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Current Developments in Bankruptcies and Workouts to Keep You Ahead of the Curve

Cooley GODWARD KRONISH LLP

BANKRUPTCY AND RESTRUCTURING GROUP

In Victory for General Growth, Bankruptcy Court Permits Subsidiaries to Stay in Chapter 11

In a very recent decision with important implications for the General Growth (GGP) bankruptcy case, the bankruptcy court dealt a victory to the debtors in refusing to grant creditor motions to dismiss the chapter 11 cases of certain GGP subsidiary debtors.

ING Clarion Capital Loan Services LLC (ING Clarion), Helios AMC, LLC (Helios), each as special servicer to certain secured lenders, and Metropolitan Life Insurance Company and KBC Bank N.V. (together, Metlife), as secured lender, filed motions to dismiss certain of the chapter 11 cases.

The creditors' primary argument for dismissal was that the bankruptcy cases of certain GGP debtors were filed in bad faith. ING Clarion and Helios argued that the cases were filed prematurely because there was no imminent threat to the financial viability of the relevant debtors. Metlife also argued that the cases were filed prematurely and that there was no chance of reorganization because there was no possibility of confirming a plan over its objection.

The bankruptcy court quoted the standard by which a chapter 11 case can be dismissed as a bad-faith filing: "a bankruptcy petition will be dismissed if both objective futility of the reorganization process and subjective bad faith in filing the petition are found."

The creditors argued that they established objective futility because the cases were

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Congressman Nadler Seeks BAPCPA Repeal Through Business Reorganization and Job Preservation Act of 2009

On April 2, 2009, Congressman Jerrold Nadler (NY-08), Chairman of the House Judiciary Subcommittee on the Constitution, Civil Rights and Civil Liberties, introduced the *Business Reorganization and Job Preservation Act of 2009* (the "Act"), which would amend the Bankruptcy Code to repeal certain provisions of the *Bankruptcy Abuse Prevention and Consumer Protection Act of 2005* ("BAPCPA"). Since its enactment in late 2005, BAPCPA has been heavily criticized by practicing attorneys and legal commentators who have attributed the disappearance of corporate reorganization (and the resulting loss of tens of thousands of jobs nationwide) to its onerous provisions curtailing the chapter 11 debtor's liquidity and ability to obtain adequate financing, including those provisions governing commercial leases, utility services, and new classes of administrative priority claims. In fact, as previously reported in the Spring 2009 edition of Absolute Priority, Cooley's own Larry Gottlieb testified before the U.S. House Judiciary Subcommittee on Commercial and Administrative Law in September 2008 in favor of the very same amendments to the Bankruptcy Code sought by the Act.

Perhaps the most widely criticized provision of BAPCPA is its amendment to section 365(d)(4) of the Bankruptcy Code, through

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from the editor

JEFFREY L. COHEN

As the dog days of Summer slowly begin to whimper, it's time to settle back in and take notice of all the signs of life that have reemerged around us – including those within the chapter 11 landscape. Over the past several months, companies have begun to emerge from chapter 11 protection as going concern operations with growing regularity, at least in comparison to the litany of liquidations witnessed since the fall of Lehman Brothers in September 2008. Of course, only time will tell if these latest developments are a sign of things to come or the result of our collective wishful thinking.

What has certainly become clear, however, is that companies seeking to emerge amidst these troubling economic times must prepare themselves for a quick chapter 11 sale process, as few, if any, companies will possess the requisite financial support to endure the significant time and cost of a true reorganization. Indeed, today's chapter 11 "success stories" almost invariably involve lightning speed sale processes and streamlined capital structures, without regard to the chapter 11 carcasses they leave behind.

This issue discusses the surgical chapter 11 sales of GM and Chrysler and highlights recent developments in bankruptcy law, including the impact of bankruptcy remote entities in the General Growth bankruptcy cases, the severability of master mortgage loan agreements, the automatic nature of good faith findings under section 364(e) of the Bankruptcy Code and Congressman Nadler's efforts to repeal BAPCPA.

Enjoy this latest issue and we look forward to hearing from you.•

SDNY Approves Fast Track Section 363 Sale of General Motors

On July 5, 2009, U.S. Bankruptcy Judge Robert Gerber approved the section 363 sale of General Motors ("GM") to a consortium of governmental and non-governmental buyers including the U.S. Treasury, two Canadian governments, a VEBA (Voluntary Employee Benefit Association) trust established for UAW retirees and the equity holders of "old" GM. The sale order, which was delayed for four days to allow time for appeals, took effect at Noon on July 10, 2009.

Prior to GM's chapter 11 filing and in response to the well-documented financial troubles plaguing the U.S. automotive industry, the U.S. Treasury and its Presidential Task Force made $13.4 billion in TARP funds available to GM in early 2009. As a condition to its receipt of those funds, GM was required to produce a long-term viability plan by March 30, 2009 or the government loan would become due thirty days thereafter. On March 30th, President Obama announced that GM's viability plan fell short. But rather than force GM into an immediate liquidation to repay the TARP funds, the President offered GM a second chance at survival through a $6 billion senior secured bridge loan that would provide GM with sufficient funding to survive for another sixty days and negotiate long-term agreements with its bondholders and the UAW. The Treasury provided GM with the $6 billion bridge loan and GM was able to successfully negotiate with its key creditor constituents by June 1, 2009, the date of its bankruptcy filing.

The U.S. Treasury and the governments of Canada and Ontario agreed to provide GM with DIP financing on the condition that a sale of GM's business and assets occur on an expedited basis so as to preserve the value of the business, quickly restore consumer confidence and avoid the potentially substantial costs of a lengthy chapter 11 process. The financing deal proposed by the U.S. and Canadian governments

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Supreme Court Halts Pension Funds Challenge of Chrysler Sale

After taking their fight all the way to the United States Supreme Court, a group of Indiana state civil service pension funds were recently defeated in their efforts to block the sale of certain of Chrysler's assets to Fiat. The well-documented Chrysler-Fiat sale resulted in Fiat's receipt of a 35% stake in the new company, the United Auto Workers receipt of a 55% stake in the new company and the U.S. and Canadian governments received a combined 10% stake. Secured debt holders received a total of $2 billion in cash, or 29 cents on the dollar, for their $6.9 billion in Chrysler bonds.

The pension funds, which held less than one percent of Chrysler's first lien bond debt totaling approximately $42.5 million, challenged the sale in bankruptcy court. The pension funds argued that the U.S. Treasury Department exceeded its authority under the Emergency Economic Stabilization Act of 2008 ("EESA") by providing Fiat with Troubled Asset Relief Program ("TARP") funds used to finance the acquisition of Chrysler. Specifically, the pension funds interpreted the EESA as providing the Treasury Department with the limited authorization to purchase troubled assets from financial institutions and argued that in aiding Fiat's purchase of a car manufacturer, the Treasury Department had exceeded its congressional mandate.

The SDNY bankruptcy court held that the pension funds lacked standing to challenge the sale and, without reaching the merits of their arguments, denied the pension funds' objection. "Standing" is a threshold issue in every federal case. In order to seek relief from a federal court, a plaintiff must first establish the existence of a case or controversy between the plaintiff and defendant under Article III of the Constitution that can be adjudicated by the court. Supreme Court jurisprudence has established three prerequisite elements to constitutional standing: (i) the plaintiff must have suffered an "injury in fact" that is actual or imminent, and that is a concrete and particularized invasion of a legally protected right; (ii) there must be a causal connection between the injury and the conduct complained of; and (iii) it must be likely, not merely speculative, that the injury will be redressed by a favorable decision.

