IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

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

POST-CONFIRMATION HEARING BRIEF OF THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS IN SUPPORT OF CONFIRMATION OF THE MODIFIED SIXTH AMENDED PLAN OF REORGANIZATION [DOCKET NO. 8073] WITH RESPECT TO INSIDER TRADING AND EQUITABLE CONDUCT ISSUES

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The Official Committee of Unsecured Creditors (the "Creditors' Committee"),[1] hereby respectfully submits this Post-Confirmation Hearing Brief In Support Of Confirmation Of The Modified Sixth Amended Plan Of Reorganization (D.I. 8073) (the "Modified Plan") With Respect To Insider Trading And Equitable Conduct Issues.

INTRODUCTION

Creditors of the Debtors have waited nearly three years for any recovery on their billions of dollars of claims. The Debtors' Modified Plan addresses each and every concern raised by the opinion denying confirmation of the Debtors' Sixth Amended Plan. Nevertheless, the Equity Committee and certain other parties all of whom are parties or representatives of parties that are, unfortunately, unlikely to receive any recovery under the Modified Plan, are in the final phase of a last-ditch attempt to derail confirmation of the Modified Plan by any means possible. Such attempted means have included using a huge portion of the seven days of hearings on confirmation to attempt to adduce evidence of insider trading or improper conduct by the Settlement Noteholders.

This brief is submitted for two purposes. First, to set forth the belief of the Creditors' Committee that the Modified Plan embodies an excellent resolution of this lengthy and difficult case, including the implementation of the Global Settlement Agreement, and should be confirmed and implemented as expeditiously as possible, irrespective of the allegations of the objecting parties. And, second, the Creditors' Committee has seen and heard nothing during seven days of confirmation hearings, reams of exhibits and hours of pre-hearing depositions to support any of the allegations of the objecting parties. To the contrary, the Creditors' Committee

[1] Capitalized terms not otherwise defined herein shall have the respective meanings ascribed to such terms in the Creditors' Committee's Reply To Insider Trading And Equitable Conduct Arguments Set Forth In Objection Of The Official Committee Of Equity Security Holders To Confirmation Of The Modified Plan (D.I. 8142).

believes that the evidence exonerates the Settlement Noteholders and provides overwhelming support for confirmation of the Modified Plan.

The *Post-Confirmation Hearing Brief of the Official Committee of Unsecured Creditors In Support Of Confirmation (Issues Other Than Alleged Insider Trading)* addresses a series of issues raised by objecting parties. This brief addresses the allegations of insider trading. With respect to the insider trading issues, the Creditors' Committee has analyzed the allegations and evidence and reached several conclusions.

The involvement of the Settlement Noteholders, as well as other significant creditors, in the process of reaching an agreement as to the terms of a plan was both necessary and important to the Debtors' ability to propose a plan that has the support of the major constituents in this case. The Debtors, the Settlement Noteholders, JPMC, the Creditors' Committee, other creditors and the FDIC participated in discussions which eventually led, after many false starts and dead ends, to the execution of the Global Settlement Agreement. As part of those discussions, and in accordance with practices observed in other large chapter 11 cases, the Settlement Noteholders and the Debtors took a number of steps to permit the Settlement Noteholders to participate in discussions without violating federal securities laws or deriving an improper informational advantage from their participation.

The Equity Committee now seeks to challenge the parties' conduct and confirmation of the Modified Plan based on allegations of insider trading or inequitable conduct by the Settlement Noteholders. The Creditors' Committee supports confirmation of the Modified Plan and, based on its careful review of the record made at the confirmation hearing, submits that the Equity Committee has failed to prove any of its allegations.

In particular, the Creditors' Committee believes that the Equity Committee has failed to establish that the Settlement Noteholders engaged in insider trading. The testimony and the confirmation hearing exhibits show that the Settlement Noteholders, as well as the Debtors, took appropriate steps to avoid trading based on material, nonpublic information ("MNPI"). These efforts included, without limitation, that the Settlement Noteholders voluntarily abstained from trading and/or maintained an ethical screen while in possession of MNPI. Moreover, the Equity Committee has failed to establish any of the elements of an insider trading claim, particularly the elements of duty and scienter.

The Creditors' Committee also believes the Equity Committee's arguments that the plan should not be confirmed or the Court should impose an interest rate other than the contract rate, based on allegations of inequitable conduct stemming from the Settlement Noteholders' participation in settlement discussions and trading activities, are without factual or legal support and would require the Court to create an entirely new body of law on an *ad hoc* and retroactive basis. Moreover, based on its review of the record, the Creditors' Committee believes that the Settlement Noteholders did not engage in any inequitable conduct and took a number of steps to avoid improper trading.

