UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re	:	Chapter 11
WASHINGTON MUTUAL, INC., *et al.*,[1]	:	Case No. 08-12229 (MFW)
Debtors.	:	Jointly Administered

POST-CONFIRMATION HEARING BRIEF OF THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS IN SUPPORT OF CONFIRMATION (ISSUES OTHER THAN ALLEGED INSIDER TRADING)

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Dated: Wilmington, Delaware
August 10, 2011

[1] The Debtors in these chapter 11 cases (the "Chapter 11 Cases") and the last four digits of each Debtor's federal tax identification numbers are: (i) Washington Mutual, Inc. (3725) and (ii) WMI Investment Corp. (5395).

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The Official Committee of Unsecured Creditors (the "Creditors' Committee") of Washington Mutual, Inc., *et al*. (the "Debtors") respectfully submits this post-Confirmation Hearing brief in support of confirmation of the Modified Plan (as defined below).[2] In a separate brief being filed today, the Creditors' Committee sets forth its post-Confirmation Hearing closing arguments regarding allegations of insider trading by certain creditors. This brief addresses: (1) jurisdiction; (2) post-petition interest; (3) classification of the PIERS; (4) release, injunction and exculpation provisions; and (5) valuation.

PRELIMINARY STATEMENT

1. When this Court issued its January 7, 2011 opinion denying confirmation of the Debtors' Sixth Amended Plan (D.I. # 6528) (the "Confirmation Opinion" or "Conf. Op."), *In re Washington Mut., Inc.*, 442 B.R. 314 (Bankr. D. Del. 2011) the Court approved the Global Settlement Agreement underlying the Sixth Amended Plan but identified specific elements of the plan that required amendment. The Modified Plan resolves the Court's open issues and meets the requirements for confirmation under 11 U.S.C. § 1129, as demonstrated in the Creditors' Committee's pre-Confirmation Hearing brief (D.I. # 8140), the Debtors' Memorandum of Law in Support of Confirmation of the Modified Plan (D.I. # 8121), and the evidence adduced in the Confirmation Hearing. Specifically, the Modified Plan (a) properly provides for the payment of post-petition interest at the applicable contract rates; (b) properly classifies the PIERS as debt; (c) properly tailors the releases and related injunction and exculpation provisions in accordance with the Confirmation opinion; and (d) properly values Reorganized WMI. Accordingly, Creditors' Committee strongly supports the Modified Plan. The Modified Plan should be promptly

[2] Capitalized terms not defined herein shall have the meaning ascribed to them in the Creditors' Committee's Memorandum of Law In Response to Certain Objections to Confirmation of the Debtors' Modified Sixth Amended Plan of Reorganization (the "Pre-Trial Brief") (D.I. # 8140).

confirmed and effectuated, and more than $7 billion in value thereby should be delivered to creditors without further delay.

STATEMENT OF FACTS[3]

2. On February 8, 2011, the Debtors filed their Modified Sixth Amended Joint Plan of Affiliated Debtors Pursuant to Chapter 11 of the United States Bankruptcy Code (the "Modified Plan") (D.I. # 6696).

3. Creditors have voted overwhelmingly in favor of approval of the Modified Plan. *See* DX-403, Corrected Declaration of Robert Q. Klamser with Respect to the Tabulation of Votes on and Elections Pursuant to the Modified Plan, ¶¶ 22-24 (D.I. # 8113). Numerous parties (the "Objecting Parties"), however, have objected to certain aspects of the Modified Plan.

4. Over the course of seven days from July 13, 2011 through July 21, 2011 (the "Confirmation Hearing"), the Court received testimony and admitted into evidence many exhibits regarding, among other things, the Modified Plan's compliance with 11 U.S.C. § 1129, including the value of Reorganized WMI, and regarding allegations of insider trading against the Settlement Noteholders.

ARGUMENT

I. THIS COURT HAS JURISDICTION TO CONFIRM THE MODIFIED PLAN

5. The TPS Consortium attempts to derail the long-awaited resolution of these chapter 11 cases by cynically challenging this Court's jurisdiction to confirm the Modified Plan on two independent bases: First, it argues that its pending appeal (the "TPS Appeal") of this Court's January 7, 2011 order granting the Debtors summary judgment in the TPS Consortium's adversary proceeding (No. 10-51387, D.I. # 180) (the "TPS Order"), *In re Washington Mut., Inc.*,

[3] The Creditors' Committee hereby incorporates by reference the Statement of Facts included in its Pre-Trial Memorandum.

442 B.R. 297 (Bankr. D. Del. 2011) divests this Court of jurisdiction to confirm the Plan until the TPS Appeal is resolved. Supplemental Objection of the TPS Consortium ("TPS Consortium Supp. Obj.") (D.I. # 7480). Second, the TPS Consortium argues that this Court lacks jurisdiction to approve the Amended Global Settlement Agreement ("Amended GSA") – which incorporates the settlement of a number of non-core claims unrelated to the TPS Appeal – under the United States Supreme Court's recent decision in *Stern v. Marshall*, 564 U.S. ___, 131 S. Ct. 2594, 79 USLW 4564 (June 23, 2011). Second Supplemental Objection of the TPS Consortium ("TPS Consortium Second Supp. Obj.") (D.I. # 8100). The TPS Consortium is wrong on both arguments.

A. The TPS Appeal Does Not Divest this Court of Jurisdiction

6. As this Court determined in the TPS Order, the TPS were automatically transferred to WMI in exchange for new Depositary Shares (the "Conditional Exchange") following the direction of the Office of Thrift Supervision ("OTS") made on September 25, 2008. *In re Washington Mut., Inc*., 442 B.R. at 300-01. WMI commenced its chapter 11 cases on September 26, 2008 and proceeded to dispute ownership of certain assets, including the TPS, with JPMorgan Chase Bank, N.A. ("JPMC") and the Federal Deposit Insurance Corporation ("FDIC"), in its corporate capacity and as receiver for Washington Mutual Bank ("WMB"). *Id*. After WMI, JPMC, the FDIC and other parties reached a global settlement, the TPS Consortium filed an adversary proceeding in this Court seeking, *inter alia*, a declaration that its members – and not WMI or JPMC – were the owners of the TPS, notwithstanding the OTS's actions and the terms of the underlying documents. *Id*. at 301.

7. This Court considered and rejected the TPS Consortium's theory that, because of the alleged failure of certain conditions precedent, the Conditional Exchange never occurred. 442 B.R. at 302-03. The TPS Consortium appealed to the District Court, challenging this

Court's determination that "the Conditional Exchange occurred" and that "title to (ownership) of the Trust Preferred Securities transfer[red] to WMI" as a result. TPS Consortium's Reply Brief on Appeal at 1 (D. Del., No. 11-124, D.I. #41). The TPS Consortium made no effort to obtain a stay pending the TPS Appeal.

8. Having failed to obtain a stay, the TPS Consortium now faces the prospect that the TPS Appeal may be rendered equitably moot when the Modified Plan is confirmed. *See, e.g., W. End Assocs., L.P. v. Sea Green Equities*, 166 B.R. 572, 575 (D.N.J. 1994) (where appeal is taken pursuant to a bankruptcy court order but a stay pending the appeal is not secured, "an appellate court is powerless to grant effective relief, and the appeal must be considered moot.") In a last-ditch effort to avoid this outcome, the TPS Consortium seeks to persuade this Court that it is jurisdictionally barred from approving the Global Settlement and confirming the Modified Plan. Specifically, the TPS Consortium asserts that this Court cannot approve settlement of the TPS claims or order any party to take steps to perfect the Conditional Exchange. TPS Consortium Supp. Obj. at 12-13 (asserting that this Court lacks jurisdiction because "the actions contemplated in the Modified Plan are identical to the issues that are central in the pending appeal.").

9. The TPS Consortium recognizes that this Court retains jurisdiction to "implement[] or enforce[] the order appealed" in the absence of a stay, though it may not "alter" it. *Id*. at 10 (citing *In re Winimo Realty Corp*., 270 B.R. 99, 105-06 (S.D.N.Y. 2001)); *see also In re Padilla*, 222 F.3d 1184, 1190 (9th Cir. 2000) ("Absent a stay . . . the trial court . . . retains jurisdiction to implement or enforce the judgment or order but may not alter or expand upon the judgment."); *In re VII Holdings Co*., 362 B.R. 663, 666 (Bankr. D. Del. 2007) (courts "retain jurisdiction to decide issues and proceedings different from and collateral to those involved in

the appeal" in the absence of a stay) (citations omitted); *DiCola v. Am. S.S. Owners Mut. Prot. and Indem. Ass'n (In re Prudential Lines, Inc.)*, 170 B.R. 222, 243 (S.D.N.Y. 1994) ("while an appeal of an order or judgment is pending, the court retains jurisdiction to implement or enforce the order or judgment.").

10. Accordingly, the TPS Consortium argues that the Modified Plan requires this Court to alter or amend the appealed judgment rather than merely implement or enforce it. TPS Consortium Supp. Obj. at 12-13. As noted above, however, the TPS Consortium's appeal challenges this Court's determination that title to ownership of the TPS transferred to WMI when the OTS effected the Conditional Exchange. TPS Consortium Reply Brief on Appeal at 1. Neither approval of the settlement nor confirmation of the Modified Plan would require this Court to alter or amend (or even revisit) its decision that ownership of the TPS passed from the TPS Consortium when its shares were "exchanged" for Depositary Shares pursuant to the Conditional Exchange.[4]

11. The cases on which the TPS Consortium primarily relies, *In re Whispering Pines Estates*, 369 B.R. 752 (B.A.P. 1st Cir. 2007), and *Winimo Realty*, 270 B.R. 99, are inapposite because they specifically concern bankruptcy court actions that actually altered or amended – or threatened to alter or amend – decisions pending appeal. TPS Supp. Obj. 9-11. In *Whispering Pines*, a bankruptcy court confirmed a plan of reorganization that required the bankruptcy trustee to sell certain mortgaged assets by a specific date. After the confirmation order was appealed, the bankruptcy court entered a new order allowing the mortgage lender to foreclose on the same property. The Bankruptcy Appellate Panel ruled that the bankruptcy court lacked jurisdiction to

[4] Section 2.3 of the Global Settlement Agreement (to which the TPS Consortium cites or refers at TPS Consortium Supp. Obj. at 5, 12-13) merely sets forth the means by which the TPS shall be transferred from WMI to JPMC. It thus cannot be construed as an injunction to "alter," "amend," or "expand" this Court's TPS Order, which determined that the TPS were the property of WMI.

enter the subsequent order because it was at odds with the confirmation order being appealed. 369 B.R. at 754-55, 760-61. In *Winimo Realty*, the District Court ruled, in keeping with Federal Arbitration Act ("FAA") § 16(a), that the appeal of an order denying a motion to compel arbitration divested the bankruptcy court of jurisdiction to litigate issues that the appellant sought to arbitrate. 270 B.R. at 107-08; *see Ehleiter v. Grapetree Shores, Inc.*, 482 F.3d 207, 215 (3d Cir. 2007) (§ 16(a) of the FAA "automatically deprives the trial court of jurisdiction to proceed until such time as the appeal is fully litigated or determined to be frivolous or forfeited"). Here, by contrast, (i) neither the FAA nor any other statute depriving this Court of jurisdiction is at issue, and (ii) there is no reason why confirmation of the Modified Plan would require re-litigation of, or is inconsistent with, the Court's order in the TPS adversary proceeding.

