YOUNG CONAWAY STARGATT & TAYLOR, LLP

SDNY BANKRUPTCY TREND WATCH

Young Conaway is pleased to provide you with the current edition of SDNY Bankruptcy Trend Watch, a service from Young Conaway that is designed to identify emerging trends in restructuring and bankruptcy law that will impact your practice and the business of your clients. This edition will focus on recent Southern District of New York bankruptcy court decisions pertaining to issues affecting private equity funds and lenders. We hope that you will find the SDNY Bankruptcy Trend Watch helpful and, as always, we are happy to field any comments or questions that you may have regarding the issues addressed in this SDNY Bankruptcy Trend Watch or the restructuring practice generally.

COURT AFFIRMS SECOND LIEN LENDERS' STANDING TO CONTEST SALE, BUT OVERRULES OBJECTIONS WITH RESPECT THERETO

In re Boston Generating, LLC, 440 B.R. 302 (Bankr. S.D.N.Y. 2010)

The Bankruptcy Court found that a secured lender's waiver of its right to object to an asset sale must be "clear beyond peradventure," particularly in the context of a sale that would effectively deprive the second lien lenders of the opportunity to vote on a plan. Despite obtaining standing to contest the sale transaction, the second lien lenders' objections were overruled and the sale was approved.

FRAUD CLAIMS STAND AGAINST LENDERS WITH ACTUAL KNOWLEDGE OF SCHEME

Buchwald Capital Advisors LLC v. JP Morgan Chase Bank, N.A. (In re M. Fabrikant & Sons, Inc.), 447 B.R. 170 (Bankr. S.D.N.Y. 2011)

The Bankruptcy Court dismissed certain fraudulent conveyance claims against the debtor's lenders because the lenders were not intimately involved in planning the fraudulent transactions and, as a result, did not have actual or constructive knowledge. The court refused to dismiss other claims because the lenders demonstrated actual knowledge of the debtor's fraudulent scheme.

COURT REFUSES TO DISTURB FINALITY OF SALE ORDER

In re Lehman Bros. Holdings Inc., 445 B.R. 143 (Bankr. S.D.N.Y. 2011)

The Bankruptcy Court denied the Rule 60(b) motions and held that it would have approved the sale of the debtors' assets regardless of additional information that came to light after the sale was approved because there was no better alternative and significantly, the sale saved thousands of jobs in a troubled industry. The court noted that sale orders should not be disturbed unless "truly special circumstances warrant judicial intervention."

SALE ORDER INSUFFICIENT TO SHIELD PURCHASER FROM

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About Young Conaway Stargatt & Taylor, LLP

Young Conaway Stargatt & Taylor, LLP, one of Delaware's largest law firms, counsels and represents national, international and local clients, handling sophisticated advisory and litigation matters involving bankruptcy, corporate law and intellectual property. Young Conaway also guides regional businesses and individuals through a myriad of employment, real estate, tax, estate planning, environmental, and banking issues from the

SUCCESSOR LIABILITY TO UNIDENTIFIED FUTURE CREDITORS

Morgan Olson, LLC v. Frederico (In re Grumman Olson Indus.), 445 B.R. 243 (Bankr. S.D.N.Y. 2011)

The Bankruptcy Court held that the purchaser of a debtor's assets was not exonerated from potential successor liability for injuries caused by any product sold prior to the sale, despite language in the sale order to the contrary, and left the resolution of whether the purchaser was actually liable as a successor to the debtor to the state court.

COURT STYMIES CREDITOR'S PURSUIT OF EQUITABLE SUBORDINATION CLAIMS

Lyme Regis Partners, LLC v. Icahn (In re Blockbuster Inc.), Ch. 11 Case No. 10-14997, Adv. Proc. No. 10-05524, 2011 Bankr. LEXIS 1025 (Bankr. S.D.N.Y. Mar. 17, 2011)

The Bankruptcy Court held that an individual creditor can only pursue an equitable subordination claim if it suffers a "particularized injury," defined as an "injury significantly different from the injuries to creditors in general."