In denying the pension funds standing to challenge the sale, the SDNY bankruptcy court reasoned that the Treasury Department's use of the TARP funds to finance Fiat's acquisition would not amount to an "injury in fact" to the pension funds for two reasons. First, the bankruptcy court found that the pension funds were bound by the agreement of the administrative agent for the first lien bondholder group to consent to the sale in exchange for the $2 million cash payment. Second, the bankruptcy court concluded that even if the pension funds were not bound by the agent's consent, they would still lack standing because they could not demonstrate an injury resulting from the Treasury Department's decision to finance the sale. The bankruptcy court explained that because the sale provided the pension funds with a pro-rata distribution of the value of their collateral (which was valued at no greater than the $2 billion in proceeds that the first lien bondholder received from the sale) no injury in fact was suffered by the bondholders.

The pensions funds appealed the bankruptcy court's ruling and moved for a stay of the sale order pending appeal. In an unusual step that reflected the uniquely time-sensitive nature of the Chrysler-Fiat transaction, the bankruptcy court approved the pension funds' request to bring their appeal before the Second Circuit Court of Appeals, bypassing the District Court

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In the News

Current Cooley Representations

In re Pacific Ethanol Holding Co. LLC, et al., Case No. 09-11713 (Bankr. D. Del. 2009) Pacific Ethanol Holding Co. LLC and its four ethanol production facilities, with a combined production capacity of 200 million gallons of ethanol per year, stand poised to capitalize on the increasing demand for low carbon fuels, driven by consumer demand and government mandated Renewable Fuel Standards. Pacific Ethanol's four ethanol plants are uniquely positioned in the Western United States, which represents one of the fastest growing markets for ethanol fuel blends. On May 17, 2009, Pacific Ethanol Holding Co. LLC and its four plant subsidiaries filed for chapter 11 protection due to sizeable fluctuations in the price of corn, natural gas and ethanol, coupled with the continued lack of liquidity in the credit markets and the difficulty in raising additional investment capital from the depressed equity markets. Cooley represents the debtors in connection with their bankruptcy case and is currently focused on assisting the debtors in formulating their plan of reorganization and exit from bankruptcy.

In re Crabtree & Evelyn, Ltd., Case No. 09-14267 (Bankr. S.D.N.Y. 2009) Crabtree & Evelyn has evolved from a small, entrepreneurial business, to a company with worldwide manufacturing and distribution capabilities and 100 retail locations in the United States, making it well-known and respected for its English-style elegance. On July 1, 2009, Crabtree & Evelyn filed a voluntary petition for chapter 11 bankruptcy protection. Cooley represents the debtor in connection with its bankruptcy case and restructuring efforts. The debtor anticipates reorganizing around a smaller retail platform, while retaining the high level of service and

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quality of its personal care products and related accessories, fragrances, comestibles (i.e., food products including cookies, teas and jams), products for the home and gift arrangements.

In re Eddie Bauer Holdings, Inc., et al., Case No. 09-12099 (Bankr. D. Del. 2009) Cooley represents the official committee of unsecured creditors of Eddie Bauer, an internationally recognized retailer operating approximately 370 retail and outlet stores throughout the United States and Canada. Approximately six weeks after filing for chapter 11 protection on June 17, 2009, Eddie Bauer was sold as a going concern to Golden Gate Capital, a San Francisco private equity firm, for $286 million plus the assumption of hundreds of millions of dollars in liabilities. The sale, which was approved by the Delaware bankruptcy court following an auction that lasted more than 15 hours, will keep open at least 336 of Eddie Bauer's 370 stores. The creditors' committee is currently pursuing an investigation of the validity and extent of the prepetition junior secured lenders' liens and claims, with a focus on providing a meaningful return to unsecured creditors.

In re Ritz Camera Centers, Inc., Case No. 09-10617 (Bankr. D. Del. 2009) As counsel to the official committee of unsecured creditors in the Ritz Camera Centers, Inc. bankruptcy, Cooley actively negotiated a deal that provided for the sale of substantially all of Ritz's assets to RCI Acquisition, LLC. The sale was consummate following a 23.5-hour marathon auction at Cooley's New York offices that included 43 rounds of bidding. As a result of the sale to RCI, the debtor, a retailer with approximately 400 stores that has been in existence for more than 90 years, will continue to operate across the

Delaware District Court Reverses New Century Chapter 11 Plan

The Delaware District Court recently reversed the confirmation of the chapter 11 plan of New Century Financial Corp., a subprime lender whose 2007 failure was a bellwether of the weakening global economy. Prior to its collapse amid rising subprime delinquencies and defaults, New Century had been the largest U.S. independent provider of home loans to individuals with poor credit histories. After defaults started to rise in 2006, the subprime mortgage market imploded in February 2007, contributing to a sell-off in the stock market and fueling fears that more weakness in housing, and tighter credit in general, would spark the economic recession of today.

In reversing the Delaware bankruptcy court's plan confirmation order, Judge Sue Robinson held that New Century's chapter 11 plan improperly separated the sixteen debtors into three distinct groups with three sets of creditors. Judge Robinson faulted the plan for failing to deliver even-handed treatment to similarly situated creditors of the defunct lender.

The decision pressed a hot-button issue in corporate bankruptcies, where significant questions have been raised regarding the ease in which affiliated debtors are permitted to "substantively consolidate" their assets and liabilities into convenient piles in order to modify the rights of creditors and exit bankruptcy. Substantive consolidation is an equitable remedy used by courts to allow affiliated debtors to disregard their corporate separateness and/or merge their assets and liabilities where warranted under the circumstances of the bankruptcy case. Because the rights and recoveries of certain creditors can be substantially impaired by a substantive consolidation of assets, particularly those creditors of a "healthier" debtor entity, courts have long held that the remedy of substantive consolidation should be used sparingly. Indeed, section 1123(a)(4) of the Bankruptcy Code requires, as a condition to confirmation, that a plan "provide the same treatment for each claim or interest of a particular class, unless the holder of a particular claim or interest agrees to a less favorable treatment of such particular claim or interest."

In the New Century case, the debtors argued that their three-company distribution scheme provided for equal treatment among similarly classified creditors. Under the confirmed plan, creditors within particular classes were entitled to receive a distribution equal to 130% of their claims in exchange for their agreement to receive less than 100% on account of their claims in other classes. In other words, Creditor A, in exchange for agreeing to receive 0% on its Class 1 claim, was entitled under the plan to receive 130% on its Class 2 claim. However, Creditor B, who held a Class 2 claim only, would only be entitled to a 100% distribution on account of the very same claim for which Creditor A received a 130% distribution.

Equating the debtors' plan to "rough justice" for those creditors who faced increased competition for a consolidated pool of assets and revalued claims, Judge Robinson concluded that the plan violated section 1123(a)(4) of the Bankruptcy Code. Judge Robinson reasoned that consent to a less favorable treatment in one class excuses disparate treatment of claims within that particular class, but is inapposite to the treatment of claims in any other class. •

Delaware Bankruptcy Court Severs American Home Mortgage Master Loan Agreement

On remand from the Delaware District Court, Judge Sontchi recently reaffirmed his decision to approve the sale of American Home Mortgage's (AHM) assets over the objection of one of AHM's creditors, DB Structured Products, Inc. (DBSP), who purchased loans from AHM prior to the bankruptcy filing. Unlike the numerous subprime mortgage lenders who have filed for chapter 11 protection over the past two years, AHM was an "Alt-A" lender of "no doc loans" made to borrowers with better credit scores, but little or no income verification. AHM and its affiliates originated, sold and serviced Alt-A residential mortgage loans prior to filing for chapter 11 protection in Delaware.

DBSP purchased loans from AHM under a master agreement providing for (i) the origination and sale of the loans and (ii) the servicing of such loans. The master agreement included certain warranties from AHM, two of which were relevant to the dispute before Judge Sontchi. First, AHM warranted that the loans would not suffer an "early payment default." An early payment default under the loans would trigger DBSP's right to require AHM to repurchase the defaulting loan. AHM also warranted that the loans sold would not be prepaid within a certain time and, in the event of a prepayment, DBSP would be entitled to a refund from AHM of the premium paid for the loan at the time of purchase (i.e., a premium recapture). Prior to the bankruptcy filing, many of the loans suffered an early payment default and/or an early prepayment. Consequently, DBSP asserted substantial early payment default and premium recapture claims against AHM.