For the foregoing reasons and based on the analysis of the facts and the law set forth below, the Creditors' Committee believes that the Equity Committee's objection to confirmation of the Modified Plan should be overruled and the Modified Plan should be confirmed. However, even if the Court were to find that one or more of the Settlement Noteholders engaged in conduct that would warrant disallowing their claims, that fact alone would not be a basis to withhold confirmation of the Modified Plan.

STATEMENT OF FACTS

Settlement negotiations in these cases lasted well over a year and fell apart several times before an agreement in principle was actually reached and incorporated into the current version of the Modified Plan. The Settlement Noteholders' roles and involvement in these negotiations, which form the basis for the Equity Committee's complaint, ebbed and flowed depending on the noteholder and the particular negotiation. Analysis of the Settlement

Noteholders' actions in this case can logically be grouped into five different time periods: (i) from the Petition Date to the first time the Settlement Noteholders became involved in settlement negotiations in March, 2009; (ii) the first "restricted period," during which the Settlement Noteholders were parties to Confidentiality Agreements in March and April, 2009; (iii) the second "non-restricted period," from May to November, 2009, which was after the first set of Confidentiality Agreements had expired and during which time no MNPI was shared from May to November, 2009; (iv) the second "restricted period," during which the Settlement Noteholders entered into a second set of Confidentiality Agreements from November 16 to December 30, 2009; and (v) the period after the expiration of the second set of Confidentiality Agreements from December 31, 2009 onward.

<u>Settlement Noteholders' Investment Activities Prior to Settlement Discussions</u>

The evidence at the confirmation hearing demonstrates that each of the Settlement Noteholders acquired significant positions in Washington Mutual Inc. ("WMI") securities *prior to* their involvement in any settlement negotiations, which is to say prior to the first time any party is alleging they became privy to any confidential information. Indeed, according to evidence at the confirmation hearing:[2] (i) Appaloosa purchased approximately $1.179 billion in various types of WMI securities between the Petition Date and March 10, 2009, the date of the first settlement meeting in this case that the principals of the Settlement Noteholders attended (7/20/2011 Hr'g Tr. 40:17 – 41:20 (Bolin), AOC-62; 7/21/2011 Hr'g Tr. 99:10-16 (Kosturos)); (ii) Aurelius purchased approximately $339 million in various WMI securities before settlement discussions began (7/18/2011 Hr'g Tr. 41:13-17, 46:5-10 (Gropper), AU-8); (iii) Centerbridge acquired over $863 million in various WMI securities prior to any settlement discussions

[2] These figures are the gross, face amount of WMI securities purchased by the Settlement Noteholders. During this same period each of the Settlement Noteholders also sold WMI securities. In addition, each of the Settlement Noteholders continued to buy and sell WMI securities during the rest of the case.

(7/20/2011 Hr'g Tr. 214:12-15, 217:18-23 (Melwani), AOC-54); and (iv) Owl Creek purchased over $796 million in WMI securities over this period (7/19/2011 Hr'g Tr. 126:14-17, 146:21-25 (Krueger), AOC-18, 19). Such acquisitions also belie the Equity Committee's arguments that the Settlement Noteholders bought up securities so as to control settlement negotiations. Rather, the evidence shows that the Settlement Noteholders, like many other investors, saw WMI securities as an investment opportunity from the early stages of this lengthy bankruptcy process and long before the Settlement Noteholders' involvement in settlement discussions. The evidence also shows that from the outset the Settlement Noteholders, like many other investors, had an interest in the outcome of this bankruptcy process.

On February 23, 2009, the Debtors, the Creditors' Committee, attorneys from the law firms of White & Case LLP ("White & Case") and Fried, Frank, Shriver & Jacobson, LLP ("Fried Frank"), the Federal Deposit Insurance Corporation ("FDIC") and JP Morgan Chase Bank, N.A. ("JPMC") met for the first of what would become a year-long (or longer) effort to agree upon terms for the settlement of numerous complex disputes among the estates, JPMC and the FDIC. (7/21/2011 Hr'g Tr. 99:7-99:23 (Kosturos).) Following that meeting, the Debtors reached out to Fried Frank and White & Case and asked that some members of their respective groups become restricted for purposes of attempting to negotiate a settlement with JPMC, on the premise that "it's very important when you have your major constituency creditors who hold very large positions in the case participating in negotiations from time to time." (7/21/2011 Hr'g Tr. 101:22-102:3 (Kosturos); 7/18/2011 Hr'g Tr. 51:3-8 (Gropper).)