12. The TPS Consortium also relies on an outlier case from the Middle District of Florida, *In re Demarco*, 258 B.R. 30 (Bankr. M.D. Fla. 2000). There, the Internal Revenue Service (the "IRS") argued that a Florida bankruptcy court lacked jurisdiction to rule on plan confirmation until the District Court decided the IRS's appeal challenging rejection of its claim. The bankruptcy court agreed, observing that the IRS's appeal could be dismissed as moot if the plan were consummated before the appeal was heard. 258 B.R. at 33-34. Yet the *Demarco* court's jurisdictional ruling was simply wrong; the possibility that the IRS's appeal might be mooted did not deprive the bankruptcy court of jurisdiction to rule on a plan consistent with the order being appealed. *See, e.g., Matter of Eddington Thread Mfg. Co., Inc.*, 189 B.R. 898, 903 (E.D. Pa. 1995) (although "[t]here is no general requirement in the Bankruptcy Code that an aggrieved party must obtain a stay pending appeal," failure to do so means "that the prevailing party may treat the order as final," and "actions might occur which cannot be reversed," potentially mooting the appeal) (citation, internal quotations, and emphasis omitted); *In re*

Genesis Health Ventures, Inc., 280 B.R. 339, 343-44 (D. Del. 2002) (citing *In re Chateaugay Corp*., 988 F.2d 322, 326 (2d Cir. 1993) for the proposition that "the party who appeals without seeking to avail himself of that [stay] protection does so at his own risk"); *In re Continental Airlines*, 91 F.3d 553, 565-66 (3d Cir. 1996) *(en banc*) (where equitable mootness is a possibility, it is "incumbent" on appellants to try to obtain a stay).

13. In sum, this Court can and should implement the TPS Order and proceed with confirmation. It should reject the TPS Consortium's meritless jurisdictional argument, which is nothing more than a thinly veiled attempt to get the stay it failed to seek or obtain under Bankruptcy Rule 8005.

B. *Stern v. Marshall* Does Not Deprive this Court of Jurisdiction to Confirm the Modified Plan

14. The TPS Consortium also argues that this Court cannot approve the Amended GSA or confirm the Modified Plan because, under *Stern*, bankruptcy courts lack jurisdiction to approve settlement of non-core claims. TPS Consortium Second Supp. Obj. at 10-19; *see id*. at 5, 18-19 (listing claims asserted by WMI, which WMI now seeks to resolve through the Amended GSA[5]). *Stern*, however, says nothing of the sort. Although *Stern* may stand for the proposition that a bankruptcy court lacks jurisdiction to render final adjudication of certain counterclaims, this Court's approval of the Amended GSA is an approval of a compromise, not a final adjudication of a counterclaim.

15. In *Stern*, the United States Supreme Court considered a chapter in the dispute between the estate of debtor Vickie Lynn Marshall and the estate of Pierce Marshall, the son of

[5] The Consortium makes no argument that this Court may not approve settlement of claims related to the TPS. Nor could it. *Stern* says nothing that would call into question a bankruptcy court's authority to approve settlement of claims involving property of the debtor's estate (or even to adjudicate them). *See, e.g., In re Salander O'Reilly Galleries*, No. 07-30005, 2011 WL 2837494, *7, 11 (Bankr. S.D.N.Y. July 18, 2011) (*Stern* did not affect bankruptcy court's authority to determine whether painting belonged to the debtor's estate).

Vickie's late husband, J. Howard. After Pierce filed a proof of claim against Vickie for defamation in the bankruptcy court, Vickie filed a counterclaim against Pierce for tortious interference with the gift she expected from J. Howard. 131 S. Ct. at 2601. The bankruptcy court dismissed Pierce's claim and awarded Vickie damages on her counterclaim. The Ninth Circuit reversed the bankruptcy court's damages award, *id*. at 2602, and the Supreme Court affirmed. According to the Supreme Court, the judgment in Vickie's favor had to be reversed because the bankruptcy court "lacked the constitutional authority to enter a final judgment on a state law counterclaim that [was] not resolved in the process of ruling on a creditor's proof of claim." *Id*. at 2620.

16. Although all counterclaims brought in the bankruptcy court are designated "core" proceedings under 28 U.S.C. § 157(b)(2)(C), the Supreme Court held that Vickie's counterclaim must be "remove[d] . . . from core bankruptcy jurisdiction," 131 S. Ct. at 2620, because it did not "stem from the bankruptcy itself" and would not "necessarily be resolved in the claims allowance process," *id*. at 2618; *see id*. at 2611, 2617. The Supreme Court did not venture beyond its "narrow" determination that Congress overstepped constitutional bounds in "one isolated respect"; indeed, the Court admonished that its decision should not "meaningfully change[] the [existing] division of labor" between bankruptcy judges and Article III judges. *Id*. at 2620.

17. By no means, then, can *Stern* be read to limit the bankruptcy courts' well-established authority to approve the settlement of claims belonging to the debtor under the Bankruptcy Code, 11 U.S.C. § 1123(b)(3), and Bankruptcy Rule 9019.[6] *See, e.g.*, Conf. Op. at 16 ("The approval of a settlement under Rule 9019 of the Federal Rules of Bankruptcy

[6] Section 1123(b)(3) provides that "a plan . . . may provide for settlement of claims and interests belonging to the estate." Rule 9019 provides that "the [bankruptcy] court may approve a compromise or settlement."

Procedure is committed to the discretion of the bankruptcy court.") (citing *Key3Media Group, Inc. v. Pulver.com Inc. (In re Key3Media Group Inc.)*, 336 B.R. 87, 92 (Bankr. D. Del. 2005)); *accord, In re World Health Alternatives, Inc.*, 344 B.R. 291, 296 (Bankr. D. Del. 2006). Indeed, it is universally recognized that "[c]ompromises are generally favored in bankruptcy" because they "help expedite case administration and minimize litigation." Conf. Op. at 16 (citing *Myers v. Martin (In re Martin)*, 91 F.3d 389, 393 (3d Cir. 1996) (citing 9 Collier on Bankruptcy ¶ 9019.03[1] (15th ed.1993))).

18. The TPS Consortium nevertheless offers a convoluted argument to suggest that *Stern* calls into question this longstanding and critical aspect of bankruptcy procedure. According to the TPS Consortium, *Stern* means that bankruptcy courts can no longer approve settlement of litigation involving any non-core causes of action, because settlement is the same as final adjudication. TPS Consortium Second Supp. Obj. at 14-19. As discussed above, *Stern* merely limits a bankruptcy court's authority to enter final judgment on a counterclaim that it has properly adjudicated, when that counterclaim is not one that "stems from the bankruptcy," or one that "would necessarily be resolved by the claims process." 131 S. Ct. at 2618. It does not cast into doubt the constitutionality of any aspect of the Bankruptcy Code or the Bankruptcy Rules, and says nothing about a bankruptcy court's authority to approve settlements of any kind.

19. The TPS Consortium's novel theory that settlement approval is tantamount to adjudication is simply unfounded. The TPS Consortium cites three types of cases to support its theory: (1) cases holding that a bankruptcy court's order approving a settlement must be based on a "full and fair assessment of the wisdom of the proposed compromise" (*Protective Comm. For Indep. Stockholders of TMT Trailer Ferry, Inc. v. Anderson (TMT Trailer)*, 390 U.S. 414, 424-25 (1968) and its progeny, cited in TPS Consortium Second Supp. Obj. at 16-17); (2) cases

holding that such orders are final for purposes of appeal (*Beaulac v. Tomsic (In re Beaulac)*, 294 B.R. 815, 818 (B.A.P. 1st Cir. 2003), and *Martin v. Pahiakos (In re Martin)*, 490 F.3d 1272, 1276-77 (11th Cir. 2007), cited in TPS Consortium Second Supp. Obj. at 14); and (3) cases holding that such orders are final for purposes of *res judicata* (remaining cases cited in TPS Consortium Second Supp. Obj. at 14-15). None of these cases stands for any novel proposition of law, nor any proposition identified nor even so much as hinted at by the Supreme Court in *Stern*. Expanding the Supreme Court's ruling in *Stern* to cover such situations would expressly contradict the Supreme Court's ruling that Congress overstepped its bounds "in one narrow respect."

20. In approving a settlement, it is undisputed that "the court must determine whether 'the compromise is fair, reasonable, and in the best interest of the estate.'" Conf. Op. at 17 (quoting *In re Louise's Inc.*, 211 B.R. 798, 801 (D. Del. 1997)). It is also undisputed that a bankruptcy settlement order itself may be "final" for the purposes of appeal, or so as to preclude parties or their privies from bringing suits based on claims discharged by settlement. *E.g.*, *In re Am. MetroComm Corp*., 303 B.R. 32, 34-35 (Bankr. D. Del. 2003). That does not mean that the underlying claims have been adjudicated.

21. As this Court has explained, in approving a settlement, "'it is not necessary for a bankruptcy court to conclusively determine claims subject to a compromise, nor must the court have all of the information necessary to resolve the factual dispute, for by so doing, there would be no need of settlement.'" *Key3Media Group*, 336 B.R. at 92 (quoting *In re Martin*, 212 B.R. 316, 319 (B.A.P. 8th Cir. 1997)). "In determining whether to approve a settlement, the court is not supposed to have a mini-trial on the merits, but should canvass the issues to see whether the settlement falls below the lowest point in the range of reasonableness." *Id*. at 93 (citing *In re*

Jasmine, Ltd., 258 B.R. 119, 123 (D.N.J. 2000)) (internal quotations omitted). As the Second Circuit has similarly stated, the responsibility of the bankruptcy judge is "*not to decide* the numerous questions of law and fact raised" by the objections, "but rather to canvass the issues and see whether the settlement falls below the lowest point in the range of reasonableness." *In re W.T. Grant Co.*, 699 F.2d 599, 608 (2d Cir. 1983) (internal quotations and alteration omitted) (emphasis added). Indeed, "requir[ing] the Bankruptcy Court to resolve claim objections before approving a settlement . . . would undermine the important policy of promoting settlements in bankruptcy proceedings by requiring the parties to litigate the very issues that the settlement seeks to resolve." *In re Kaiser Aluminum Corp.*, 339 B.R. 91, 94 (D. Del. 2006).[7]

22. In sum, this Court should reject the TPS Consortium's effort to create confusion about the *Stern* decision in a tactical effort to delay confirmation and implementation of the Modified Plan.