In the course of its bankruptcy proceeding, AHM sought approval to sell its loan servicing business to a third party buyer, which included the master agreement which DBSP. In connection with the purchase, however, the buyer refused to assume any non-servicing liabilities, such as AHM's early payment default and premium recapture obligations. DBSP objected to the sale, arguing that the buyer must assume the master agreement *cum onere* as a condition to assignment and therefore was precluded from satisfying AHM's obligations under the master agreement, including DBSP's claims arising from the early payment default and premium recapture provisions. DBSP also argued that even if the master agreement could be severed so as to permit AHM to transfer the loan servicing business independently of the loan purchase and sale business, any such transfer would require DBSP's consent as a condition to approval and consummation. Finally, DBSP argued that the buyer's lack of Freddie Mac qualification, as such was required under the provisions of the master agreement, meant that the buyer could not provide adequate assurance of future performance under the agreement and therefore the sale could not be approved.

Judge Sontchi approved the sale over DBSP's objections, concluding that the master agreement could be severed into two distinct agreements, one concerning the servicing of the mortgage loans for which the buyer sought to assume and one concerning the purchase and sale of mortgage loans for which the buyer was not seeking to assume. In following, Judge Sontchi concluded that, notwithstanding the existence of a single master agreement governing AHM's servicing, origination and sale obligations, AHM could sell the mortgage servicing business free and clear of any claims relating to the mortgage origination or sale business. DBSP promptly appealed the ruling in the Delaware District Court, which ultimately remanded the issue back to the bankruptcy court for a ruling. On remand, AHM and

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United States. The Committee will now turn its attention to assisting the debtor in liquidating the remaining property of the estate, which includes 6 owned real estate properties.

In re Filene's Basement, Inc., et al., Case No. 09-11525 (Bankr. D. Del. 2009) After the purchaser of substantially all of Filene's assets operated the company for nearly 10 years after its 1999 bankruptcy, Filene's again filed for bankruptcy protection on May 4, 2009. Cooley represents the official committee of unsecured creditors. Filene's is the oldest off-price retailer in America with 26 operating retail locations and approximately $422 million in annual sales. While the debtors examined various alternatives to address their projected liquidity shortfall, none of these alternatives proved viable, and the debtors determined that a sale of their operations was the best option to maximize the value of their business. Cooley was instrumental in utilizing the auction process to maximize recoveries for unsecured creditors. At the end of a three-day auction, a joint venture of Syms Corp. and Vornado Realty acquired substantially all of the assets of Filene's for approximately $63 million—a figure substantially higher than the $22 million stalking horse bid. Under the sale, the Syms/Vornado joint venture acquired leases for 23 retail stores and a distribution center, along with inventory, fixed assets and equipment at all locations, as well as certain Filene's contracts, intellectual property, trade names and related assets. The sale assured that Filene's would continue to operate throughout the Northeast and Midwest and projects to provide a substantial distribution to general unsecured creditors.

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In re BT Tires Group Holding, LLC, et al., Case No. 09-11173 (Bankr. D. Del. 2009) Cooley represents the official committee of unsecured creditors of Big 10 Tire Stores, one of the largest independent tire dealers in the Southeastern United States. For 54 years, Big 10 Tire has specialized in offering its customer base a broad selection of tire products and competitive pricing. On April 2, 2009, Big 10 Tire filed for chapter 11 and, approximately three months later, the Delaware bankruptcy court approved the sale of Big 10 Tire as a going concern to an affiliate of Sun Capital Partners, Inc., a private investment firm. Cooley successfully negotiated a return for creditors with the buyer and is now focused on assisting with the wind-down of the bankruptcy case.

In re Gottschalk's, Inc., Case No. 09-10157 (Bankr. D. Del. 2009) Founded in 1904, Gottschalk's, Inc. operated 50 full-line department stores and three specialty stores in six western states. Cooley, on behalf of the creditors' committee, played a key role in revising the terms of the debtor's post petition financing to ensure that the company possessed sufficient liquidity to fully market its assets. Cooley has been instrumental in maximizing the value of the estate for the benefit of unsecured creditors through the Debtor's liquidation, as Cooley negotiated a stalking horse asset purchase agreement for the sale of the Debtor's inventory that set the stage for a robust auction and the commencement of going out of business sales in April 2009. In addition, Cooley has negotiated agreements for the sale of Gottschalk's lease portfolio and owned real property that have added more than $20 million of value to the estate.

First Circuit BAP Infers Lender's Good Faith Under Section 364(e)

The First Circuit Bankruptcy Appellate Panel recently held that a postpetition financing order does not need to include an explicit finding that the financing arrangement has been extended in good faith in order to provide postpetition lenders with the benefit and protection of section 364(e) of the Bankruptcy Code. Section 364(e) provides a crucial protection to postpetition lenders by nullifying the effect on the validity or priority of any lien or claim granted to postpetition lenders on account of a reversal or modification on appeal of the bankruptcy court's initial authorization. A postpetition lender is entitled to such protection under section 364(e) so long as it acts in good faith in extending credit to a debtor and such authorization is not stayed pending appeal.

In *Keltic Financial Partners, LP v. Foreside Management Co., LLC,* et al., 51 BCD 90 (1st Cir BAP 2009), the debtor was a warehouse owner and leased space to tenants. The debtor's warehouse contained a specialized racking system which was owned by the debtor and used by certain tenants under the terms of their leases. Prior to the bankruptcy filing, Keltic Financing loaned $3 million to one of the debtor's tenants. The debtor agreed to guarantee the loan and, as further security for its tenant's repayment, granted Keltic a security interest in the racking system. Additionally, the debtor's primary secured lender, Chittenden Trust, agreed to subordinate its security interest in the racking systems in favor of Keltic.

When the debtor's tenant defaulted on the loan, Keltic sought to foreclose on its collateral and a public auction was held. The rules of the auction expressly prohibited the winning bidder from subsequently transferring its purchase to another bidder. The debtor participated in the auction, but was outbid by the auction winner American Surplus, Inc. Following the conclusion of the auction, the debtor filed a chapter 11 petition and, still seeking to obtain the racking equipment, sought the authorization of the bankruptcy court to (a) purchase the equipment from ASI; (b) partially finance the purchase of the racking equipment through a prepayment agreement with a tenant who wanted to lease additional warehouse space; and (c) borrow an additional $50,000 from Chittenden, secured by existing collateral, in the form of postpetition debtor-in-possession financing and to use the proceeds to pay the balance of the purchase price.

Dissatisfied with the auction proceeds and the subsequently proposed return sale to the debtor, Keltic opposed the debtor's financing motion on grounds of collusion. In response to Keltic's objection, the debtor filed an amended financing motion which purported to resolve Keltic's collusion claim by requiring Chittenden – the postpetition lender – to purchase the equipment directly from ASI and then sell it to the debtor on the same terms proposed by the debtor in the initial financing motion. The bankruptcy court granted the debtor's amended motion and Keltic appealed. The order granting the amended financing motion did not include an express finding by the court that the Chittenden's agreement to extend the postpetition financing was made in good faith. Additionally, Keltic did not seek or obtain a stay of the financing order pending its appeal.

The First Circuit Bankruptcy Appellate Panel dismissed the appeal as moot in light of Keltic's failure to obtain a stay of the financing order pending appeal. The Court rejected Keltic's argument that a stay pending appeal was unnecessary under the circumstances since Chittenden had already advanced the funds to the debtor.

