the necessary paperwork, and that he waited until Mr. Ketchum advised him that a LightSquared trade needed to close and then arranged for the necessary liquidity. (Jan. 10 Tr. (Kiser) 62:1–17, 95:20–96:4, 129:23–130:1.) Yet, Mr. Kiser admitted that, even when provided with notice that counterparties were ready to close, he sought to defer settlement as long as possible. (Jan. 10 Tr. (Kiser) 64:5–25, 97:23–98:6.) There were numerous instances over a course of months in which SPSO's counterparties repeatedly asked Sound Point to settle hundreds of millions in open trades before Messrs. Kiser and Ergen finally arranged for settlement. (See e.g., Jan. 15 Tr. (Ketchum) 85:2–13; PX0859.)

*311 255. Mr. Ketchum testified that he had no conversations with Mr. Kiser as to why funds were not available for closing and had no understanding of Mr. Ergen's liquidity at that time. (Jan. 15 Tr. (Ketchum) 70:7–15.) When funds did not arrive timely, he assumed, based on remarks "from Mr. Kiser that things had to be sold, cash had to be raised to settle those trades, and so informed counterparties." (Jan. 15 Tr. (Ketchum) 84:10–14.)

XI. LightSquared and its Creditors Were Injured by SPSO's Conduct

256. At various points during LightSquared's bankruptcy, LightSquared, Harbinger, and the Ad Hoc Secured Group attempted to work together on the terms of a consensual plan of reorganization. (Jan. 17 Tr. (Hootnick) 21:24–22:24; Jan. 9 Tr. (Smith) 130:3–18; Montagner Dep. 75:21–76:5.)

257. On February 13, 2013, this Court entered the Second Exclusivity Extension Order, incorporating the terms of the Exclusivity Stipulation. (Docket No. 522; PX0852.) The Exclusivity Stipulation extended LightSquared's exclusivity period to July 15, 2013, and required the parties to engage in good faith negotiations regarding the terms of a consensual chapter 11 plan. (PX0852 at 3–4.) If a consensual plan was not reached by July 15, 2013, a sales process for LightSquared's assets would begin. (PX0852 at Ex. A \P 6.) The Exclusivity Stipulation also provided that it could be terminated if the Ad Hoc Secured Group, collectively, ceased to be the largest holder of the LP Debt. (Id. at \P 15.)

A. Negotiations with the Ad Hoc Secured Group Are Affected by SPSO's Pending LP Debt Trades

258. In late March 2013, Sound Point entered into trades with Fortress and Providence Capital LLC ("*Providence*") to purchase their significant LP Debt holdings, as well as their LP Preferred Interests. (DX136; DX139.) As a result of these trades, Fortress and Providence thereafter ceased participating in negotiations with respect to a consensual plan of reorganization for the Debtors. (Jan. 17 Tr. (Hootnick) 21:4–17, 22:4–23:7; Jan. 16 Tr. (Falcone) 75:13–76:8; PX0611; *see also* PX0617.) In an April 18, 2013 meeting of the LightSquared Board of Directors, Mr. Montagner reported that LightSquared had met with several large holders of the LP Debt to explore ideas for a consensual plan of reorganization. However, "further discussions were halted after Sound Point agreed to purchase the LP preferred stock from these investors." (PX0443 at L2AP0000924.)

259. As Sound Point continued to purchase large blocks of the LP Debt, LightSquared was not sure which lenders to negotiate with and whether the Ad Hoc Secured Group was able to carry a class such that it could enter into a binding commitment with respect to a plan. (Jan. 9 Tr. (Smith) 130:3–131:12; Jan. 17. Tr. (Hootnick) 69:1–12; Jan. 16 Tr. (Falcone) 14:9–20, 22:15–21, 145:5–15, 151:24–152:2; PX0465; PX0486.)

B. Once SPSO Discloses its Blocking Position and Joins the Ad Hoc Secured Group, Plan Negotiations Cease

260. Mr. Ergen made the LBAC Bid on May 15, 2013 and announced his LP Debt holdings on May 21, 2013. The LBAC Bid and Mr. Ergen's announcement were made at a time when LightSquared's Board and management team were

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exploring whether a joint venture or strategic partnership would allow LightSquared to raise capital and form the basis for a plan to emerge from bankruptcy. (Jan. 17 Tr. *312 (Hootnick) 27:11–22; Jan. 9 Tr. (Smith) 134:22–135:1.)

261. Beginning in late May 2013 and continuing thereafter, LightSquared's financial advisor Moelis contacted over 90 parties to discuss a joint venture or strategic partnership. (Jan. 17 Tr. (Hootnick) 28:6–16.) Parties approached included the "existing telecom parties with wireless operations in the United States: AT & T, Verizon, Sprint and T–Mobile." (Jan. 17 Tr. (Hootnick) 28:17–23, 77:16–18.) LightSquared and Moelis proposed a "low-cost option" for an equity investment by strategic investors, but advised that LightSquared was "certainly open to anything." (Jan. 9 Tr. (Smith) 140:21–142:11.)

262. On June 7, 2013, the Debtors received Court approval to enter into and perform under an engagement letter with Jefferies in connection with securing potential exit financing for the Debtors [Bankr. Docket No. 667], after which a "road show" kicked off to seek to raise capital.

263. On July 1, 2013, Mr. Montagner reported to the LightSquared Board that, after the Bankruptcy Court approved the engagement letter with Jefferies, LightSquared "immediately embarked on marketing efforts, including approximately 50 investor meetings. The Company is seeking a commitment from investors by July 15th with two pre-conditions to funding: 1) FCC approval of the Company's alternative spectrum plan and 2) court approval of a plan of reorganization." (PX0679; Montagner Dep. 165:25–166:22.)

264. According to Mr. Hootnick, with respect to meetings with Sprint, AT & T, and TMobile, "there was a lot of interest in the L-Band ... [b]ut one of the main reactions was doesn't Charlie Ergen already own this." While Moelis went to "great lengths" to assure potential partners that Mr. Ergen did not own LightSquared, Mr. Hootnick stated that "it was somewhat challenging" in light of a *Bloomberg* article reporting that Mr. Ergen was "on his way to acquiring LightSquared." (Jan. 17 Tr. (Hootnick) 28:17–23, 29:21–30:22, 77:13–78:1.)

265. Similarly, Mr. Smith, who attended the meetings with Sprint, AT & T, T–Mobile, and Verizon, testified that these parties questioned whether they should get involved in light of Mr. Ergen's blocking position and the LBAC Bid; strategics believed that LightSquared's ownership was a "foregone conclusion." (Jan. 9 Tr. (Smith) 137:9–138:13.)

266. Mr. Hootnick testified that potential strategic partners were also concerned about Mr. Ergen's involvement because they believed that he was acquiring spectrum "to warehouse" it and "not for a financial return." (Jan. 17 Tr. (Hootnick) 32:4–34:14.) At Trial, Mr. Cullen confirmed that, despite the fact that DISH has not yet deployed the spectrum assets it acquired from DBSD and TerreStar in March 2012, it continues to pursue additional spectrum, and intended to participate in the then-upcoming auctions for H Block and AWS–3 spectrum assets. He also testified that DISH intends to wait until it can "understand the totality of spectrum" that it can "partner or pair[,] before you start deploying on any towers." (Jan. 17 Tr. (Cullen) 149:5–150:3.)

267. On June 15, 2013, Mr. Hootnick advised Mr. Falcone that Moelis was "pushing forward with some of the strategic discussions and [we']re reviewing smaller capital raises" but "[c]learly the ad hoc group changes have chilled that avenue." (PX0645.)

C. Within Weeks of SPSO's Joining the Ad Hoc Secured Group, the LBAC Bid is Adopted

*313 268. On June 13, 2013, SPSO joined the Ad Hoc Secured Group in order to keep the Exclusivity Stipulation in effect. (PX0858 at ¶ 13; PX0852 at Ex. A ¶¶ 7, 8.) 38 After SPSO joined the Ad Hoc Secured Group, neither Mr. Ergen nor SPSO participated in any meetings of the Ad Hoc Secured Group (Jan. 13 Tr. (Ergen) 89:7–9).

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- SPSO's counsel also stated in closing arguments of the Trial that SPSO joined the Ad Hoc Secured Group solely for the purpose of maintaining the "lender protections" of the Exclusivity Stipulation. Mar. 17 Tr. (Strickland) 189:12–191:4 ("[SPSO] was very much focused on those lender protections, and that's why it joined the group.")
- 269. Within days of SPSO's joining the Ad Hoc Secured Group, several hundred million dollars of its "hung" trades closed, making SPSO the controlling member of the group by virtue of the size of its holdings. (PX0649 at L2AP0008732; PX0625; PX0859.)
- 270. On April 4, 2013, the Ad Hoc Secured Group had submitted a proposed plan term sheet to LightSquared and indicated its willingness to commence discussions with respect thereto. (PX0410.) The term sheet contemplated a plan in which all creditor and preferred equity classes would receive a full recovery and LightSquared would emerge from bankruptcy with its spectrum assets intact. (*Id.* at HARBAP00015399–400; *see also* Jan. 17 Tr. (Hootnick) 21:24–22:24.) Also, on May 15, 2013—the same day that Mr. Ergen submitted the LBAC Bid—the parties exchanged a revised term sheet for a consensual plan of reorganization. (PX0505; DX335; DX174.) The revised term sheet provided for an infusion of new capital to be obtained by Harbinger and/or LightSquared and a reorganization, such that a sale of LightSquared's assets would be avoided. (PX0505 at HARBAP00005107–13.)
- While a sale of LightSquared's assets was a possible resolution, it was not the primary goal the parties contemplated at that time. Indeed, prior to the summer of 2013, Moelis did not engage in any discussions regarding a sale. (Jan. 17 Tr. (Hootnick) 83:15-23.)
- 271. On May 21, 2013, the parties began to consider a plan that bifurcated the class of creditors holding LP Debt by providing a different recovery scheme for SPSO and non-SPSO holders of LP Debt. For example, a term sheet exchanged with the Ad Hoc Secured Group on May 24, 2013 envisioned that SPSO would receive full cash recovery while non-SPSO lenders would receive cash recovery and warrants. (PX0561.)
- 272. Once SPSO had acquired a blocking position and joined the Ad Hoc Secured Group, LightSquared believed it was effectively impossible for it to reach a consensual deal with the Ad Hoc Secured Group. (Jan. 16 Tr. (Falcone) 182:23–183:2; 226:4–16.)
- D. LightSquared's Negotiations with Creditors Come to an End After the Filing of the Ad Hoc Secured Group Plan 273. Approximately one month after SPSO joined the Ad Hoc Secured Group, on July 23, 2013, the Ad Hoc Secured Group filed the PSA, seeking approval of the DISH/LBAC Bid. (PX0823.) Negotiations towards a plan in which LightSquared would continue as a going concern came to an end. (Jan. 16 Tr. (Falcone) 76:9–25, 225:14–20; PX0823.)
- 274. The PSA bound the Ad Hoc Secured Group to support the DISH/LBAC Bid, stating that the parties to the PSA "[s]hall not directly or indirectly seek, solicit, support, or vote in favor of any other plan, sale, proposal, or offer of dissolution, *314 winding up, liquidation, reorganization, merger, or restructuring of the Debtors other than the Plan[.]" (PX0823 at 1.1(a)(6).) Accordingly, at that time and pursuant to its contractual obligations, the Ad Hoc Secured Group ceased negotiating with any other party, including LightSquared, toward any other plan of reorganization.

E. LBAC and DISH Seek to Obtain Broad Releases for Themselves and Their Affiliates in the Ad Hoc Secured Group Plan

275. The Ad Hoc Secured Group Plan and the APA filed therewith included broad releases for LBAC and its affiliates, including DISH, EchoStar, and Mr. Ergen and his affiliates, including SPSO, requiring that SPSO's claim be allowed in its full face amount. (See First Amended Joint Chapter 11 Plan for LightSquared LP, et al., Proposed by the Ad Hoc Secured Group of LightSquared LP Lenders [Bankr. Docket No. 970, Ex. A] § 13.1; Stalking Horse Agreement, filed October 28, 2013 [Bankr. Docket No. 970, Ex. F] § 3.2(a)(ii) & n.9.)

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276. On multiple occasions, Defendants represented that the DISH/LBAC Bid and SPSO's LP Debt purchases were separate and independent transactions. (PX0731 at 29:18–31:4; PX0766 at 9:4–24.) Other than characterizing the releases as "customary," Defendants were unable to explain why, if Mr. Ergen and SPSO were not acting for DISH, the APA—which was between DISH and LightSquared—included a release for Mr. Ergen personally as well as for SPSO. (PX0765; Dec. 10 Tr. 137:16–21.)

277. The Nevada Court presiding over the action captioned *In re DISH Network Corporation Derivative Litigation*, Case No.: A–1 3–686775–B also recognized the conflict of interest inherent in a DISH release that benefits Mr. Ergen personally. In granting a limited preliminary injunction on November 27, 2013, the Nevada Court found that "the U.S. Bankruptcy Trustee has made an objection to the scope of the release in the bankruptcy plans, including the Ad Hoc Secured Group's plan," and that while "DISH has a significant interest in exploring the possibility of ... modifying the release and carving out claims against SPSO and Ergen," it was also the case that "DISH is unable to explore this option so long as DISH's actions in the LightSquared bankruptcy relating to the release provisions are controlled by Ergen." (PX0780 (Findings of Fact and Conclusions of Law, dated November 27, 2013, issued by District Judge Gonzalez) at 15.) Accordingly, the Nevada Court enjoined "Ergen or anyone acting on his behalf ... from participation, including any review, comment, or negotiations related to the release ... for any conduct which was outside the scope of his activities related to DISH and LBAC." (*Id.*)

DISCUSSION

I. Introduction

The Complaints assert a variety of causes of action against Defendants DISH, EchoStar, SPSO, and Mr. Ergen. The Complaints seek redress against Mr. Ergen and the entities he controls for his allegedly unlawful conduct in purchasing the LP Debt in violation of the provisions of the Credit Agreement that prohibit Disqualified Companies from purchasing LP Debt. Under one or more of several theories of liability, ⁴⁰ Plaintiffs maintain that *315 SPSO is not an Eligible Assignee and that, therefore, the claim of SPSO ⁴¹ should be disallowed or, in the alternative, subordinated, pursuant to section 510(c) of the Bankruptcy Code. The Complaints also assert that SPSO and Mr. Ergen engaged in additional inequitable conduct during the course of these cases, conduct which Plaintiffs assert provides further reason for the Court to impose the remedy of equitable subordination to redress the harm caused to innocent creditors. For the reasons discussed below, the Court has determined that, although the SPSO Claim shall not be disallowed, it shall be equitably subordinated in an amount to be determined. ⁴²

- Plaintiffs must prove their claims for breach of contract and tortious interference by a preponderance of the evidence. See Dollar Phone Corp. v. Dun & Bradstreet Corp., No. 13–1428–cv, 559 Fed.Appx. 71, 72, 2014 WL 1042916 at *1 (2d Cir. March 19, 2014) (holding that in order to recover from a defendant for breach of contract, a plaintiff must prove the elements of breach by a preponderance of the evidence) (citing Diesel Props S.r.l. v. Greystone Bus. Credit II LLC, 631 F.3d 42, 52 (2d Cir.2011)); Raymond v. Marks, No. 96–9337, 1197 WL 345984 at *1 (2d Cir. June 24, 1997) ("Under New York law, the party asserting a breach of contract claim has the burden of proving the material allegations in the complaint by a fair preponderance of the evidence."); In re Cross Media Marketing Corp., 367 B.R. 435, 460 (S.D.N.Y.2007) (holding that plaintiff failed to meet the standard of proving tortious interference with a contract by a preponderance of the evidence). To establish a claim by a preponderance of the evidence means "to prove that something is more likely so than not so." Abrams v. United States, No. 66–CIV–1585, 1970 WL 432 at *1 (S.D.N.Y. Nov. 19, 1970).
- 41 As a holder of LP Debt under the Credit Agreement, SPSO holds a secured claim against LightSquared LP on account of such debt. This claim will be referred to herein as the "SPSO Claim."
- The Court is permitted to make inferences from the evidence presented, including concerning a party's intent, motive and purpose. See Bankr. Servs., Inc. v. Ernst & Young (In re CBI Holding Co.), 529 F.3d 432, 450–53 (2d Cir.2008) (finding that the inferences made by the court from certain witness testimony were not "clearly erroneous" where there was an absence of "direct evidence" and such testimony was not contradicted by extrinsic evidence). While it is clear that an inferences must

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be "more than a guess" *Seneca Meadows, Inc. v. ECI Liquidating, Inc.*, 427 F.Supp.2d 279, 300 (W.D.N.Y.2006), the Court is permitted to make an inference that is reasonably drawn from the evidence proffered. *See Dep't of Econ. Dev. v. Arthur Andersen & Co. (U.S.A.)*, 924 F.Supp. 449, 474 (S.D.N.Y.1996) ("An inference ... is a logical conclusion drawn from facts ... not a guess that is merely consistent with such facts."). "According to the Restatement, "[t]he word "intent" is used ... to denote that the actor desires to cause consequences of his act, or that that he believes that the consequences are substantially certain to result from it." *Tronox Inc. v. Kerr McGee Corp. (In re Tronox Inc.)*, 503 B.R. 239, 279 (Bankr.S.D.N.Y.2013) (citations omitted).

II. SPSO Cannot Be Held Liable for Breach of the Express Terms of the Credit Agreement

A. SPSO Was Not Technically Prohibited from Purchasing LP Debt

[1] At the center of this contractual dispute is the term "Eligible Assignee," a common term included in loan agreements in order to limit a lending institution's ability to assign the loan to other entities. See, e.g., Meridian Sunrise Village, LLC v. NB Distressed Debt Investment Fund Limited (In re Meridian Sunrise Village LLC), No. 13–40342, 2014 WL 909219 (W.D.Wash. Mar. 7, 2014). Here, the Credit Agreement permits only "Eligible Assignees" to acquire LP Debt. Excluded from the definition of "Eligible Assignee" are (i) natural persons and (ii) "Disqualified Companies" and, as such, these entities are not eligible to purchase LP Debt. A "Disqualified Company" is defined in the *316 Credit Agreement, in relevant part, as "any operating company which is a direct competitor of the Borrower," and set forth on Schedule 1.01(a), as well as "any known subsidiary thereof." Although "Subsidiary" (uppercase) is defined in the Credit Agreement, in relevant part, as "any other person that is otherwise Controlled 44 by the parent and/or one or more subsidiaries of the parent," the word "subsidiary" as used in the definition of Disqualified Company is not capitalized.

- DX5 (Credit Agreement) § 1.01.
- "Control" under the Credit Agreement is defined, in relevant part, as "the possession, directly or indirectly, of the power to direct or cause the direction of the management or policies of a person, whether through ownership of voting securities, by contract or otherwise...." Credit Agreement § 1.01.

As "Disqualified Companies" included on Schedule 1.01(a), DISH and EchoStar were not permitted to purchase the LP Debt. Nor was Mr. Ergen permitted to purchase the debt personally, as the Credit Agreement does not permit a "natural person" to be an Eligible Assignee. SPSO, however, was not precluded by the express terms of the Credit Agreement from purchasing the LP Debt, inasmuch as it is not an operating company which is a direct competitor of LightSquared listed on Schedule 1.01(a). If, however, SPSO is a "known subsidiary" of a Disqualified Company, it cannot be an Eligible Assignee.

Because the capitalized term "Subsidiary" was not utilized in the definition of Disqualified Company, the Court looks to the commonly understood definition of the word "subsidiary." The dictionary definition of "subsidiary," used as a noun, is a shortened version of "subsidiary corporation," which is defined by *Black's Law Dictionary* as "[a] corporation in which a parent corporation has a controlling share." Similarly, courts have held that a subsidiary is commonly understood to mean a corporation "that is controlled by another corporation by reason of the latter's ownership of at least a majority of the shares of the capital stock." *Nat'l Gear & Piston, Inc. v. Cummins Power Sys., LLC,* 975 F.Supp.2d 392 (S.D.N.Y.2013) (quoting William Meade Fletcher, FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS § 26 (2012)). As the Delaware Supreme Court has observed, the "ordinary and plain meaning" of subsidiary requires ownership of more than half the stock of the subsidiary by the parent. *Liggett Grp., Inc. v. Ace Prop. & Cas. Ins. Co.,* 798 A.2d 1024, 1035 (Del.2002); *see* 18 AM. JUR. 2d *Corporations* § 41 ("a subsidiary corporation is one in which another corporation, a parent corporation, owns a majority of the shares of its stock"). Neither DISH nor EchoStar controls SPSO by reason of its ownership of a majority of the shares of SPSO. In fact, the evidence has established that Mr. Ergen wholly owns SPSO. SPSO is not a subsidiary of DISH or EchoStar.

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- 45 Black's Law Dictionary (9th Ed. 2009).
- Defendants also emphasize that, under established principles of contract interpretation, all words in a contract must be given effect. Under the express terms of the Credit Agreement, only an entity that is a "known subsidiary" of a "Disqualified Company" may be ineligible to acquire the LP Debt. (Credit Agreement §§ 1.01, 10.04(b) (emphasis added).) By its terms, this provision requires that the "subsidiary" be "known" to the Lender, as Section 10.04 relates only to the Lenders' right to assign the LP Debt, and only a Lender can breach Section 10.04. There is no evidence in the record that any Lender knew that SPSO was a "subsidiary" of DISH or EchoStar, such that SPSO would be rendered a "known subsidiary."