II. THE MODIFIED PLAN PROPERLY PROVIDES FOR THE PAYMENT OF POST-PETITION INTEREST

23. The Modified Plan properly provides for the payment of post-petition interest to creditors prior to the payment of claims subordinated pursuant to section 510(b), and for such post-petition interest to be paid at the applicable contract rate. Modified Plan §§ 1.151, 22.1, Ex. G. Several parties objected to these provisions in the Modified Plan. However, this Court already has held that (a) the payment priority scheme in section 726(a) of the Bankruptcy Code is

[7] It likewise has been held in other contexts that courts may approve the settlement of claims even when they lack authority to adjudicate them. In *Matsushita Elec. Indus. Co., Ltd. v. Epstein*, 516 U.S. 367, 381-83 (1996), for example, the United States Supreme Court rejected an argument that a state court could not approve settlement of an Exchange Act claim that could only be adjudicated by a federal court: "While it is true that the state court assessed the general worth of the federal claims in determining the fairness of the settlement, such assessment does not amount to a judgment on the merits of the claims." *Id.* at 383 (citing *TBK Partners, Ltd. v. Western Union Corp.*, 675 F.2d 456, 461 (2d Cir. 1982) ("Approval of a [stockholder class] settlement does not call for findings of fact regarding the claims to be compromised. The court is concerned only with the likelihood of success or failure; the actual merits of the controversy are not to be determined.") (citation omitted)); *see also United States v. Davis*, 5 F.3d 541 (unpublished table decision), 1993 WL 339760, at *1 (9th Cir. 1993) (rejecting argument that EEOC improperly "adjudicated" Title VII claims by administering settlement of those claims).

expressly subject to the subordination provisions of section 510; and (b) absent special circumstances, post-petition interest must be paid at the applicable contract rate. The record amply shows that no such special circumstances exist; to the contrary, the specific facts of this case support payment of interest at the contract rate. Furthermore, deviation from the contract rate will cause unintended consequences to creditors wholly unrelated to those who were accused of wrongdoing.

A. The Modified Plan Properly Provides for the Payment of Post-Petition Interest Prior to Claims Subordinated Under Section 510(b)

24. As explained in the Confirmation Order and the Pre-Trial Brief, when a chapter 11 debtor has sufficient assets to satisfy each claim of the type set forth under paragraphs (1), (2), (3) and (4) of section 726(a), the best interests of creditors test requires that the debtor must also pay post-petition interest on those claims before shareholders receive any distribution. Conf. Op. at 87-88 (citing 11 U.S.C. § 726(a)(5)); Pre-Trial Br., ¶¶ 23-26 (same).

25. WMI is such a debtor. No evidence was introduced at the Confirmation Hearing to refute that WMI has sufficient assets to satisfy allowed claims of the type set forth under paragraphs (1), (2), (3) and (4) of section 726(a), and none of the Objecting Parties has argued that WMI's unsecured creditors are not entitled to post-petition interest. Thus, the Modified Plan's provision for payment of post-petition interest is appropriate and mandatory under section 726(a)(5).

26. Furthermore, the Court already has ruled that post-petition interest should be paid prior to subordinated claims. Conf. Op. at 89 ("[t]he priority of distributions established under section 726(a) . . . is expressly subject to subordination under section 510."); *see also* Pre-Trial Br., ¶¶ 30-33 (explaining the significance of this ruling in the context of certain objections to plan confirmation). As the issue of the priority of distributions under the Bankruptcy Code is a

legal question that this Court has already answered, and there was no evidence introduced at trial that would impact the Court's determination, the Creditors' Committee will not re-address the issue here.[8]

B. Post-Petition Interest Should Be Paid At The Contract Rate

27. As a general rule, absent compelling equitable reasons that would warrant payment at the federal judgment rate ("FJR"), the proper rate of post-petition interest is the contract rate. Conf. Op. at 94; Pre-Trial Br., ¶ 27. Here, none of the facts in the record supports imposition of the FJR; to the contrary, the evidence adduced at the Confirmation Hearing demonstrates that the Court should enforce the contract rate.

28. In *In re Coram Healthcare Corp.*, 315 B.R. 321 (Bankr. D. Del. 2004), this Court provided a framework for identifying the types of equitable considerations that might justify imposition of the FJR. In *Coram*, three institutions owned 100% of the issuance of certain notes and acted in concert throughout the bankruptcy proceeding. 315 B.R. at 327. One of these institutions created an egregious conflict of interest that substantially delayed the debtors' restructuring and ultimate emergence from bankruptcy, during which time the noteholders would have been accruing a default rate of 15% interest on their notes. *Id.* at 343. The delays caused by the noteholders' behavior thereby increased the amount of post-petition interest accrued by the noteholders. *Id.* at 346-47. Based on these circumstances, the Court held that application of the FJR, as opposed to the high default contract rate, was appropriate. *Id.* at 346 (noting that "[i]t would be grossly unfair to pay the Noteholders default interest during [the] delay" that they caused).

[8]The Creditors' Committee reserves the right to raise and address this issue – or any other – at oral argument, if the Court deems oral argument necessary or appropriate.

29. As explained in the Creditors' Committee's separate post-Confirmation Hearing brief addressing alleged insider trading issues, the evidence elicited at trial did not establish insider trading or any other inequitable conduct by the Settlement Note Holders ("SNHs"). Moreover, there is no default rate for any of the funded debt, and there never was any allegation that inequitable conduct benefited all classes – or all holders of any class – of unsecured creditors. In contrast to *Coram*, where creditors benefited from the delay by earning default interest, further delay has only hurt the PIERS, who are required to pay up their recovery to senior creditors. Thus, there are no equitable circumstances here, such as those in *Coram*, that would warrant imposition of the FJR.

30. Yet even if such circumstances did exist, the remedy suggested in *Coram* would be entirely inappropriate in this case. In *Coram*, the only creditors impacted by the imposition of the FJR were the three institutions that held 100% of Coram's outstanding notes, all of which benefitted from the delay. Conversely, here there are thousands of individual creditors, and none outside of the four SNHs are alleged to have engaged in any wrongdoing. *See, e.g.*, DX-403, Corrected Declaration of Robert Q. Klamser With Respect to The Tabulation of Votes on and Elections Pursuant to the Modified Sixth Amended Joint Plan of Affiliated Debtors, ¶ 24 (stating that votes to accept the Modified Plan were received in 1,120 ballots on behalf of Senior Notes Claims, 487 ballots on behalf of Senior Subordinated Notes Claims, 5 ballots on behalf of CCB-1 Guarantees Claims, 4 ballots on behalf of CCB-2 Guarantees Claims, 213 ballots on behalf of PIERS Claims, and 145 ballots on behalf of General Unsecured Claims ("GUCs")). Nevertheless, the Objecting Parties seek to have the Court apply the FJR to all creditors' claims. Many of these creditors have not benefited at all from the long delay in these cases; in fact, the extended wait has nearly obliterated the PIERS' recovery. 7/14/2011 Hr'g Tr. at 49:2-4 (Mr.

Goulding: "The PIERS are subordinated to all other senior indebtedness, and therefore, the brunt of the delay and the change in value is borne almost exclusively by the PIERS").

31. Furthermore, application of the FJR to all creditors would cause unintended consequences to creditors unrelated to the SNHs. The impact of applying the FJR as compared to applicable contract rates was shown in the Debtors' Liquidation Analyses. DX-375, July 6, 2011 Updated Liquidation Analyses, at 4-5. Mr. Goulding, Vice President and Treasurer of WMI, testified that the payment of post-petition interest at the FJR as of the Petition Date – based on specified assumptions of the Effective Date and the quantity of GUCs ultimately allowed – would impact the recoveries of only the PIERS claims and the GUCs, because of intercreditor subordination agreements. 7/14/2011 Hr'g Tr. at 61:23-62:13. Under these particular assumptions, holders of PIERS Claims actually would receive a slightly higher recovery under the proposed application of the FJR. *Id.* at 82:18-22. The only class that would suffer a diminished recovery as a result of the application of the FJR, based on these assumptions, would be holders of GUCs. *Id.* at 170:6-9. There was not even an allegation that holders of GUCs did anything wrong, yet GUCs would be the group injured by an across-the-board application of the FJR.

32. Additionally, the evidence at the Confirmation Hearing demonstrated that the PIERS' recovery is highly sensitive to further delay. Mr. Goulding compared two liquidation analyses that he prepared: (i) the first was dated May 7, 2011, and assumed a June 30, 2011 effective date, *see* DX-254, Notice of Filing of Updated Liquidation Analyses, and (ii) the second was the July 6, 2011 Updated Liquidation Analyses referenced above, DX-375, which assumed an August 31, 2011 effective date. Mr. Goulding testified that the only difference between the two analyses was the shifting of the assumed effective date by two months.

7/14/2011 Hr'g Tr. at 43:14-21 (Goulding). He testified that the two month delay gave "rise to an additional two months of professionals fees and costs of the estate, as well as the continued accrual of post-petition interest for that two-month period." *Id.* at 44:1-4 (Goulding). As a result of the two month delay, the percentage of the PIERS' recovery on the basis of the PIERS' prepetition claim decreased from an estimated 43% to 35%. *Compare* DX-254 at 4, *with* DX-375 at 4. The percentage of the PIERS' total recovery, on the basis of the PIERS' prepetition and post-petition claims, decreased from an estimated 34% to 28%. *Id.*

33. Additionally, application of the FJR likely would lead to the unintended consequence of further delay and therefore, further erosion of recoveries of other junior creditors. If the Court were to decline to confirm the Modified Plan due to the interest rate feature, the Modified Plan would fail because it provides for post-petition interest to be paid at the contract rate. Modified Plan § 1.151. Mr. Goulding testified that if the Modified Plan is not confirmed, there likely will be at least a three- to four-month delay while another plan of reorganization is promulgated and voted on. 7/14/2011 Hr'g. Tr. at 171:2-8 (Goulding). Such a delay likely would cost the estate an additional $90 million to $120 million in operational expenses, professional fees, and continued accrual of post-petition interest. *Id.* at 171:9-17. In such a scenario, the PIERS' recovery would be significantly diminished, harming creditors unrelated to the SNHs. *Id.* at 171:18-172:5; *see* DX-375 at 5.