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Eighth Circuit Broadly Interprets "Settlement Payment Defense"

The Court of Appeals for the Eighth Circuit recently weighed in on the issue of whether the so-called "settlement payment defense" shields prepetition transferors of privately held securities from liability to the bankruptcy estate. Pursuant to section 546(e) of the Bankruptcy Code, a debtor may not avoid a transfer that is a settlement payment made by or to a financial institution. The term "settlement payment" is broadly defined by the Bankruptcy Code as a payment commonly used in the securities trade. In holding that the defense applies regardless of whether the securities were publicly or privately held, the Eighth Circuit has joined a growing list of courts who have extended the defense to shareholders of privately held companies who sell their equity pursuant to a leveraged buyout transaction ("LBO").

In Contemporary *Indus. Corp. v. Frost*, Case No. 08-1325, 2009 WL 1159174 (8th Cir. Apr. 29, 2009), shareholders of the debtor, a privately-held corporation, sold their shares prior to the bankruptcy filing to an outside investment group. In order to finance the equity purchase, the investment group obtained loans secured by the debtor's assets. To facilitate the transaction, a new holding corporation of the debtor was created and an account in the holding corporation's name was maintained at First National Bank of Omaha. Approximately $26.5 million was transferred into the account by the lenders and investment group and the selling shareholders deposited their shares with First National as well.

Approximately four years after the LBO transaction was consummated, the debtor filed its chapter 11 case and commenced an adversary proceeding against the former shareholders seeking to recover the payments received in exchange for their stock as fraudulent transfers. The shareholders raised the "settlement payment defense" in response to the action, contending that section 546(e) of the Bankruptcy Code immunizes the payments from recovery because such payments constitute settlement payments made by a financial institution. The debtor argued in response that section 546(e) of the Bankruptcy Code is intended to protect payments made to settle public securities transactions and does not shield from recovery transferors of privately held securities. The debtor also argued that, even if section 546(e) applied to privately held security transactions, the defense would not aid the shareholders because First National never obtained a beneficial interest in the cash and securities held in its account and therefore the payments were not made "by or to a financial institution."

The Eighth Circuit first considered whether the "settlement payment defense" applies only to payments made to settle public securities. The Court was persuaded by the reasoning of other circuit courts who have previously determined that, in the absence of express language limiting the defense to settlements of public securities, section 546(e) is clear and unambiguous in its application to the settlement of both public and private securities. Like other circuit courts who have found the language of section 546(e) to be clear and unambiguous, the Court rejected the argument that the "settlement payment defense" was intended only to protect financial markets against instability caused by the reversal of securities transaction and therefore should be limited in application to settlements of public securities.

The Court also rejected the debtor's argument that the payments made to the shareholders were not made "by or to a financial institution" because First National never obtained a beneficial interest in the cash and securities held in its accounts. The

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In re G.I. Joe's Holding Corp., et al., Case No. 09-10713 (Bankr. D. Del. 2009) Cooley represents the official committee of unsecured creditors of G.I. Joe's Inc., a sporting goods retailer which operated 31 stores in Washington, Oregon and Idaho prior to its chapter 11 filing in March 2009 and subsequent liquidation. G.I. Joe's filed its chapter 11 case with substantial first and second lien secured debt that will not be paid in full from the proceeds of the company's store closing and intellectual property sales. Nevertheless, the committee was successful in achieving a significant "carve out" from the secured lenders' collateral, which proceeds shall be distributed exclusively to unsecured creditors at the conclusion of the case.

In re Against All Odds, Inc., Case No. 09-10117 (Bankr. D.N.J. 2009) In May 2009, Against All Odds, USA, Inc., sold its assets and 30 of its leases to New Deal, LLC, which will continue to run the debtor's business as a going concern. Cooley is counsel to the official committee of unsecured creditors in the case and led the negotiations with New Deal. Against All Odds, an urban-style clothing retailer, filed for bankruptcy protection in early January 2009. As a result of the sale to New Deal, unsecured creditors are guaranteed a return on their debt that far exceeds liquidation value.

Receivership of Silverton Bank, N.A. Cooley advised the Federal Deposit Insurance Company (FDIC) as receiver, in connection with the failure of Silverton Bank, N.A. Silverton was an Atlanta-based commercial bank that provided correspondent banking services to its client banks. Silverton had approximately $4.1 billion in assets and $3.3 billion in deposits, with 1,400 client banks in 44 states,

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and operated six regional offices. Cooley was engaged to provide advice and counsel relative to numerous insolvency issues that arose with respect to several Silverton special purpose entities.

In re Anchor Blue Retail Group, Inc., et al., Case No. 09-11770 (Bankr. D. Del. 2009) Cooley represented Levi Strauss & Co., the "stalking horse" and ultimately successful purchaser of 73 Levi's® and Docker's® Outlets by MOST stores, in the chapter 11 bankruptcy cases filed by Anchor Blue Retail Group, Inc. and its affiliates on May 27, 2009 in the Bankruptcy Court for the District of Delaware. Anchor Blue, a leading specialty apparel retailer, was Levi Strauss & Co.'s licensee with respect to the outlet stores and also operated more than 150 of its own Anchor Blue stores. The sale, which closed in mid-July 2009, encompassed the inventory, fixtures and equipment associated with the outlet stores. The purchase price was $72 million, subject to certain post-closing adjustments.

In re Silicon Graphics, Inc, et al., Case No. 09-11701 (Bankr. S.D.N.Y. 2009) Cooley represented Rackable Systems, Inc., a leading provider of highly scalable computer servers and high-capacity storage systems for medium to large-scale data centers, as the purchaser of substantially all of the assets of Silicon Graphics, Inc., a leader in high performance computing and data management. On April 1, 2009, Silicon Graphics and multiple subsidiaries, filed chapter 11 petitions (their second visit to Chapter 11 in approximately three years) in the Bankruptcy Court for the Southern District of New York. Prior to the bankruptcy filing, Rackable and Silicon Graphics entered into an asset purchase agreement, which provided that Rackable would be the "stalking horse" purchaser

SDNY Denies Class Action Certification to Employee Wage Claimants

In *In re Bally's Total Fitness of Greater New York, Inc.*, 402 B.R. 616 (Bankr. S.D.N.Y. April 7, 2009) aff'd 2009 U.S. Dist. LEXIS 51690 (S.D.N.Y. June, 15, 2009), the United States Bankruptcy Court for the Southern District of New York recently rejected the motions of two groups of employees of Bally's Total Fitness seeking class action certification and authority to file a class proof of claim on behalf of employees alleging, among other things, claims for unpaid wages.

Prior to the commencement of the bankruptcy case, Bally's employees initiated two class action lawsuits on behalf of thousands of employees, including personal trainers, program directors and sales managers, asserting claims for, among other things, off-the-clock work, forfeiture of sales commissions, failure to provide meal and rest periods mandated by applicable state law and failure to reimburse business expenses. Bally's filed for bankruptcy protection before a class was certified in either lawsuit.

Once the bankruptcy was filed, however, certain employees sought to pursue one of the pending class actions in the bankruptcy court by filing two proofs of claim totaling $250 million, one on behalf of fitness instructions and one on behalf of personal trainers, and moved the bankruptcy court to certify the respective classes.

The Court noted that while there is no absolute right to file a class proof of claim under the Bankruptcy Code, bankruptcy courts may, and often have, exercised their discretion to permit the filing of a class proof of claim if the procedural requirements of Rule 23 of the Federal Rules of Civil Procedure (governing class actions) are satisfied and the benefits to be derived from the class claim are consistent with the general goals of bankruptcy law.