The First Restricted Period: March 9, 2009 through May 8, 2009

The Settlement Noteholders became involved in negotiations in March, 2009, and the record indicates that from the start, the Settlement Noteholders and the Debtors were cognizant of their duties with respect to trading on MNPI, and therefore adopted a variety of measures to preserve the confidentiality of information exchanged during settlement negotiations. Thus, on March 9, 2009, in advance of a March 10, 2009 settlement meeting to be held at the offices of JPMC's counsel, the Debtors and each of the Settlement Noteholders executed confidentiality agreements. (7/21/2011 Hr'g Tr. 101:5-102:21 (Kosturos); AU-16 (Confidentiality Agreement (Limited) with Aurelius Capital Management, L.P. dated Mar. 9, 2009); EC-24 (Confidentiality Agreement (Limited) with Appaloosa Management, L.P. on behalf of certain funds for which it acts as an investment advisor dated Mar. 9, 2009); EC-111 (Confidentiality Agreement (Limited) with Centerbridge Partners, L.P. on behalf of certain funds for which it acts as an investment advisor dated Mar. 9, 2009); EC-141 (Confidentiality Agreement (Limited) with Owl Creek Asset Management L.P. dated Mar. 9, 2009).)

The March, 2009 Confidentiality Agreements provided for termination upon the earlier of the Debtors filing a disclosure statement, agreement of the parties, or sixty days after execution. (*See, e.g.*, AU-16 at ¶ 13 (Confidentiality Agreement (Limited) with Aurelius).) The Confidentiality Agreements also required the Debtors to disclose publicly all material information shared during negotiations at the conclusion of the agreements. (*See id*. (requiring the Debtors to make public disclosure of "any Confidential Information that constitutes material non-public information under U.S. federal securities laws"); *see also* 7/21/2011 Hr'g Tr. 102:4-21 (Kosturos); 7/18/2011 Hr'g Tr. 53:17-54:12 (Gropper); 7/19/2011 Hr'g Tr. 129:3-7 (Krueger); 7/20/2011 Hr'g Tr. 48:6-17 (Bolin); 7/20/2011 Hr'g Tr. 230:10-231:9 (Melwani).) Pursuant to the confidentiality agreements, each of the Settlement Noteholders agreed either to restrict its entire firm from trading in securities of WMI or to impose an ethical wall to shield confidential information from those trading in WMI securities.

Trading records and confirmation hearing testimony show that Owl Creek, Appaloosa, and Centerbridge did not trade in WMI securities during the period covered by the Confidentiality Agreements. (*See* 7/20/2011 Hr'g Tr. 230:10-231:22 (Melwani); 7/19/2011 Hr'g Tr. 127:9-16, 128:8-129:1 (Krueger); 7/20/2011 Tr. 42:3-10, 52:6-9 (Bolin); AOC-18, 19, 54;

AOC-62.) Likewise, confirmation hearing testimony also shows that Aurelius established an ethical wall to screen those involved in negotiations from those engaged in investments in WMI securities. (*See* 7/18/2011 Hr'g Tr. 50:17-51:23, 54:13-21, 55:25-56:2, 57:1-59:16 (Gropper).) Mr. Gropper further testified that he was the only person at Aurelius permitted to receive confidential information during the first confidentiality period, and described the elaborate steps taken to ensure the efficacy of the ethical wall that separated him from those engaged in trading of WMI securities. (*See id.* at 55:20-56:2, 57:5-58:4.) There was no evidence adduced during the confirmation hearing that would suggest that this ethical wall was breached. Moreover, a review by the Aurelius chief compliance officer at the time did not reveal anything of significance. (*Id.* at 59:13-16.)

After executing the Confidentiality Agreements, the Debtors sent term sheets outlining a proposed JPMC settlement to the Settlement Noteholders on March 9, 2009 and revealed, among other information, that WMI expected a tax refund in the range of $2.6 to $3 billion for the two years preceding the bankruptcy. (*See* 7/20/2011 Hr'g Tr. 232:4-17 (Melwani); 7/20/2011 Hr'g Tr. 46:24-25 (Bolin).) The evidence shows that between March 9, 2009 and the end of April, 2009, the Debtors and JPMC exchanged four term sheets. (*See* AU-18 (Mar. 11, 2009 proposal); AU-19 (Mar. 18, 2009 proposal); EC-11 (comparing 4/16/09 and 4/24/09 proposals).) The evidence also indicates that the Settlement Noteholders did not become aware of the terms set forth in the second set of term sheets until, at the earliest, July, 2009. (7/20/2011 Hr'g Tr., 56:11-24 (Bolin); 7/20/2011 Hr'g Tr., 281:8-282:3 (Melwani).)