While the term "subsidiary" is well-understood to reference ownership, the *317 broader term "affiliate" (used elsewhere throughout the Credit Agreement) includes entities controlled by, or under common control with, one another. See Del. Ins. Guar. Ass'n v. Christiana Care Health Servs., Inc., 892 A.2d 1073, 1077 (Del. 2006) ("[T]he terms 'affiliate' and 'subsidiary' carry their own legal significance[.] ... Affiliate refers to a 'corporation that is related to another corporation by shareholding or other means of control,' and subsidiary refers to a 'corporation in which a parent corporation has a controlling share[.]"). While SPSO may in fact be an affiliate of DISH and EchoStar, the definition of "Disqualified Company" in the Credit Agreement does not include the term "Affiliate" (which the Credit Agreement defines, in relevant part, as "with respect to a specified person, another person that ... is under common Control with the person specified..."). By its terms, the Credit Agreement does not prohibit affiliates of Disqualified Companies from buying LP Debt.

Moreover, as this Court previously observed in its Decision on the Motions to Dismiss, even if one were to assume that the term "subsidiary" as used in the definition of "Disqualified Company" has the meaning of the defined term "Subsidiary" ⁴⁷ such that control by DISH or EchoStar was the key inquiry, Plaintiffs have not proven that DISH or EchoStar has the ability to control SPSO or that Mr. Ergen acts subject to the control of Dish or EchoStar as an agent would. In fact, Plaintiffs allege just the opposite—that Mr. Ergen controls DISH and EchoStar, makes decisions on their behalf, and acts with complete authority for DISH and EchoStar to carry out those decisions. Accordingly, in analyzing the plain words of the Credit Agreement, SPSO is an Eligible Assignee, and the Court finds no breach of an express term of the Credit Agreement. ⁴⁸

- As noted *supra*, "Subsidiary" is defined in the Credit Agreement, in relevant part, as "any other person that is otherwise Controlled by the parent and/or one or more subsidiaries of the parent," and "Control" is defined, in relevant part, as "the possession, directly or indirectly, of the power to direct or cause the direction of the management or policies of a person, whether through ownership of voting securities, by contract or otherwise...." Credit Agreement § 1.01.
- The Complaints assert tortious interference claims against DISH, EchoStar, and Mr. Ergen. To recover on a claim for tortious interference, a party must prove (i) the existence of a valid contract between the plaintiff and a third party, (ii) defendant's knowledge of the contract, (iii) defendant's intentional procurement of the third party's breach of the contract without justification, (iv) actual breach of the contract, and (v) damages resulting therefrom. See Kirch v. Liberty Media Corp., 449 F.3d 388, 401–02 (2d Cir.2006). Because the Court finds no breach of an express term of a contract, the Court also finds that Plaintiffs have failed to prove their claims against DISH, EchoStar, and Mr. Ergen for tortious interference with contract.

III. SPSO's Acquisition of the LP Debt Violated the Spirit of the Credit Agreement and is a Breach of the Implied Covenant of Good Faith and Fair Dealing

[2] Although the Court declines to find that SPSO breached an express term of the Credit Agreement, there nonetheless remains the question of whether SPSO's acquisition of LP Debt was made on behalf of DISH or for the benefit of DISH and, if so, what consequences flow from that conclusion. There is overwhelming evidence in the record that SPSO's acquisition of LP Debt, at least as of April 2013 and possibly earlier, was carried out for the benefit of DISH, with the tacit approval of (or at least no interference by) the members of the DISH Board and certain members *318 of DISH senior management, including its CFO and General Counsel. The facts are these.

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A. SPSO's LP Debt Purchases

1. Mr. Ergen Identifies LightSquared as "Attractive" in the Fall of 2011 and Begins Buying LP Debt in April 2012

Mr. Ergen testified that, in the fall of 2011, he believed the spectrum and satellites of LightSquared might be an attractive investment opportunity for DISH and therefore began looking into acquiring LightSquared's LP Debt. He asked Jason Kiser, the Treasurer of DISH and a Vice President of Corporate Development at DISH and EchoStar, to provide him with information. Mr. Kiser testified at Trial that, until it was clear that DISH and EchoStar could not purchase the debt, the LightSquared investment was considered a corporate opportunity. After reviewing the Credit Agreement and consulting with Sound Point and Sullivan & Cromwell, DISH's corporate counsel (and not Mr. Ergen's personal counsel), Mr. Kiser determined that both DISH and EchoStar were prohibited from buying the LP Debt, and communicated this to Mr. Ergen. No evidence was submitted that Mr. Kiser or Mr. Ergen made a more formal inquiry to the Boards of Directors of DISH or EchoStar or consulted with management of either company prior to making any personal purchases of LP Debt. Having gotten the "all clear" from Mr. Kiser, Mr. Ergen, through Bal Harbour Capital and then SPSO, began purchasing the LP Debt in April 2012.

In order to enable Mr. Ergen to purchase the LP Debt, Mr. Kiser created two limited liability companies, the Bal Harbour Entities, which were subsequently replaced by two other entities: (i) Special Opportunities Holdings LLC, which is solely owned by Mr. Ergen, and (ii) its wholly owned subsidiary, SPSO. Mr. Kiser testified that the change to SPSO as the investment vehicle was necessary because the formation documents of the Bal Harbour Entities listed a Littleton, Colorado address, which Mr. Ergen and Mr. Kiser determined may have compromised Mr. Ergen's anonymity and "might lead people to Mr. Ergen's doorstep." ⁴⁹ Defendants maintain that Mr. Ergen desires to keep his personal investments confidential; Plaintiffs allege that the desire for anonymity here stems from Mr. Ergen's intent to conceal his purchases of LP Debt to facilitate his intentional violation of the Credit Agreement.

49 See Post-Trial Brief of Defendants SP Special Opportunities, LLC and Charles W. Ergen, p. 8.

2. The LP Debt is "a good investment"

Between April 13, 2012 and April 26, 2013, Mr. Ergen, through SPSO, contracted to purchase over \$1 billion in face amount of LP Debt, of which SPSO actually closed trades for approximately \$844 million in face amount. Specifically, prior to LightSquared's Petition Date on May 14, 2012, SPSO purchased a total of approximately \$287 million in face amount of LP Debt, with SPSO's largest purchase comprised of the May 4, 2012 purchase of Carl Icahn's approximately \$247 million dollar position. These initial purchases were made at prices between 48.75 cents and 60.25 cents on the dollar. Mr. Ergen testified that, at this time, he believed the debt was "a good investment" and that he did not have an idea of how much debt SPSO would eventually buy. ⁵⁰

50 Jan. 13 Tr. (Ergen) 43:17–44:8.

*319 3. "I would have them vote no" on LightSquared's Forbearance Request

On May 4, 2012, after Mr. Ergen agreed to purchase Mr. Icahn's \$247 million dollar position in the LP Debt but before the trade closed, SPSO was given the option of directing the seller's vote on whether to authorize an amendment to the Credit Agreement pursuant to which the Lenders would forbear from exercising remedies and which would have allowed LightSquared to continue to work toward a consensual arrangement with its lenders and possibly avoid a bankruptcy filing. Despite (i) being told that Mr. Icahn was inclined to support the request for a short forbearance and (ii) not having

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reviewed the terms of the amendment itself, Mr. Ergen directed a "no" vote on the Friday evening prior to the Monday response deadline. His testimony that he voted "no" because he had been unable to review the proposed amendment was not credible, as the evidence reveals that the amendment documents could have been obtained by Sound Point, had Mr. Ergen and Mr. Kiser indicated an interest in reviewing them over the weekend. ⁵¹ There was also no evidence introduced that Mr. Kiser or Mr. Ergen made any effort to discuss the proposed amendment with any of the other Lenders. While the Debtors argue that these actions on the part of Mr. Ergen reveal that, with respect to LP Debt, Mr. Ergen was not interested in acting like a traditional creditor, it is worth noting that there is nothing that requires a creditor to support a forbearance request. That Messrs. Kiser and Ergen failed to testify truthfully about the reasons for the "no" vote is significant, however, and it is part of a troubling pattern of non-credible testimony.

When confronted at Trial with the information that Mr. Kiser had been told by Sound Point that it could potentially obtain the documents for Mr. Kiser's review, Mr. Ergen blamed Mr. Kiser, testifying, "I'm disappointed that [Kiser] answered no.... That's not the way I would have done it." (Jan. 13 Tr. (Ergen) 262:13–263:8.)

4. There "might be some truth" to the Press Reports of Mr. Ergen's LightSquared LP Debt Purchases

After SPSO purchased Mr. Icahn's \$247 million dollar position in the LP Debt, *The Denver Post* reported that Mr. Ergen had "snatched up" \$350 million of LightSquared debt. This article prompted an email from Gary Howard, a DISH Board member, to Stanton Dodge, DISH's General Counsel, and two other members of the DISH Board, asking if the story was accurate. Mr. Dodge's May 16, 2012 email reply, on which he copied the entire DISH Board, including Mr. Ergen, stated, "further to gary's email below and since another board member inquired about the recent press reports regarding LightSquared bonds, I wanted to send a brief note to the full board. [T]he company [DISH] did not buy any LightSquared bonds."

Notably, Mr. Dodge's reply did not address the direct question of whether Mr. Ergen had purchased LightSquared debt personally and there is no evidence that any member of the DISH Board followed up in order to receive a clear response to this question, consistent with the fiduciary duties owed by the DISH directors to examine whether the purchases may have been a corporate opportunity. While the Court will not insert itself in matters of DISH corporate governance that are the province of DISH and its shareholders, the Court will infer from this inaction that the members of the DISH Board, who, from press reports, had more than an inkling of Mr. Ergen's purchases, were tacitly acquiescing to Mr. Ergen's foray into LightSquared's capital structure, and they *320 did not see fit to double check the corporate opportunity questions it obviously raised. Mr. Dodge's reply reveals the apparent attitude of members of the DISH Board and senior management that, where Mr. Ergen was concerned, it was best not to ask a lot of questions and to let him conduct his business as he saw fit.

Members of DISH senior management also first learned from the press of Mr. Ergen's LP Debt purchases, made their own inquiries to Mr. Ergen directly, and were rebuffed. After Mr. Ergen did not provide them with candid answers, they also did not inquire further. Specifically, when Mr. Dodge confronted Mr. Ergen about a press report of his purported purchases of the LP Debt, Mr. Ergen responded, coyly, that there "might be some truth" to the report. ⁵² There is no evidence that Mr. Dodge made further inquiry. ⁵³ Mr. Cullen, who, as Executive Vice President of Corporate Development, leads DISH's strategic acquisitions and is considered to be "Ergen's closest confidante on all things wireless," also asked Mr. Ergen about the reports of his LightSquared debt purchases but was only able to elicit confirmation from Mr. Ergen that there either "is" or "might be" "some truth" to the reports. ⁵⁴ At Trial, Mr. Cullen acknowledged that he owed fiduciary duties to DISH, but testified that, upon learning of Mr. Ergen's purchases of LP Debt, he (i) did not ask Mr. Ergen why DISH was not buying the debt, (ii) did not ask in-house counsel whether there was an issue with Mr. Ergen making a personal investment in the debt, and (iii) did not take any steps to determine whether Mr. Ergen's purchases were a corporate opportunity. ⁵⁵

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- Jan. 13 Tr. (Ergen) 116:3–22, 118:23–119:19. There also no evidence in the record that Mr. Ergen ever told Mr. Dodge that Mr. Kiser had investigated previously whether DISH could purchase the debt and consulted on that topic with Sullivan & Cromwell.
- At Trial, in response to a question from the Court about whether no stone had been left unturned to find a way for DISH to participate in purchasing LightSquared Debt, Mr. Ergen testified that, before any trades closed, he "had a conversation" with Mr. Dodge and it was his "understanding that [Mr. Dodge] checked with outside counsel himself as to whether there was any opportunity for DISH." (Jan. 13 Tr. (Ergen) 243:7–19.) This testimony is inconsistent with all other evidence in the record that Mr. Ergen checked solely with Mr. Kiser, who checked with Mr. Ketchum and with Sullivan & Cromwell, before purchasing LP Debt.
- 54 Jan. 17 Tr. (Cullen) 117:8–18; Jan. 13 Tr. (Ergen) 116:3–22.
- Jan. 17 Tr. (Cullen) 143:1–24. In April 2013, DISH spokesman Bob Toevs also sent several emails to Mr. Ergen and several senior officers, including Messrs. Cullen, Dodge, Clayton, and Jeff Blum (a Senior Vice President and Deputy General Counsel), about a news article discussing DISH amassing LightSquared debt through Sound Point, and noting that Toevs "has not commented." (PX0393; PX0407; PX0408.) Mr. Toevs' April 2, 2013 email referred to past coverage on the very same issue and had links to news stories dating back to May 2012. (PX0393; PX0408.) No evidence was provided that any of these top DISH executives responded to the e-mail to inquire whether Mr. Ergen in fact was buying the LP Debt.

Together, these emails and conversations reveal a striking lack of candor between Mr. Ergen and members of DISH's board of directors and senior management. In addition to demonstrating that Mr. Ergen directed the actions of the DISH Board, as stated by one of its members, ⁵⁶ *321 the inquiries (or lack thereof) posed to Mr. Ergen also suggest that the DISH Board and senior executives may have been unconcerned about Mr. Ergen's personal LightSquared debt purchases (and later, his LBAC Bid) because they had confidence that his strategy would inure to the benefit of DISH. Regardless, it is notable that there were no further inquiries; Mr. Ergen testified at Trial that, apart from Messrs. Kiser, Cullen, and Dodge, he did not speak to anyone regarding his LP Debt purchases until the May 2 board presentation. ⁵⁷

- DISH's independent director, Mr. Goodbarn, acknowledged Mr. Ergen's domination of the DISH Board. When asked if "[i]t was [his] view that nobody else [on the Board] could act in an independent way of Charlie," Mr. Goodbarn responded, "[t]hat is correct." (PX0767 (Goodbarn Nevada Dep.) at 233:25–234:3.)
- 57 Jan. 13 Tr. (Ergen) 116:3–22, 119:20–24.

5. "If we can't be sure the company can buy ... then I am interested to increase my position"

After his initial purchases in April and May of 2012, Mr. Ergen did not pursue any purchases of LP Debt until October 4, 2012. Around that time, Mr. Ergen asked Mr. Kiser to check whether the restrictions on DISH's ability to acquire LightSquared debt had changed as a result of LightSquared's bankruptcy filing. After Mr. Kiser wrote to Mr. Ergen that he could not get confirmation that the restrictions on DISH purchasing the debt had fallen away, Mr. Ergen responded, "[i]f we can't be sure the company can buy them, then I am interested to increase my position at the 75 level at least up to a 33% ownership level of the class." ⁵⁸

58 PX0243

This statement by Mr. Ergen establishes that, at least as of that moment in time, the preferred purchaser of the LP Debt was DISH. Mr. Kiser's testimony that the reason for again checking the Credit Agreement was to confirm that there was no corporate opportunity for DISH was not credible and is not consistent with the precise words of Mr. Ergen's directive. In fact, it would appear that there did exist a path for DISH to become a Lender under the Credit Agreement: the Credit Agreement, by its express terms, contains no restrictions on affiliates of Disqualified Companies becoming Lenders.

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The Court was presented with no evidence that the DISH Board was in fact aware of this and considered whether to create an affiliate to purchase LP Debt, nor any other evidence to support the contention that Mr. Ergen's focus was on making sure that he was not usurping a DISH corporate opportunity. ⁵⁹ Notwithstanding, from Mr. Ergen's choice of words in inquiring about whether DISH could purchase the LP Debt, the Court can reasonably draw an inference that Mr. Ergen's oft-repeated statement that his investment was conceived of and always intended to be purely for personal purposes was not truthful. It is clear that DISH was the preferred purchaser.

Mr. Howard, one of two independent board members on the Special Committee formed by the DISH Board of directors on May 8, 2013, testified that, while the Special Committee had been advised by Mr. Ergen of "his view" that the Credit Agreement precluded DISH from acquiring LightSquared securities, "[t]he Special Committee did not, however, reach a conclusion regarding whether the LightSquared credit agreement resolved the issue...." (PX0768 (Howard Nevada Affidavit) at ¶ 17.) Mr. Howard also testified at his deposition that the Special Committee was interested in determining whether there was a way that DISH could have bought LP Debt notwithstanding the transfer restrictions. (Howard Dep. 204:14–205:15.)

After Mr. Ergen decided to acquire, through SPSO, at least a 33 percent stake in LightSquared debt, Mr. Kiser asked Mr. Ketchum to track whether SPSO had a blocking position. ⁶⁰ Although *322 Mr. Ketchum initially testified that he did not recall discussing with Mr. Kiser the acquisition of a blocking position, he later admitted that Mr. Kiser told him "he was very interested in tracking whether or not SPSO had a blocking position with respect to LightSquared." ⁶¹ Mr. Ketchum was not a credible witness on this point and many others.

- As Defendants point out, the term "blocking position" refers to acquiring one-third of a debt issuance, but it does not formally "block" anything. Section 1126(c) of the Bankruptcy Code provides that a class of creditors is deemed to have voted in favor of a plan of reorganization if two-thirds in amount and more than one-half in number of such creditors votes in favor of the plan, meaning that a class of creditors with more than one-third in amount voting to reject a plan will not be an accepting class.
- Defendants emphasize that Mr. Ergen turned down three offers to purchase large amounts of LP Debt on October 9, 2012 (which purchases would have given Mr. Ergen a blocking position) because the prices were too high as proof that SPSO's purchases of LP Debt were for investment purposes only. The Court find that this fact only proves that Mr. Ergen's acquisition strategy may not yet have been fully formed at that point in time, and thus, he was in fact acting primarily as an investor in the fall of 2012.

6. March 28, 2013: "you just bought a spectrum company"

When asked about the desire for a blocking position, both Mr. Kiser and Mr. Ergen testified that 33 percent ownership of the LP Debt would provide SPSO, and therefore Mr. Ergen, with a "blocking" position such that SPSO could enforce "certain rights" during the bankruptcy proceeding. ⁶² However, neither Mr. Ergen nor Mr. Kiser would admit to any intended linkage between obtaining a blocking position in LP Debt and a making a bid for LightSquared, or how the former could pave the way for the latter—DISH's acquisition of LightSquared spectrum. ⁶³

- (Jan. 10 Tr. (Kiser) 47:22–48:10, 56:11–14; Jan. 13 Tr. (Ergen) 172:10–174:2; DX047.) Mr. Ergen testified that he believed that 33 percent was a "meaningful percentage in bankruptcy," and that with that percentage, he "couldn't get jammed with a different kind of currency than somebody else in that class might get." (Jan. 13 Tr. (Ergen) 51:12–18, 172:25–173:3.) Mr. Ergen testified that he had a sizeable enough position in LightSquared to protect that he decided to get a blocking position. (Jan. 13 Tr. (Ergen) 51:12–24.)
- Plaintiffs emphasize how DISH and EchoStar have executed this "loan-to-own strategy" in other cases—namely, DBSD and Terrestar—where acquisition of a blocking position in the debt facilitated an acquisition of the assets at a discount. Plaintiffs argue that the purchase of LightSquared debt here reprises the strategy that DISH and EchoStar have pursued before. (See

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Plaintiff's Post–Trial Brief [Adv. Docket No. 133] at pp. 8, 17.) The Court is disinclined to consider Defendants' past practices as proof of anything in this matter and, accordingly, gives little weight to such comparisons.

It is clear from the evidence, however, that such a strategy began to emerge by late March/early April of 2013. By March 25, 2013, Mr. Ergen needed to purchase another \$112 million of LP Debt to reach a blocking position. On March 28, 2013, he initiated a trade for \$168 million face amount of LP Debt at 96 cents on the dollar—almost double the price he initially paid for LP Debt in April 2012. Notably, in this trade, he also sought to purchase the LP Preferred Interests that were bundled with the LP Debt and offered to pay between 92 and 95 cents on the dollar for that—or approximately \$122 million—just so, as Mr. Kiser testified, Mr. Ergen could have the "privilege" of obtaining that LP Debt. ⁶⁴ At Trial, Mr. Ergen continued to deny the fact that he was willing to pay that price because he wanted to secure a blocking position, instead stating that he bought substantial amounts at close to par *323 because he "loved the investment." ⁶⁵ Notwithstanding, on March 28, 2013—the date Messrs. Ergen and Kiser believed they had achieved their intended goal of obtaining a blocking position, provided the trade closed ⁶⁶—Mr. Ketchum sent an email to Mr. Kiser, stating "You just bought a spectrum company." Later in that same email chain, Mr. Ketchum noted internally to his colleague, "we now control the company." ⁶⁷

- 64 Jan. 10 Tr. (Kiser) 136:7–14.
- 65 Jan. 13 Tr. (Ergen) 174:3–18.
- As set forth in footnote 17, *supra*, the March 28, 2013 bundled trade remained open for several months afterwards but never closed, and Mr. Ergen does not own the LP Debt that was the subject of this trade. Regardless, Mr. Ergen's April 2013 trades brought him to a "blocking position."
- 67 PX0385.