The Court denied certification to the proposed employee class based on this latter consideration, reasoning that class certification would adversely affect the administration of the Bally's bankruptcy estate by adding layers of factual and procedural complexity to the resolution of employee wage claims, thereby siphoning the company's resources and interfering with its orderly reorganization process. The Court gave significant consideration to the substantial legal fees and costs that the Bally's estate would be required to pay in defending the proposed class actions —which costs would be substantially lessened if class members were required to file and prosecute individual proofs of claim. The Court also observed that, in the event the class action was to succeed against the Bally's estate, class counsel would likely be entitled to payment of legal fees and costs from the estate, thereby reducing the funds available for creditor distributions. Given these considerations, the Court concluded that the proposed class action was not the superior method for the fair and efficient adjudication of the employee claims.

The Bally's ruling is an important decision, particularly since bankruptcy courts have been asked to certify classes of employee wage and benefits claimants, gift card and merchandise credit claimants and other classes of claims with increasing frequency. Often, these purported classes include claimants holding fact sensitive claims and seek priority and allowance under fact intensive provisions of the Bankruptcy Code that should not be decided on a consolidated basis in fairness to other creditors. The Bally's decision supports this view and perhaps signals a recognition by bankruptcy courts of these considerations, as well as the increased inefficiency and administrative costs associated with the class action mechanism. •

Prior Course of Dealing Critical to Ordinary Course of Business Defense

The Eleventh Circuit Court of Appeals recently held that a brief business relationship between a creditor and a debtor substantially raises the creditor's hurdle to satisfy the subjective component of the ordinary course of business defense to preference actions—i.e., whether the transfers at issue were made in the ordinary course of business between the specific creditor and debtor at issue.

In *In re Globe Manufacturing Corp.*, 51 BCD 168 (11th Cir. 2009), the trustee filed a complaint against a creditor, Carrier Corporation, to recover $615,831 in payments made by the debtor to Carrier within the ninety-day preference period. Carrier's relationship with the debtor traced back to only six months prior to the bankruptcy filing and this brief relationship weighed heavily in the Court's determination that the payments made to Carrier did not fall within the ordinary course of its business relationship with the debtor.

Importantly, the *Globe Manufacturing* case was commenced prior to the effective date of BAPCPA's amendment to section 547(c)(2) of the Bankruptcy Code. Accordingly, in order to satisfy the requirements of the ordinary course of business defense, Carrier was required to prove that the payments were (i) made in the ordinary course of business of the debtor and creditor (i.e., subjectively ordinary as between the individual debtor and creditor) and (ii) made according to ordinary business terms (i.e., objectively ordinary in relation to industry norms). As amended in 2005, the conjunctive language of former section 547(c)(2) was rewritten in the disjunctive, in an effort to lessen the burden on creditors seeking the benefits of the ordinary course of business defense. As a result of the amendment, creditors are now required to prove that the subject transfer was subjectively or objectively ordinary—they need not prove both.

Given the absence of an extensive history between Carrier and the debtor that might have established a pattern of late payments, the Court was left without a historical reference with which to consider the subject transfer. As the payment was made to Carrier 30 days beyond the agreed upon due date, and because untimely payments are generally more likely to be considered outside of the ordinary course of business, the Court held that Carrier could not satisfy the subjective component of the ordinary course of business defense.

Although creditors are no longer required to prove both prongs of the ordinary course of business defense, the subjective test remains the more useful standard for creditors seeking to utilize the defense, because it avoids the often substantial costs of expert analysis and testimony needed to satisfy the objective test. Accordingly, this decision will perhaps serve as a cautionary tale for vendors considering whether to extend credit to already distressed businesses. •

IN THE NEWS continued

in a section 363 sale. During the auction, Rackable was able to negotiate the release of the secured creditors' liens from the purchased assets by increasing its bid. In May 2009, the sale closed and Rackable paid the secured creditors $42.5 million in cash and substantial additional amounts to contract counterparties and administrative creditors. Following the closing, Rackable has adopted SGI® as its global name and brand.

In re Boscov's, Inc. et al., Case No. 08-11637 (Bankr. D. Del. 2008). Boscov's Inc., through its operating subsidiary Boscov's Department Store, LLC and other debtor subsidiaries, owns and operates the nation's largest family-owned department store chain, with 39 locations across five states in the Mid Atlantic region generating approximately $1 billion in sales on an annual basis as the date of its bankruptcy filing on August 12, 2008. Cooley, as counsel for the official committee of unsecured creditors, has been actively involved in all aspects of these cases. Cooley has been intimately involved in every aspect of the sale process which resulted in the assets of Boscov's being sold to members of the founding families of Boscov's as a going concern. In addition, Cooley's investigation of the leveraged recapitalization of Boscov's resulted in a Court-approved settlement, which enhanced the purchase price paid by the founding families, for the benefit unsecured creditors. Lastly, Cooley assumed a lead role in the estates' successful litigation with a disgruntled bidder for the assets of Boscov's that sought to be paid a $4 million break-up fee. On July 31, 2009, and after presiding over an arbitration at which both sides made their case, the Court ruled that the bidder was not entitled to a break-up fee.

IN THE NEWS continued

In re Mervyn's Holdings, LLC, et al., Case No. 08-11586 (Bankr. D. Del. 2008) Mervyn's, a chain of approximately 175 family-friendly, promotional department stores predominantly located in California and the southwestern United States, filed for chapter 11 protection on July 29, 2008. Cooley represents the official committee of unsecured creditors. The company implemented a number of strategic operational initiatives, including the immediate liquidation of 26 underperforming stores and cost-cutting measures. Unfortunately, against the backdrop of the global economic crisis, Mervyn's determined, after consultation with the creditors' committee and other constituents, that the best course of action to maximize value for creditors was to close all of their remaining stores and liquidate all of the estates' assets, including the debtors' intellectual property assets. The debtors conducted store closing sales during the 2008 holiday season and have completed such sales and the sale of their intellectual property. The creditors' committee is currently pursuing causes of action related to the 2004 acquisition of Mervyn's by an entity formed by affiliates of various private equity firms, including avoidance of certain transactions and recovery of certain transfers consummated in connection with such acquisition. The creditors' committee is also pursuing causes of action against the debtors' second lien lender relating to the validity of its liens.

In re KB Toys, Inc., et al., Case No. 08-13269 (Bankr. D. Del. 2008) After having emerged from bankruptcy in 2004 pursuant to a plan of reorganization under which Prentice Capital Management acquired a majority ownership of the debtors, KB Toys again filed for bankruptcy on December 11, 2008.

GENERAL GROWTH continued from page 1

prematurely filed. The creditors stated that the relevant debtors should have waited until closer to the maturity date of their mortgages (which was March 2010 at the earliest) until they filed bankruptcy petitions. The bankruptcy court disagreed, holding that it is not required "to examine the issue of good faith as if each Debtor were wholly independent" but, rather, could look to the interests of the GGP group as a whole to determine whether the relevant debtors were in sufficient financial distress to warrant a bankruptcy filing. When it looked to the group as a whole, including consideration of the collapse of the financial and real estate markets and their effect on the GGP group, the bankruptcy court found that the filings at issue were warranted.

In addition, Metlife argued that objective futility was established because the relevant debtor would be unable to confirm a plan over Metlife's opposition. Metlife stated that because it holds the only impaired claim, the debtors would never be able to propose a plan that would be accepted by one class of impaired creditors, as is required by the Bankruptcy Code. The bankruptcy court, noting the irony, found that this argument was premature, holding that a debtor need not prove a plan is confirmable in order to file a bankruptcy petition.

Next, the creditors argued that the debtors did not exercise subjective good faith in filing the relevant subsidiaries. They stated that the debtors failed to negotiate with them prior to the filing. The bankruptcy court held that there is no requirement that a borrower negotiate with its lender prior to filing a bankruptcy petition. Moreover, testimony at trial revealed that it appeared the lenders would have been unwilling to negotiate (and the court pointed out that this was evidenced by Metlife's position that a plan would not be confirmed because it would not vote in favor of a plan impairing its claim).