34. Application of the FJR also would have the unintended consequence of adding significant complexity and litigation to these already-complex and hotly-litigated chapter 11 cases. Imposition of the FJR will result in a scenario in which junior creditors will receive post-petition interest at one rate from the estate, but will be required to pay post-petition interest to senior creditors at a higher rate, pursuant to contractual subordination agreements that are

enforceable pursuant to section 510(a) of the Bankruptcy Code and applicable state law. If the Court imposes the FJR, litigation of these contractual subordination agreements is almost guaranteed to follow.[9]

35. Moreover, certain Objecting Parties have argued for imposition of a FJR as of a date other than the Petition Date, although the issue is not before the Court at this time. These arguments are entirely baseless. The Equity Committee does not cite a single case holding that the federal judgment rate as of the Effective Date should be applied. *See* Equity Committee Obj. at ¶¶ 72-73. Indeed, courts that have considered this issue have found that if the federal judgment rate is applied, it must be calculated as of the Petition Date. *E.g.*, *In re Chiapetta*, 159 B.R. 152, 161 (Bankr. E.D. Pa. 1993) (holding that "since a claim is like a judgment entered at the time of the bankruptcy filing, the applicable rate should be the federal judgment rate in effect at the time of the bankruptcy filing"); *In re Evans*, No. 10-80446C, 2010 WL 2976165, at *2 (Bankr. M.D.N.C. July 28, 2010) ("The date on which the applicable federal judgment rate is to be determined for purposes of section 726(a)(5) is the federal judgment rate in effect on the petition date."); *In re Gulfport Pilots Ass'n, Inc*., 434 B.R. 380, 392-93 (Bankr. S.D. Miss. 2010) (holding that if debtor was required to pay post-petition interest, creditor "would be entitled to post-petition interest [calculated as of] the date of the filing of the petition"); *see* 4 Norton Bankr. Law & Practice 3d § 85:7 (2008 & Supp. 2011).

[9] Courts have considered the complexity of calculating various contractual rates as a reason to impose the FJR, but complexity, in this case, clearly does not weigh in favor of the FJR. *Compare In re Cardelucci*, 285 F.3d 1231, 1236 (9th Cir. 2002) (declaring calculating appropriate rate for each investor would overwhelm otherwise simple process) *and In re Beguelin*, 220 B.R. 94, 101 (B.A.P 9th Cir. 1998) ("it is not hard to imagine the administrative nightmare that bankruptcy trustees would otherwise face if they were required to calculate a different interest rate, based on a different source of interest rate, for each creditor"), *with In re Fast*, 318 B.R. 183, 192 (Bankr. D. Colo. 2004) (holding that the contract rate was appropriate for, among other reasons, that it was "a small case, with a limited number of creditors, and the effort and difficulty in determining the contract rate and apply[ing] it [was] minimal"). Here, while the cases and amounts at issue are large, application of the contract rate is efficient and simple, because nearly all the required work and analysis was completed long ago.

36. Moreover, imposition of the FJR at the rate as of the Effective Date rather than the Petition Date would have an extremely detrimental effect on numerous classes of unsecured creditors. Mr. Goulding testified that if the FJR were applied at 0.25% rather than 1.95%, GUCs would be "very badly affected" because "their post-petition interest would be significantly reduced." *See* 7/14/2011 Hr'g Tr. 173:11:16 (Goulding). Likewise, holders of the PIERS would also be "very badly affected" because they would still have to pay interest up through subordination agreements at the contract rate. *See id.* at 173:17-19 (Goulding). It is even conceivable that holders of the CCBs would "have an impairment in their claim as a result of" the FJR being imposed at 0.25%. *See id.* at 173:20-24 (Goulding). With the FJR at 0.16% or lower, the recoveries to those junior classes would be even more significantly reduced.

37. Thus, application of the FJR – which the Equity Committee and other Objecting Parties contend is necessary to remedy alleged inequitable conduct by the SNHs – may have the perverse impact of decreasing the recoveries of unrelated parties. This conclusion demonstrates the true motivation driving the Objecting Parties is not to ensure that the rate of post-petition interest paid to creditors is fair and equitable – as was this Court's concern in *Coram* – but instead to defeat confirmation of the Modified Plan with the hope that the Debtors and the estates' legitimate creditors will pay a ransom to out-of-the-money interest holders. The Court should not countenance these tactics. Accordingly, enforcement of the applicable contract rates is the only logical and fair way for this Court to proceed.

III. THE PIERS ARE PROPERLY CLASSIFIED AS DEBT

38. The evidence adduced at the Confirmation Hearing conclusively showed that the PIERS are properly classified as debt, and that the amount of the allowed PIERS claim is properly calculated.

39. The evidence showed that WMI established Washington Mutual Capital Trust 2001 ("WMCT 2001") in accordance with the Amended and Restated Declaration of Trust (the "Trust Agreement"), dated as of April 30, 2001 (DX-295), in order to issue Trust Preferred Income Equity Redeemable Securities (the "PIERS Units") to investors. *See* DX-253 Revised Supplemental Disclosure Statement for the Modified Plan, dated March 25, 2011, at 10. WMCT 2001 issued 23 million PIERS Units to investors, who paid $1.15 billion, and issued 711,300 PIERS Common Securities to WMI, with a face value of approximately $35 million. *Id*. Each PIERS Unit consists of a preferred security with a stated liquidation preference of $50.00 and a stated coupon of 5.375%, in addition to a detachable warrant to purchase 1.2081 shares of common stock of WMI at any time prior to the close of business on May 3, 2041. *Id*. With the proceeds from the issuance of the PIERS Common Securities and the PIERS Units, WMCT 2001 purchased approximately $1.185 billion of junior subordinated deferrable interest debentures issued by WMI (the "Junior Subordinated Debentures"), due in 2041. *Id*. The preferred securities represent an undivided beneficial interest in the assets of WMCT 2001, which consist solely of the Junior Subordinated Debentures. *See* DX-289 WMCT 2001 Form S-3, filed June 27, 2001, at 1.

40. Of the $50.00 initial purchase price of each PIERS Unit, $32.33 was allocated to the preferred security and $17.67 was allocated to the warrant. *Id*. at 19. Thus the preferred securities have a stated redemption price at maturity ($50.00) greater than their issue price ($32.33). *Id*. at 14. Since the preferred securities were issued at a discount (the "original issue discount" or "OID"), their value accreted over time toward the $50 redemption price upon maturity. *See* DX-295, Trust Agreement at §§ 1.2, 6.1(a)(i). Under the Trust Agreement, the accreted value of the preferred security could be calculated by looking to the accreted value of a

Junior Subordinated Debenture with a $50 aggregate principal amount. *Id*. at §1.2. In order to determine the allowable amount of the claim filed by Wells Fargo Bank, National Association, as Indenture Trustee (the "PIERS Claim"), the Debtors used the Trust Agreement's formula to calculate the accreted value of a Junior Subordinated Debenture. *See* DX-285, Objection to Proof of Claim Number 2134 Filed by Wells Fargo Bank, National Association, as Indenture Trustee, dated December 18, 2009 (D.I. # 2039) (the "PIERS Claim Objection"), at 7. Thus, the Court's January 28, 2009 order allowing a reduced PIERS Claim totaling approximately $789 million (reduced from a face value of $1.185 billion) properly took into account the accretion of OID on the preferred securities. *See* DX-286, Order Granting Debtors' Objection to Proof of Claim 2134 Filed by Wells Fargo Bank, National Association, as Indenture Trustee, dated January 28, 2010 (D.I. # 2262) (the "PIERS Claim Order").

41. In the Confirmation Opinion, the Court held that as long as WMCT 2001 had not merged into WMI, "then [PIERS holders] are properly treated as creditors under the Plan because they do not hold stock in the Debtors but only stock in WMCT 2001, which is a creditor of the Debtors." Conf. Op. at 101. The record leaves no room for doubt that WMCT 2001 continues to exist as an independent separate entity, and therefore the PIERS are properly treated as debt.

42. First, the Debtors provided a certificate of good standing of WMCT 2001, dated March 16, 2011, in their omnibus response to objections to the Supplemental Disclosure Statement. *See* Debtors' Omnibus Response to Objections to the Supplemental Disclosure Statement at Ex. D (D.I. 6963). Second, at the Confirmation Hearing, the Debtors provided an updated certificate of good standing of WMCT 2001, dated July 12, 2011. DX-401. After Mr. Goulding authenticated the new certificate of good standing and stated that it reflected that the

trust was still outstanding as of July 12, 2011, the Court admitted the new certificate of good standing into evidence. *See* 7/14/2011 Hr'g Tr. at 21:5-10; 52:17-18. Mr. Goulding then testified that he was not aware of any occurrence that would have changed the new certificate of good standing between the date of its issuance and the date of the hearing. *See id*. at 21:11-14. Mr. Goulding also testified that WMI is a separate entity from WMCT 2001; that WMCT 2001 was still in existence that day; and that WMI and WMCT 2001 never merged with one another. *See id*. at 21:17-24. Mr. Goulding's testimony, in conjunction with the WMCT 2001 certificates of good standing that the Debtors have submitted, establishes conclusively WMCT 2001's continuing status as an independent entity and thus the propriety of treating the PIERS as debt.

43. Furthermore, the evidence showed that the Debtors always treated the PIERS preferred securities as debt because they are undivided interests in the assets of WMCT 2001, which, as discussed above in paragraph 39, consist solely of the Junior Subordinated Debentures. During the Confirmation Hearing, the Court admitted into evidence the June 27, 2001 Form S-3 that was filed in connection with the issuance of the PIERS units, which specified that "purchasers of preferred securities will be treated as owning an undivided beneficial ownership interest in the debentures and the debentures will be treated as debt." *See* DX-289, WMCT 2001 Form S-3, filed June 27, 2001, 8; 7/14/2011 Hr'g Tr. at 52:16-17. Likewise, the Court admitted WMI's Form 10-K filings for 2001 and 2007, both of which listed the junior subordinated notes as "Other Indebtedness" or "Other Borrowings" in the Notes to Consolidated Financial Statements. *See* DX-293, WMI 2007 Form 10-K for the year ended December 31, 2007, and filed on February 29, 2008, at 146; 7/14/2011 Hr'g Tr. at 52:24-25; DX-298, WMI 2001 Form 10-K for the year ended December 31, 2001, and filed on March 19, 2002, at 91; 7/14/2011 Hr'g Tr. at 52:16-17.

44. No Objecting Party offered any evidence to suggest that the PIERS should be treated as anything other than debt. Thus, there is no question that the PIERS are debt.

45. Despite the Court's explicit finding that PIERS Claims would be properly treated as debt if the Debtors could demonstrate that WMCT 2001 was not merged into WMI, the LTW Holders attempted to confuse the issue by suggesting that a portion of the accreted value of the PIERS somehow is attributable to the value of the equity warrants. The evidence from the Confirmation Hearing indicated that this was not the case.