COURT HOLDS § 546(e) SAFE-HARBOR PROVISION DOES NOT APPLY TO PRIVATE LBOs

Geltzer v. Mooney (In re Macmenamin's Grill Ltd.), 450 B.R. 414 (Bankr. S.D.N.Y. 2011)

The Bankruptcy Court held that § 546(e)'s safe harbor provision did not apply to a private leveraged buyout; concluding that § 546(e) was inapplicable because of the small size of the transactions involved, the lack of any evidence that the parties were acting as participants in a securities market, and because avoiding the transfers would not threaten the functioning of any securities market.

PARENT OWES FIDUCIARY DUTY TO SUBSIDIARY WITH MINORITY SHAREHOLDERS

Tronox Inc. v. Anadarko Petroleum Corp. (In re Tronox Inc.), 450 B.R. 432 (Bankr. S.D.N.Y. 2011)

The Bankruptcy Court found that, as the parent of a subsidiary with minority shareholders and the parent of an insolvent subsidiary, the debtor's former parent owed fiduciary duties to the debtor. In addition, the court found that the parent may have owed fiduciary duties to the debtor as a promoter due to certain actions taken by the former parent related to the debtor's IPO.

LENDER WITHOUT ACTUAL OR CONSTRUCTIVE KNOWLEDGE OF FRAUDULENT SCHEME OF DEBTOR NOT LIABLE

Gowan v. Wachovia Bank, N.A. (In re Dreier LLP), 453 B.R. 499 (Bankr. S.D.N.Y. 2011)

The Bankruptcy Court found that a supermajority of the lender's liens and obligations were not subject to avoidance because the lender had no actual or constructive knowledge of the debtor's scheme. However, with respect to one $9 million loan, the court concluded that the trustee's allegations could support an inference that the lender had knowledge of the debtor's fraudulent scheme because the lender deposited the proceeds into an account that did not belong to the debtor.

COURT UPHOLDS LIEN ON ECONOMIC VALUE OF FCC LICENSES

Sprint Nextel Corp. v. U.S. Bank Nat'l Ass'n (In re Terrestar Networks, Inc.), 457 B.R. 254 (Bankr. S.D.N.Y. 2011)

The Bankruptcy Court recognized the distinction between a private right to grant liens on the economic value of an FCC license and the public right to regulate the license itself, and held that the noteholders' lien on the economic value of the licenses was valid.

EXPRESS RESERVATION OF BANKRUPTCY COURT JURISDICTION DOES NOT ENSURE BANKRUPTCY COURT CONSIDERATION

In re Motors Liquidation Company, 457 B.R. 276 (Bankr. S.D.N.Y. 2011)

The Bankruptcy Court abstained from deciding the dispute between a union and a purchaser of the debtors' assets because: (1) the controversy would not affect the debtors' chapter 11 cases; (2) the bankruptcy judge did not possess any particular knowledge warranting exercise of exclusive jurisdiction; and (3) the federal district court could decide the controversy at least as well as the bankruptcy court.

COURT AFFIRMS ABILITY OF BUYER TO PURCHASE CAUSES OF ACTION AGAINST DEBTORS' OFFICERS/DIRECTORS/AGENTS

In re Grubb & Ellis Co., Ch. 11 Case No. 12-10685, 2012 Bankr. LEXIS 1279 (Bankr. S.D.N.Y. Mar. 27, 2012)

The Bankruptcy Court held that inclusion of the debtors' causes of action in a stalking horse bid was proper because the causes of action were an "integral part" of the stalking horse bidder's offer and the deal was structured in a way that allowed the debtors and the stalking horse bidder to share any proceeds from the causes of action.

COURT DISMISSES CERTAIN CLAIMS AGAINST OFFICERS AND DIRECTORS BECAUSE CAUSATION COULD NOT BE ESTABLISHED DUE TO INTERVENING FRAUD

Fox v. Koplik (In re Perry H. Koplik & Sons, Inc.), Ch. 11 Case No. 02-B-40648, Adv. Pro. 04-02490, 2012 Bankr. LEXIS 1649 (Bankr. S.D.N.Y. Mar. 30, 2012)

After a trial was held, the Bankruptcy Court ruled that the debtor's officers and directors were not liable for breaches of the duties of care stemming from loans made to the debtor's customer because, while the officers' and directors' conduct was "outrageous" and they clearly failed to act with due care, causation could not be established because the customer's financial statements were fraudulent. Thus, the trustee failed to establish that the directors' and officers' lack of care caused the losses resulting from the loans made to the customer.