Although the bankruptcy court explicitly made no claim to determining issues of substantive consolidation, an issue not before the court, the decision is an important step in GGP's bankruptcy cases. As the bankruptcy court stated, the motions were "a diversion" and now, with a favorable decision in hand, GGP can commence negotiations to get out of bankruptcy.

The decision will also have broader implications beyond General Growth's bankruptcy cases. Indeed, it highlights that a "bankruptcy remote" entity is not "bankruptcy proof". It will be interesting to see the impact of the decision on the prevalence of these entities going forward. •

CHRYSLER SALE continued from page 3

for the Southern District of New York. Less than a week later, the Second Circuit entered an order affirming the bankruptcy court's decision for substantially the same reasons. In a decision released on August 5, 2009, the Second Circuit stated that while "the scope of TARP is a consequential and vexed issue that may inevitably require resolution in some later case…this Court lacks the power to resolve it in the present dispute."

Undaunted by the Second Circuit's ruling, the pension funds filed an application for a writ of certiorari to the U.S. Supreme Court. One day following the filing, Justice Ruth Bader Ginsberg temporarily halted the sale with no explanation, giving the pension funds hope that the full Supreme Court would hear the appeal. However, the Supreme Court declined to hear the merits of the appeal the very next day and the Chrysler-Fiat sale was closed shortly thereafter. •

CONGRESSMAN NADLER continued from page 1

which a debtor now has only 210 days to decide whether to assume or reject its real estate leases. Prior to BAPCPA, a debtor had 60 days to make its assumption/rejection decisions, but could seek, and would frequently obtain, numerous court authorized extensions of this period. Although the practice of obtaining these extensions was often met with significant backlash from landlords, the debtor's ability to regularly obtain these extensions was crucial to its lender's willingness to extend sufficient financing to fund the reorganization process.

BAPCPA's 210-day cap on the assumption/rejection period has significantly reduced lenders' willingness to fund the reorganization process for more than a few months, since lenders invariably require assurance that sufficient time will be had to conduct "going out of business sales" in the debtor's store locations in the event the reorganization stalls. The Act would return section 365(d)(4) to its prior form, giving debtors 60 days to assume or reject these leases and empowering courts to extend that deadline for cause shown.

Another frequently criticized feature of BAPCPA is its amendment to section 366 of the Bankruptcy Code, which requires a debtor, within the first 20 days of the filing, to provide its utility providers (e.g., electric, gas, water, telephone) with adequate assurance of future payment in the form of a cash deposit or other security—in an amount generally ranging from two weeks to two months of service - in order to prevent the provider's discontinuation of services. BAPCPA's revision of section 366 abrogated the long-standing practice that adequate assurance of future payment did not require a guarantee of payment, as courts routinely held that administrative priority claims granted to utility providers were sufficient to assure the debtor's future performance. Revised section 366 expressly rejects the granting of administrative priority claims as a means to provide utility providers with assurance of the debtor's future payment.

BAPCPA's amendment to section 366 has been heavily criticized for its negative impact on the debtor's liquidity at the very beginning of the bankruptcy case, particularly with respect to retail debtors with numerous locations requiring multiple utility services. The Act would eliminate the specifically delineated forms of adequate assurance of future payment introduced by BAPCPA, thereby empowering courts to return to the past practice of deeming administrative claim grants sufficient to protect utility providers against subsequent non-performance by the debtor.

The addition of section 503(b)(9) of the Bankruptcy Code is another frequently criticized creature of BAPCPA. Section 503(b)(9) creates an administrative claim, not available prior to BAPCPA, for trade vendors whose goods were actually received by the debtor within the 20 days prior to the chapter 11 filing. Critics of this provision argue that for large retailers receiving high volumes of inventory with a reasonable turnover rate, section 503(b)(9) creates a new, and often massive, class of administrative claims that must be paid in full upon confirmation of a plan of reorganization. Prior to BAPCPA, a debtor's failure to pay for goods received within the 20 days preceding the commencement of its case gave rise to an unsecured prepetition claim, subject to very limited reclamation rights. These prepetition claims would ordinarily be paid by a debtor on the same pro rata basis as other unsecured claims under a confirmed plan, often at a severe discount.

Although trade vendors initially lauded this addition to the Bankruptcy Code as a significant improvement in the treatment of their claims, section 503(b)(9) has frequently proved to be little more than an empty promise, as retailers have not

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IN THE NEWS continued

Cooley represents the official committee of unsecured creditors. KB was the nation's leading mall-based specialty toy retailer with approximately 277 retail locations and approximately $480 million in annual sales. Although the debtors examined various alternatives to address their projected liquidity shortfall, none of such alternatives proved to be viable and, accordingly, the debtors determined that the liquidation of their retail-based operations through expedited and orderly going-out-of-business sales within chapter 11 was the best option for the debtors to maximize the value of their business. The creditors' committee is pursuing an investigation of the purportedly secured debt of Prentice, with a focus on achieving administrative solvency of the estates, including payment of "stub rent" and claims under section 503(b)(9) of the Bankruptcy Code.

In re BTWW Retail, L.P., et al., Case No. 08-35725 (Bankr. N.D. Tex. 2008)
BTWW Retail, L.P. and its wholly-owned affiliates are operators of western apparel and boot stores as well as a nationally known mail-order catalog that sells western wear. Prior to the filing of the bankruptcy cases in November 2008, Cooley served as counsel to an ad hoc committee of unsecured trade vendors and secured a payment on behalf of the unsecured trade creditor body. Cooley was then retained as counsel to the official committee of unsecured creditors and facilitated the sale of substantially all of BTWW's inventory and intellectual property, including the sale of 14 of its stores as a going concern to Boot Barn, Inc. and the liquidation of the inventory at its remaining stores to a joint venture led by Hudson Capital Partners. Subsequently, Cooley negotiated favorable settlements reducing the claims of senior secured

IN THE NEWS continued

creditors. Accordingly, BTWW Retail may be able to propose a plan providing for a distribution to unsecured creditors after an active review of priority tax claims is completed.

In re Landmark Luggage & Gifts, LLC, Case No. 09-00444 (Bankr. S.D. Iowa 2009) Landmark Luggage & Gifts is a regional leather luggage and accessories retailer which operates six stores located in five states in the Upper Midwest. Cooley was retained to advise the official committee of unsecured creditors after the filing of Landmark Luggage's bankruptcy petition on February 12, 2009. On August 11, 2009, the debtors filed a plan of reorganization that provides for a sale of substantially all of the company's assets to an entity which will continue to operate the business as a going concern through four of the established locations. Cooley is currently analyzing the proposed sale and the potential recovery to unsecured creditors.

In re Innovation Luggage, Inc., Case No. 09-10564 (Bankr. D.N.J. 2009) Innovation Luggage is a regional luggage and travel specialty retailer that operates a website and 10 stores located in New York, New Jersey, Connecticut and Washington D.C. After the filing of Innovation's bankruptcy petition on February 10, 2009, Cooley was retained to represent the official committee of unsecured creditors. The creditors' committee is currently analyzing the company's go-forward business plan and investigating the October 2008 transaction pursuant to which the debtor's assets were transferred to an insider of the debtor's secured lender. •

SALE OF GENERAL MOTORS continued from page 2

was conditioned on the approval of a section 363 sale by no later than July 10, 2009—only 39 days following GM's chapter 11 filing.

Under the sale proposed by GM, "New GM" acquired all of the assets of "Old GM" except for avoidance actions and the Pontiac, Saturn, Saab and Hummer brands. New GM is owned by the U.S. Treasury (60.8%), the two Canadian governments (11.7%), a new VEBA trust (17.5%), and Old GM (10%). The sale also required Old GM to assume and assign to New GM approximately 4,100 of its 6,000 dealer franchise agreements.