The testimony supports the conclusion that the parties remained far apart during the course of those exchanges. In describing JPMC's March 18, 2009 proposal as a "non-response response" to the Debtors' March 11 offer, for example, Mr. Gropper noted:

> [I]t was light-years apart. I mean, basically JPMorgan's response was, you guys get the deposit. And keep in mind that JPMorgan and the debtors were actually negotiating a stipulation at the

> beginning of these cases where JPMorgan was going to just give back the deposit to the debtors. And this was obviously all publicly reported, all occurred in this courtroom. So you know, the fact that JPMorgan was willing to give over the deposit was, you know, not news, because they had already talked about doing it kind of in exchange for nothing else very early on in the case. But other than that, JPMorgan effectively said, we win on every other legal dispute, which I frankly found to be not at all commensurate with the legal rights of the parties.

(7/18/2011 Hr'g Tr. 69:19 – 70:6 (Gropper).)

The uncontroverted testimony shows that these negotiations ended without an agreement being reached and with the negotiating parties so far apart in their respective positions that there was no realistic hope of a compromise on the terms exchanged. The evidence at the confirmation hearing was that the parties, at that time, were "very far apart. They were nowhere close to an agreement or common ground." (7/20/2011 Hr'g Tr. 237:15-19 (Melwani); *see* 7/18/2011 Hr'g Tr. 84:1-17 (Gropper); 7/19/2011 Hr'g Tr. 138:10-21 (Krueger); 7/20/2011 Hr'g Tr. 51:24-52:2 (Bolin) (stating that the settlement discussions "were clearly over and dead.").) It appeared that JPMC was uninterested in acceding to the Settlement Noteholders' or WMI's positions, and the Debtors found JPMC's position – which offered the Debtors the disputed deposit accounts but made few other concessions – unacceptable. (*See also* 7/21/2011 Hr'g Tr. 112:23-113:1 (Kosturos) (noting that parties were "well over three billion dollars apart" in negotiations).) In the midst of those term sheet exchanges, litigation broke out: on March 24, 2009, JPMC commenced its litigation against Debtors regarding the deposit accounts; on April 27, 2009, the Debtors filed the Turnover Action[3]; and on May 1, 2009, the Debtors filed their motion for leave to conduct a Rule 2004 investigation of the business tort claims against JPMC.

[3] "Turnover Action" means that certain adversary proceeding captioned *Washington Mutual, Inc., et al. v. JPMorgan Chase Bank, N.A., et al. (In re Washington Mutual, Inc., et al.),* (Adv. Proc. No. 09-50934), commenced in this Court on April 27, 2009.

On April 30, 2009, the Debtors made good on their promise in the Confidentiality Agreements to disclose publicly all MNPI that had been shared during the negotiations, by filing their March, 2009 Monthly Operating Report and Form 8-K with the SEC. (DX-427.) The Monthly Operating Report disclosed that "[the] current estimate for the total expected refunds, net of potential payments, is in the range of approximately $2.6 - $3.0 billion." (DX-427 (Mar. 2009 Monthly Operating Report) at 9, n. 5.) In addition, the report disclosed details about restricted cash and accrued liabilities. (*See* 7/21/2011 Tr. 114:21-115:13 (Kosturos).) The Monthly Operating Report also disclosed that "JPMorgan . . . may seek to claim all or a portion of the expected tax refunds." (DX-427 (Mar. 2009 Monthly Operating Report) at 9, n. 5.)

On May 6, 2009, two days prior to the expiration of the first confidentiality period, the Settlement Noteholders met with the Debtors and certain of their professionals, including Quinn Emmanuel. (7/18/2011 Hr'g Tr. 76:22 – 77:7 (Gropper).) While the Equity Committee suggests that the Settlement Noteholders received MNPI at this meeting (Equity Committee Objection, ¶ 15), that contention was not borne out by the record. At that meeting, Mr. Rosen of Weil Gotshal & Manges advised that no MNPI would be provided at the meeting. (7/18/2011 Hr'g Tr. 78:24-79:1 (Gropper).) "Mr. Rosen also said at that meeting that based on disclosures that had been made in the monthly operating report or that had been filed prior to that meeting that everyone at the meeting was free to trade." (7/18/2011 Hr'g Tr. 79:1-5 (Gropper).)