B. Mr. Ergen's Conduct in the Spring of 2013 Establishes that He Was Acting for DISH

Mr. Ergen acknowledged at Trial that his LightSquared strategy had changed as of April 2013. Mr. Ergen testified that, at that time, because of changes in the wireless industry and at the FCC, he saw a "window of opportunity." He stopped looking at LightSquared as a debt investment and began to view it as a potential acquisition candidate. Mr. Ergen testified that he had a general understanding of the Exclusivity Stipulation and believed that if he wanted to make a bid for LightSquared, he would have to do so by July. He hired Willkie Farr as bankruptcy counsel because, in his words, "I don't need them for an investment, but I need then if I'm going to reach out, if I'm potentially going to look at LightSquared as an acquisition." To

- 68 Jan. 13 Tr. (Ergen) 65:4–66:3.
- Jan. 13 Tr. (Ergen) 66:9–15 ("... and then there also was the fact that the bankruptcy was coming up in July. And if I was interested, I would have to ...—either you're going to make a bid there or somebody else was going to. And while I didn't know in that time frame that I would make a bid, I knew that it would take time to prepare."). The Court understands Mr. Ergen's mention of the "bankruptcy coming up in July" to refer to the stipulated date for termination of the Debtors' exclusive periods to file a plan, which was approaching on July 15, 2013.
- 70 Jan. 13 Tr. (Ergen) 67:1–11.

1. \$320 million of LP Debt at 96 Cents on the Dollar and Confidence in the Collateral

Through four separate trades entered into between April 1, 2013 and April 26, 2013, Mr. Ergen, through SPSO, purchased approximately \$320 million of LP Debt at 96 cents on the dollar. These were the final purchases of LP Debt completed by SPSO, bringing its total ownership of LP Debt to approximately \$844 million in face value, the face amount

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it still owns today. When asked about his substantial purchases at 96 cents on the dollar, Mr. Ergen testified that he "was very confident in the collateral" and, as a result, he bought whatever people would sell at that price because he "felt that it was a great investment." ⁷¹

71 Jan. 13 Tr. (Ergen) 66:19–25.

Noticeably absent from the picture painted by Mr. Ergen's testimony is the fact that SPSO's April 2013 acquisitions of \$320 million face amount of LP Debt at 96 cents on the dollar (which gave SPSO more than 50 percent ownership of the LP Debt) achieved by indirection something that it could not have achieved directly—the creation of leverage for DISH to acquire LightSquared's assets. It is within the scope of Mr. Ergen's broad authority as chairman of the Boards of Directors of both DISH and EchoStar to lead DISH *324 and EchoStar's strategic acquisitions of spectrum assets, and the evidence demonstrates that Mr. Ergen's objective beginning in April 2013 included preserving for DISH the option to bid for LightSquared's spectrum assets. While, in May 2012, it may have been unclear even to Mr. Ergen whether he was investing in LP Debt for his own benefit or for the benefit of DISH, as of April 26, 2013—a few days before Mr. Ergen formally presented the opportunity to DISH—there is no doubt that he was acting for the benefit of DISH.

Approximately one week after Mr. Ergen acquired a blocking position in the LP Debt, and at the same time he was contemplating making what he has characterized as a personal bid for LightSquared's assets, DISH issued a series of notes that raised \$2.3 billion in capital (the "April 3 Capital Raise"), approximately the same amount as DISH's ultimate bid for LightSquared. DISH's press release for the April 3 Capital Raise specifically stated the "net proceeds of the offering are intended to be used for general corporate purposes, which may include wireless and spectrum-related strategic transactions." (PX0847; Jan. 13 Tr. (Ergen) 178:4–179:2; PX0904; PX0906.) Defendants, under no obligation to do so, did not provide any evidence regarding DISH's intended use of the funds from the April 3 Capital Raise, and Plaintiffs did not meet their burden to show that the intended use of the April 3 Capital Raise was to pay for a DISH acquisition of LightSquared's assets. Accordingly, the Court will draw no inferences on this topic. The Court has been informed that the notes issued in connection with the April 3 Capital Raise remained outstanding as of the date of the conclusion of Trial.

2. "Mr. Ergen's substantial interests in L2 debt and preferred stock compliment [sic] any acquisition strategy"

Mr. Ergen's actions at the DISH and EchoStar board meetings held on May 1 and 2, 2013—shortly after SPSO obtained its blocking position and DISH completed the April 3 Capital Raise—further reveal his intention to benefit DISH by his debt acquisition and pave the way for DISH to acquire LightSquared's spectrum assets. After disclosing his LP Debt acquisition to the boards of DISH and EchoStar for the first time, Mr. Ergen gave the Ergen Presentation, indicating his proposal for "any combination of Mr. Ergen, EchoStar, and/or DISH based on company interest" to acquire LightSquared's assets for \$2 to \$2.1 billion. ⁷³ Specifically, the Ergen Presentation informed each board that Mr. Ergen's blocking position in the LP Debt could help facilitate any bid for LightSquared's assets:

Mr. Ergen's substantial interests in L2 debt and preferred stock compliment [sic] any acquisition strategy and could have significant influence in L2's chapter 11 cases. ⁷⁴

- 73 The Ergen Presentation states that the proposed acquisition vehicle would be "NewCo," which would be "formed by any combination of Mr. Ergen, EchoStar, and/or DISH based on company interest." (PX0867 at SPSO00011825).
- 74 Ergen Presentation, PX0867 at SPSO-00011824.

Mr. Ergen understood the critical nature of the timing of any bid, and he testified at Trial that, given the July 15 termination of the Debtors' exclusive periods, it was likely that LightSquared would "begin exploring strategic alternatives in early June if no restructuring or sale strategy emerges." This understanding was that "anyone could come to the Court to make an offer for LightSquared, that that might be a corporate opportunity for DISH and for

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EchoStar." ⁷⁶ Because Mr. Ergen recognized, however, that the DISH Board was at the time focusing on the potential Sprint and Clearwire transactions, *325 had performed no analysis of LightSquared, and did not authorize a bid for LightSquared at that time, Mr. Ergen planned to make a bid "personally" to preserve "optionality" for DISH and/or EchoStar to bid on LightSquared assets. ⁷⁷ He did not, however, seek approval from either board to make a bid personally.

- 75 Ergen Presentation, PX0867 at SPSO-00011828.
- 76 Jan. 13 Tr. (Ergen) 77:10–17.
- Mr. Ergen's testimony that he pursued LightSquared as an alternative for DISH if the Sprint and Clearwire acquisitions fell through—as they ultimately did—is clear on this point. (See PX0832 (Ergen Nevada Dep.) at 135:23–136:3 (a DISH bid for LightSquared could be a "Plan B" if potential deal with Sprint did not work out), 140:22–141:23 (Mr. Ergen made the bid for LightSquared's spectrum to preserve DISH and EchoStar's "optionality" to participate); Jan. 13 Tr. (Ergen) 186:25–187:20 (the bid "opened up the optionality for DISH to the extent they lost Sprint").)

3. Mr. Ergen Makes a Bid Himself, Keeping Options Open for DISH

Two weeks later, on May 15, 2013, Mr. Ergen, by his counsel, submitted an unsolicited cash bid for LightSquared's spectrum for \$2 billion ⁷⁸ on behalf of LBAC, which had not yet been formed. ⁷⁹ The wording of the LBAC Bid provided optionality for DISH to be the ultimate purchaser, stating that the newly-formed buyer would be "owned by one or more of Charles Ergen, affiliated companies and/or other third parties." ⁸⁰ Non-binding and expiring on May 31, 2013, the bid emphasized LBAC's "willingness to fund the Purchase Prices, *on a non-refundable basis*, prior to receipt of FCC and Industry Canada approvals and authorizations ...", ⁸¹ and it explicitly stated that the cash purchase price of \$2 billion could be used to pay off the LP Debt. With its lack of conditionality and offer of cash consideration sufficient to pay off the LP Debt in full, the LBAC Bid accomplished the objective, set forth in the Ergen Presentation given to the DISH Board less than two weeks earlier, of proposing a bid that would "be highly attractive to stakeholders and put pressure on L2 fiduciaries to consider [the] proposal." ⁸²

- 78 PX0504.
- 79 LBAC was formed approximately two weeks later, on May 28, 2013.
- 80 PX0504 at GH_L2_00450.
- PX504 (emphasis in original).
- 82 PX0867 at SPSO-00011826.

The existence of the LBAC Bid quickly hit the press. Upon learning of the bid, no member of the Boards of Directors or management of DISH or EchoStar formally objected to Mr. Ergen having made a personal bid for LightSquared's assets. Mr. Cullen, a top DISH executive, stated that he learned of the LBAC Bid through news reports but did not ask Mr. Ergen if he was usurping a corporate opportunity, despite not being aware at that time that Mr. Ergen had presented the DISH Board with the option to make a bid. ⁸³ The Court can infer from the inaction of DISH's Board and management upon learning of Mr. Ergen's personal bid that they either (i) understood that the LBAC Bid and the strategy behind it were ultimately for the benefit of DISH, even if the bid was made by Mr. Ergen personally at that time or (ii) did not wish to impede Mr. Ergen's forward movement on his own bid, notwithstanding their fiduciary obligations.

83 Jan. 17 Tr. (Cullen) 143:25–145:19.

4. "You are way ahead of your skis here"

On May 8, 2013 (one week *prior* to the LBAC Bid), the DISH Board had formed a special committee consisting of two directors independent of Mr. Ergen—Mr. Goodbarn and Mr. Howard. Pursuant to *326 board resolutions, the Special Committee was vested with the power and authority to: (i) review and evaluate (including any potential conflicts of interest arising out of Mr. Ergen's proposal to the DISH board regarding LightSquared and his personal interest in LightSquared) a potential bid for LightSquared and whether such a bid was in the best interests of DISH and its shareholders, and to discuss and/or negotiate such a transaction; (ii) negotiate definitive agreements with the parties concerning the terms and conditions of the potential transaction; and (iii) determine whether such terms and conditions were fair to DISH. ⁸⁴ The board formally resolved that the Special Committee's authority would expire only upon the Special Committee's "determination, in its sole and absolute discretion, as set forth in its written notice to the Chairman of the Board of Directors" as long as a bid for LightSquared remains viable. ⁸⁵ As it turned out, such resolutions were not worth the paper they were written on.

- 84 PX0768 (Howard Nevada Affidavit) ¶ 9; PX0491 at DISH_ NY000000002-4.
- 85 PX0491 at DISH_NY0000000005.

The evidence reveals that these board resolutions were quickly and flagrantly disregarded. Despite being in existence for three months, the Special Committee was forced to work under a compressed timetable because of Mr. Ergen's interference with its ability to begin its task. Upon learning on May 22, 2013 of the Special Committee's recent engagement of independent counsel, Mr. Ergen pushed its members to hold off, asking why Special Committee counsel was needed and cautioning that "[y]ou are way ahead of your skis here." ⁸⁶ Similarly, at a May 31, 2013 meeting, Mr. Ergen suggested that the Special Committee should delay engaging its financial advisor, as, in Mr. Ergen's view, there would "be little activity, if any, in the coming weeks" regarding a LightSquared transaction. ⁸⁷ After delaying the retention of its professionals and keeping the committee in what Mr. Howard later described as a "holding pattern," Mr. Ergen suddenly reversed course in early July, urging the Special Committee to complete its evaluation quickly and make a recommendation to the DISH Board. ⁸⁸

- DX0188, see also PX0767 (Goodbarn Nevada Dep.) at 102:2–103:15 ("[Ergen] felt we were moving too fast as a committee" given that the Special Committee was trying to seek trading information from him, he had unsettled trades, and he was tied up with Sprint and Clearwire at the time).
- PX0768 at ¶ 25. PWP, the financial advisor to the Special Committee, was ultimately retained on June 28, 2013, after the Sprint and Clearwire deals had failed to proceed. See DX0224 (email from Gary Howard to DISH Board); PX0768 at ¶ 33.
- PX0768 at ¶ 34.

The existence and amount of the LBAC Bid created a significant challenge to the Special Committee's task of evaluating a potential DISH bid and determining what terms and conditions were fair to DISH. Upon learning of the LBAC Bid from news alerts on May 20 and 21, 2013, ⁸⁹ Mr. Howard *327 stated that he was surprised, as it "was [his] expectation that Mr. Ergen would not make any LightSquared bid without first discussing it with the DISH Board and the Special Committee in order to get their approval, since any such bid could impact DISH's own strategy vis-à -vis LightSquared." ⁹⁰

Mr. Howard stated that he was not aware that Mr. Ergen had made a personal bid to purchase LightSquared's assets until Mr. Goodbarn forwarded to him the updated Charles Schwab news alert on May 21, 2013. See PX0768 at ¶ 15. He confirmed that the Special Committee had not been advised of and had not approved of the LBAC Bid. Id. at ¶ 20. He also articulated his concern that, by making the bid, "Mr. Ergen was narrowing the scope and ability of the Special Committee to fully explore

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alternative strategies for DISH to pursue with respect to LightSquared, as well as to define and/or negotiate Mr. Ergen's role with respect to DISH's strategy." Id. at $\P 21$.

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When asked whether the Special Committee considered proposing that DISH make a bid for LightSquared's spectrum below the amount of the LBAC Bid, Mr. Goodbarn stated that the LBAC Bid "made it difficult socially to do that ... [b]ecause [Ergen's] put a line in the sand on a bid and we're part of a, you know, a DISH board and he owns a majority of the company." ⁹¹ Pressed further on why it would be difficult for DISH to make a bid lower than Mr. Ergen's bid, Mr. Goodbarn explained that, if Mr. Ergen had committed to a \$2 billion bid with no other bidder present, and the Special Committee then bid \$1.5 billion, Mr. Ergen may take "a big loss" on his debt investment and "that does not make a very happy chairman." ⁹² These statements by an independent board member demonstrate that Mr. Ergen, as chairman of the Board and majority owner of DISH, exercised significant control. The Special Committee did not determine to bid at a lower price, as Mr. Ergen had already staked out the territory with a bid that would ensure that he, as a substantial holder of LP Debt, would be paid in full, and no one was interested in making him unhappy by altering that.

- 91 PX0767 (Goodbarn Nevada Dep.) at 100:7–21.
- 92 PX0767 (Goodbarn Nevada Dep.) at 100:22–101:5.

Furthermore, although the role of the Special Committee included evaluating any potential conflicts of interest, the repeated requests of the Special Committee to Mr. Ergen for information regarding his LP Debt trades were ignored, and Mr. Ergen never provided the Special Committee with the requested schedule of his trades. The Special Committee's stated reasons for seeking such information were significant—"to assess Mr. Ergen's conflict, to determine the potential profit that Mr. Ergen would make if DISH made a successful bid ..., and to assess whether DISH should have been entitled to pursue the corporate opportunity of buying LightSquared debt before permitting Mr. Ergen to do so for his personal account." ⁹³ Mr. Howard stated that he did not recall ever hearing from Mr. Ergen or his counsel that the Committee's requests for information were improper or that Mr. Ergen had no obligation under DISH's charter to bring potential corporate opportunities to the attention of the DISH Board, ⁹⁴ yet, Mr. Ergen provided no reason for leaving the Special Committee in the dark on this key inquiry. ⁹⁵

- 93 PX0768 (Howard Nevada Affidavit) at ¶ 16.
- 94 PX0768 (Howard Nevada Affidavit) at ¶ 18.
- PX0767 (Goodbarn Nevada Dep.) 92:10–93:15; 128:35–130:5; see also DX0224 (July 6, 2013 email from Howard to DISH board in which Mr. Howard writes "[f]or reasons better articulated by Charlie, the special committee has no further insight into the bond purchases made by Charlie's entity."), PX0768 (Howard Nevada Affidavit) at ¶ 17 ("Despite repeated requests and discussions, Mr. Ergen never provided the Special Committee with the requested documentation regarding his investment in and ownership of LightSquared debt or preferred stock.")

On July 3, 2013, Mr. Ergen sent to the Special Committee and David Moskowitz, an in-house attorney and a Senior Vice President for DISH and EchoStar, via email, a presentation for the Special Committee *328 and the DISH Board. ⁹⁶ In the email, Mr. Ergen stated, "This is just a high level view of lightsquared and its potential relation to dish. Please feel free to share with the board or advisors. Also, not on here would be the possibility of freeing up at least two of the existing dbsd/terrestar satellites that could possibly be monetized." ⁹⁷ The presentation, dated July 8, 2013, was entitled "Strategic Investment Opportunity—L–Band Acquisition, LLC." ⁹⁸ It was delivered to the DISH Board of Directors by Mr. Ergen at a special meeting on July 8, 2013. The Ergen July 8 Presentation provided, for discussion purposes in the context of considering whether DISH would participate in the LBAC Bid, certain valuation information relating to LightSquared's spectrum as of that date.

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- 96 PX0927
- 97 *Id.* at DISH_PLAN000003150.
- 98 PX0928.

Under a line item entitled "Implied Net Primary Asset Value," the Ergen July 8 Presentation lists a range of values of between \$3.341 billion and \$5.213 billion, with a midpoint of \$4.277 billion, referring to Mr. Ergen's estimate of the value of 20 MHz of LightSquared's spectrum assets and its satellites, excluding its 10MHz of lower downlink spectrum. Under the heading "Implied Supplemental Asset Value," the Ergen July 8 Presentation lists a range of values of between \$1.833 billion and \$3.783 billion, with a midpoint of \$2.308 billion, for what it identifies as the total of (i) 5.0 MHz of "Reclaimed Unuseable [sic] AWS-4," (ii) 5.0 MHz of "Reclaimed Impaired AWS-4," and (iii) "L-Band Downlink Spectrum." ⁹⁹ The Implied Supplemental Asset Value was Mr. Ergen's estimate of (a) the increase in value of DISH's existing spectrum that would flow from DISH's acquisition of LightSquared's spectrum, which would permit unusable and impaired uplink AWS-4 spectrum to be converted to downlink and (b) his range of values for 20 MHz of LightSquared's downlink spectrum. In other words, the supplemental value of LightSquared's assets to DISH was estimated by Mr. Ergen to be between \$1.833 billion and \$3.783 billion. Combined with the Implied Net Primary Asset Value of \$3.341 billion to \$5.213 billion, the total value of LightSquared's assets in DISH's hands was estimated by Mr. Ergen to be between \$5.174 billion and \$8.996 billion, with a midpoint of \$7.085 billion.

99 *Id.* at 5

On July 21, 2013, the Special Committee presented its conclusions to the DISH Board, ¹⁰⁰ recommending that DISH pursue the LBAC Bid for \$2.2 billion, subject to five express conditions, four of which implicated further review and decision making by the Special Committee:

- (vi) that any material changes to the terms of the bid and/or APA would be subject to the review and approval of the Committee;
- (vii) that DISH would acquire one hundred percent of LBAC, to the exclusion of EchoStar;
- (viii) that the Committee and its legal and financial advisors would remain involved in all negotiations *329 regarding the proposed transaction going forward;
- (ix) that the Committee would review and approve the terms of the acquisition by DISH of Mr. Ergen's interest in LBAC; and
- (x) that the Committee expressly reserved the right to obtain all of the requested information regarding Mr. Ergen's acquisition of debt and/or other securities issued by LightSquared as well as the right to evaluate potential corporate opportunity issues. ¹⁰¹
- At this meeting, PWP provided a nine-page presentation entitled "Project Discus Summary Conclusions" to the DISH Board. (PX0929 at 2.) In a section captioned "Illustrative Value of DISH's Use Cases Related to LightSquared," the PWP Report concludes, "The cumulative value of the illustrative use cases that leverage the LightSquared LP acquisition is estimated to be \$4.4—\$13.3bn." (Id. at 39 (DISH_PLAN135).)
- 101 (PX0716 at GH_L2_000973-74.); PX0768 at ¶ 47. According to Mr. Howard, because the Special Committee had not yet received the requested information on Mr. Ergen's purchases of LP Debt, the Special Committee "informed the Board that it had been unable to completed its evaluation of potential conflicts of interest associated with the LightSquared acquisition, but made clear that it would continue to evaluate those potential conflicts and take appropriate action once its evaluation was completed." *Id.* at ¶ 49.

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Even though the DISH board resolutions permitted disbandment of the Special Committee only upon the Committee's own decision so long as a bid for LightSquared remained viable, the DISH Board abruptly disbanded the Special Committee without advance notice immediately after the Special Committee delivered its conditional approval of the LBAC Bid. Other than Messrs. Howard and Goodbarn, who abstained, the DISH Board's vote was unanimous. ¹⁰² On July 22, 2013, DISH agreed to buy LBAC from Mr. Ergen for one dollar without the Special Committee ever reviewing the terms of the acquisition agreement. ¹⁰³ On July 23, 2013, DISH announced its intention to bid through LBAC for LightSquared's spectrum. ¹⁰⁴

- PX0768 (Howard Nevada Affidavit) ¶¶ 49–50; DX400. Mr. Howard testified that, at the time the vote was taken, he "did not believe that the Special Committee had completed all of its work and therefore did not believe that it should be disbanded at that time." PX0768 at ¶ 50. On July 24, 2013, Mr. Goodbarn and Mr. Howard sent a letter to the DISH Board in which they reiterated their conditional recommendation in favor of a potential LightSquared acquisition and stated that they did not recommend or endorse the disbandment of the Special Committee. *Id.* at ¶ 52. No response to that letter was introduced into evidence
- 103 Howard Dep. 315:10–316:3; Jan. 13 Tr. (Ergen) 195:6–8.
- On July 24, 2013, the Special Committee wrote a letter to the DISH Board expressing its surprise at its disbandment and noting that the five conditions remained unsatisfied. (PX0736.) On July 25, 2013, Mr. Howard resigned from the board, an action taken so suddenly that DISH risked delisting from the NASDAQ. PX0746; see also PX0741; DX313.