Judge Gerber of the United States Bankruptcy Court for the Southern District of New York approved the GM sale pursuant to section 363 of the Bankruptcy Code, the bankruptcy statute that permits companies to sell all or substantially all of their assets outside of a plan of reorganization or liquidation. At the hearing to consider the proposed sale, GM argued that the expedited nature of the sale process was essential, since it was the only way to avoid a liquidation of assets and preserve the business as a going concern. Judge Gerber agreed with GM on this point and applied the deferential "business judgment" test to GM's decision to conduct the expedited sale process and sell the business to the proposed buyers. The "business judgment" test was first articulated by the Second Circuit in its 1983 decision in the *Lionel Corp.* bankruptcy case. This test was also applied by Judge Gonzalez of the SDNY in approving the section 363 sale proposed in the *Chrysler* bankruptcy case only a few months earlier.

Applying the "business judgment" test, Judge Gerber found that there were no other DIP lenders or interested buyers, and that the U.S. and Canadian governments were the only parties prepared to invest in GM's future. Judge Gerber explained that "[b]ankruptcy courts have the power to authorize sales of assets at a time when there is still value to preserve—to prevent the death of the patient on the operating table." In light of the DIP financing conditions imposed by the U.S. and Canadian governments, the mounting losses that GM would otherwise suffer and the need to quickly address consumer and franchisee confidence issues, the Court concluded that GM possessed a sound business justification for proceeding with the expedited section 363 sale. In so holding, Judge Gerber noted that unsecured creditors would not receive less through the section 363 sale than in a liquidation of GM's assets, that the government debt was not subject to recharacterization or equitable subordination, and that New GM's agreement to purchase the company was negotiated in good faith.

The Court also rejected the argument advanced by certain objectors that the GM sale was really a sub rosa plan, pursuant to which the terms of the sale dictate the terms of a plan of reorganization without the same disclosure and voting requirements. Judge Gerber explained that the sub rosa prohibition first enunciated in In re *Braniff Airways, Inc.* (5th Cir. 1983)—that a "debtor and the Bankruptcy Court should not be able to short circuit the requirements of Chapter 11 for confirmation of a reorganization plan by establishing the terms of a plan sub rosa in connection with a sale of assets"—was inapplicable to the GM case because the sale did not seek to constrain parties from exercising their confirmation rights or to dictate the distribution of sale proceeds among different classes of creditors. Rather, the Court viewed the sale as one providing only for the sale of Old GM's assets, without any intent to obviate the chapter 11 plan process or distribute proceeds in a manner inconsistent with statutory priorities.

Finally, the Court rejected challenges to New GM's acquisition of Old GM's assets free and clear of any successor liabilities other than those expressly assumed by

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AMERICAN HOME MORTGAGE continued from page 5

DBSP stipulated that the master agreement is a non-executory contract.

Judge Sontchi first addressed DBSP's appeal of his findings concerning the severability of the master agreement and applied the three-part test established by *In re Gardinier, Inc.*, 831 F.2d 974 (11th Cir. 1987). First, the Court found that the nature and purpose of the loan servicing and loan sale provisions of the master agreement were different. Second, the Court reiterated its previous finding that the consideration underlying the loan sale provisions and the loan servicing provisions of the master agreement were separate and distinct. Specifically, the Court found it obvious that the consideration supporting the servicing of mortgage loans under the master agreement was the servicing fee and the consideration supporting the purchase and sale of loans under the master agreement was the purchase price paid for the loans together with the corresponding warranties. Third, the Court reaffirmed its previous holding that the obligations with respect to the sale of loans and the servicing thereof were not interrelated because they were not economically interdependent and, accordingly, the servicing provisions of the agreement could be sold independently of the purchase and sale provisions.

Judge Sontchi next addressed DBSP's argument that the loan servicing agreement could not be transferred absent its consent. The Court deemed DBSP's refusal to consent to the sale unreasonable, given that, apart from the buyer's lack of Freddie Mac qualification, the only reason DBSP articulated for withholding its consent to the sale was the buyer's refusal to assume AHM's early payment default and premium recapture liabilities. Finally, Judge Sontchi rejected DBSP's argument that the agreement could not be sold to the buyer because it did not qualify as a Freddie Mac servicer and therefore could not provide DBSP with adequate assurance of future performance pursuant to section 365 of the Bankruptcy Code. The Court held that (i) the parties' stipulation that the master agreement was non-executory dictated that section 365 of the Bankruptcy Code did not apply and (ii) even if the parties had not so stipulated and the agreement was deemed executory, the Freddie Mac qualification provision was an immaterial term of the agreement and buyer's performance would be excused.

This decision is certainly an important one for the bankruptcy community, as it signals an increased willingness on the part of bankruptcy courts to adopt creative reasoning by debtors seeking to maximize estate value for the benefit of creditors generally in these difficult financial times. •

CONGRESSMAN NADLER

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been able to obtain financing sufficient to reorganize their businesses and pay administrative claims in full at confirmation. The Act would eliminate section 503(b)(9) altogether, thereby returning to the past practice of treating claims for goods received by the debtor within the 20 days prior to the bankruptcy filing as prepetition unsecured claims. •

Bankruptcy & Restructuring Event Calendar
Fall 2009 Cooley Godward Kronish Speaking Appearances

Event	Date/Location	Cooley Godward Kronish Participant/Topic
American Bankruptcy Institute: Southwest Bankruptcy Conference	September 11, 2009 South Lake Tahoe, CA	Robert Eisenbach / Con Panelist Great Debates – Resolved: Administratively insolvent cases may be administered for the benefit of secured creditors
Information Management Network: Western Symposium on Distressed Residential Real Estate	September 15, 2009 Los Angeles, CA	Robert Eisenbach / Panelist "Bankruptcy: What Happens & What are the Actual Implications?"
National Association of Credit Managers: 2009 Credit Professionals Conference	September 17, 2009 Kansas City, KS	Lawrence Gottlieb / Speaker "Preferences, Fraudulent Conveyance & Annoying Notices from the Bankruptcy Court"
Turnaround Management Association: Annual Convention	October 8, 2009 Phoenix, AZ	Cathy Hershcopf / Panelist "Capital: Who is Where on the Right Side of the Balance Sheet?"
Licensing Executives Society: Annual Meeting	October 21, 2009 San Francisco, CA	Robert Eisenbach / Panelist "Preparing for the Worst: Understanding and Mitigating the Effects of Bankruptcy on Intellectual Property Licenses"
International Council of Shopping Centers: 2009 U.S. Shopping Centers Law Conference	October 22, 2009 Phoenix, AZ	Cathy Hershcopf / Speaker "Restructuring the Retailer's Portfolio"

"SETTLEMENT PAYMENT" DEFENSE continued from page 7

Court reasoned that section 546(e) does not expressly require that financial institutions obtain a beneficial interest in funds as a condition to using the defense.

The Eighth Circuit's decision follows the reasoning set forth by Judge Gross of the Delaware Bankruptcy Court in his 2007 decision in the *In re Plassein International Corporation* case, 366 B.R. 318 (Bankr. D. Del. 2007) aff'd 388 B.R. 46 (D. Del. 2008). In *Plassein*, Judge Gross similarly held that section 546(e) shields from avoidance payments made to the shareholders of a private company pursuant to a failed LBO. Judge Gross reasoned that the term "settlement payment" encompasses any transfer of cash or securities that was made to complete a securities transaction. With respect to the statute's "by or to a financial institution" component, Judge Gross concluded that the statute encompasses any payment made by a financial institution by wire transfer. The *Plassein* decision is currently pending appeal in the Third Circuit.

The unsettling conclusion to be drawn from these cases is that LBO participants seeking to insulate themselves from liability need only to channel the payments through the wire transfers of one or more financial institutions. However, a broader review of the case law reveals that many courts have refused to apply the settlement payment defense in the context of settlements of privately held securities.