The Second Non-Restricted Period: May 9, 2009 through November 16, 2009

The record reflects that at the conclusion of the first restricted period, and prior to re-commencing trading on WMI securities, the Settlement Noteholders took a number of precautions to avoid trading on MNPI. First, the Settlement Noteholders requested and received from the Debtors written confirmation that the Debtors had disclosed all confidential information that constituted MNPI. (*See, e.g.*, AU-25 (May 7, 2009 Email from Brian Rosen to Gerard Uzzi); AU-31 (Dec. 28, 2009 Email from Brian Rosen to Matthew Roose); *see also* 7/21/2011

Hr'g Tr. 113:12-17, 115:14-24 (Kosturos) (stating Debtor complied with Confidentiality Agreement and disclosed all MNPI).) In addition, the Settlement Noteholders testified that they made independent assessments that all MNPI had been disclosed. (*See* 7/20/2011 Hr'g Tr. 233:3-20 (Melwani); 7/18/2011 Hr'g Tr. 81:11-82:12 (Gropper); 7/19/2011 Hr'g Tr. 136:22-137:7 (Krueger), 7/20/2011 Hr'g Tr. 52:21-53:8, 53:15-54:19 (Bolin).)

While some discussions continued during this non-restricted period, confirmation hearing testimony demonstrates that no MNPI was shared during this time. Indeed, the evidence at the confirmation hearing demonstrates that the Debtors and the Settlement Noteholders, when they talked, limited discussions to public information during periods when there were no Confidentiality Agreements in effect. (*See* 7/20/2011 Hr'g Tr. 228:13-229:4 (Melwani); 7/18/2011 Hr'g Tr. 93:14-94:4, 116:9-14, 118:4-18 (Gropper); 7/21/2011 Hr'g Tr. 122:8-11 (Kosturos) (discussing first non-restricted period); 7/19/2011 Hr'g Tr. 144:11-14 (Krueger) (discussing second non-restricted period and stating not involved in settlement discussions at that time).) Moreover, the Debtors and the Settlement Noteholders each engaged in their own independent analysis of these discussions to assess whether there had been any inadvertent disclosure of MNPI. (*See, e.g.,* 7/21/2011 Tr. 154:22-155:19 (Kosturos) (explaining that communications with Settlement Noteholders outside of the confidentiality periods were either vetted through counsel or, if directly with Settlement Noteholders, then only public information was discussed).)

During this non-restricted period (summer and fall of 2009), and subject to the aforementioned precautions, Appaloosa and Centerbridge entered into discussions with JPMC in what one witness testified was an attempt to "find a common ground." In fact, the Appaloosa/Centerbridge proposal was not even committed to writing. (7/20/2011 Hr'g Tr. 2421:18-23 (Melwani); 7/20/2011 Tr. 55:8-18, 58:18-23 (Bolin).) During these discussions the parties did not discuss MNPI. (7/20/2011 Hr'g Tr. 60:3-8 (Bolin).) Even in the absence of

MNPI, however, each voluntarily and independently refrained from trading in WMI securities. Appaloosa's witness testified that it voluntarily restricted trading in WMI securities from some time in July, 2009 until the talks ended on September 2, 2009. (7/20/2011 Hr'g Tr. 42:11-13, 42:17-19 (Bolin).) Centerbridge's trading records show that from August 18, 2009, when JPMC sent a proposal to Appaloosa and Centerbridge, until September 8, 2009, six days after settlement discussions ended, Centerbridge likewise did not purchase or sell any WMI securities. (7/20/2011 Hr'g Tr. 243:22-244:3, 244:25-245:17 (Melwani); AOC-54.)

Like the first stage of negotiations, settlement discussions during the summer of 2009 proved unsuccessful because of the large divergence between the negotiating parties' respective positions, and these discussions were terminated in early September. (7/20/2011 Hr'g Tr. 58:6-59:13 (Bolin) (describing September 2, 2009 meeting with JPMC at which **JPMC withdrew its settlement proposal** and rejected counter-proposals from Appaloosa and Centerbridge, and stating that discussions with JPMC "were dead at that point") (emphasis added); 7/20/2011 Hr'g Tr. 245:2-13 (Melwani) (describing the failure of the summer 2009 negotiations, JPMC's withdrawal of its settlement offer, and JPMC's statement at such meeting that they didn't think "there was anything more to talk about at this point, and they were retracting their proposal from August 18th.").)