The Special Committee had been disbanded despite the fact that its conditions remained unsatisfied; in particular, the Committee had neither negotiated nor approved the draft plan support agreement or the draft asset purchase agreement, which were filed with the Court together with the Ad Hoc Secured Group Plan on July 23, 2013 ¹⁰⁵ and which explicitly stated that they were subject to further negotiations and approval by DISH. ¹⁰⁶ One notable *330 feature of the APA, incorporated by reference into the PSA, was its broad release of all claims against Mr. Ergen, DISH, EchoStar, and SPSO and contemplation of the full allowance of the SPSO Claim. ¹⁰⁷ The proposal of such a release belies the assertions made by SPSO and DISH that they have no ties to one another and supports the inference that Mr. Ergen and SPSO were acting for DISH in creating a path for DISH, through LBAC, to take over as purchaser, while still protecting Mr. Ergen from any downside on his substantial investment. Despite many attempts to characterize it otherwise, the proposal of such a release reveals the strong linkage between SPSO's debt and DISH's bid and the inability to disguise such linkage with so-called "separate hats."

- The joint chapter 11 plan of reorganization filed on July 23, 2013 was proposed by the Ad Hoc Group of Secured Lenders, of which SPSO was a member at that time. SeeFirst Amended Joint Chapter 11 Plan for LightSquared LP, et al., Proposed by the Ad Hoc Secured Group of LightSquared LP Lenders [Bankr. Docket No. 970].
- Mr. Howard testified that the first time he heard that Mr. Ergen was negotiating a proposed joint chapter 11 plan with the Ad Hoc Secured Group was during a July 18, 2013 board meeting. The Special Committee and its advisors were not invited to participate in these negotiations with the Ad Hoc Secured Group. See PX0768 at ¶ 42. At a meeting of the Special Committee on July 21, 2013, counsel for the committee discussed a draft asset purchase agreement with the committee that had been provided to counsel by Mr. Ergen's counsel. Mr. Howard stated that neither the committee nor its counsel had been involved in negotiating this agreement. Id. at ¶ 46. Mr. Howard further testified that he learned of the existence of the PSA after a draft of it was annexed to a Form 8–K filed by DISH, and the Special Committee was neither involved in negotiating this agreement nor had they recommended that DISH enter into it. Id. at ¶ 51.
- See First Amended Joint Chapter 11 Plan for Light Squared LP, et al., Proposed by the Ad Hoc Secured Group of Light Squared LP Lenders [Bankr. Docket No. 970, Ex. A] § 13.1; Stalking Horse Agreement, filed October 28, 2013, [Bankr. Docket No. 970, Ex. F] § 3.2(a)(ii) & n.9.

While it is not the Court's role to pass judgment on the corporate governance practices of DISH, the Court nonetheless concludes that the facts surrounding the Special Committee process show that, notwithstanding the existence of the

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Special Committee, Mr. Ergen himself was the driving force behind each step DISH took on the path toward the DISH/LBAC Bid, including the actions taken in connection with Mr. Ergen's evolving acquisition strategy in the spring and summer of 2013. Although the Special Committee was created to be independent, the blatant disregard of the conditions set forth in its recommendation for DISH's participation in a LightSquared acquisition, its abrupt dissolution by the DISH Board, and its lack of involvement in the negotiations of the LBAC transactional documents as they evolved in the late summer and into the fall of 2013, despite the explicit board resolutions to the contrary, indicate that the Special Committee was little more than window dressing. ¹⁰⁸

While not part of the record of the Adversary Proceeding, the Court notes that, on the evening of January 7, 2014, DISH, by counsel, terminated the DISH/LBAC Bid. Additional grounds for equitable subordination in connection with the termination have been alleged by the Debtors and the Ad Hoc Secured Group, and such matters are part of the record on confirmation of the Debtors' Third Amended Joint Plan of Reorganization Pursuant to Chapter 11 of Bankruptcy Code.

5. Mr. Ergen was Not Acting Solely on His Own Behalf in Making a "Personal" Bid or in Purchasing LP Debt

Even after acknowledging his change of strategy in April 2013 and his interest in making a bid for LightSquared, ¹⁰⁹ and faced with allegations that his debt purchases and the LBAC Bid were made in contemplation of a potential DISH acquisition of LightSquared spectrum, Mr. Ergen has continued to deny that he acted other than for his own personal benefit. Specifically, Mr. Ergen steadfastly maintains that he had an interest in purchasing and owning LightSquared's spectrum assets *personally* and was prepared to own and operate a spectrum business himself. In *331 response to the Court's questioning, Mr. Ergen testified that he believes he could operate a spectrum business without creating a conflict with DISH. ¹¹⁰ At the time of the May 15 LBAC Bid, however, Mr. Ergen did not have any financing agreements lined up with investors and had not even received a term sheet related to a possible financing; a draft term sheet was only received by Mr. Ergen on July 18, 2013, ¹¹¹ and its draft form indicated that no deal had been reached. Mr. Ergen also stated that, at the time of the LBAC Bid, he had made no decisions about headquarters, employees, or management of his personal spectrum company. ¹¹² Taken as a whole, Mr. Ergen's statements that he was prepared to run a spectrum business personally (and in competition with DISH) are farfetched, to say the least. Rather, they cause the Court to conclude that, at the time of the April 2013 LP Debt purchases and the LBAC Bid, the intended strategic investor was not Mr. Ergen, but rather, DISH. ¹¹³

- 109 Jan. 13 Tr. (Ergen) 65:4–66:15.
- Jan. 13 Tr. (Ergen) 245:17–247:20(suggesting possible uses for spectrum that did not conflict with DISH, such as "ground-to-air communications" and "machine-to-machine").
- The LBAC Bid stated that its proposal expired on May 31, 2013 if not accepted by LightSquared prior to that time. See PX0504. It was subsequently extended beyond that date.
- Jan. 13 Tr. (Ergen) 244:16–245:12 ("I had seen where LightSquared headquarters were; I know something about LightSquared and their business. And I would have plenty of time to—I wouldn't be able to manage the company until the FCC approved it. So I would have plenty of time to make all those decisions.")
- Notably, Mr. Ergen confirmed at Trial that, had DISH won its bid for Sprint, he would have withdrawn his personal bid for LightSquared. (Jan. 13 Tr. (Ergen) 188:11–190:15.) While his stated reason for such action was that, under those circumstances, he would not have had the personal time to go through the two or three-year process with the FCC to "clean up" LightSquared, an inference can be drawn that the true reason for withdrawal of the LBAC Bid would be that DISH, Mr. Ergen's intended buyer for LightSquared's assets, would not have the capital necessary to complete both transactions.

The evidence demonstrates that Mr. Ergen's substantial investment in LightSquared debt in April 2013 was made in full contemplation and in furtherance of DISH's potential acquisition of LightSquared spectrum. The Ergen July

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8 Presentation and the valuation contained therein demonstrate the significant benefit to DISH from acquiring LightSquared's spectrum, with the "Implied Net Supplemental Asset Value" to DISH (which had a midpoint of \$2.308 billion) alone coming in above the LBAC Bid amount of \$2.2 billion, without even looking at the total aggregate value of the spectrum to DISH, which Mr. Ergen estimated at a value of between \$5.174 billion and \$8.996 billion. Such an enormous value could not have simply occurred to Mr. Ergen in an epiphany in the days or weeks before making such a detailed presentation to the DISH Board; rather, Mr. Ergen must have perceived the synergistic value reflected in this presentation much earlier, as he monitored the actions of the FCC and the movement of the pieces on the wireless spectrum chessboard, some of which he himself was moving.

In their post-trial brief, SPSO and Mr. Ergen also argue that the evidence does not establish that SPSO's LP Debt purchases were for the benefit of DISH because, as an initial matter, purchasing even one-third of the outstanding debt of the company did not confer on SPSO any *332 rights to acquire the company. 114 As Mr. Ergen himself stated in the Ergen Presentation, however, his "substantial interests in L2 debt and preferred stock compliment [sic] any acquisition strategy and could have significant influence in L2's chapter 11 cases." 115 A competitor who obtains a substantial position in the debt of a distressed company and then bids for the assets often has a significant advantage, which dissuades other bidders from participating in any sale process. While Mr. Ergen's substantial near-par purchases of LP Debt in April 2013 are consistent with a plan to obtain a blocking position in order to acquire the underlying company, they are somewhat inconsistent with a personal investment by a typical creditor seeking to make a profit on distressed debt by buying low and selling high. Indeed, Mr. Ergen's final purchase of LP Debt on April 26, 2013 was made just one week prior to his presentation to the DISH Board on May 2, 2013, 116 and less than three weeks before he made the LBAC Bid. While Mr. Ergen's substantial investment in LP Debt reflects (he says) his confidence in the intrinsic value of LightSquared's spectrum assets, it also reflects his certainty, that, in his capacity as DISH's controlling shareholder and chairman of its board of directors, he could cause DISH to do what he wanted to effect the acquisition of the assets at a price that would return his investment, and possibly make a profit, while also benefiting DISH with valuable spectrum. And the Ergen July 8 Presentation makes clear just how valuable LightSquared spectrum could be for DISH, permitting unusable and impaired uplink AWS-4 spectrum owned by DISH to be converted to downlink and yielding a supplemental value to DISH of \$1.833 billion to \$3.783 billion. Given the control Mr. Ergen exercised over the DISH Board (as evidenced in particular by his bullying of the Special Committee), it is clear that Mr. Ergen believed that, after making the LBAC Bid, he could and would get DISH to step in as purchaser. 117

- See Post-Trial Brief of Defendants SP Special Opportunities, LLC and Charles W. Ergen [Adv. Docket No. 142], p. 34.
- 115 PX0867.
- The Court notes the importance of the specific dates on which events occurred in this matter. In his pleadings and at oral argument, Mr. Ergen's broad-brush approach to dates (for example, stating "Spring 2013" instead of "April 26, 2013") clearly is a device to deflect focus on the specific timeline of Mr. Ergen's conduct.
- As discussed *supra*, the stated unwillingness of the Special Committee to propose a DISH bid for LightSquared's assets in an amount lower than the LBAC Bid (which bid provided Mr. Ergen with payment in full on his LP Debt) confirms that even the independent members of the DISH Board believed they could not propose a bid lower than Mr. Ergen's.

Finally, Mr. Ergen's substantial LP Debt purchases are wholly inconsistent with his investing history. The evidence demonstrates that, before his investment in LightSquared, Mr. Ergen had a history of diversified investing in conservative, low-risk, liquid assets, rather than investing a substantial sum in the distressed debt of a single company. In fact, the evidence reveals that Mr. Ergen had never made a personal investment in distressed debt of anything close to the magnitude of his eventual \$844 million investment in LightSquared, nor had he ever made a significant personal investment (i) in a competitor of DISH or EchoStar, (ii) in a company considered a strategic investment for either one, or (iii) in any company owning spectrum assets. According to Mr. Ergen, he did not even discuss the almost \$1 billion investment with his wife, *333 who was also the co-trustee of the trust that funded the purchases. Mr. Ergen, who

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testified that, as the chairman of DISH, he focuses "on strategic direction of the company," ¹¹⁸ was clearly planning for DISH, and the inconsistency of his LightSquared investment with his prior investing history only lends further support to the inference that SPSO's debt purchases were made to pave the way for DISH to acquire control of LightSquared's assets.

Jan. 13 Tr. (Ergen) 95:6–9.

C. Breach of the Implied Covenant of Good Faith and Fair Dealing

[3] Based on the foregoing, the Court concludes that the conduct of Mr. Ergen and SPSO, undertaken on behalf of or for the benefit of DISH, was an end-run around the Eligible Assignee provisions of the Credit Agreement that breached the implied covenant of good faith and fair dealing arising under the Credit Agreement. ¹¹⁹ See Standard Chartered Bank v. AWB (USA) Ltd., No. 05 Civ.2013(AKH), 2010 WL 532515, at *14 (S.D.N.Y. Feb. 16, 2010). Simply put, that which a corporation is contractually unable to accomplish itself in its own name cannot be accomplished by interposing a shell company. As the court stated in Standard Chartered, "[i]t is not a matter of piercing corporate veils.... It is a matter of requiring a party to ... honor the contract and its covenants and not attempt to defeat assigned rights by interjecting an affiliated company." Id.

- While a party is precluded from recovering on both a claim for breach of the implied covenant of good faith and fair dealing and a claim for breach of contract at the same time (see, e.g., Hard Rock Cafe Int'l, (USA), Inc. v. Hard Rock Hotel Holdings, LLC, 808 F.Supp.2d 552, 567 (S.D.N.Y.2011)), where the meaning of a contact is in doubt, a party may plead breach of the implied covenant of good faith and fair dealing as an alternative theory to its breach of contract claim. Id.; see also Fantozzi v. Axsys Techs., Inc., 2008 WL 4866054 at *7-8, 2008 U.S. Dist. LEXIS 94040 (S.D.N.Y. Nov. 6, 2008) at *21-22. Here, LightSquared has asserted a single claim for recovery in the form of a breach of contract claim, presenting its equitable theory of breach of the implied covenant of good faith and fair dealing in the alternative, which the Court finds permissible.
- [4] [5] [6] Under New York law, every contract contains an implied covenant of good faith and fair dealing in the course of performance. See Empresas Cablevision, S.A.B. de C.V. v. JPMorgan Chase Bank, N.A., 680 F.Supp.2d 625, 631 (S.D.N.Y.2010), aff'd in relevant part, 381 Fed.Appx. 117 (2d Cir.2010) ("Empresas"). That implied covenant is, in spirit "a pledge that 'neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract.' "Id. (citing Dalton v. Educational Testing Serv., 87 N.Y.2d 384, 389, 639 N.Y.S.2d 977, 663 N.E.2d 289 (1995) (citation omitted)). 120 In Empresas, a case in this District, District Judge Rakoff found that conduct technically permissible under a credit agreement may nevertheless give rise to a breach of the implied covenant of good faith and fair dealing if it is intended to achieve a result that is prohibited by the agreement and which would do away with the "fruits" of the contract. Id. at 632.
- 120 See also RESTATEMENT (SECOND) OF CONTRACTS § 205 cmt. d (1981) ("Subterfuges and evasions violate the obligation of good faith in performance even though the actor believes his conduct to be justified ... [where the actor evades] the spirit of the bargain...."); InterDigital Comme'ns Corp. v. Nokia Corp., 407 F.Supp.2d 522, 536 (S.D.N.Y.2005) (quoting Restatement).

The facts of *Empresas* are straightforward. Empresas Cablevisión ("Cablevi *334 sión") borrowed \$225 million from JPMorgan Chase ("JPMorgan"). The governing credit agreement restricted JPMorgan's ability to assign the loan to another party without Cablevisión's prior written consent. Id. at 627. The credit agreement did allow JPMorgan to sell "participations" in the loan (which it could do without Cablevisión's consent), but only if the relationship between JPMorgan and Cablevisión, as well as JPMorgan's rights and obligations under the credit agreement, remained unchanged. Id. In his decision, Judge Rakoff noted that Cablevisión negotiated for and obtained a veto right over assignments in order to protect against the possibility of an "unsuitable party" being given the rights to enforce restrictive covenants or to receive information under the loan. Id. at 631.

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Subsequently, JPMorgan agreed to assign 90 percent of the loan to Banco Inbursa, S.A. ("Inbursa"), a bank under common ownership with a competitor of Cablevisión. ¹²¹ *Id.* at 629. After JPMorgan sought Cablevisión's consent, Cablevisión's counsel replied by letter stating that it would not consent to the proposed assignment because

... it would be inappropriate, and could cause serious harm to our business and our competitive position if one of our major competitors is allowed to gain access to confidential and competitively sensitive information about us, or to exert any control over our business affairs and hinder the development of our business.

The letter also stated that JPMorgan's sale of a participation of 90 percent of the loan to Inbursa (instead of an assignment) would similarly be unacceptable and would violate the "duty of good faith" owed by JPMorgan under the credit agreement. Notwithstanding, JPMorgan proceeded ahead with negotiating a sale of a 90 percent participation in the loan to Inbursa and did not disclose the participation to Cablevisión even after the participation agreement was signed. ¹²² By selling a participation rather than assigning the loan, JPMorgan avoided the transfer restrictions in the credit agreement that necessitated borrower consent.

- Inbursa is a Mexican bank controlled by Carlos Slim Helú and his family, who also held a controlling interest in Telmex, a Mexican communications conglomerate that owned over 80 percent of telephone land lines in Mexico and was seeking to expand into other telecommunications markets at the time of the *Empresas* decision. *Id.* at 627.
- The participation agreement also contained numerous non-standard terms, including permitting Inbursa to request and receive nearly unlimited information from Cablevisión and providing that in the event of default by Cablevisión, "the Participation Agreement 'shall be terminated and replaced by an assignment agreement ... whereupon the Participant shall become a Lender.' "Id. at 630. Inbursa also obtained a provision that would have allowed it to declare an event of default and trigger the outright assignment in the event that Cablevisión refused to provide the confidential information requested. Id. at 632.

When Cablevisión learned of the agreement between JPMorgan and Inbursa, it promptly sought a preliminary injunction preventing JPMorgan from effectuating the transfer. It argued that the participation agreement was, for all relevant purposes, "a disguised but unconsented-to assignment" that breached the credit agreement or that "so subverts the purposes underlying Cablevisión's right to veto assignments of the loan as to breach the *335 covenant of good faith and fair dealing implied by law in the Credit Agreement." *Id.* at 631.

Judge Rakoff enjoined the transfer, finding that JPMorgan violated the implied covenant of good faith and fair dealing by attempting, through the "guise" of a purported participation, to effectuate a prohibited assignment that it could not have implemented directly. *Id.* at 631. While the court observed that JPMorgan's argument that the participation agreement was "technically consistent" with the credit agreement "[s]uperficially ... may be correct," its actions were nevertheless impermissible because they "effectuated what is in substance a forbidden assignment" that the transfer restrictions were designed to prevent, thus undermining Cablevisión's veto rights under the credit agreement. *Id.* at 631, 633. Had the transfer been allowed, the participation agreement would have given Inbursa the potential to access extensive confidential information about the business, affairs, and financial condition of Cablevisión, all of which Cablevisión desired to keep its competitors from obtaining. *Id.* at 630–631. Thus, the Court granted Cablevisión's request for a preliminary injunction, concluding that "JPMorgan violated, at a minimum, the covenant of good faith and fair dealing automatically implied by law in the credit agreement" and that "[s]uch an end-run, if not a downright sham" was not permissible as it did away with the "fruits" of the contract. ¹²³ *Id.* at 632.

At closing argument in the Adversary Proceeding, counsel for DISH informed the Court that, on appeal, the Second Circuit subsequently reversed Judge Rakoff's *Empresas* order. (Mar. 17 Tr. (Giuffra) 300:23–303:3 ("The Second Circuit, in a summary order, reversed the injunction, insofar as the participation was not allowed ...").) This interpretation of the Second Circuit's order is incorrect. As counsel for the Debtors correctly pointed out, the Second Circuit affirmed Judge Rakoff's *Empresas* decision. Because Inbursa and JPMorgan had already completed the transfer of a 90 percent participation interest

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in the loan, however, the Second Circuit, after affirming Judge Rakoff's order, simply ordered the District Court to review and modify the injunction to require JPMorgan to comply with the implied covenant of good faith and fair dealing by prohibiting, pending a trial to determine whether or not damages were owed, the exercise of any right under the participation agreement that might give Inbursa or its affiliates a competitive advantage over Cablevisión. *See* 381 Fed.Appx. 117 (2d Cir.2010); Mar. 17 Tr. (Leblane) 350:25–351:20.

Here, as in *Empresas*, in which consent to sell a participation was technically not required by the credit agreement, the Court's finding that SPSO is technically an Eligible Assignee under the Credit Agreement might end the analysis. But, as in *Empresas*, contractual language must be read in context. ¹²⁴ The context here requires *336 reading the Eligible Assignee provision and the rest of the Credit Agreement in the context of the intent, on the part of LightSquared, to prevent competitors from gaining access to its capital structure. This intent was readily apparent from the face of the Credit Agreement and is overtly evidenced by (i) the language utilized in the definitions of Eligible Assignee and of "Disqualified Company" (which refers to direct competitors of LightSquared) designed to limit ownership of the LP Debt ¹²⁵ and (ii) LightSquared's May 9 and May 12, 2012 amendments to the Credit Agreement to add additional LightSquared competitors, including DISH, to the list of Disqualified Companies. ¹²⁶

- In this Adversary Proceeding, DISH, LBAC, and SPSO have argued that the Court should look only to the literal terms of the document, without regard to context, when adjudicating the asserted claim for breach of the Credit Agreement. Notably, however, these parties have made the contrary argument in the Debtors' main cases when seeking a declaration that both the PSA and the DISH/LBAC Bid were terminated in their entirety. In arguing that the DISH/LBAC Bid did not remain irrevocable until the earlier of sixty days after entry of the Confirmation Order and February 15, 2014, DISH and LBAC sought to avoid the application of the literal terms of the bid procedures order entered in the Debtors' cases [Bankr. Docket No. 892], which so stated, by relying on context and the parties' intent. See Objection of LBAC to the January 13, 2014 Statement of the Ad Hoc Secured Group and Notice of Intent to Proceed with Confirmation of the First Amended Joint Chapter 11 Plan and Motion for Declaratory Relief [Bankr. Docket No. 1232] at 14 ("Examined in its full context ..., the plain language of the pertinent provision which was added at the Court's request, paragraph (j) of the Bid Procedures [Order], makes clear that this was the extent of LBAC's commitment"), 14–17 (citing to numerous hearing transcripts to demonstrate that "the statements of ... parties ... subsequent to the September 30 hearing further clarify all parties' understanding that LBAC's commitment to move forward with the LBAC Bid was governed by the PSA, not the Bid Procedures Order").
- See, e.g., Meridian Sunrise Village, LLC v. NB Distressed Debt Investment Fund Limited (In re Meridian Sunrise Village LLC), 2014 WL 909219 (holding that, while courts will first look to the face of the document and the plain language of the agreement to determine its meaning, a court may rely on extrinsic evidence even in the absence of ambiguity, and finding that the parties had intentionally limited the term "Eligible Assignees" in the loan agreement at issue in order to exclude assignment to "distressed asset hedge funds who candidly admit they seek to 'obtain outright control' of assets").
- As Mr. Smith testified at Trial, LightSquared amended the Disqualified Company (pre-bankruptcy) list "to make sure that the list of disqualified companies included all of [LightSquared's] competitors, because we didn't want competitors involved in the capital structure. We thought it was important as we were entering bankruptcy to make these updates." Jan. 9 Tr. (Smith) 126:22–127:24; PX0161.