46. As Mr. Goulding testified, and as discussed above in ¶39, *supra*, the preferred security and the equity warrant are essentially two separate securities. The original aggregate value of the preferred securities based on their $32.33 initial purchase price was approximately $743 million. 7/14/2011 Hr'g Trans. 98:9-16. Over time, the value of the preferred securities increased. *See* Trust Agreement at §§ 1.2, 6.1(a)(i).

> [MR. STEINBERG:] And isn't that the $17.67 that's attributable to the original issue discount related to the value of the equity warrant?
>
> [MR. GOULDING:] It's a way to carve up the initial fifty purchase price to say that the 17.67 is the value of the warrant. But from the date of issuance, you can look at them as two separate securities. One is a 32.33 security that accretes to 50 over time, and the other is the value of the warrant.

7/14/2011 Hr'g Tr. 100:16-23. By September 2008, the total value of the preferred securities had increased to approximately $765 million, of which approximately $9.4 million was attributable to pre-petition interest due. *Id.* at 31:10-20. The remaining $13 million increase in value is wholly attributable to the accretion of the preferred security. *See* DX-285, PIERS Claim Objection at 7 (calculating unamortized original issue discount by using the Accreted Value formula provided in the Trust Agreement); DX-295, Trust Agreement §§ 1.2 (" 'Accreted Value' means . . . with respect to any Security, the Accreted Value of a Debenture having an aggregate principal amount equal to the aggregate stated liquidation amount of such Security.").

47. Lastly, the full $789 million claim against the estate related to the 5.375% Junior Subordinated Deferrable Interest Debentures also includes the approximately $23.6 million value of the WMCT 2001 common securities that were initially issued to WMI. *See* DX-286, PIERS Claim Order. As Mr. Goulding testified, however, WMI is not receiving any recovery under the Modified Plan on account of the common securities. 7/14/2011 Hr'g Trans. 32:16-18. *See also* Modified Plan § 20.1. The Trust Agreement requires that WMCT 2001 pay to the holders of the preferred securities any recovery WMCT 2001 receives on account of the debt owed by WMI to WMCT 2001 under the Junior Subordinated Debentures prior to any payment to the holder of the common securities. In this case, the Debtors' projections indicate that there will be an insufficient recovery by WMCT 2001 to pay even the preferred securities. In any event, the Plan provides that if the preferred securities are paid in full, additional recoveries will be paid to the next tier in accordance with the Waterfall Recovery Matrix, which is Ex. "G" to the Modified Plan.

48. For the above reasons, the Debtors have established (1) that WMCT 2001 continues to exist as an independent entity, and (2) the propriety of treating the PIERS as debt. Additionally, the value attributable to the accretion of the OID on the preferred securities is in no way attributable to the equity warrants, and the LTW Holders' arguments regarding this issue should be rejected. The entire $789 million claim is properly classified as debt.

IV. THE RELEASES AND RELATED INJUNCTION AND EXCULPATION PROVISIONS ARE REASONABLE

49. In the Confirmation Opinion, the Court identified certain features of the release, injunction and exculpation provisions in Article XLIII of the Sixth Amended Plan that required modification. Conf. Op. at 60-87. The Debtors have addressed all of the areas of concern

identified by the Court by implementing the following adjustments to the release, injunction and exculpation provisions in Article XLIII of the Modified Plan.

A. Section 43.5 of the Modified Plan: Releases by the Debtors

50. In the Confirmation Opinion, the Court identified two main problems with the releases granted by the Debtors under section 43.5 of the Modified Plan: (1) too many parties were bound by the releases (Conf. Op. at 62-63), and (2) too many parties were receiving releases (Conf. Op. at 67-72). The Debtors appropriately have amended section 43.5 of the Modified Plan in response to these concerns.

(1) Parties Bound by Releases

51. First, the Court noted that the releases granted by the Debtors under section 43.5 of the Sixth Amended Plan appeared to bind parties other than the Debtors, such as the Liquidating Trustee Beneficiaries and their Related Persons. Conf. Op. at 62-63, n.33. The Debtors have clarified this issue in the Modified Plan by removing the Liquidating Trust, the Liquidating Trustee, the Liquidating Trust Beneficiaries, and each of their Related Persons from the list of entities granting releases under section 43.5. Modified Plan § 43.5.

(2) Parties Receiving Releases

52. Second, the Court concluded that section 43.5 of the Sixth Amended Plan released certain entities that were not entitled to releases. Specifically, the definition of "Released Parties" included the SNHs, the Creditors' Committee and its members, the Indenture Trustees, and the Liquidating Trust and Trustee. Conf. Op. at 67. The Debtors have thus modified the definition of "Released Parties" in section 1.165 of the Modified Plan to exclude the SNHs, the Creditors' Committee and its members, the Indenture Trustees, the Liquidating Trust, and the Liquidating Trustee. Modified Plan § 1.165. Section 1.165 now limits the definition of "Released Parties" to "each of the Debtors, WMB, each of the Debtors' estates, the

JPMC Entities, the FDIC Receiver and FDIC Corporate, and the Related Persons of each of the JPMC Entities, FDIC Corporate and the FDIC Receiver." *Id.*

53. The Court also found that there was no basis for the Debtors to grant releases to current or former "directors and officers or any professionals of the Debtors." Conf. Op. at 69-72. As explained above, the Debtors have addressed this concern by (1) excluding Related Persons of the Debtors from the definition of "Released Parties" in section 1.165 of the Modified Plan and (2) removing the Related Persons of the Released Parties from the group of parties being released in section 43.5. Modified Plan §§ 1.165, 43.5. Moreover, William Kosturos, WMI's Chief Restructuring Officer, explained that the Debtors, the Creditors' Committee and the Equity Committee entered into tolling agreements with various third parties, including current and former directors and officers and professionals, preserving the estates' claims against those individuals. 7/21/2011 Hr'g Tr. at 206:22–210:22 (discussing the tolling agreements entered into with directors and officers); 208:6-21 (discussing tolling agreements with certain third parties); 222:19-24 (same).

54. Additionally, the Court held that there was no explanation why all present and former Affiliates of Released Parties should receive releases by the Debtors. Conf. Op. at 72. In response, the definition of "Related Persons" in section 1.163 of the Modified Plan only includes present Affiliates. Modified Plan § 1.163.

55. As a result of these modifications, the releases granted by the Debtors no longer include the SNHs, the Creditors' Committee and its members, the Indenture Trustees, the Liquidating Trust and Trustee, the Debtors' Related Persons, or any of the former Affiliates of Released Parties, and the releases that remain do not bind the Liquidating Trust. Accordingly,

the release provisions of section 43.5 of the Modified Plan are consistent with the Confirmation Opinion and with applicable law.

B. Section 43.6 of the Modified Plan: Releases By Third Parties

56. In the Confirmation Opinion, the Court found several problems with section 43.6 of the Sixth Amended Plan, which governed releases by holders of claims. First, the Court expressed concern that the terms of the GSA, which provided for broad releases of all signatories thereto, would control in the event of a conflict with the provisions of section 43.6 of the Sixth Amended Plan. Conf. Op. at 79. In section 2.1 of the Modified Plan, the Debtors have resolved this issue by specifying that the terms of the Modified Plan will control in the event of inconsistencies between the Amended GSA and the Modified Plan with respect to the releases provided in section 43.6. Modified Plan § 2.1(a).

57. Second, in order to ensure that releases provided by non-debtor third parties are based on the consent of the releasing party, the Debtors have drafted section 43.6 of the Modified Plan to apply the releases only to third parties who are entitled to a distribution, had an opportunity to consent to the releases, and affirmatively did so by returning a ballot and either not opting out of the release or opting into it. *Id*. at § 43.6(a).

58. Third, the Court found in the Confirmation Opinion that the third party releases should not extend to the Debtors' Related Persons, including the Debtors' officers, directors, and Affiliates. Conf. Op. at 81-82. As explained in ¶53, *supra*, the definition of "Released Parties" in section 1.165 no longer includes Related Persons of the Debtors.[10] Thus, holders of claims

[10] Section 1.160 of the Sixth Amended Plan also included WMI Entities in the definition of "Released Parties." The term "WMI Entities," in both the Sixth Amended Plan and the Modified Plan, includes WMI, WMI Investment, Ahmanson Obligation Company, H.S. Loan Corporation, WAMU 1031 Exchange, WM Mortgage Reinsurance Company, Inc., WM Citation Holdings, LLC, WMI Rainier LLC and Washington Mutual Capital Trust 2001. Section 1.165 of the Modified Plan, on the other hand, does not include WMI Entities in the definition of "Released Parties."

who provide releases to the Released Parties do not release the Debtors' officers, directors, and Affiliates.

59. Fourth, the Court found that section 43.6 of the Sixth Amended Plan inappropriately required the present and former affiliates of creditors to grant releases even though some of those affiliates had no relationship to these chapter 11 cases. Conf. Op. at 82-83. In response, the group of parties granting releases under section 43.6 of the Modified Plan no longer includes the Related Persons of the holders of Released Claims. Modified Plan § 43.6(a).

60. Fifth, the Debtors addressed the Court's concerns regarding releases pertaining to particular claimants by carving out from the release, exculpation, and injunction provisions (1) the ANICO Plaintiffs' prosecution of direct claims against any non-Debtor entity, *id*. at § 43.6(g), (2) claims against non-Debtor entities in connection with claims relating to the BKK Litigation, *id*. at § 43.6(c), (3) claims against any non-Debtor entities in the Securities Litigations, *id*. at § 43.6(d), and (4) the Tranquility Claim, *id*. at § 43.6(e).

61. Lastly, in the Confirmation Opinion, the Court held that the third party releases were too broad because they included all claims that "arise from or relate to any act, omission, event or circumstance relating to any WMI Entity, or any current or former subsidiary of any WMI Entity." Conf. Op. at 81. Section 1.164 of the Modified Plan now defines "Released Claims" more narrowly, as only including causes of action that could have been asserted (1) by the Debtors with respect to releases given by the Debtors, (2) by Creditors relating to Claims against the Debtors, or (3) by holders of Equity Interests relating to Equity Interests. Modified Plan § 1.164(b)(ii).

62. As a result of the above modifications, the third party releases provided in the Modified Plan are purely consensual. In order to grant a release, the releasing party must be

entitled to a distribution under the Modified Plan and must have returned a ballot. On the ballot, the releasing party must have elected to grant the release by checking a box to "opt in" to granting the release or by not checking a box to "opt out" of granting the release. Because the releasing parties must demonstrate their consent, and the Debtors have addressed all of the Court's other concerns related to the third party releases, the third party release provisions in the Modified Plan should be approved. *See In re Exide Techs*., 303 B.R. 48, 74 (Bankr. D. Del. 2003) ("Because [the release] is consensual, there is no need to consider the [*Master Mortgage*] factors.").