The court did find the directors and officers liable for violations of their duties of care relating to trade insurance and knowing violations of the debtor's revolver, as well as violations of duties of care and loyalty for forgiveness of loans against the directors and officers.

DISTRICT COURT ENFORCES § 546(e) EXEMPTION

Official Comm. of Unsecured Creditors of Quebecor World (USA) Inc. v. Am. United Life Ins. Co. (In re Quebecor World (USA) Inc.), No. 11 Civ. 7530 (JMF), 2012 U.S. Dist. LEXIS 141141 (S.D.N.Y. Sept. 28, 2012)

The district court affirmed the bankruptcy court's holding with respect to a payment by a debtor to purchase notes issued by an affiliate, finding that the noteholders were shielded from liability pursuant to § 546(e) of the Bankruptcy Code because the payment represented a "settlement payment" and a "transfer in connection with a securities contract." The creditors' committee argued that the payment did not qualify as a settlement payment for the purposes of § 546(e) because a formal settlement process was not used and the financial institution involved in the transaction was merely an "intermediary or conduit." However, the district court rejected these arguments, finding that nothing in § 546(e) requires the use of a formal settlement system or that financial institutions have a beneficial interest in the transferred funds. According to the district court, a settlement payment is simply a transfer of cash to a financial institution made to complete a securities transaction, and the debtor's payment fell squarely within this definition. Moreover, the district court concluded that the transaction at issue was made in connection with a securities contract, which is defined as a contract for the purchase, sale or loan of a security. Although the debtor initially structured the transaction as redemption, it ultimately decided to restructure the deal as a purchase of the notes.

COURT RULES THAT THE "FAIR MARKET" METHOD MUST BE USED TO VALUE ASSETS SOLD IN DEBTORS' BANKRUPTCY

In re Motors Liquidation Co., Ch. 11 Case No. 09-50026 (Bankr. S.D.N.Y. Oct. 16, 2012).

A dispute arose between the purchaser of the debtors' assets and certain secured creditors regarding the method used to value the secured creditors' collateral for the purposes of determining the amount of their secured claims. The bankruptcy court held that where property has been subject to a sale process, the fair market method must be used to determine the value of such property. The court rejected the secured creditors' argument that the sale was a "fiction" in light of the purchaser's use of the collateral in connection with its continuation of the debtors' business. Instead, the court found that the debtors sold the collateral to a separate (although related) legal entity and, therefore, the fair market method must be used to calculate the value of the collateral.

COURT APPROVES COUNSEL FEES FOR LENDER IN CONTESTED CHAPTER 11 PROCEEDING

T-Bone Rest. LLC v. Gen. Elec. Capital Corp. (In re The Glazier Grp.), No. 10-16099, Adv. No. 12-01878, 2012 BL 315376 (Bankr. S.D.N.Y. Nov. 30, 2012) (Gropper, J.).

Plaintiffs sought a declaratory judgment that attorneys' fees sought by the defendant, a lender, in connection with the debtor's chapter 11 proceeding were unreasonable and should be disallowed or reduced. The defendant/lender counterclaimed and filed a third-party complaint for the additional attorneys' fees that arose in connection with the defendant's defense against the declaratory judgment action. The court denied the plaintiffs' motion to dismiss the counterclaims and third-party claims, holding that (i) the loan agreement clearly applied to disputes among the parties to the agreement based on broad indemnification language included throughout and (ii) the payoff letter was clearly limited to claims that arose up to the date of the payoff letter and did not limit the lenders right to indemnification for claims that arose after that date.

If you have any questions or would like to discuss the decision further, please contact any of the Bankruptcy and Corporate Restructuring partners at Young Conaway. The Firm is also available for complimentary Delaware Update CLE programs to address any aspects of Delaware law that are of interest to our friends and colleagues around the country.