As set forth in detail in paragraphs 32–34, *supra*, pursuant to the Credit Agreement, Eligible Assignees are entitled to receive substantial non-public information about LightSquared and are granted access to LightSquared's officers and employees for information regarding LightSquared's ongoing business and operations ¹²⁷ and also receive a right to vote on certain material matters, including waivers, exercises of remedies, and other similar matters. The Debtors have appropriately pointed out that one could reasonably expect a competitor to vote differently than a non-competitor lender on material matters concerning LightSquared, and, more significantly, a competitor given access to material non-public information about LightSquared may use it to LightSquared's detriment, given that a competitor may possess a desire to see LightSquared fail. As a result, LightSquared has a legitimate basis for its desire to prohibit competitors from becoming holders of its LP Debt.

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See, e.g., Credit Agreement § 3.04 (requiring LightSquared to provide several years of financial statements and projections), § 3.05 (listing all real property owned or leased), § 3.06 (listing all intellectual property owned or licensed), § 3.09 (all material agreements relating to LightSquared's business), § 5.01(a) and § 5.01(b) (requiring annual and quarterly updates containing information that would be included on SEC Forms 10–K and 10–Q), § 5.01(h) (annual and quarterly budgets), and § 5.01(j) (a general catchall for information reasonably requested by a Lender). In addition, under Section 5.07(a), each Lender also has the right to inspect LightSquared's properties and "discuss the affairs, finances accounts and condition" of LightSquared with its officers, employees, accountants and advisors.

The problem is that the Credit Agreement was not crafted sharply enough to achieve that intent. Moreover, the problem was exacerbated by the lack of action by LightSquared in the face of rampant public speculation about the debt purchases. ¹²⁸ Mr. Ergen found a loophole in *337 the express terms of the Credit Agreement and exploited it. That is not wrong in and of itself. The wrong arises from Mr. Ergen's purchases of the LP Debt, beginning in the spring of 2013, when he intended his "substantial interests" in the debt to complement any acquisition strategy and have "significant influence" in the bankruptcy cases; ¹²⁹ he intended and preferred that it be DISH that acquired LightSquared debt (and ultimately its spectrum), and he pursued such purchases to preserve valuable options for the benefit of DISH. These purchases violate the spirit of the Credit Agreement, as the harm that LightSquared sought to avoid—a competitor entering its capital structure and acting against its interests—has now come to pass. Mr. Ergen's use of SPSO to evade the terms of the Credit Agreement that prevented him and DISH from buying the LP Debt thus deprived LightSquared of the fruits of the Credit Agreement's restrictions.

- SPSO focuses on the notable distinction between the facts of *Empresas* and the Adversary Proceeding on this point. In *Empresas*, Cablevisión actively opposed Inbursa's use of a participation structure to circumvent the assignment restrictions. *See Empresas*, 680 F.Supp.2d at 628. Here, the evidence demonstrates that Plaintiffs were aware as early as May 2012 that there was at least some possibility that Mr. Ergen was behind SPSO's debt purchases. Yet, as SPSO continued to acquire additional LP Debt, Plaintiffs did not act in any way to seek to prohibit SPSO from making such purchases. As will be discussed more fully *infra*, for this reason, the Court declines to award damages to Plaintiffs.
- See PX0867 (Ergen Presentation).

While technically permitted to buy LP Debt, SPSO was essentially a front used by Mr. Ergen to implement his strategy for the benefit of DISH, a forbidden Lender under the Credit Agreement. That SPSO's acquisition strategy was formulated specifically to achieve an end-run around the restrictions in the Credit Agreement is amply supported by the record. The Court thus concludes that, at least as of mid-April 2013, during the period in which SPSO acquired an additional \$320 million of LP Debt, Mr. Ergen, through SPSO, was not acting on his own behalf to acquire LP Debt as a personal investment; rather, he was acting to acquire a strategic advantage which he knew he would have to tender to the DISH Board to give DISH the option of making a bid LightSquared's spectrum assets, assets which were clearly attractive to DISH, whether or not DISH consummated a transaction with Sprint. ¹³⁰

130 See Ergen Presentation (stating that Mr. Ergen's "substantial interests in L2 debt and preferred stock compliment [sic] any acquisition strategy and could have significant influence in L2's chapter 11 cases."); see also Ergen July 8 Presentation.

The record also supports the conclusion that Mr. Ergen's strategy was deployed on behalf of DISH as early as October 2012, when he told Mr. Kiser, "[i]f we can't be sure the company can buy them, then I am interested to increase my position at the 75 level at least up to a 33% ownership level of the class." Simply put, had he then been advised that DISH was permitted to buy the LP Debt, Mr. Ergen's words reflect his preference that DISH (not SPSO) buy the debt. But having identified a roadblock in the Credit Agreement, Mr. Ergen simply created a special purpose vehicle, drove around the roadblock, and took an alternate route to his destination.

Nor can it be seriously maintained that Mr. Ergen did not personally direct and indeed control virtually every aspect of the process leading to the formulation of the LBAC Bid and its ultimate pursuit by DISH. From his stunning lack of candor with the DISH Board and management to the stonewalling and disbanding of the Special Committee, the

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message is loud and clear: no one crosses or even questions the actions of the Chairman. Charles Ergen is, in every sense, the controlling *338 shareholder of DISH and wields that control as he sees fit. His acquisition through SPSO of the LP Debt violated the covenant of good faith and fair dealing automatically implied by law in the Credit Agreement. ¹³¹

Because the Court has declined to hold any of the Defendants liable for breach of the express terms of the Credit Agreement, it is not necessary to address the parties' myriad arguments regarding the applicability of the doctrines of agency, imputation, ratification, and alter ego.

Indeed, the extent to which DISH itself believed an end-run around the terms of the Credit Agreement was perfectly acceptable was made crystal clear during closing arguments. When asked by the Court if an affiliate of DISH could have purchased LP Debt without running afoul of the Credit Agreement, counsel for DISH agreed, "based on the words of the contract." ¹³² After a further hypothetical situation was posed to counsel—if SPSO hypothetically had a side agreement with DISH that DISH would guarantee the return of Mr. Ergen's capital on his investment of LP Debt—counsel responded that he still believed that SPSO would not have breached the Credit Agreement under such a scenario, even if SPSO was hedged with a Disqualified Company such as DISH. ¹³³ DISH's view, in other words, is that if the Credit Agreement does not explicitly prohibit a particular transfer by its express terms, any contrivance or subterfuge to avoid running afoul of those express terms is a-ok. This cannot be correct.

- Mar. 17 Tr. (Giuffra) 293:14–21. Counsel further added that "there is a definition of affiliate in this contract, which does what they want it to do, which would have picked up SPSO, which would have picked up Mr. Ergen. And that's not what it says in the transfer provision." *Id.* at 300:8–11.
- 133 See Mar. 17 Tr. (Giuffra) 313:17–315:1 ("Your Honor, it's because the contract wasn't drafted with a broad transfer restriction.... I think we still win.").

Finally, Defendants' attempts to distinguish *Empresas* are unavailing. They argue that *Empresas* is entirely different from this case because, in *Empresas*, JPMorgan *colluded* with Inbursa to alter fundamentally the agreement between Cablevisión and JPMorgan, and Inbursa actively bargained for non-standard provisions in the participation agreement with JPMorgan, both facts which are not present here. ¹³⁴ Regardless of whether collusion occurred here or not (and there have been no allegations that Mr. Ergen in fact colluded with any Lenders from whom he purchased LP Debt), and notwithstanding the fact that SPSO's LP Debt purchases were made under standard terms, the violation of the spirit of the Credit Agreement in each case remains the same. Having been informed more than once that DISH and EchoStar could not purchase the LP Debt under the express terms of the Credit Agreement, Mr. Ergen sought to do indirectly what he knew was not permitted directly. As in *Empresas*, although the LP Debt purchases by SPSO may have appeared "superficially" permissible, those purchases (which, by April 2013, were made essentially for DISH in contemplation of a potential DISH acquisition) were intended to circumvent the Credit Agreement's restrictions on transfers to DISH. Contrary to Defendants' assertions, the restrictions on competitors *339 becoming Lenders were bargained for by LightSquared in the same way that Cablevisión bargained for the right to veto assignees but neglected to include in such provision the right to veto parties purchasing participations.

Defendants also argue that the legal analysis in *Empresas* is distinguishable based on the procedural posture of the case. This argument lacks merit because the legal analysis concerning the parties' good faith and fair dealing or lack thereof remains unchanged, whether evaluated in the context of a preliminary injunction or, as here, in the liability phase.

SPSO must be held accountable for its conduct, in context. Mr. Ergen's multiple hats—personal, SPSO, LBAC, DISH—cannot be selectively deployed to disguise SPSO or insulate SPSO from responsibility for its actions in using a "guise" to achieve an "end run" around the substance of the Eligible Assignee restrictions in the Credit Agreement and undercut what Mr. Ergen certainly knew the restrictions were designed to prevent. See Empresas, 680 F.Supp.2d 625.

IV. The SPSO Claim Shall Not Be Disallowed

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A. The SPSO Claim is Not Void or Voidable Even Though the Court Finds an Implied Breach and Even if the Court Were to Have Found an Express Breach

[7] Section 502 of the Bankruptcy Code provides that a properly filed proof of claim is deemed allowed unless a party in interest objects. 11 U.S.C. § 502(a). Various other subsections of section 502 set forth the grounds for disallowing a claim, including section 502(b)(1), which authorizes disallowance because the claim is unenforceable under any agreement or applicable law. Section 502(b) provides: "[T]he court ... shall allow such claim in such amount, except to the extent that (1) such claim is unenforceable against the debtor and property of the debtor, under any agreement or applicable law...." 11 U.S.C. § 502(b).

SPSO maintains that, even if it was not an Eligible Assignee, the SPSO Claim would *still* be enforceable against the LightSquared LP estate, as nothing in the Credit Agreement treats transfers as void or voidable even if they are made in violation of the transfer restrictions. The Court concludes that SPSO is correct on this point. Even if the Court had found that SPSO breached the express terms of the Credit Agreement and was not an Eligible Assignee, the plain language of the Credit Agreement does not support disallowance of the SPSO Claim.

Plaintiffs argue that the Credit Agreement provides that a transferee who is not an Eligible Assignee acquires no rights under the Credit Agreement, and, therefore, such transferee cannot assert a claim against the company with respect to any purchase of LP Debt. Accordingly, they argue, any claim of SPSO based on the Credit Agreement must be disallowed. In support of this argument, Plaintiffs rely on Section 10.04(a) of the Credit Agreement, which provides that

Nothing in this Agreement, express or implied, shall be construed to confer upon any person (other than the parties hereto, their respective successors and assigns permitted hereby, Participants to the extent provided in paragraph (d) of this Section and, to the extent expressly contemplated hereby, the other Indemnities) any legal or equitable right, remedy or claim under or by reason of this Agreement.

Credit Agreement § 10.04(a).

As Mr. Ergen and SPSO point out, however, Plaintiffs fail to mention other relevant provisions of the Credit Agreement which provide that any breach by any Lender or participant ¹³⁵ of the transfer *340 restrictions under the Credit Agreement does not excuse performance by LightSquared. Specifically, Section 10.04(d) of the Credit Agreement provides, in pertinent part, that LightSquared

agrees that any breach by any Lender or participant or sub-participant of the restrictions on assignment hereunder (including, without limitation, to Disqualified Companies) shall not excuse, in any respect, performance by the Borrower under the Loan Documents.

Credit Agreement § 10.04(d). Contrary to Plaintiffs' argument, Section 10.04(d) of the Agreement makes clear that neither a breach of the express terms of the Credit Agreement nor a breach of the implied covenant of good faith and fair dealing renders wrongfully transferred debt claims unenforceable against LightSquared and therefore disallowable. SPSO also points out that similar language has been found insufficient to invalidate transfers. See LCE Lux HoldCo S.a.r.l. v. Entretenimiento GM de Mexico S.A. de C.V., 287 F.R.D. 230, 235 (S.D.N.Y.2012). 136

Section 10.04(b) of the Credit Agreement provides that "[a]ny assignment or transfer by a Lender of rights or obligations under [the Credit] Agreement that does not comply with this paragraph shall be treated for purposes of this Agreement as a sale by such Lender of a participation in such rights and obligations in accordance with Section 10.04(d)." Credit Agreement § 10.04(b). Thus, even if an assignment by a Lender is invalid, it would be treated as a sale of a participation, and, pursuant to Section 10.04(d), a breach by a participant still does not excuse performance by LightSquared.

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In LCE Lux HoldCo S.a.r.l. v. Entretenimiento GM de Mexico S.A. de C.V., the agreement at issue contained a provision prohibiting assignment without consent, specifically stating that "[n]either party may assign any of its right under the Agreement without the prior written consent of the other parties, which will not be unreasonably withheld." The agreement went on to provide that "[s]ubject to the preceding sentence, this Agreement will apply ... to give any Person other than the parties to this Agreement any legal or equitable right, remedy, or claim under or with respect to this Agreement or any provision of this Agreement." 287 F.R.D. at 235. The defendant argued that the only way to give meaning to the phrase "subject to the preceding sentence" was to read the second sentence to mean that the benefits of the agreement inured only to permitted assigns, thus rendering an assignment in violation of the agreement void. The court found that the agreement did "not contain the typical 'talismanic' language that renders an assignment void," and that, given the ambiguities in the phrasing of the agreement on this point, was unwilling to void the assignment at issue. Id. at 235–36 (stating that "assignments made in contravention of a prohibition clause in a contract are void if the contract contains clear, definite, and appropriate language declaring the invalidity of such assignments") (citation omitted).

Under any circumstances, even in the case of an express breach, in order for a claim to be disallowable, the contract must expressly provide that any breach of the contract, such as an assignment in violation of the agreement, shall render the assignment wholly void or invalid. See In re 785 Partners LLC, 2012 WL 401497 at *3 (Bankr.S.D.N.Y. Feb. 7, 2012) (citing Pravin Banker Assocs., Ltd. v. Banco Popular Del Peru, 109 F.3d 850, 856 (2d Cir.1997) (assignment of a loan is valid, rendering the assignee "a secured creditor and party in interest" in the bankruptcy, even if the assignee did not meet the definition of an Eligible Lender, where the contract lacked language invalidating an improper assignment)); see also See Purchase Partners, LLC v. Carver Fed. Sav. Bank, 914 F.Supp.2d 480, 505 (S.D.N.Y.2012) (contractual provisions prohibiting assignments are not enforceable except where "the relevant provision of the contract contains 'clear, definite, and appropriate' language declaring an assignment invalid") (quoting Sullivan v. Int'l Fid. Ins. Co., 96 A.D.2d 555, 556, 465 N.Y.S.2d 235 (2d Dep't 1983)); *341 In re Britton, 288 B.R. 170, 173 (Bankr.N.D.N.Y.2002) (quoting Pravin Banker Assocs. Ltd. v. Banco Popular Del Peru, 109 F.3d at 856) (finding that under New York law, "to preclude the power to assign, or cause an assignment violative of contractual provisions to be wholly void, [a contractual] clause must contain express provisions that any assignment shall be void or invalid if not made in a certain specified way").

Here, the Credit Agreement does not contain clear language voiding an assignment to a party that is not an Eligible Assignee or invalidating a claim by such party relating to the Credit Agreement; thus, even if the Court had found that SPSO is not an Eligible Assignee under the express terms of the Credit Agreement, the SPSO Claim would not be void or voidable.

B. The Inaction and Delay of LightSquared and Harbinger Preclude the Award of Affirmative Damages

[8] Beginning in May 2012, LightSquared and Harbinger knew or had strong reason to believe that Mr. Ergen was purchasing LP Debt. Substantial documentary evidence in the record reflects that, at a minimum, beginning with the sale of Carl Icahn's \$247 million LP Debt position to a Sound Point client on May 4, 2012, which was reported in the press, 137 the Debtors and Mr. Falcone harbored serious suspicions that Mr. Ergen had entered LightSquared's capital structure. For example, on May 5, 2012, Mr. Falcone responded to an email from a LightSquared creditor, writing "[m]aybe we shouldn't file if [Ergen] is circling the wagons. Though I think [it] is a positive. May bring in another strategic." (DX035 (Falcone to Ara Cohen of Knighthead); see also DX040 (May 7, 2012, Marc Montagner of LightSquared to Stan Holtz of Moelis: "Ketchum, with his 175MM fund, bought 350 of the debt on Friday. He is probably a front for Charlie Ergen."); DX382 (May 8, 2012, Falcone to Ara Cohen: "I can understand why u guys balked; Charlie will definitely give u guys 25% and an independent board and your full claim.").) Sarcasm aside, Mr. Falcone's surmise that the buyer of LP Debt was Mr. Ergen was also set forth in a number of emails he sent to members of the press. See DX037 (May 6, 2012, Falcone to Matthew Goldstein of Reuters: "Ergen. Will prompt more strategics to step in."); DX386 (May 16, 2012, Falcone to Greg Bensinger of The Wall Street Journal: "Carlos Slim apparently [is] involved with Ergen" as purchasers of LP Debt, and, after questions from Mr. Bensinger, adding that "He clearly wants the spectrum and the satellites. Let me know before I tell someone else if u are going to write anything.") After sending these emails, Mr. Falcone testified, he understood that The Wall Street Journal may write an article based on the information provided. 138

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- See, e.g., DX396 (May 10, 2012, Wall Street Journal blog, "Deal Journal," entry titled "Ergen Builds Cash Pile Amid LightSquared Restructuring Talks").
- 138 See Jan. 16 Tr. (Falcone) 54:15–22, 108:25–109:4.

- Jan. 16 Tr. (Falcone) 109:6–8. When asked at Trial about why he exchanged emails with reporters, Mr. Falcone testified that "[s]ometimes they have good information," as he was trying to find out who was buying LightSquared debt. Id. at 36:9–16.
- 140 Mr. Jaffrey is now a principal of Melody Capital Partners, one of the sponsors of the Debtors' Third Amended Joint Plan of Reorganization.
- Jan. 16 Tr. (Falcone) 56:17–57:5. On May 8, 2012, Mr. Falcone had sent a similar email to Gil Ha, a banker at Greenhill & Co., who had a relationship with AT & T, stating "Ergen now involved in LS." DX043. Mr. Falcone testified that he sent this email to both (i) fish for intelligence as to who had purchased Mr. Icahn's position and (ii) see if AT & T, after viewing Mr. Ergen's investment as validation, would possibly be interested in investing in LightSquared. Id. at 41:17–42:9; 118:21–119:14.
- Jan. 16 Tr. (Falcone) 35:3–10. Other emails admitted into evidence show that Mr. Falcone had also contacted DISH directly in what appears to have been an attempt to goad them into corroborating that Mr. Ergen was purchasing LP Debt. See DX0378 (May 7, 2012, Falcone to Thomas Cullen of DISH, "Good purchase."); DX097 (December 18, 2012, Falcone to Thomas Cullen of DISH: "Tom, we should talk. I know you guys are buying the bonds through Sound Point. One of his guys has been talking.").

None of these emails reflects alarm on the part of Mr. Falcone or LightSquared that a competitor who might act against LightSquared's interests had likely entered its capital structure or that the uncertain identity of such party was troubling to them. Quite the contrary, the correspondence in evidence reveals that Mr. Falcone conveniently used his suspicions of Mr. Ergen's trading in LP Debt as an item to publicize in order to drum up possible interest in LightSquared from strategic investors, some of whom were themselves LightSquared competitors. And, as the trading price of LP Debt increased from 48 cents on the dollar in April 2012 to 96 cents on the dollar in April 2013, Mr. Falcone seemed even less inclined to complain about the allegedly harmful presence of a competitor in the capital structure. Even as late as March 28, 2013, Mr. Falcone and Drew McKnight of Fortress both expressed in an email exchange their views that it was beneficial that a potential strategic investor, Mr. Ergen, was also buying LP Preferred Interests in addition to LP Debt. Am. Falcone explained at Trial that he considered this a validation of spectrum value, and, in addition, as stated in the email exchange, he felt that Mr. Ergen's LP Debt acquisition could help to "blow up" the Ad Hoc Secured Group unless Mr. Ergen joined *343 them. Had While, at Trial, he denied that he knew the details of the Exclusivity Stipulation (which required the Debtors to start preparatory work on a sale process on June 3, 2013 and to commence a formal sale process on July 15, 2013 upon the termination of exclusivity, if the Ad Hoc Secured Group still remained

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the largest group of holders of LP Debt and no consensual deal between the parties had been achieved), Mr. Falcone admitted that he understood that such requirement would fall away if Mr. Ergen became the largest holder of LP Debt.