C. Section 43.7 of the Modified Plan: Injunctions

63. The Court held in the Confirmation Opinion that the injunction provisions in section 43.7 of the Sixth Amended Plan expanded the releases "through the back door." Conf. Op. at 87. In order to eliminate any possibility that the injunction provisions could operate against holders of claims or equity interests not subject to the release provisions, section 43.7 of the Modified Plan no longer applies to "all other parties in interest" or Related Persons of holders of released claims or equity interests. Modified Plan § 43.7. Likewise, sections 43.2(b), 43.3, 43.9, and 43.12 all now limit the injunctions to the terms of the permissible releases and thus comply with applicable law. As a result, the injunction provisions of the Modified Plan comply with the Court's Confirmation Opinion.

D. Section 43.8 of the Modified Plan: Exculpation Clause

64. Section 43.8 of the Modified Plan limits liability for acts or omissions in connection with the restructuring negotiations, the Modified Plan, and the implementation thereof. In the Confirmation Opinion, the Court found the extension of this exculpation to "all Released Parties and each of their Related Persons" to be overly broad because it included parties that were not estate fiduciaries. Conf. Op. at 73. The Debtors structured the exculpation

provision in section 43.8 of the Modified Plan to provide exculpations only to estate fiduciaries: the Debtors, the Debtors' officers and directors serving during the bankruptcy case, the Creditors' Committee and its members, the Equity Committee and its members, and each of their professionals. Modified Plan § 43.8.

65. The Court also required a carve-out of any claims related to the LTW Adversary Proceeding until the merits of the LTW Holders' claims are resolved. Conf. Op. at 74. The Debtors have thus included a clause within section 43.8 that broadly establishes that the exculpation provisions will not affect the liability of "any member of the Debtors' Board of Directors and officers with respect to actions asserted in the Dime Warrant Litigation and relating to the period from Petition Date up to and including the Effective Date." Modified Plan § 43.8.

66. Lastly, as the Court noted in the Confirmation Opinion, the Debtors had previously amended the Debtors' releases of third parties in the October 29, 2010 modification to ensure that those releases did "not extend to acts of gross negligence or willful misconduct." Conf. Op. at 74. In the Modified Plan, the Debtors have incorporated this limitation directly into section 43.8 by providing that the exculpation provisions shall not affect liability arising from acts or omissions "determined in a Final Order to have constituted gross negligence or willful misconduct." Modified Plan § 43.8.

67. Because the Debtors have addressed all of the issues related to exculpation that the Court identified in the Confirmation Opinion, the exculpation provisions of section 43.8 of the Modified Plan should be approved.

V. THE EVIDENCE CONCLUSIVELY ESTABLISHED THAT BLACKSTONE'S VALUATION OF REORGANIZED WMI IS REASONABLE

68. The evidence presented during the Confirmation Hearing conclusively established that the valuation performed by the Debtors' valuation expert, Steven Zelin of Blackstone Advisory Partners, L.P. ("Blackstone"), was reasonable and should be relied upon by this Court in determining the value of the stock of Reorganized WMI for purposes of distributions under the Modified Plan. Ultimately the Equity Committee's own valuation expert, Anders Maxwell of Peter J. Solomon Company, admitted under oath that he does not believe Blackstone undervalued Reorganized WMI.

> Q: Well, in the equity committee objection, it said the debtors have undervalued reorganized WMI both as a run-off company and as it will actually be used in the hands of the settlement noteholders who will take control of the company.
>
> ***Now, you do not believe that Blackstone undervalued reorganized WMI, correct?***
>
> A. ***That is correct.***

7/15/2011 Hr'g Tr. 69:22-70:4 (Maxwell) (emphasis added). Accordingly, as supported by both sides' tax experts' testimony described below, the Blackstone valuation is reasonable and should be adopted by the Court in confirming the Modified Plan.

A. The Experts Agree On the Value of Reorganized WMI's Run-Off Portfolio

69. Reorganized WMI has two principal assets: (i) the stock of Washington Mutual Mortgage Reinsurance Corp. ("WMMRC"), a reinsurance portfolio in run-off since the Petition Date, and (ii) net operating losses ("NOLs") principally related to the Debtors' abandonment of its stock of WMB, part of which may be used to shield income. *See* 7/13/2011 Hr'g Tr. 269:7-9 (Zelin); 296:16-20 (Zelin).

70. Blackstone estimated an enterprise value range of $135 million to $180 million by valuing three components of Reorganized WMI: (i) the value of the existing run-off portfolio,

excluding any value attributable to the NOLs ($115 million to $140 million), (ii) the value of utilizing the NOLs to shield income generated by the existing run-off portfolio ($10 million to $20 million), and (iii) the potential value of the NOLs to shield additional income generated through a new corporate opportunity after a post-emergence equity raise (the "Corporate Opportunity NOLs") ($10 million to $25 million). *See* DX-341, Updated Expert Report of Steve Zelin, Blackstone Advisory Partners, L.P., dated June 23, 2011, (the "Blackstone Report") at 8. In doing so, Blackstone relied upon two commonly-used valuation methodologies, a discounted cash-flow analysis ("DCF Analysis") and a comparable precedent transaction analysis ("Precedent Transaction Analysis").[11] *See id.* at 13; *see also Coram*, 315 B.R. at 337. Blackstone appropriately placed little weight on the Precedent Transaction Analysis because of a lack of recent comparable transactions. *See* 7/13/2011 Hr'g Tr. 267:10-268:2 (Zelin); *see also In re Lids Corp.*, 281 B.R. 535, 545 (Bankr. D. Del 2002) (finding precedent transaction analysis not probative where comparable transactions were "outdated" and "failed to account for the current economic environment and market conditions").[12]

71. Blackstone concluded that the value of Reorganized WMI's existing run-off reinsurance portfolio and the NOLs that could be used to shield that income is $125 million to $160 million. Similarly, Mr. Maxwell concluded that the value of Reorganized WMI for purposes of distributions of its stock pursuant to the Modified Plan is $130 million to $135

[11] Blackstone considered a comparable company analysis, but did not rely upon it because WMMRC is not comparable to any publicly-traded companies due to its size and the nature of its business. *See* DX-341, Blackstone Report at 14; *see also* 7/13/2011 Hr'g Tr. at 270:21-271:17 (Zelin).

[12] Mr. Maxwell, on the other hand, gave a 40% weighting to his Precedent Transaction Analysis, even though all five of his comparable transactions occurred prior to 2007, and four of the five were more than 10 years old. *See* EC 154, Residual Washington Mutual, Inc. Valuation Critique, dated April 29, 2011, (the "Maxwell Report") at 7; *see also* 7/15/2011 Hr'g Tr. 103:20-22 (Maxwell). By using outdated transactions, his Precedent Transaction Analysis resulted in a higher value than it would if the transactions reflected today's market. *See id*. at 104:4-6 (Maxwell). He admitted, however, that this weighting was based on a misreading of Blackstone's expert report. *See id*. at 105:13-16 (Maxwell). Had he applied his own professional judgment, Mr. Maxwell testified that he would have given his Precedent Transaction Analysis less weight. *See id*. at 131:22-25 (Maxwell).

million. *See* 7/15/2011 Hr'g Tr. at 68:9-13 (Maxwell). The midpoint of Blackstone's valuation of the existing run-off reinsurance portfolio is actually $12.5 million ***higher*** than that of Mr. Maxwell.[13]

72. Thus, Blackstone's analysis of the first two components of its valuation (those related to the value of the existing run-off reinsurance portfolio) is not controversial. Mr. Maxwell testified that he agreed with Blackstone's valuation of the existing run-off reinsurance portfolio.

> Q: Okay. And you agree with Blackstone's valuation of the reinsurance run-off portfolio, right?
>
> A: Effectively that is correct.

Id. at 68:14-16 (Maxwell). Moreover, nothing contained in Mr. Maxwell's expert report or his testimony at confirmation was meant to challenge Blackstone's valuation of the existing run-off reinsurance portfolio.

> Q: Okay. And your report is not meant to challenge the debtor's or Blackstone's valuation of the reinsurance run-off portfolio, correct?
>
> A: As it is qualified under the plan, that is correct.

Id. at 69:12-15 (Maxwell).

B. The Evidence Established That Blackstone Reasonably and Appropriately Valued the Corporate Opportunity NOLs

73. The remaining source of value inherent in Reorganized WMI is the company's potential ability to utilize large NOLs after a post-emergence capital raise. Here, the valuation experts' testimony relied upon tax experts on each side. The evidence demonstrated the

[13] Blackstone reaches this conclusion after having determined that it was reasonable to adjust the WMMRC financial projections prepared by Milliman, Inc. ("Millliman"), the Debtors' actuary, upward to account for a 10% improvement in the performance of WMMRC's reinsurance contracts. *See* DX-341 at 14; *see also* 7/13/2011 Hr'g Tr. at 262:14-263:2 (Zelin). Mr. Maxwell, on the other hand, testified that he did not undertake to adjust Milliman's projections because he was not privy to the same information as Blackstone. *See* 7/15/2011 Hr'g Tr. at 46:8-20 (Maxwell).

existence of a genuine risk of disallowance under section 269 of the Internal Revenue Code ("IRC"), and that Blackstone properly accounted for this risk.

74. Assuming an effective date of August 31, 2011, the Debtors estimate that Reorganized WMI will have NOLs of $6 billion, principally due to a worthless stock deduction associated with its abandonment of WMB stock. *See* 7/13/2011 Hr'g Tr. 106:4-20 (Carreon). While approximately $4 billion of the available NOLs will be subject to an annual limitation pursuant to IRC section 382, approximately $2 billion of the NOLs will not be subject to any such limitation. *See id.* at 108:21-109:9 (Carreon). As discussed above, both the Debtors' and the Equity Committee's experts essentially agree on how the NOLs can be utilized to shield income that will be generated by the existing reinsurance run-off portfolio. The experts disagree, however, about Reorganized WMI's ability to utilize those NOLs following a post-emergence capital raise.

75. Blackstone ascribes a value of $10 million to $25 million to the Corporate Opportunity NOLs after assuming that Reorganized WMI will undertake a post-emergence equity raise of $127.5 million, equal to the current value of Reorganized WMI's non-tax assets. *See* DX-341, Blackstone Report at 35. In doing so, Blackstone relied on advice of its tax counsel and appropriately and necessarily accounted for the risks that the NOLs may not be utilized. *See* 7/13/2011 Hr'g Tr. 279:3-280:4 (Zelin). First, Blackstone considered the risk that Reorganized WMI's NOLs could be subject to disallowance pursuant to section 269 of the IRC if it is determined that the principal purpose for the creditors' acquisition of control of Reorganized WMI was to avoid taxes. *See id.* at 278:15-24 (Zelin); 290:23-291:15 (Zelin). Second, Blackstone also considered various risks associated with the execution of the corporate

opportunity, including Reorganized WMI's ability to operate as a going concern and raise capital post-emergence. *See id.* at 277:21-278:14 (Zelin).