Indeed, the Bankruptcy Court for the Eastern District of New York has held that section 546(e) does not bar a fraudulent transfer action against the selling shareholders in a private LBO simply because the payments at issue were made by wire transfer. In *In re Norstan Apparel Shops, Inc., et al*, 367 B.R. 68 (Bankr. E.D.N.Y. 2007), Chief Judge Craig was faced with a set of facts similar to those in *Plassein*. In *Norstan*, the official committee of unsecured creditors, represented by Cooley, initiated an adversary proceeding against the former shareholders of the debtors, who had received $55 million by wire transfer in exchange for their equity in the company pursuant to an LBO transaction consummated a few years before the bankruptcy was commenced. The selling shareholders moved to dismiss the proceeding on the ground that the payments received in exchange for their equity constituted settlement payments under section 546(e).

Judge Craig rejected the shareholders' argument that the settlement payment defense should be so broadly interpreted so as to insulate transfers made pursuant to private LBOs, reasoning that while the term "settlement payment" is to be read broadly, the term is not boundless. Judge Craig also reasoned that the settlement payment defense must be construed in light of Congress's intent to minimize the displacement caused in the commodities and securities markets in the event of a major bankruptcy affecting those industries, and to prevent the ripple effect created by the insolvency of one commodity or security firm from spreading to other firms and possibly threatening the collapse of the affected industry. Accordingly, Judge Craig deemed section 546(e) inapplicable to transactions concerning the settlement of privately held securities.

Moreover, the consequences of the *Contemporary Industries* and *Plassein* decisions were expressly recognized by Judge Craig, who observed that if the term "settlement payment" is construed to encompass any payment made for securities, whether or not involving a public securities market, then any leveraged buyout, if structured as a direct purchase of stock from the shareholders, would fall within section 546(e)'s safe harbor and effectively nullify the extensive body of case law under which LBOs have been challenged and analyzed for fairness and adequacy of consideration.

As illustrated by the foregoing, the application of the settlement payment defense in the context of an LBO has been far from uniform. Accordingly, the extent to which wire transfers may insulate LBO payments from attack appears to hinge more on the venue of the bankruptcy proceeding than on the facts of the transaction at issue. The Third Circuit's ruling on the *Plassein* appeal will certainly be an important decision to unsecured creditors of the many chapter 11 debtors who file in Delaware, and we will certainly address that decision once it is rendered. •

GOOD FAITH FINDINGS

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The Court reasoned that the purpose of this provision is to encourage lenders to extend credit to debtors in bankruptcy by eliminating the risk that any lien securing the loan will be modified on appeal.

The Court was also not persuaded by Keltic's argument that a stay pending appeal was unnecessary in the absence of an explicit finding by the bankruptcy court than Chittenden had acted in good faith. The Court reasoned that because section 364(e) does not require such a finding as a condition to its effectiveness, a lender's good faith should be presumed subject to rebuttal by a challenging party. Noting that the record included findings by the bankruptcy court that Chittenden had acted without collusion or violation of the terms of the prepetition auction, the Court inferred good faith on the part of Chittenden.

This decision reinforces the important notion that a party seeking to appeal a post-petition financing order must first obtain a stay of the order pending appeal in order to avoid dismissal of the appeal on grounds of mootness, irrespective of whether an explicit determination of the lender's good faith is made by the bankruptcy court. •

SALE OF GENERAL MOTORS

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New GM (such as product liability claims arising from post-sale accidents regardless of when the vehicles involved were purchased). Judge Gerber explained that while the Circuit Courts are split on the issue of whether section 363 provides a basis for "free and clear" sales, the Second Circuit has unequivocally empowered bankruptcy courts to approve such sales where the purchaser does not and would not voluntarily agree to accept successor liability. Noting that such a result is particularly warranted in cases such as GM where the proposed purchase price would be significantly lower if the buyer were forced to assume pre-existing liabilities, Judge Gerber approved the sale free and clear of all unassumed successor liabilities, including the significant tort and asbestos claims against Old GM which, as a result, could only be satisfied from any remaining sale proceeds received by Old GM and not from the assets of New GM.

Numerous scholars and legal commentators have attributed the SDNY's approval of this 39-day sale process to the central roles played by the U.S. and Canadian governments in financing the GM case. Certainly, the role played by government in expediting the GM and Chrysler sale processes, and the substantial public attention paid to these cases under the looming shadow of a failed domestic automotive industry, should not be discounted. However, the sale procedures and time frames approved in the GM and Chrysler cases should come as no surprise to those who have followed the cases of other retailers who have liquidated or sold their businesses outside the context of a chapter 11 plan over the past few years. In reality, the GM and Chrysler sales have only perpetuated the now common practice of resolving retail chapter 11 cases through section 363 sales, since few, if any, retailers today possess the financial ability or support to emerge from bankruptcy as reorganized entities. •

Retail Bankruptcy Round-Up

The following cases are retail chapter 11 bankruptcies that were filed within the last several months. Cooley Godward Kronish represents the Creditors' Committee in many of these cases (please see sidebar for summaries of current representations).

Case Name	Petition Date	Case Number	Bankruptcy Court
Drug Fair	March 18, 2009	09-10897	D. Del. (Wilmington)
Active Ride Shop	March 23, 2009	09-15370	C.D. Ca. (Riverside)
BI-LO	March 23, 2009	09-02140	D. S.C. (Columbia)
Mark Shale	March 23, 2009	09-09825	N.D. Ill. (Chicago)
Sportsman's Warehouse	March 24, 2009	09-10990	D. Del. (Wilmington)
Big 10 Tire Stores, Inc.	April 3, 2009	09-11173	D. Del. (Wilmington)
Ultra Stores	April 9, 2009	09-11854	S.D.N.Y. (Manhattan)
Z Gallerie	April 10, 2009	09-18400	C.D. Ca. (Riverside)
Fred Leighton Holdings	April 14, 2009	08-11363	S.D.N.Y. (Manhattan)
Filene's Basement	May 4, 2009	09-11525	D. Del. (Wilmington)
Bachrach	May 7, 2009	09-12918	S.D.N.Y. (Manhattan)
Stock Building Supply	May 8, 2009	09-11572	D. Del. (Wilmington)
Furniture-In-Parts Corp (Door Store)	May 28, 2009	09-13399	S.D.N.Y. (Manhattan)
Anchor Blue	May 29, 2009	09-11770	D. Del. (Wilmington)
Oilily USA	May 29, 2009	09-13464	S.D.N.Y. (Manhattan)
EJ's Shoes Inc.	June 5, 2009	09-45350	E.D. Mo. (Saint Louis)
Berean Christian Stores	June 8, 2009	09-13640	S.D. Oh. (Cincinnati)
Eddie Bauer	June 17, 2009	09-12099	D. Del. (Wilmington)
Crabtree & Evelyn	July 1, 2009	09-14267	S.D.N.Y. (Manhattan)
Golfer's Warehouse	July 10, 2009	09-21911	D. CT. (Hartford)
Basha's	July 13, 2009	09-16050	D. A.Z. (Phoenix)
Finlay Fine Jewelry	August 5, 2009	09-14873	S.D.N.Y. (Manhattan)

Road to Recovery

Our list of Creditors' Committees is a mile long....

▶ Gottschalks

▶ The Sharper Image
Successful auction to save the brand

▶ Ritz Cameras

▶ Bob's Stores
Creative Asset Disposition; 98.5% recovery for unsecured creditors

▶ Filene's Basement
Successful sale as a going concern for $41 million more than the stalking horse bid

▶ Eddie Bauer
Successful sale as a going concern, plus the assumption of hundreds of millions of dollars in liabilities

▶ Loehmann's
Successful stand alone reorganization with 100% payout to unsecured creditors

▶ Montgomery Ward
Obtained over $80 million settlement with GE for creditors

▶ Boscov's
Successful sale as a going concern

▶ Hancock Fabrics
First successful retail reorganization since the 2005 amendments to the Bankruptcy Code with a recovery of 100% plus interest for unsecured creditors

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