- DX0395 (McKnight to Falcone: "... at end of day really need a strategic involved here to maximize value and I think you're getting it. Pretty huge for them to pay up on preferred. Think it's a positive all around." Falcone reply: "I do too.")
- 144 Jan. 16 Tr. (Falcone) 141:11–143:17.

At Trial, Mr. Falcone maintained that, depending on the day and the information he received, his belief changed as to who was behind Sound Point's purchases. For example, when asked if, on May 9, 2012, he still believed that it was Mr. Ergen buying the LP Debt, he answered that "I don't know if it was the Carlos Slim and Charlie Ergen day, but it could have been one or the other." (Jan. 16 Tr. (Falcone) 115:4–5; see also id. at 58:4–11 ("I just didn't know. You know, depending on—at this point in time what minute of the day it was, I had believed, on one hand, it could be AT & T, and then six minutes later I changed my mind, I think it's Ergen.").) The contention that Mr. Falcone and LightSquared were unsure whether the purchaser of the LP Debt was related to DISH, rather than Carlos Slim (the owner of one of the largest telecommunications empires in the world) or Cablevision (one of the largest cable providers in the United States and a Disqualified Company)—all competitors of LightSquared—suggests that LightSquared was not overly concerned about the presence of any these parties in its capital structure. In fact, the addition of DISH to the Credit Agreement's list of Disqualified Companies on May 9, 2012, appears to have been pursued by Mr. Falcone at least partially in spite in order to trap Mr. Ergen in a minority position in the LP Debt after he had acquired Mr. Icahn's position. On May 6, 2012, after learning of the purchase of Mr. Icahn's \$247 million position in the LP Debt, Mr. Falcone wrote to Ara Cohen of Knighthead, "Well I'm working on giving [Ergen] a nice surprise" by adding DISH to the list of Disqualified Companies. (DX038).

Despite the significant amount of documentary evidence indicating that they knew or should have known, LightSquared and Harbinger maintain that it was not until May 21, 2013 that they first received confirmation that Mr. Ergen was the party behind SPSO's purchases of LP Debt. ¹⁴⁵ They argue that, prior to being informed by SPSO's counsel on May 21, 2013, public information provided them with no certainty as to who was behind SPSO's purchases. They emphasize the widespread speculation in the media and that news reports, blogs, and rumors at various times pointed to Carlos Slim, the Dolan Family, or Mr. Ergen as the purchaser. ¹⁴⁶ Moreover, *344 LightSquared and Harbinger maintain that they made diligent efforts to determine who was behind Sound Point's purchases of LP Debt, pointing to, among other things, voicemails left by Mr. Montagner for Mr. Ketchum; efforts by Moelis to obtain information from Mr. Ketchum and from Willkie Farr; ¹⁴⁷ their attempts through UBS; and Mr. Falcone's efforts to reach out to "people on the street" such as reporters, Mr. Cullen, and representatives of AT & T and Sprint. ¹⁴⁸

- As support for this assertion, LightSquared and Harbinger point to emails exchanged between Mr. Falcone and representatives and advisors for Harbinger and LightSquared on May 21, 2013, when they purportedly did not yet know the identity of Sound Point's client. In those emails, Falcone stated that "[i]f I were a betting man I would say that Sound Point is Slim." (Jan. 16 Tr. (Falcone) 72:25–73:18; PX0540.) Upon receipt of the email from counsel confirming Ergen was in fact the ultimate buyer of Sound Point's LP Debt purchases, Falcone responded "[f]ortunately, I'm not a betting man." (Jan. 16 Tr. (Falcone) 73:19–74:9; PX0537.)
- See, e.g., PX0095 (May 4, 2012, trader at Harbinger to Falcone: "[Ketchum] is the guy running South Point. An old article, but looks like the guy has close ties with the Dolan family."); PX149 (May 10, 2012, email from Harbinger employee to Falcone that he had "heard from a couple of people that [E]rgen may not be the guy behind [K]etchum. Some rumors are that it might be the [D]olans, who like [E]rgen are close to [K]etchum."); PX0304 (July 9, 2012, Forbes article noting that "holes have appeared in the thesis that Ergen is backing Sound Point" and "people involved have begun to speculate it might be Carlos Slim or others behind the purchase. Sources have speculated that Cablevision, owned by the Dolan family and one of the country's largest telecom and media company [sic], could be a potential suitor as well."); DX045 (May 9, 2012, LCD News story headlined "LightSquared [Term Loan] trades north of 70 as Ergen enters the picture.").

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- Mr. Hootnick testified at Trial that Moelis called "Mr. Ketchum regularly and [met] with him regularly, and ... continu[ed] during that period [i.e., spring 2013] to try and find out who Sound Point—if they were representing somebody and what their intention was." Mr. Ketchum continued to refuse to identify its investors or intentions. (Jan. 17 Tr. (Hootnick) 23:13–24; Jan. 15 Tr. (Ketchum) 88:22–89:22; PX0443.) Mr. Hootnick directly "ask[ed] Mr. Ketchum if he was working with Mr. Ergen ... but [Ketchum] refused to answer any of those questions." (Jan. 17 Tr. (Hootnick) 19:8–20.) Mr. Hootnick also reached out to Rachel Strickland of Willkie Farr, who had represented Ergen in the TerreStar bankruptcy, to see whether she would shed light on whether Mr. Ergen was involved in SPSO's LP Debt purchases. (Jan. 17 Tr. (Hootnick) 19:21–21:3, 64:3–9.) Despite more than six phone calls and "a couple" of lunch meetings, Mr. Ergen's counsel would not confirm whether he was involved. (Jan. 17 Tr. (Hootnick) 20:22–21:3.)
- Jan. 16 Tr. (Falcone) 22:1–11.

Notwithstanding the fact that, beginning in May 2012, there was a long history of speculation in the press but no definitive confirmation that Mr. Ergen was the purchaser, ¹⁴⁹ it is clear from the totality of the evidence that, for nearly a year, LightSquared knew or had reason to believe that Mr. Ergen was behind SPSO. Despite LightSquared's protestations that it attempted to ascertain the identity of the purchaser (and the efforts to which it points), the fact remains that LightSquared, a chapter 11 debtor, did nothing to seek to obtain that information through the many tools available to it, including Bankruptcy Rule 2004, or to seek any relief from this Court with respect to the debt purchases by SPSO, which relief may have included a motion to enforce the restrictions in the Credit Agreement or an injunction similar to that obtained in *Empresas*. In fact, there appears to have been a certain degree of ambivalence as to whether the presence of Mr. Ergen was a positive or a negative for LightSquared (i) in its search for strategic investors and (ii) in terms of the implication of Mr. Ergen's holdings on the requirements set forth in the Exclusivity Stipulation. Regardless of LightSquared's ultimate view, what is clear that is that no action was ever taken.

- Indeed, an April 4, 2013 Wall Street Journal article noted, "[i]t is unclear whether Mr. Ergen or his company, satellite-television operator Dish Network Corp.... has played a role in Sound Point's trading. Mr. Ergen hasn't addressed the trades, and the company declined to comment." (DX144.)
- [9] [10] LightSquared's breach of contract allegations have been asserted too late in the game to be actionable. The equitable doctrine of laches requires that the following elements be shown: (i) conduct giving rise to the situation complained of, (ii) delay by the plaintiff in asserting a claim despite the opportunity to do so, (iii) *345 lack of knowledge on the defendant's part that a claim would be asserted, and (iv) injury or prejudice to the defendant if relief is granted to the plaintiff. *Caldor Corp. v. S Plaza Assocs. (In re Caldor Inc.)*, 217 B.R. 121, 134 (Bankr.S.D.N.Y.1998) (citations omitted). To equitably estop a plaintiff from asserting its claims, a defendant must demonstrate that the plaintiff (i) made a false representation or concealed material facts, (ii) intended that such conduct would be acted upon by the defendant, and (iii) had knowledge of the true facts. *Id.* (citations omitted). In their answer to the LightSquared Complaint, ¹⁵⁰ SPSO and Mr. Ergen raise each of these equitable doctrines (and others) as defenses barring any recovery against them.
- 150 Adv. Docket No. 102.

The Court finds that, while all of the elements of the doctrines of laches or equitable estoppel may not have been met, sufficient elements of each doctrine have been satisfied to preclude the pursuit or award of affirmative damages to LightSquared and Harbinger with respect to SPSO's conduct in acquiring LP Debt. The Court has concluded that LightSquared and Harbinger knew or had strong suspicions that Mr. Ergen was behind SPSO's purchases through Sound Point. Yet, even assuming any uncertainty on the part of LightSquared and Harbinger, they failed to act to confirm the identity of the purchaser of LP Debt and, once confirmed, they failed to take any action to prevent Mr. Ergen from closing trade after trade, instead delaying in filing suit until after Mr. Ergen had acquired \$844 million in LP Debt and had made a bid for LightSquared's assets. Meanwhile, for over one year, SPSO had purchased its LP Debt and, other than in connection with the bundled March 28, 2013 trade, never heard a peep of protest from LightSquared. As far as SPSO could reasonably conclude, the Debtors appeared to have no concern about SPSO's status as a purchaser. Such

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inaction and delay now preclude the Court from making an affirmative award of damages to LightSquared on account of Mr. Ergen's conduct. ¹⁵¹

The conduct of LightSquared and Harbinger upon learning of SPSO's LP Debt purchases, however, has no effect on whether or not the conduct of Mr. Ergen and SPSO in acquiring the LP Debt satisfies the first and second prongs of the *Mobile Steel* test for equitable subordination of SPSO's claim—whether SPSO and Mr. Ergen engaged in "inequitable conduct" and whether such conduct harmed innocent creditors. Subject to limited exceptions, "[c]ourts generally have not applied common law equitable defenses to causes of action created under Chapter 5 of the Bankruptcy Code." *In re Auto. Professionals, Inc.*, 398 B.R. 256, 262 (Bankr.N.D.III.2008). With respect to "equitable subordination, [the test] focuses only on the actions of guilty creditors and the resulting impact on innocent creditors." *Id.* at 260. "Inequitable conduct by the debtor is noticeably absent from the list of relevant considerations." *Id.* Thus, consideration of the debtor's conduct, as opposed to the guilty creditor, and allowing the unclean hands defense "would be inconsistent with the traditional test for equitable subordination, the substantial case law allowing subordination despite debtors' participation in wrongdoing, and the purpose of equitable subordination." *Id.*; accord In re Applied Theory Corp., 345 B.R. 56, 59 (S.D.N.Y.2006) ("The purpose of equitable subordination is to undo wrongdoing by an individual creditor in the interest of the other creditors."), aff'd, 493 F.3d 82 (2d Cir.2007).

V. SPSO's Claim Shall Be Equitably Subordinated to the Extent of Injury Caused to Innocent Creditors

Although SPSO cannot be found to have breached the technical requirements of the Credit Agreement, its conduct and that of its principal are nonetheless far from blameless. Mr. Ergen's carefully crafted *346 and strategically deployed decision to acquire the LP Debt despite the restrictions in the Credit Agreement and in furtherance, at least as of April 2013, of his strategic objective to acquire LightSquared's assets for DISH supports equitable subordination of SPSO's claim to the extent creditors have been injured by such conduct. Moreover, as discussed in detail below, SPSO's additional misconduct in connection with the delayed closing of hundreds of millions of dollars of LP Debt trades—and its stunning lack of candor on this issue—provides an additional basis for equitable subordination of the SPSO Claim. Taken as a whole, SPSO's conduct not only violates the covenant of good faith and fair dealing implied in all contracts but also constitutes an affront to the duty of good faith imposed on those who participate in chapter 11 proceedings.

A. Applicable Law

[11] Bankruptcy courts have broad equitable powers and have the ability to invoke equitable principles to achieve fairness and justice in the reorganization process. See Momentum Mfg. Corp. v. Employee Creditors Comm. (In re Momentum Mfg. Corp.), 25 F.3d 1132, 1136 (2d Cir.1994); 11 U.S.C. § 105(a) ("The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title"); see also Law v. Siegel, — U.S. —, 134 S.Ct. 1188, 1195, 188 L.Ed.2d 146 (2014) (a bankruptcy court has statutory authority to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of" the Bankruptcy Code (quoting 11 U.S.C. § 105(a)), but the bankruptcy court's equitable powers, including the power to impose sanctions, must be "exercised within the confines of the Bankruptcy Code" (internal quotations and citations omitted)). The doctrine of equitable subordination, codified in section 510(c) of the Bankruptcy Code, is one such equitable power that a bankruptcy court may employ to rearrange the priorities of creditors' interests and to place all or part of a wrongdoer's claim in an inferior status, in order to achieve a just result in the reorganization of a debtor.

[12] [13] The equitable subordination doctrine empowers a bankruptcy court to consider whether, "notwithstanding the apparent legal validity of a particular claim, the conduct of the claimant in relation to other creditors is or was such that it would be unjust or unfair to permit the claimant to share *pro rata* with the other claimants of equal status." *In re Adler, Coleman Clearing Corp.*, 277 B.R. 520, 563 (S.D.N.Y.2002) (Gerber, J.) ("*Adler*") (citing *80 Nassau Assocs. v. Crossland Fed. Sav. Bank (In re 80 Nassau Assocs.)*, 169 B.R. 832 (Bankr.S.D.N.Y.1994) (Bernstein, C.J.) ("*80 Nassau Assocs.*")); *In re Enron Corp.*, 333 B.R. 205, 221 (Bankr.S.D.N.Y.2005) (Gonzalez, J.) ("*In re Enron*") ("a bankruptcy court can subordinate any claim held by a creditor found to have engaged in inequitable conduct to achieve a 'just' result for the debtor's estate"). First articulated in the seminal case of *Pepper v. Litton*, 308 U.S. 295, 60 S.Ct. 238, 84 L.Ed.

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281 (1939), the doctrine itself empowers the court to look beyond the apparent facial validity of a claim and evaluate the conduct giving rise to the claim.

[14] The test for equitable subordination was originally articulated in *Benjamin v. Diamond (In re Mobile Steel Corp.)*, 563 F.2d 692 (5th Cir.1977) ("*Mobile Steel"*), and has since been adopted by Courts in the Southern District of New York. *See 80 Nassau Assocs.*, 277 B.R. at 563; *Adler*, 277 B.R. at 564; *In re Enron*, 333 B.R. at 217; *347 *ABF Capital Mgmt. v. Kidder, Peabody & Co. (In re Granite Partners)*, 210 B.R. 508, 514 (Bankr.S.D.N.Y.1997) (Bernstein, C.J.) ("*Granite Partners*"). As such, in order for this Court to exercise its power of equitable subordination, three conditions must be satisfied: (i) "[t]he claimant must have engaged in some type of inequitable conduct;" (ii) "[t]he misconduct must have resulted in injury to the creditors of the bankrupt or conferred an unfair advantage on the claimant;" and (iii) "[e]quitable subordination of the claim must not be inconsistent with the provisions of the Bankruptcy Act." *Mobile Steel*, 563 F.2d at 700; *80 Nassau Assocs.*, 277 B.R. at 563; *Granite Partners*, 210 B.R. at 514. ¹⁵²

- Although the second prong of the *Mobile Steel* test is stated in the disjunctive, the better view (and the one followed by courts in this District) is that injury must be shown; and "unfair" advantage to the claimant, in the absence of injury to creditors, is not sufficient. *See Nisselson v. Softbank AM Corp. (In re MarketXT Holdings Corp.)*, 361 B.R. 369, 388 (Bankr.S.D.N.Y.2007) (Gropper, J.); *see also In re Mr. R's Prepared Foods, Inc.* 251 B.R. 24, 29 (Bankr.D.Conn.2000) ("In the [Second Circuit], the second requirement for equitable subordination involves a conjunctive test, requiring a showing of both unfair advantage to one creditor and harm to the debtor or its other creditors." (citing *Cosoff v. Rodman (In re W.T. Grant Co.)*, 699 F.2d 599, 611 (2d Cir.1983) (grammatical changes in original))); *In re Vermont Electric Generation & Transmission Cooperative, Inc. v. Rural Utility Serv., U.S. Dep't of Agric.*, 240 B.R. 476, 485 (Bankr.D.Vt.1999).
- [15] [16] [17] In determining whether these three conditions are satisfied, *Mobile Steel* instructs the Court to be mindful of three principles. First, inequitable conduct directed against the debtor or its creditors may be sufficient to warrant subordination of a claim irrespective of whether it was related to the acquisition or assertion of that claim. ¹⁵³ *Mobile Steel*, 563 F.2d at 700–01; *see also Citicorp Venture Capital Ltd. v. Comm. of Creditors Holding Unsecured Claims*, 323 F.3d 228, 234 (3d Cir.2003), *cert. denied*, 540 U.S. 825, 124 S.Ct. 178, 157 L.Ed.2d 46 (2003). ("*Papercraft*") ¹⁵⁴ ("The inequitable conduct may arise out of any unfair act by the creditor as long as the conduct affects the bankruptcy results of other creditors"). Second, a claim or claims should be subordinated to the extent (and only to the extent) necessary to offset the harm which the debtor and its creditors suffered on account of the inequitable conduct. *Id.* And third, an objection resting on equitable grounds must contain some substantial factual basis to support its allegation of impropriety. *Id.*
- This Decision reflects a disposition of the Complaints asserted by the Debtors and Harbinger in the Adversary Proceeding; SPSO's conduct in these cases which is unrelated to claim acquisition is the subject of objections asserted in connection with the Debtors' Third Amended Joint Plan of Reorganization.
- For ease of comprehension and unless otherwise noted, all references to *Papercraft* are to the Third Circuit's opinion, 323 F.3d 228 (3d Cir.2003), *cert. denied*, 540 U.S. 825, 124 S.Ct. 178, 157 L.Ed.2d 46 (2003).

1. Mobile Steel Prong I: Inequitable Conduct

[18] [19] [20] Prong I of the *Mobile Steel* tests requires a showing that the claimant engaged in some type of inequitable conduct. Inequitable conduct is not limited to fraud or breach of contract, rather, it includes even lawful conduct that shocks one's good conscience. As Judge Bernstein noted in *80 Nassau Assocs.*, inequitable conduct means, among other things,

a secret or open fraud, lack of faith or guardianship by a fiduciary; an unjust enrichment, not enrichment by bon chance, astuteness or business acumen, but enrichment through another's loss

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brought about by one's own unconscionable, *348 unjust, unfair, close or double dealing or foul conduct."

169 B.R. at 837 (quoting *In re Tampa Chain Co.*, 53 B.R. 772, 779 (Bankr.S.D.N.Y.1985)) (other citations omitted); *In re Lois/USA, Inc.*, 264 B.R. 69, 134 (Bankr.S.D.N.Y.2001) (Gerber, J.) ("*Lois/USA*"); *Adler*, 277 B.R. at 563–564. Traditionally, equitable subordination was inapplicable to ordinary creditors (as opposed to insiders), but it is now well-settled that the doctrine applies to general creditors or "non-insiders," though the circumstances warranting equitable subordination of a non-insider's claim arise less frequently because the opportunities for abuses triggering equitable subordination tend to be more readily available to insiders. *See Lois/USA*, 264 B.R. at 134 (citing *80 Nassau Assocs.*, 169 B.R. at 838) (other citations omitted).

[21] [22] In order to identify the precise type of conduct supporting equitable subordination of a non-insider's claim, some courts have applied a heightened standard of wrongdoing, the majority requiring conduct that is "gross and egregious." 80 Nassau Assocs., 169 B.R. at 838 (citing Waslow v. MNC Commercial Corp. (In re M. Paolella & Sons, Inc.), 161 B.R. 107, 119 (E.D.Pa.1993)); Bank of New Richmond v. Production Credit Ass'n (In re Osborne), 42 B.R. 988, 997 (W.D.Wisc.1984). However, courts in this District have held that there is no different or heightened standard by which to judge a non-insider's conduct, though there may be fewer traditional grounds available because neither undercapitalization nor breach of fiduciary duty applies to the conduct of a non-insider. See 80 Nassau Assocs., 169 B.R. at 839. Unless the non-insider has dominated or controlled the debtor to gain an unfair advantage, the type of inequitable conduct that justifies subordination of a non-insider's claim is "breach of an existing, legally recognized duty arising under contract, tort or other area of the law." Id. at 838; accord Lois/USA, 264 B.R. at 136; In re Monahan Ford Corp. of Flushing, 340 B.R. 1, 44 (Bankr.E.D.N.Y.2006).

In commercial cases, the proponent of equitable subordination must demonstrate, for example, "a substantial breach of contract and advantage-taking by the creditor." 80 Nassau Assocs., 169 B.R. at 838 (citations omitted); accord Lois/USA, 264 B.R. at 136. Where a proponent is able to establish inequitable conduct in connection with contractual obligations, courts have granted equitable subordination. See Developmental Specialists, Inc. v. Hamilton Bank, N.A. (In re Model Imperial, Inc.), 250 B.R. 776, 804–05 (Bankr.S.D.Fl.2000) (holding that creditor's creation of a scheme to circumvent contractual obligations, including negative covenants in the loan documents, which provided it with an unfair advantage warranted equitable subordination of its allowed claim).