(1) The Tax Experts' Testimony Established That Section 269 May Apply to the Creditors' Initial Acquisition of Control of Reorganized WMI

76. During the Confirmation Hearing, two experts testified about the potential application of section 269 of the IRC to Reorganized WMI's use of its NOLs. The Debtors' tax expert, Richard L. Reinhold of Willkie Farr & Gallagher LLP, opined that there is some level of risk that the IRS would use section 269 to disallow Reorganized WMI's use of the NOLs in connection with the acquisition of control of Reorganized WMI by the creditors at emergence. *See* 7/13/2011 Hr'g Tr. 193:6-19 (Reinhold). The Equity Committee's tax expert, Kevin D. Anderson of BDO USA, LLP, on the other hand, opined that section 269 likely would not apply to any subsequent acquisitions of control of other companies or assets by Reorganized WMI. *See id.* at 143:1-8 (Anderson). Mr. Anderson, however, did not opine on the application of section 269 to the creditors' initial acquisition of control of Reorganized WMI pursuant to the Modified Plan. *See id.* at 151:10-21 (Anderson).

77. Section 269 allows the IRS to disallow the use of NOLs where (i) there was an acquisition of at least 50% control of a corporation by a person or group of persons and (ii) the principal purpose for the acquisition was to obtain the use of such tax benefits. *See* 26 U.S.C. § 269. Thus, even though a substantial portion of Reorganized WMI's NOLs are not disallowed (in whole or part) under section 382, section 269 might be applied to disallow their use. *See* Treas. Reg. § 1.269-7. Moreover, if the IRS challenges Reorganized WMI's use of its NOLs because it determines that the principal purpose for the creditors' acquisition of control of Reorganized WMI was tax avoidance, then the burden of proof will be on Reorganized WMI to prove that the principal purpose of the acquisition of control was not tax avoidance. *See, e.g.*,

Vulcan Materials Co. v. United States, 446 F.2d 690, 699 (5th Cir. 1971), *cert. denied*, 404 U.S. 942 (1971) ("[T]he burden is on the taxpayer to prove that the Commissioner's determination of the tax was erroneous.").

78. Both experts agreed that the creditors' expected receipt of the stock of Reorganized WMI pursuant to the Modified Plan would be an acquisition of at least 50% control for purposes of section 269. *See* 7/13/2011 Hr'g Tr. 147:16-23 (Anderson); 166:10-13 (Anderson); 193:6-19 (Reinhold). Therefore, if the principal purpose of the acquisition of control is deemed to be tax avoidance, section 269 may apply to disallow Reorganized WMI's use of the NOLs. *See id.* at 192:22-25 (Reinhold); 193:3-6 (Reinhold).

79. To determine whether an acquisition of control was made for the principal purpose of tax avoidance, both experts also agreed that a court would apply a fact-based test, scrutinizing all facts and circumstances of the transaction, including future actions that may be indicative of present intention at the time the acquisition of control. *See id.* at 167:7-21 (Anderson); 193:25-194:16 (Reinhold).

80. Mr. Reinhold applied a "facts and circumstances" test to the creditors' expected acquisition of control of Reorganized WMI pursuant to the Modified Plan and considered four factors relevant:

a. That the amount of the unlimited NOLs available greatly outnumbers the value of Reorganized WMI's non-tax assets;
b. That Reorganized WMI has no significant ongoing business and could be viewed as a shell company with significant tax attributes;
c. The extent to which capital is raised by the acquiring owners of Reorganized WMI; and
d. The fact that the creditors participated in the negotiation of the Modified Plan reflects consciousness of the availability of tax assets.

See id. at 196:1-198:11 (Reinhold). Mr. Reinhold's opinion was supported by case law that has applied section 269 in situations where:

- The amount of the tax asset significantly outweighed the non-federal income tax benefit to the acquirer of the corporation. *See, e.g., Scroll, Inc. v. C.I.R.*, 447 F.2d 612, 617 (5th Cir. 1971) (applying section 269, in part, because the non-federal income tax benefit to an acquisition was "undoubtedly insubstantial" compared to the federal income tax benefit).

- The acquired corporation had been operated as a shell corporation rather than as an ongoing concern. *See, e.g., U.S. Shelter Corp. v. United States*, 13 Cl. Ct. 606, 623 (1987) (acquisition of a "shell" corporation rather than a going concern indicates a principal purpose of tax avoidance under section 269).

- Subsequent actions by the corporation after the acquisition demonstrate that the acquirers were more interested in utilizing the NOLs than in the non-tax assets acquired. *See, e.g., Scroll, Inc.*, 447 F.2d at 617-18 (applying section 269, in part, because the loss corporation, soon after the acquisition merged with and into a profitable business); *U.S. Shelter Corp.*, 13 Cl. Ct. at 623 (taking into account "subsequent actions" to "shed light on the intent and motives" of the acquirers).

81. Of the aforementioned facts and circumstances to be examined, Mr. Reinhold determined that the amount of capital raised by Reorganized WMI in the future, after the creditors acquire control pursuant to the Modified Plan, would be the most critical element because it could lead to an inference of the purpose for the acquisition. *See* 7/13/2011 Hr'g Tr. 200:1-7; 201:8-202:6 (Reinhold). As long as Reorganized WMI limits its future capital raises to the value of its non-tax assets or less, Mr. Reinhold opined that it is more likely than not that the IRS would not seek to disallow Reorganized WMI's use of the NOLs pursuant to section 269. *See id.* at 200:8-22. Conversely, Mr. Reinhold opined that if Reorganized WMI raises capital in excess of its non-tax assets, then there is a greater risk that the IRS would find—and a court would uphold—that the principal purpose for the acquisition of control was tax avoidance. *See id.* at 200:23-201:4; 201:17-22 ("The capital raised subsequent to the acquisition will suggest the purpose for the acquisition. That is to say, if the amount raised were in excess of a hundred and twenty-seven and a half million dollars, it would suggest that the parties acquired the shares with the purpose, principally for the purpose of acquiring[,] accessing [those] tax benefits."). In that situation, Mr. Reinhold testified that he would no longer be able to give "more likely than not"

advice (*i.e.*, more likely than not that the IRS would not seek to disallow Reorganized WMI's use of the NOLs). *See id*. at 201:5-201:7 (Reinhold).

(2) Mr. Anderson's Expert Reports and Testimony Are Not Relevant Because He Ignored Whether Section 269 Could Apply to the Creditors' Initial Acquisition of Control of Reorganized WMI, and Speculated as to Hypothetical Future Transactions

82. Mr. Anderson was the only other tax expert to submit an expert report and testify during the Confirmation Hearing, and his testimony provided no relevant evidence to rebut Mr. Reinhold's expert opinion on the application of section 269 to the creditors' initial acquisition of control of Reorganized WMI through the confirmation of the Modified Plan. Mr. Anderson testified that he considered section 269 only as it applied to hypothetical future acquisitions of control ***by Reorganized WMI of other companies or assets***.

> Q: And in terms of periods of time, you know, emergence and post-emergence, are there different acquisitions of control that one could consider in assessing the Section 269 risk?
>
> A: Yes, there are. One is an acquisition of control that occurs simply because upon emergence the creditors will acquire control of the corporation, but then separately, there might be future acquisitions of control by reorganized WMI of other corporations.
>
> Q: And which of those acquisitions of control did you focus on in your reports?
>
> A: I had focused on the latter, the subsequent acquisitions of control.

7/13/2011 Hr'g Tr. 147:16-148:2 (Anderson).

83. Mr. Anderson did not, as he should have, analyze section 269 as it applied to the acquisition of control of Reorganized WMI by its creditors. *See id.* at 166:10-13; 166:21-24. He did not, as he should have, apply the facts and circumstances to that acquisition of control. *See id.* at 173:13-23. He did not, as he should have, advise Mr. Maxwell on the potential for section

269 to apply to the acquisition of control by creditors in any of Mr. Maxwell's speculative, hypothetical going concern valuation scenarios. *See id.* at 151:14-21.

84. Instead, Mr. Anderson focused only on hypothetical transactions that may or may not happen at some point in the future.[14] *See id.* at 177:1-9 (Anderson). Since the facts and circumstances of those transactions are not yet known, Mr. Anderson merely assumed that it would be possible for Reorganized WMI to acquire other companies or assets without the primary purpose of that acquisition being tax avoidance:

> Q: And in terms of gathering facts to apply, what sources did you consult to gather facts?
>
> A: Well, my focus had been on potential future acquisitions of profitable businesses. And so without having specific transactions in front of me, I concluded that there were at least a class of acquisitions that reorganized WMI could make without running afoul of Section 269.

Id. at 145:12-18.

85. Because Mr. Anderson did not undertake an analysis of whether section 269 could apply as a result of creditors' initial acquisition of control of Reorganized WMI pursuant to the Modified Plan, his expert opinion regarding section 269 (and, by extension, Mr. Maxwell's "critique" of Blackstone's analysis) in no way rebuts Mr. Reinhold's or Blackstone's analyses. His opinion on this point is simply not relevant.

(3) <u>Blackstone Reasonably Took Section 269 Risk Into Account When Valuing the Corporate Opportunity NOLs</u>

86. Given the risks associated with the potential application of IRC section 269, Blackstone appropriately assumed, for purposes of its Corporate Opportunity NOLs valuation,

[14] Mr. Anderson also opined that section 269 would not apply in certain circumstances because the IRS could use section 382 to limit the use of the NOLs. *See* 7/13/2011 Hr'g Tr. 184:12-17 (Anderson). He admitted on cross examination, however, that section 382 would not apply to limit a significant portion of Reorganized WMI's NOLs. *See id.* at 186:15-21 (Anderson). He further admitted that if section 269 were applicable by its terms, he would have no reason to think the IRS would ignore it. *See id.* at 175:6-8 (Anderson).

that Reorganized WMI would attempt to raise no more than $127.5 million – the value of the run-off reinsurance portfolio, its only non-tax asset – in new capital after creditors acquire control of the corporation. *See* DX-341, Blackstone Report at 35; *see also* 7/13/2011 Hr'g Tr. 281:24-282:8 (Zelin). It is reasonable to assume that those managing Reorganized WMI would not seek to raise capital at a level that would jeopardize the company's ability to utilize any of its NOLs. This is particularly true because if section 269 applied, it could apply to all of Reorganized WMI's NOLs, including the $10 million to $20 million in value from the portion used to shelter income generated by the run-off reinsurance portfolio. *See id.* at 204:3-11 (Reinhold).