[23] [24] [25] In the absence of a contractual breach, the proponent must demonstrate "fraud, misrepresentation, estoppel or similar conduct that justifies the intervention of equity." 80 Nassau Assocs., 169 B.R. at 838 (citations omitted); accord Lois/USA, 264 B.R. at 136. A violation of the implied covenant of good faith and fair dealing may provide grounds for equitable subordination. See Lois/USA, 264 B.R. at 136 & n. 167 (declining to make a substantive determination with respect to the extent to which a claim for violation of the implied covenant of good faith and fair dealing would support equitable subordination pending further development of the facts, but noting that, if proven, such conduct may justify equitable subordination); see also In re Enron, 333 B.R. at 220 (holding that section 510(c) of the Bankruptcy Code affords the court discretion when considering *349 subordination of claims based on common law concepts of the equitable doctrine, and stating that "the bankruptcy court has the [equitable] power to sift the circumstances surrounding any claim to see that injustice or unfairness is not done in administration of the bankrupt estate") (quoting Pepper v. Litton, 308 U.S. at 305, 60 S.Ct. 238) (grammatical changes in original). Accordingly, creditor misconduct in connection with the chapter 11 process itself—irrespective of applicable non-bankruptcy law—provides an appropriate predicate for equitable subordination of such creditor's claim.

2. Mobile Steel Prong II: Injury

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[26] Once inequitable conduct has been found, the Court must next determine whether the claimant's conduct caused injury to the debtor or its creditors, or resulted in an unfair advantage to the claimant. *Mobile Steel*, 563 F.2d at 700–01; *In re Vargas Enterprises, Inc.* 440 B.R. 224, 240 (S.D.N.Y.2010) (Sullivan, J.). For a creditor to have achieved an unfair advantage as required under the *Mobile Steel* test, there must have been a benefit to the creditor. In turn, for equitable subordination to be warranted, such a benefit, or unfair advantage, must have resulted in an injury to the debtor or its creditors. Without injury, there would be no reason to equitably subordinate the claim. *See 9281 Shore Road Owners Corp. v. Seminole Realty Co.*, 187 B.R. 837, 853–854 (E.D.N.Y.1995); *see also Nisselson v. Softbank AM Corp. (In re MarketXT Holdings Corp.)*, 361 B.R. 369, 388 (Bankr.S.D.N.Y.2007) (Gropper, J.) (denying non-insider creditor's motion to dismiss, finding that the complaint raised core equitable subordination issues that were sufficient to state a claim under the *Mobile Steel* test that the creditor "engaged in (x) some type of inequitable conduct that (y) resulted in injury to other creditors *and* an unfair advantage to itself" (emphasis added)).

[27] [28] [29] Equitable subordination requires that a party prove unfair advantage and injury to creditors because subordination is a remedial measure designed to offset the harm resulting from the inequitable conduct; it is not penal in nature. See Mobile Steel, 563 F.2d at 700 ("a claim or claims should be subordinated only to the extent necessary to offset the harm which the bankrupt and its creditors suffered on account of the inequitable conduct"). In calculating the extent to which a claim should be subordinated, the bankruptcy court should "attempt to identify the nature and extent of the harm it intends to compensate in a manner that will permit a judgment to be made regarding the proportionality of the remedy to the injury that has been suffered by those who will benefit from the subordination." In re Papercraft Corp. v. Citicorp Venture Capital, Ltd., Civil Action No. 00–2180, 2002 WL 34702177 at *3 (W.D.Pa. Feb. 20, 2002). While the harm and amount of injury should be based upon the supportive evidence of the record, id. the remedy of equitable subordination should remain flexible to deal with the inequitable conduct at issue. As the court noted in In re Teltronics Servs., Inc.:

The remedy of equitable subordination must remain sufficiently flexible to deal with manifest injustice resulting from the violation of the rules of fair play ... where ingenuity spawns unprecedented vagaries of unfairness, bankruptcy courts should not decline to recognize their marks, nor hesitate to turn the twilight for offending claimants into a new dawn for other creditors.

29 B.R. 139, 172 (Bankr.E.D.N.Y.1983).

[30] [31] [32] [33] Because equitable subordination is remedial rather than punitive in nature, the extent of equitable subordination *350 of a claim is not related to the amount paid for the claim by the offending claimant. The purpose of equitable subordination is to protect creditors against unfairness and to restore creditors to the position that they would have been in if the misconduct did not occur. ¹⁵⁵ As such, there is no justification for linking equitable subordination of a claim to the amount the creditor paid for the claim or the profit the creditor received or may receive from such purchase; if the injury sustained by the estate and other creditors is greater, the equitable subordination should be greater. Conversely, if the injury to creditors is less than the profit realized by the offending creditor, the extent of equitable subordination should be less. Simply put, and contrary to *Papercraft*, there is no nexus between the amount a creditor pays for its claim and the amount of injury sustained by other creditors of the estate as a result of the creditor's misconduct. Indeed, capping the recovery on a creditor's claim at the amount it paid for the claim is inconsistent with the notion that equitable subordination is remedial in nature. ¹⁵⁶ Rather, a court should engage in an evaluation of the harm that the estate's other creditors suffered as a result of the creditor's misconduct based upon the supportive evidence of the record.

As this Court made clear in its Decision on the Motions to Dismiss, section 510(c) of the Bankruptcy Code does not provide for the subordination of a claim to an equity interest. See e.g., Shearer v. Tepsic (In re Emergency Monitoring Techs., Inc.), 366 B.R. 476, 504 (Bankr.W.D.Pa.2007) (Section 510(c) only "authorizes the subordination of claims to other claims or interests to other interests but its language does not extend to treatment of interests vis-à -vis claims") (citations omitted) (emphasis in original); Town & Country Corp. v. Hare & Co. (In re Town & Country Corp.), 2000 WL 35915909 at *5–6, 2000 Bankr.LEXIS

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1755 at *16–17 (1st Cir. BAP 2000) (Section 510(c) is designed to "deal with equitable subordination of claims to other claims or interest to other interests.... The Panel will not import some other interpretation to § 510(c) when its language is clear and unambiguous on its face."); 80 Nassau Assocs. v. Crossland Fed. Sav. Bank (In re 80 Nassau Assocs.), 169 B.R. 832, 836–837 (Bankr.S.D.N.Y.1994) (Section 510(c) "empowers the Bankruptcy Court, under 'principles of equitable subordination,' to subordinate, for purposes of distribution, claims to other claims, and interests to other interests...."); 4 COLLIER ON BANKRUPTCY ¶ 510.05 at 510–17 (16th ed. 2013) ("Under subsection (c)(1), claims may be subordinated to claims, and interests may be subordinated to interests, but claims may not be subordinated to interests."). This is so because equitable subordination of debt to equity would constitute a penalty, not a remedy, as there is nothing equitable about allowing a debtor to evade a valid obligation enforceable under applicable law.

Linking equitable subordination (or other bankruptcy rights and remedies) to the amount paid for a claim in the secondary market opens a Pandora's Box of sizable proportions.

To that end, *Papercraft* identifies three categories of economic harm that provide a useful template for determining the extent of equitable subordination: (1) quantifiable monetary harm that results from delay; (2) harm that results from uncertainty; and (3) harm that results from delay that can be measured by professional fees and administrative expenses incurred by the estate as a result of the litigation. *Papercraft*, 323 F.3d at 232.

The facts of *Papercraft* (a ten-year litigation saga that resulted in a suite of eight decisions) are instructive. Citicorp Venture Capital ("CVC"), an insider and fiduciary of the debtor, Papercraft, attempted to take control of Papercraft's assets and obtain a significant profit at the expense of other creditors by secretly purchasing claims against Papercraft for a deeply discounted amount and then objecting to the confirmation of a plan of reorganization *351 proposed by the debtor, in favor of a competing plan favoring CVC. *Id.* at 231–232 (citing *In re Papercraft Corp. v. Citicorp Venture Capital, Ltd.,* 165 B.R. 980 (Bankr.W.D.Pa.1994)). Papercraft's unsecured creditors' committee filed a motion for summary judgment seeking to limit the allowance of claims held by CVC. *Id.* The bankruptcy court issued a Memorandum Opinion and Order, finding that the purchases at issue were all found to have occurred during the seven month period between the time that debtor filed its plan of reorganization and the time it filed its disclosure statement, and therefore, CVC's purchases at a discount, without disclosure, while an insider, constituted breaches of CVC's fiduciary duty to Papercraft. *Id.* at 231 (citing *In re Papercraft Corp. v. Citicorp Venture Capital, Ltd.,* 187 B.R. 486, at 498–99 (Bankr.W.D.Pa.1995)). Accordingly, the bankruptcy court limited CVC's allowed claim and distribution in the plan of reorganization to the purchase price of the claim. *Id.*

After a subsequent trial on the issue of equitable subordination of CVC's claim, the court withdrew and vacated its prior decision, finding that CVC breached its fiduciary duty to debtor as an insider for failing to disclose its identity in purchasing the claims and, as an equitable subordination remedy, limiting CVC's claim to the purchase price of the claim. *Id.* at 231; *In re Papercraft Corp. v. Citicorp Venture Capital, Ltd.*, 187 B.R. 486. But the bankruptcy court declined to equitably subordinate CVC's claim, holding that further subordination of CVC's thus-limited claim pursuant to the principles of equitable subordination was not appropriate because the bankruptcy court was already limiting CVC's allowed claim to the amount it paid for such claim. *Papercraft*, 323 F.3d at 231 (citing *In re Papercraft Corp. v. Citicorp Venture Capital, Ltd.*, 187 B.R. at 501–502).

The parties then cross-appealed, and, on appeal, the district court affirmed the bankruptcy court's factual findings that CVC acted inequitably and caused injury to Papercraft and its creditors and agreed with the bankruptcy court's finding that CVC's claim should be limited to the amount it paid for such claim so as to eliminate any potential profit. *Papercraft*, 323 F.3d at 232 (citing *In re Papercraft Corp. v. Comm. of Creditors Holding Unsecured Claims*, 211 B.R. 813, 827 (W.D.Pa.1997)). The district court reversed the bankruptcy court on the issue of further subordination and held that any subordination beyond the limitation of CVC's recovery to the amount paid for such claims should be supported by factual findings and reconciled with principles of equity. Accordingly, the district court remanded the case to the bankruptcy court for a further finding on the extent to which CVC's limited allowed claim should be equitably subordinated. *Papercraft*, 323 F.3d at 232 (citing *In re Papercraft Corp. v. Comm. of Creditors Holding Unsecured Claims*, 211 B.R. at 827).

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On remand, the bankruptcy court found that CVC's recovery would be further subordinated for (i) additional administrative expenses incurred during the delay caused by CVC, (ii) interest and dividends lost by creditors during the delay, and (iii) professional fees and expenses incurred and/or paid by the estate. *Papercraft*, 323 F.3d at 232 (citing *In re Papercraft Corp. v. Citicorp Venture Capital, Ltd.*, 247 B.R. 625, 628 (Bankr.W.D.Pa.2002)).

Additional appeals ensued, and the district court affirmed the bankruptcy court's decision, but the court reduced the lost interest component of the subordinated claim. *352 In re Papercraft Corp. v. Citicorp Venture Capital, Ltd., Civil Action No. 00–2180, 2002 WL 34702177 (W.D.Pa. Feb. 20, 2002). Ultimately, the Third Circuit upheld the additional subordination of CVC's claim for attorneys' fees, reasoning that the bankruptcy court did not award a monetary judgment for attorneys' fees to penalize CVC, but rather, to return other creditors to the position they would have been in had CVC not acted inequitably, and affirmed the district court's reduction of the lost interest component of CVC's subordinated claim. Papercraft, 323 F.3d at 234.

In determining the amount of harm, the bankruptcy court in *Papercraft* explained that it need not arrive at a figure with "precise accuracy" and that any difficulty in precisely quantifying the harm should not redound to the benefit of the wrongdoer. *In re Papercraft Corp. v. Citicorp Venture Capital, Ltd.*, Civil Action No. 00–2180, 2002 WL 34702177 at *9–10 (citing *In re Papercraft Corp.*, 247 B.R. at 630).

3. Mobile Steel Prong III: Consistency with the Bankruptcy Code

[34] The third prong of the *Mobile Steel* test acknowledges that equitable subordination cannot be used to alter the statutory scheme imposed by bankruptcy law. Accordingly, while a bankruptcy court can apply the equitable doctrine at its discretion, its power to subordinate an allowed claim is not boundless and courts cannot use equitable principles to disregard unambiguous statutory language of the Bankruptcy Code. *In re Enron*, 333 B.R. at 218–19 (citing *United States v. Noland*, 517 U.S. 535, 543, 116 S.Ct. 1524, 134 L.Ed.2d 748 (1996) (citations omitted)); *Law v. Siegel*, — U.S. —, 134 S.Ct. 1188, 1195, 188 L.Ed.2d 146 (2014).

The application of the third prong of the *Mobile Steel* test ensures that the "full breadth of the remedy of equitable subordination is available while ensuring that its reach does not violate any provision of the Bankruptcy Code or become punitive as opposed to remedial." *In re Enron*, 333 B.R. at 219. The requirement that subordination be consistent with bankruptcy law comes into play only after the Court has concluded that the first two prongs have been satisfied. *80 Nassau Assocs.*, 169 B.R. at 841. By virtue of the codification of the doctrine in section 510(c) of the Code, the third prong of the *Mobile Steel* doctrine warrants little attention.

B. Mobile Steel Prong I: SPSO's Inequitable Conduct

1. Breach of the Implied Covenant of Good Faith and Fair Dealing

[35] As the Court has found, Mr. Ergen's acquisition of LP Debt through SPSO violated the spirit and purpose of the Credit Agreement restrictions designed to prevent competitors from purchasing LP Debt and breached the Credit Agreement's implied covenant of good faith and fair dealing. This Court has held that a violation of the implied covenant of good faith and fair dealing may provide grounds for equitable subordination. See Lois/USA, 264 B.R. at 136, n.167 (declining to make a substantive determination with respect to the extent to which a claim for violation of the implied covenant of good faith and fair dealing would support equitable subordination pending further development of the facts, but noting that if proven, such conduct may justify equitable subordination). Although many aspects of SPSO's conduct are, as has been suggested, "perfectly lawful" 157—including making *353 purchases anonymously, acquiring

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a blocking position, and making an unsolicited cash bid for distressed assets—its purchase of LP Debt in order to preserve a strategic option for the benefit of DISH, a Disqualified Company, violated the spirit of the Credit Agreement's restrictions on competitors owning LP Debt. Such conduct, as described more fully above, constitutes inequitable conduct sufficient to warrant equitable subordination of the SPSO Claim.

See Post-Trial Brief of Defendants SP Special Opportunities, LLC and Charles W. Ergen [Adv. Docket No. 142], pp. 7–8.

2. SPSO, Through the Conduct of Messrs. Kiser and Ketchum, Purposefully Delayed the Closing of LP Debt Trades

In addition to SPSO's inequitable conduct in acquiring the LP Debt, SPSO also engaged in inequitable conduct by effectively sidelining hundreds of millions of dollars of LP Debt during the weeks and months leading to the Court-sanctioned termination of exclusivity on July 15, 2013, all while SPSO, Mr. Ergen, and, eventually LBAC/DISH, fine-tuned their bid strategy. SPSO, through Mr. Ergen, did so by purposefully delaying the closing of LP Debt trades in the face of repeated demands to close and despite the ready availability of the funds necessary to close. Even if SPSO's acquisition of LP Debt was faultless, its intentional delay in closing its trades of LP Debt alone is sufficient to constitute the type of inequitable conduct necessary for the imposition of equitable subordination by the Court. The evidence of purposeful delay could not be more clear.

SPSO was formed by Mr. Ergen with an initial capital contribution of only ten dollars, and its operating agreement did not require additional capital contributions from Mr. Ergen as Managing Member. ¹⁵⁸ Even though Sound Point knew that SPSO was funded with an insufficient amount of initial capital to buy a significant amount of LP Debt, Sound Point nevertheless traded for SPSO because Mr. Ketchum understood that SPSO was backstopped by Mr. Ergen. ¹⁵⁹ The evidence establishes that, after Sound Point executed a trade for SPSO, the trade would be funded only very shortly before or on the closing date. At that time, Mr. Kiser would contact Mr. Ergen's asset manager, Bear Creek, and tell Bear Creek how much money was needed to close the trade, after which Mr. Ergen would then authorize the wire transfer and Bear Creek would liquidate investments to fund the transfer. ¹⁶⁰ Liquidity was not created by Mr. Kiser immediately upon placing a trade; rather, as admitted by Mr. Kiser at Trial, only after delaying for as long as possible on closing a trade were the funds for the purchase wired for closing. ¹⁶¹

- 158 PX0221 at LSQ-SPCD-000005553, 5561("[t]he Managing Member is entitled, but not required, to make additional contributions to the capital of the Company").
- Jan. 15 Tr. (Ketchum) 18:8–21, 20:4–13; PX0023; PX0024; PX0046; PX0048; PX0052; PX0056; PX0058; PX0059; PX0074.
- Mr. Ergen was the only person who could authorize the transfer of funds from his account at Bear Creek to Bal Harbour or SPSO for settlement of the LightSquared trades. Jan. 10 Tr. (Kiser) 21:23–22:13, 58:7–12.
- Jan. 10 Tr. (Kiser) (Q: Well, in fact, you didn't want to pay unless-you didn't want to pay until you absolutely had to, right? A: That's right. We were in no rush to close. Q: You wanted to wait until the last possible minute? A: Well, as I said before, there was no economic benefit.)

Of the 25 trades entered into by SPSO for purchases of LP Debt, eighteen of them took over two months to settle, and, of those eighteen trades, six took over four *354 months to settle. ¹⁶² By May 20, 2013, SPSO had contracted for, but had failed to settle, approximately \$593,757,000 in face amount of LP Debt trades (and approximately \$610,000,000 counting trades held by brokers on that date)—more than 33 percent of the total outstanding LP Debt obligations—and had kept open a number of trades that it had entered into as far back as December 12, 2012. ¹⁶³

162 PX0859.

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163 PX0859.

Mr. Kiser explained the delays as stemming from the fact that he and Mr. Ergen were not in any rush to close the trades of LP Debt; in their view, the trades "didn't need to be closed until you absolutely had to," as "there wasn't an economic benefit to doing it." 164 As Mr. Kiser testified, Mr. Ergen "was getting a return on his capital and his investments. So if he didn't have to pay for it and he can make money on another end where his money was invested, that seemed like a smart move." 165 The documentary evidence on this point is to the contrary, as account statements produced by Bear Creek indicate that Mr. Ergen earned a relatively low rate of interest on the funds in his trust accounts. 166 In addition, there were economic penalties imposed on SPSO for leaving LP Debt trades open for an extended period of time, including having to forgo adequate protection payments; 167 this fact further undermines the "economic" explanation advanced by Mr. Kiser to explain the delay. Moreover, no evidence was introduced that either Mr. Ergen or Mr. Kiser took the possibility of a penalty to SPSO into account in determining (i) when to close unsettled trades or (ii) which of Mr. Ergen's assets to liquidate to pay for SPSO's LP Debt trades, despite the fact that Messrs. Ergen and Kiser had been made aware of how the adequate protection payments worked. 168 Bear Creek, which independently selected which of Mr. Ergen's assets would be liquidated to fund the trades, was not even made aware that SPSO possibly would have to pay cost of carry fees and forego adequate protection payments if the LP Debt trades were not closed by a certain date. ¹⁶⁹ In fact, there is no evidence that any analysis at all was done by Mr. Ergen, Mr. Kiser, or Bear Creek to determine the return on any of the assets in Mr. Ergen's personal trust to determine which assets to liquidate for closing. The "economic benefit" justification *355 for delaying the closing of trades simply does not pass muster.

- Jan. 10 Tr. (Kiser) 64:17–25 (stating that Mr. Ergen had his capital invested elsewhere and was making a return on money that would have been liquidated).
- Jan. 10 Tr. (Kiser) 98:3–6.
- 166 PX0796-818.
- If SPSO failed to close certain LP Debt trades within the closing date specified in the purchase agreement, it was charged a penalty "cost of carry fee" and in some instances had to forgo receiving a share of Adequate Protection Payments for the unsettled trade. (SeeAgreed Final Order (A) Authorizing Debtors to Use Cash Collateral, (B) Granting Adequate Protection to Prepetition Secured Parties, and (C) Modifying Automatic Stay [Bankr. Docket No. 136] at 18 (granting adequate protection for Lenders); Jan. 15, 2014 (Ketchum) 81:1–82:3; PX0493; DX104 at LSQ–SPCD–000000176 (imposing "AP Payment" and "cost of carry" fees from T+20 to settlement date); DX109 at LSQ–SPCD–000000285; PX0851 at SPSO–00000072; PX0650 at LSQ–SPCD000000073.)
- PX0258; PX0256; PX0259 (emails discussing adequate protection payments).
- Roddy Dep. 86:5–87:3. Bear Creek selected assets for liquidation based on "which ones are the easiest to liquidate closest to the market value," and generally selected assets with low interest rates, consistent with the overall conservative nature of the Trust. (Roddy Dep. 57:9–58:3, 58:20–22, 59:6–12, 69:7–11; Jan. 13 Tr. (Ergen) 168:4–14.)