87. Blackstone appropriately discounted its Corporate Opportunity NOLs valuation to account for risks and uncertainty related to section 269 and Reorganized WMI's ability to operate as a going concern or raise capital (discussed below). *See* DX-341, Blackstone Report at 35-36. This Court and others have held that valuation experts properly discounted the value of NOLs when there were risks associated with utilizing the NOLs. *See Coram*, 315 B.R. at 342 (because expert testimony established the "IRS could successfully challenge the Debtors' tax positions," the Court "[r]ecogniz[ed] that there is a level of risk associated with the NOLs" and "conclude[d] that it is proper to value them" at the debtors' valuation expert's "risk adjusted present value"); *see also In re Jartran, Inc.*, 44 B.R. 331, 380-81 (N.D. Ill. 1984) (holding that "a substantial discount" to the value of NOLs "would be required" due to "a number of contingencies, including . . . potential challenge under § 269 of the Internal Revenue Code"); *In re Imperial 400 Nat'l Inc.*, 374 F. Supp. 949, 954-55 (D.N.J. 1974) (holding "that is appropriate to substantially discount the alleged value of the net operating loss carryforward" because, among other things, "[n]ot every proponent may be able to take advantage of the net operating

loss carryforward" and "[t]he preservation of a pre-proceedings net operating loss carryforward to offset post-proceeding profits is seldom allowed by Internal Revenue Service or the courts").

(4) Blackstone Reasonably Accounted for Various Execution Risks When Valuing the Corporate Opportunity NOLs

88. Finally, Blackstone's Corporate Opportunity NOLs valuation appropriately takes into account various execution risks, including: (i) Reorganized WMI's lack of an existing, experienced management team, (ii) the fact that Reorganized WMI is currently operating as a run-off portfolio rather than as a going concern, (iii) the lack of a business plan, (iv) uncertainty surrounding the availability of capital, (v) uncertainty surrounding the availability of portfolios to be acquired, and (vi) a continued deterioration of Reorganized WMI's existing mortgage portfolios that may divert proceeds from new opportunities to cover future losses. *See* DX-341, Blackstone Report at 35 (listing "execution risks"); *see also* 7/13/2011 Hr'g Tr. 277:21-278:24 (Zelin) (discussing risks limiting Reorganized WMI's ability to raise capital); 287:24-288:14 (Zelin) (discussing risks related to Corporate Opportunity NOLs valuation); 290:23-291:24 (Zelin) (discussing execution risks). In fact, the Equity Committee's valuation expert, Mr. Maxwell, recognizes and acknowledges many of the same execution risks, yet does not take them into account in his analysis. *See* 7/15/2011 Hr'g Tr. 107:18-108:10 (Maxwell) (acknowledging each execution risk from page 35 of the Blackstone Report (DX-341)). [15]

89. Blackstone reflects these risks in its discount rate for the Corporate Opportunity NOLs valuation and in an adjustment to the value of the Corporate Opportunity NOLs,

[15] During his direct examination, Mr. Maxwell stated that if the court made three changes to Blackstone's Corporate Opportunity NOLs valuation, Blackstone's valuation of the Corporate Opportunity NOLs would increase by $123 million. Those three changes were: (i) substituting Blackstone's discount rates with the lowest discount rate applied by Mr. Maxwell, (ii) applying Mr. Maxwell's estimated rate of return on capital, and (iii) eliminating Blackstone's $5 million to $20 million adjustment. *See* 7/15/2011 Hr'g Tr. 59:2-25 (Maxwell). By making these changes, however, Mr. Maxwell does not account for ***any*** section 269 risk or execution risks. *See id.* at 108:11-16 (Maxwell). Essentially, Mr. Maxwell's adjustment to Blackstone's Corporate Opportunity NOLs valuation eliminates almost all of the assumptions upon which the valuation was based.

decreasing it by $5 million to $20 million. *See* DX-341 at 37; *see also* 7/13/2011 Hr'g Tr. 287:6-23 (Zelin). Both the discount rate and the adjustment are appropriate because it is not clear whether Reorganized WMI will be able operate as a going concern, raise the necessary equity capital, or even purchase assets which will generate the level of income that Blackstone assumes. *See, e.g., In re Spansion, Inc.*, 426 B.R. 114, 131-32 (Bankr. D. Del. 2009) (holding that valuation experts appropriately considered "downside analyses," adjusted to reflect various risks facing the post-emergence reorganized debtor).

C. Mr. Maxwell Did Not Conduct a "Valuation" of Reorganized WMI

90. As Mr. Maxwell readily admitted during cross examination, his expert report is not a valuation of the type normally relied upon by a court. *See* 7/15/2011 Hr'g Tr. 73:13-15 (Maxwell). In fact, Mr. Maxwell did not conduct a valuation of Reorganized WMI at all. *See id.* at 36:23-24 (Maxwell) (stating he did not perform a valuation of WMMRC). Instead, Mr. Maxwell stated that he did a "critique" of Blackstone's valuation, yet agreed with Blackstone's valuation of Reorganized WMI's run-off reinsurance portfolio and opined that Blackstone has not undervalued Reorganized WMI. *See id.* at 68:9-15 (Maxwell) (agreeing with Blackstone's valuation of the run-off reinsurance portfolio); 69:22-70:4 (Maxwell) (stating that he does not believe Blackstone undervalued Reorganized WMI).

91. In his "critique", which includes an analysis of the incremental value of capital raises, Mr. Maxwell created a hypothetical, speculative start-up company with little relation to Reorganized WMI as it will exist upon emergence from bankruptcy, other than its NOLs.

> Q: So in your critique, what you're presenting is not a valuation of the legacy business of reorganized WMI.
>
> A: That is correct.
>
> Q: Instead, it's really taking that new 300 million dollars of capital and creating a new business, isn't it?

> A: That is correct.
>
> Q: So in essence it's creating a start-up company?
>
> A: It is creating a start-up company around the shell of a legacy portfolio, that was what was contemplated.

7/15/2011 Hr'g Tr. 117:24-118:7 (Maxwell); *see also* EC 154, Maxwell Report at 11.

92. Furthermore, rather than limit his analysis to a valuation of the assets Reorganized WMI will have at emergence – its run-off reinsurance portfolio and its ability to utilize some of its NOLs –Mr. Maxwell creates a hypothetical new business from the money of the future owners of Reorganized WMI and analyzes the value those investments could create unrelated to the NOLs.

> Q: In creating an ongoing business here, you're not just valuing the opportunity that we just discussed, the NOL, which is the unique opportunity that [WMMRC], reorganized WMI presents compared to investing in some other reinsurance company? You're not valuing just that, correct?
>
> A: That is correct.
>
> Q: You're creating a whole new business and taking credit for all the value that you assume could be created.
>
> A: In the scenario that we put forward, that is correct.

Id. at 110:13-21 (Maxwell). This type of speculation is not a proper basis for a valuation. *See generally Coram*, 315 B.R. at 337-38, 341 (Bankr. D. Del. 2004) (valuations conducted as part of bankruptcy confirmation should determine the debtor's value at the time of confirmation).

93. In fact, more than two-thirds of Mr. Maxwell's valuation related to incremental capital raises is attributable to the value of the hypothetical new start-up business rather than the existing run-off business and Reorganized WMI's NOLs. *See* 7/15/2011 Hr'g Tr. at 153:18-154:17 (Maxwell). That value is not inherent in Reorganized WMI and just as easily could be created – if Mr. Maxwell's assumptions are to be believed – in any start-up reinsurance company not in bankruptcy. *See id.* at 75:14-17 (Maxwell) (agreeing that the value of Reorganized WMI

as a going concern is not inherent in Reorganized WMI today, but would be added by a future owner).

94. Because Mr. Maxwell's expert report does not attempt to value Reorganized WMI, it is not relevant to any issue before this Court.

D. Mr. Maxwell's Expert Report and Testimony Are Improperly Speculative, Based on Hypotheticals, And Do Not Account for Risk

95. As Mr. Maxwell admits, his report is highly speculative as to the value of Reorganized WMI as a going concern. *See id.* at 83:12-14 (Maxwell). First, his residual value analysis is premised on the key assumption that Reorganized WMI will be operated as a going concern, but he does not opine on the likelihood that Reorganized WMI will be operated as a going concern. *See id.* at 74:9-15; 74:19-22 (Maxwell). In fact, Mr. Maxwell readily acknowledges that he cannot speak to goals, objectives, and intentions of the future owners of Reorganized WMI who will make that determination. *See id.* at 70:19-22. He also recognizes that Reorganized WMI currently only operates as a run-off reinsurance portfolio, *see id.* at 70:16-18, does not have a business plan or management team, *see id.* at 72:7-9, no means of originating business, *see id.* at 75:24-76:1, and no ongoing relationship with customers or vendors, *see id.* at 76:6-13.

96. Moreover, to operate as a going concern, Mr. Maxwell testified that Reorganized WMI would need to, among other things, find a manager, develop a business plan, raise equity, arrange financing, and develop an implementation plan to turn the business plan into an operating entity. *See id.* at 78:22-79:13. He further admitted that each of these steps would involve time and costs and that there would be some level of risk inherent in Reorganized WMI's ability to complete any of those steps. *See id.* at 79:14-15; 79:21-23. Yet Mr. Maxwell did not

account for any of these costs in converting Reorganized WMI into a hypothetical going concern, nor did he account for the risks that it might not be successful. *See id.* at 80:11-81:7; 81:20-24.

97. Finally, Mr. Maxwell's analysis is predicated on Reorganized WMI raising a substantial future investment, but he does not opine on the likelihood that additional capital will be raised. *See id.* at 83:15-24; 84:17-19. Nor does he know of any qualified investor who is interested today in investing in Reorganized WMI. *See id.* at 83:25-84:3. He could not opine on the likelihood that Reorganized WMI will be able to raise the more than $200 million in debt that his analysis assumes. *See id.* at 97:24-98:8. And yet his analysis did not account for any risk that Reorganized WMI will not be able to raise substantial additional capital. *See* EC 154, Maxwell Report at 5, 11-12.

E. Mr. Maxwell's Analysis of the Potential Value of the NOLs is Not His Expert Opinion of the Value of Reorganized WMI's NOLs

98. Lastly, Mr. Maxwell's expert report purports to value Reorganized WMI's NOLs, assuming they are utilized in full, at a range of $240 million to $420 million. *See id.*, Maxwell Report at 8. During cross-examination, however, he acknowledged that Reorganized WMI would need an investment of more than $1 billion to achieve these scenarios. *See* 7/15/2011 Hr'g Tr. 85:20-86:1 (Maxwell). He admitted that this analysis was not his expert opinion as to the value of Reorganized WMI's NOLs. *See id.* at 86:9-18. Therefore, this Court should not take that analysis into account when determining the value of Reorganized WMI.

CONCLUSION

WHEREFORE, for the reasons stated above, the Creditors' Committee respectfully requests that the Court (1) overrule the objections to confirmation of the Modified Plan, and (2) enter an Order confirming the Modified Plan.

Dated: Wilmington, Delaware
August 10, 2011

Respectfully submitted,

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