Liquidity concerns were another purported reason for the delayed closing of the LP Debt trades, according to Mr. Kiser. ¹⁷⁰ At Trial, Mr. Kiser initially denied that liquidity reasons caused any delays, until he was reminded that he had testified otherwise at his deposition and then recalled giving that as an explanation. ¹⁷¹ Asked if there was ever a time when Mr. Ergen lacked the liquidity to promptly close a trade, Mr. Kiser testified at Trial that, where Mr. Ergen may not have had "immediate funds available, [yes], that occurred." ¹⁷² Mr. Kiser equivocated, however, when pressed as to whether he could identify any investments that Mr. Ergen would have needed to exit which would take longer than three days, saying that "it depended.... [Mr. Ergen] had things that were all over the gamut of types of investments.... [some] were a lot less liquid." ¹⁷³ Mr. Kiser's testimony on the liquidity issue lacks credibility; and even Mr. Ergen admitted that, as far as he knew, there was not a delay in closing because of any liquidity issues, stating that "I don't believe, other

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than several days, or perhaps a Friday where it didn't make economic sense to wire money, that there was [sic] any delays because of that reason." ¹⁷⁴ Bear Creek also confirmed that, after Mr. Ergen authorized a wire transfer from his personal trust, Bear Creek could make it available for transfer within several days. ¹⁷⁵ Mr. Ergen's account statements reflect that funds were liquidated on a rolling basis from the investments held by his personal trust, with hundreds of millions of dollars in cash sometimes sitting in Mr. Ergen's trust account for several weeks before it was used to fund a trade. ¹⁷⁶ The evidence further shows that, in at least one case, liquid funds were readily available, but Mr. Kiser instructed Bear Creek to hold off on wiring funds. ¹⁷⁷ The alleged liquidity issue was clearly manufactured by Mr. Kiser; and the lies to counterparties regarding liquidity were passed along by Mr. Ketchum, who was often informed by Mr. Kiser that funds were "not available" to close a trade ¹⁷⁸ and asked no further questions.

- Mr. Ketchum testified that it was his "understanding from [Mr]. Kiser that things had to be sold, cash had to be raised to settle those trades." Jan. 15 Tr. (Ketchum) 84:13–14. When asked about the lengthy delays between the trade and settlement dates and whether all of these delays were because the money was not coming from the Ergen family office, Mr. Ketchum responded, "Correct." *Id*.:1–3.
- 171 Jan. 10 Tr. (Kiser) 128:24–129:13; 129:23–130:1.
- Jan. 10 Tr. (Kiser) 129:23–130:6.
- 173 *Id*.:7–131:23.
- 174 Jan. 13 Tr. (Ergen) 159:13–19.
- Roddy Dep. 66:12–67:14. Around that time, Bear Creek managed between \$626 million and likely \$750 million dollars for Mr. Ergen. (Roddy Dep. 71:11–18.)
- The account statements produced by Bear Creek reflect that, as of April 30, 2013, some \$461 million held in the Trust account had been liquidated, and, as of May 31, 2013, approximately \$207 million in liquid funds still remained in the Trust account. (PX0810: PX0812.)
- See PX0530 (Mr. Kiser instructing Bear Creek on May 20, 2013 to "[w]ait for the green light from me prior [to] sending. Obviously it's not going today so just check with me each morning."). By that time, at least \$207 million in assets which had been liquidated by Bear Creek in order to fund trades remained in the Trust account. (PX0812.)
- Jan. 15 Tr. (Ketchum) 74:12–20 (testifying as to his understanding that trades that had been delayed for over a month or more could not be closed by Sound Point because the funds had not been sent by Mr. Ergen's family office, and Mr. Ketchum had been told that such trades could not close because the funds were "not available.").
- *356 Mr. Kiser and Mr. Ergen also blamed the delays in closing the SPSO LP Debt trades on the need to complete "upstream" paperwork and on "false starts" from both the seller and the SPSO sides of the trades. Neither of these was a credible explanation for what the documentary evidence clearly reveals was a concerted effort to delay on the part of Messrs. Kiser and Ergen. Mr. Ergen testified that the variation in the dates between trading and closing an LP Debt trade had to do with the upstream paperwork that had to be done to verify who the actual owners were, which "was not that easy" and "could take anywhere from weeks to months." ¹⁷⁹ Because of this time to "verify" and the need to have both documents and funding ready to close a trade, Mr. Kiser testified that there were a lot of "false starts" that "went both ways." ¹⁸⁰ None of this testimony was credible.
- 179 Jan. 13 Tr. (Ergen) 62:17–63:6.
- Jan. 10 Tr. (Kiser) 63:13–25.

The volume of emails admitted into evidence reveals that counterparties to the trades that had been held open for months were, in fact, ready and eager to close, and they became more frustrated as time went on. Parties repeatedly reached out to

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Sound Point to settle trades, but often they could get little traction. (See, e.g., PX0319 (Sound Point e-mail on January 14, 2013, replying "[s]orry but we are not able to settle that one right now" in response to weekly inquiries from UBS seeking to close a trade); PX0364 (March 7, 2013 Sound Point email stating it would be able to settle "next week" in response to repeated inquiries since February 2013 regarding a December 2012 trade).) In particular, Jefferies, the executing broker for the majority of the LP Debt trades, was pushed aside for months by Sound Point, which provided excuse after excuse for the failure to close numerous open trades. In February 2013, Jefferies sent ongoing email and telephone requests to Sound Point to close multiple trades, with trade dates dating back as early as October 23, 2012. 181 At that time, an employee of Mr. Ketchum's reminded him that "[wle have been pushing Jefferies off for nearly 3 weeks." 182 On April 23, 2013, Mr. Ketchum wrote to Mr. Kiser that "Kevin [of Sound Point] thinks we can hold [Jefferies] off on any payments until at least May 15" in connection with over \$289 million in LP Debt trades that had not settled. 183 After Jefferies followed up with Sound Point on April 25, 2013, seeking to close \$88 million of open trades, ¹⁸⁴ Mr. Ketchum inquired internally whether he could plausibly blame SPSO's delay on the "upstreams," but he was told by Sound Point personnel that the work had already been completed. 185 Mr. Ketchum then emailed back and forth with a colleague about which lie to use—whether he should tell the counterparty "that we are still doing legal work on the upstreams," that "we are waiting for funding from our investor," or that "we are in the process of exiting some other large positions we have to pay for this." It was ultimately determined that the colleague should use the latter excuse, together with the statement that Mr. Ketchum "[has] spoken with Steve Sander *357 (head of sales) [at Jefferies] about this." 186 The need to delay Jefferies was based on Mr. Ketchum's understanding from Mr. Kiser that SPSO did not have capital available to fund the trade and, thus, Jefferies needed to be "put off" for a period of time. 187

- 181 PX0347; PX0859.
- 182 PX0347.
- 183 PX0458; PX0441; PX0859.
- 184 PX0466.
- PX0466; Jan. 15 Tr. (Ketchum) 76:9–77:8.
- PX0466; see also Jan. 15 Tr. (Ketchum) 76:20–78:7; PX0308 (Jefferies repeatedly inquiring whether funds are available); PX0341 (Sound Point writing to Jefferies that they are "still waiting on the funds"); Jan. 10 Tr. (Kiser) 63:15–20.
- 187 *Id* ·18–79·15

As of May 9, 2013, SPSO had seven open trades with Jefferies, totaling approximately \$588 million in LP Debt trades dating back as far as January 2013. Jefferies was imploring Sound Point to close the trades. ¹⁸⁸ Mr. Sander of Jefferies appealed to Mr. Ketchum: "this is a big problem for me. I would like to come down and talk to you this afternoon around 4 or 5pm mano a mano[.] Is this possible?" Mr. Ketchum replied that he was waiting for other "trades to settle" (a lie) and that he had "already pushed extremely hard to get to where we are now in terms of closing." ¹⁸⁹ None of the open trades closed for another several weeks. ¹⁹⁰

- 188 PX0498.
- 189 PX0498.
- 190 PX0859.

As he knew Mr. Ergen did not like to hold up funds which could be invested elsewhere, ¹⁹¹ Mr. Kiser testified that he instructed Mr. Ketchum to prepare a schedule for him showing unsettled trades and expected settlement dates so that he could have the money available on those dates, in order to avoid the "back-and-forth" with counterparties who may

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not have been ready to close when the funds were made available. 192 This testimony was not credible. Mr. Ketchum also testified that proposed settlement dates for the unsettled trades were requested by Jefferies, and he tried to act as an intermediary between SPSO and Jefferies "an anxious counterparty who was trying to get trades settled." 193 Mr. Ketchum stated that the "proposed settlement dates" in the schedule he emailed to Mr. Kiser on May 8, 2013, which were up to four months or more after the trade date, were suggested by Mr. Ketchum as a "compromise solution" in order to get the open Jefferies trades settled, and he proposed the schedule to Mr. Kiser before conveying such dates to Jefferies in order to see if a schedule of this kind was capable of execution by SPSO. 194 While it is not clear whether such proposed dates were actually sent to Jefferies, Mr. Ketchum's testimony on this point was not credible. The proposed settlement dates contained in the *358 schedule emailed from Mr. Ketchum to Mr. Kiser on May 8, 2013 reflect not a prediction for liquidity planning purposes of when trades would be ready to close, but rather a gameplan for delaying the closing of the open trades for as long as possible. In fact, in addition to this schedule, Sound Point had also prepared an analysis of the average days it took to settle an LP Debt trade with Jefferies after the trade date (69 days) and the average days after the industry-norm "contractual settlement date" of "T+20," or twenty days after the trade date (38 days). 195 There is no reason for Sound Point to have performed such an analysis other than to provide support for its proposed further delays. In fact, with the exception of the Icahn trade, all of SPSO's trades failed to close before a T +20 contractual settlement date. ¹⁹⁶

- See, e.g., PX041 (March 26, 2012 email from Ketchum to Kiser in which Ketchum suggests setting up a prime brokerage account at BNP to fund the trades and wiring \$500,000 to open the account, to which Kiser replies "[i]t'll be a lot easier if we don't have to fund \$\$ until we have a trade to settle ... [Ergen] won't be a big fan of just putting \$\$ out for opening an account.")
- Jan. 10 Tr. (Kiser) 63:25–64:14 ("And it got to a point where I told Steve, hey, look, get me a list and tell me when these things will trade so that we can have the money available for them rather than doing this back-and-forth type of thing"); PX0495.
- 193 Jan. 15 Tr. (Ketchum) 123:14–124:17.
- 194 Id. see also id.:8-15 ("my job was to find a date, propose a date to SPSO that I thought was reasonable in the context of closing distressed trades, obtain permission from SPSO, and in particular, Jason, to go back and offer those dates to Jefferies so that they could be mollified and feel that there was some sort of definition around when the trades would be closed.")
- 195 PX0493.
- On March 17, 2014, during closing arguments in the Adversary Proceeding, counsel for SPSO and Mr. Ergen argued, for the first time, that the delay in closing SPSO's LP Debt trades during the period between March and June 2013 was caused by a "moratorium" imposed by Jefferies as the trade intermediary. Counsel represented that this "moratorium" was reflected in a document in the existing record. After the hearing, counsel filed a letter to the Court which attached emails reflecting the purported "moratorium," none of which had been previously produced or were otherwise in the record. On March 21, 2014, counsel for the Plaintiffs filed a supplement to their previously-filed motion for sanctions, seeking additional sanctions in connection with, among other "discovery misconduct," SPSO's failure to have produced the "moratorium" document. [Adv. Docket No. 148]. The sanctions motions remain sub judice.

Astonishingly, Mr. Ketchum testified on direct examination that, even when the counterparty to a trade was ready and eager to settle a trade, Mr. Kiser had instructed him to delay the closing. See Jan. 15 Tr. (Ketchum) 69:3–6 (Q: "Did you ever have a discussion with Mr. Kiser in which you and Mr. Kiser agreed that you should delay the closing of the trade?" A: "Yes."); see also PX0204 (Sound Point employee emailing Mr. Ketchum on June 4, 2012 regarding a LightSquared trade entered into on May 3, 2012 and stating, "Jefferies is looking to settle the other two trades. Do you want to? Or delay?"). Mr. Kiser admitted that even when directly informed that counterparties were ready to close, he sought to defer settlement as long as possible. ¹⁹⁷ This goal was evident in much of the documentary evidence submitted. (See, e.g., PX0495 (Mr. Ketchum to Mr. Kiser "We need to close our March 25 trade before month end, for example May 25 or so, to stave off Jefferies"); PX0466).

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197 Jan. 10 Tr. (Kiser) 64:5–25, 97:23–98:6.

The time period in which the foregoing delays occurred was a crucial time in the Debtors' chapter 11 cases. The Exclusivity Stipulation, approved by this Court in February 2013, extended the Debtors' exclusive periods to file a plan of reorganization to July 15, 2013. If the parties did not reach a deal for a consensual plan by June 3, 2013, preparatory work for a sale process for all or substantially all of the Debtors' assets was required to begin, with the formal sale process commencing on July 15, 2013. 198 In the spring of 2013, LightSquared and its stakeholders—in particular, significant holders of LP Debt—were involved in negotiations with respect to terms for a consensual plan of reorganization. ¹⁹⁹ Beginning in late May *359 2013 and continuing thereafter, Moelis also contacted over 90 parties to discuss a joint venture or strategic partnership. 200 On June 7, 2013, the Debtors received Court approval to enter into and perform under an engagement letter with Jefferies in connection with securing potential exit financing for the Debtors, ²⁰¹ after which a "road show" kicked off to seek to raise capital. During this period, SPSO continued to amass large quantities of LP Debt and intentionally delayed the closing of large blocks of trades, all without formally revealing its identity. As a result, all of these parallel movements forward by the parties were stymied. LightSquared has alleged that it was not sure which lenders to negotiate with and whether the Ad Hoc Secured Group would be able to carry a class such that it could enter into a binding commitment with respect to a plan, such that any hope of achieving a consensual plan during this period was derailed. Without spending the cash necessary to close hundreds of millions of dollars of open trades and by intentionally leaving them in limbo for three to four months or longer, Mr. Ergen arrogated to himself the power to control the forward motion or lack thereof of the bankruptcy cases beginning in April 2013.

- 198 PX0852 at Ex. A.
- On April 4, 2013, the Ad Hoc Secured Group submitted a proposed plan term sheet to LightSquared and indicated their willingness to commence discussions with respect thereto. (PX0410.) The term sheet contemplated a plan in which all creditor and preferred equity classes would receive a full recovery and LightSquared would emerge from bankruptcy with its spectrum assets intact. (Id. at HARBAP00015399–400; see also Jan. 17 Tr. (Hootnick) 21:24–22:24.) Also, on May 15, 2013—the same day that LBAC submitted its bid for LightSquared's assets—the parties exchanged a revised term sheet for a consensual plan of negotiation. (PX0505; DX335; DX174.) The revised term sheet provided for an infusion of new capital to be obtained by Harbinger and/or LightSquared, and reorganization, such that a sale of LightSquared's assets would be avoided. (PX0505 at HARBAP00005107–13.) A term sheet exchanged with the Ad Hoc Secured Group on May 24, 2013 envisioned that SPSO would receive full cash recovery while non-SPSO lenders would receive cash recovery and warrants. (PX0561.)
- 200 Jan. 17 Tr. (Hootnick) 28:6–16.
- Bankr. Docket No. 667.

Indeed, the Exclusivity Stipulation provided that it could be terminated if the Ad Hoc Secured Group, collectively, ceased to be the largest holder of LP Debt. On June 13, 2013, SPSO "joined" the Ad Hoc Secured Group, specifically to ensure that the termination conditions contained in Paragraph 15 of the stipulation would not be triggered. ²⁰² Within days of nominally joining the Ad Hoc Secured Group, several hundreds of millions of dollars in "hung" trades just happened to close, making SPSO the controlling member of the group by virtue of the size of its holdings. ²⁰³ SPSO's decision to join the Ad Hoc Secured Group was undoubtedly made for the strategic purpose of controlling the sale process for the Debtors' assets, with DISH as the buyer, and the fact that it rendered the negotiated and Court-ordered exclusive period meaningless was ignored. Mr. Ergen understood that the Exclusivity Stipulation would terminate in *360 July, ²⁰⁴ and enabling the stipulation to remain in place until then furthered his interest of keeping the status quo until the DISH Board had authorized DISH to step into the shoes of LBAC and pursue the LBAC Bid. While a creditor who is not an insider is not a fiduciary, a creditor nevertheless does not have the unfettered right to engage in such purposeful obstruction of the process. SPSO failed to act in a way that is consistent with the most basic concepts of good faith that are fairly to be expected of chapter 11 creditors, especially those who voluntarily join the capital structure of a debtor well after distress has set in.

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- PX0858 (Stipulation by SP Special Opportunities, LLC in Aid of Discovery in Connection with Emergency Motion of the Ad Hoc Secured Group of LightSquared LP Lenders to Enforce This Court's Order Pursuant to 11 U.S.C. § 1121(d) Further Extending LightSquared's Exclusive Periods to File a Plan of Reorganization and to Solicit Acceptances Thereof, dated July 3, 2013) at ¶ 13. SPSO's counsel also stated in closing arguments of the Trial that SPSO joined the Ad Hoc Secured Group solely for the purpose of maintaining the "lender protections" of the Exclusivity Stipulation. (Mar. 17 Tr. (Strickland) 189:12–191:4 ("[SPSO] was very much focused on those lender protections, and that's why it joined the group."))
- 203 PX0649 at L2AP0008732; PX0625; PX0859.
- Jan. 13 Tr. (Ergen) 66:9–15 ("... and then there also was the fact that the bankruptcy was coming up in July. And if I was interested, I would have to ...—either you're going to make a bid there or somebody else was going to. And while I didn't know in that time frame that I would make a bid, I knew that it would take time to prepare."). The Court understands Mr. Ergen's mention of the "bankruptcy coming up in July" to refer to the stipulated date for termination of the Debtors' exclusive periods to file a plan, which was approaching on July 15, 2013.

As SPSO vehemently maintains, many aspects of SPSO's conduct are entirely acceptable (albeit aggressive) and do not provide grounds for equitable subordination. Such lawful and acceptable conduct includes: buying distressed debt; buying distressed debt anonymously; buying distressed debt anonymously at prices close to par; acquiring a blocking position in a class of debt; and making an unsolicited bid for assets of a debtor. Nothing in the Court's decision should in any way alter such conduct in the distressed debt marketplace. The Bankruptcy Code and the chapter 11 process tolerate and even contemplate self-interested and aggressive creditor behavior. Nevertheless, SPSO's conduct in acquiring the LP Debt and in controlling the conduct of the chapter 11 case through purposeful delays in closing hundreds of millions of dollars of LP Debt trades during a critical timeframe in these cases breaches the outer limits of what can be tolerated.

While it is generally acceptable to obtain and deploy a blocking position to control the vote of a class with respect to a proposed plan of reorganization, it is not acceptable to deploy a blocking position to control the conduct of the case itself, to subvert the intended operation of a court-approved exclusivity termination arrangement, and to prevent the Court from directing and having visibility into events unfolding in the case. In response to the allegations that they purposefully sidelined hundreds of millions of dollars in debt and prevented the chapter 11 cases from moving forward, SPSO and Mr. Ergen say "no harm, no foul," citing to the fact that there is no evidence that SPSO's conduct had any impact on plan negotiations in the spring and summer of 2013. But that is not true. Had there been clarity with respect to the ownership of LP Debt during that time period, the parties may have made substantial progress on a plan, and it is possible that the Debtors' exclusive periods could have been extended, which would have been a "game changer" in the course of the Debtors' cases.

C. Mobile Steel Prong II: SPSO's Conduct Harmed LightSquared's Creditors

Having acquired a controlling position in the LP Debt by the use of a special purpose vehicle whose special purpose was to achieve an end-run around the Credit Agreement, and then purposefully sidelining hundreds of millions of dollars of LP Debt while fine-tuning its acquisition strategy, SPSO has harmed the creditors of *361 LightSquared. Having seized control of the class of LP Debt, SPSO then seized control of the case itself, rendering meaningless the heavily negotiated and Court-ordered process leading to the termination of exclusivity on July 15, 2013. SPSO's inequitable conduct has inflicted as yet unquantified harm on LightSquared's creditors as a result of the delay, uncertainty, and increased administrative costs suffered by these estates. While various numbers and calculations of harm have been suggested by Plaintiffs and by the Ad Hoc Secured Group, quantification of the amount of harm is beyond the agreed-upon scope of this first phase of the Adversary Proceeding and will be determined after further proceedings before this Court. ²⁰⁵

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The third prong of the test for equitable subordination set forth in *Mobile Steel* test states that equitable subordination cannot be used to alter the statutory scheme imposed by bankruptcy law. As equitable subordination has since been codified in section 510(c) of the Bankruptcy Code, the Court need not address the third prong of the *Mobile Steel* separately in this Decision.

CONCLUSION

SPSO has gone to great lengths to identify the many things it did that are "perfectly lawful" and just plain "smart" and warns, ominously, that any finding of liability would roil the debt markets. But its otherwise lawful pursuit of aggressive and profitable distressed debt transactions does not entitle it to do what it did to the LightSquared estates and cases. As Mr. Ergen so colorfully explained during Trial, "[y]ou can live in a bubble if you want to ... and probably never get any disease. But you go play in the mud and the dirt and you probably aren't going to get disease either because you get immune to it. So you pick your poison and I think we choose to go play in the mud." ²⁰⁶ Here, playing in the mud involved end-running the LightSquared Credit Agreement and then purposefully holding in limbo hundreds of millions of dollars of debt trades and undermining the ability of the Debtors, the constituents, and even the Court to conduct the case. Determining the amount of harm that has occurred to these estates as a result of SPSO's conduct, while difficult, will not be impossible and the SPSO Claim will be subordinated accordingly.

206 Jan. 13 Tr. (Ergen) 199:23–200:4 (video played at Trial).

For all of the foregoing reasons, the Court finds that the SPSO Claim shall be equitably subordinated in an amount to be determined after further proceedings before this Court.

IT IS SO ORDERED.

All Citations

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