<u>The Second Restricted Period: November 16, 2009 through December 31, 2009</u>

On November 16, 2009, each Settlement Noteholder entered into a second Confidentiality Agreement with the Debtors. (7/21/2011 Hr'g Tr. 122:12-25 (Kosturos); AU-27 (Confidentiality Agreement (Limited) with Aurelius Capital Management, L.P. for itself and on behalf of its managed fund entities dated Nov. 16, 2009); DX-412 (Confidentiality Agreement (Limited) with Appaloosa Management, L.P. on behalf of certain funds for which it acts as an investment adviser dated Nov. 16, 2009); DX-413 (Confidentiality Agreement (Limited) with Centerbridge Partners, L.P., on behalf of certain funds for which it acts as an investment adviser dated Nov. 16, 2009).) Again, these Confidentiality Agreements provided for termination upon the earlier of the Debtors filing a disclosure statement, agreement of the parties, or a date certain: December 31, 2009. (*Id.*) Representatives of all four Settlement Noteholders testified that they placed WMI securities on their restricted lists for the duration of this period and trading records confirm that they did not trade in WMI securities. (*See* 7/20/2011 Hr'g Tr. 245:21-247:21 (Melwani); 7/19/2011 Hr'g Tr. 104:18-20, 105:3-5 (Gropper); 7/19/2011 Hr'g Tr. 139:6-8, 139:20-140:16 (Krueger); 7/20/2011 Hr'g Tr. 42:22-43:2, 66:14-17 (Bolin); AOC-18, 19, 54, 62; AU-8.)

As with the initial round of negotiations, the record shows that settlement discussions during the second confidentiality period ended with a vast divide between the parties' negotiating positions. Following execution of the second set of Confidentiality Agreements, and while the Settlement Noteholders had restricted themselves from trading, the Settlement Noteholders met with the Debtors and were advised of the expected value of the additional tax refund – $2.6 billion – that would be available as a result of enactment of the Worker, Homeownership, and Business Assistance Act of 2009.[4] (7/18/2011 Hr'g Tr. 105:11-20 (Gropper).) There is no dispute that the value of that additional refund was MNPI (*see id.* at 105:21-106:1), but the Settlement Noteholders were not trading at that time.

On November 23, 2009, the Debtors re-engaged JPMC in settlement discussions by sending a new settlement proposal that they had vetted with the Settlement Noteholders. (*See* EC-119.) While there were numerous provisions in that term sheet (7/21/2011 Hr'g Tr. 123:24-11 (Kosturos)), "the real meat of this proposal was in the box called taxes . . . whereby WMI would receive . . . thirty nine percent . . . of the tax refunds for years one, two, and three. And

[4] On November 6, 2009, President Obama signed into law The Worker, Homeownership, And Business Assistance Act of 2009, which allowed companies to elect to carry such net operating losses for five years rather than only two years. This affected the Debtors by providing an additional second tax refund opportunity.

JPMorgan would receive the remainder. And then the additional NOL carry back, that's the 2.6 billion dollars that we learned about at the meeting a week prior, was proposed to be split fifty/fifty between WMI and JPMorgan." 7/18/2011 Hr'g Tr. 107:1-11 (Gropper).)

Instead of countering based on the construct of the Debtors' proposal, JPMC made an offer that Mr. Kosturos described as "resetting the bookends." (7/21/2011 Hr'g Tr. 124:14-126:8 (Kosturos); EC-120.) Under that counteroffer, JPMC would receive 100% of the first tax refund and WMI would receive 100% of the second tax refund. In other words, JPMC would take 100% of the refund that was a sure thing and leave WMI with all the risk that the second refund would actually be approved by the IRS and the Congressional Oversight Committee. The Debtors "found this proposal to be really nonresponsive and really had changed the whole dynamics and constructs of what we had been talking about previously" with the result that the parties remained "[v]ery far apart." (7/21/2011 Hr'g Tr. 125-:20-126:8 (Kosturos).) Likewise, JPMC acknowledged after the exchange of term sheets that the parties "remain[ed] fairly far apart in [their] views." (AU-29 (Nov. 30, 2009 Email from Donald McCree to Bill Kosturos).) Confirmation hearing testimony shows that the Debtors' and JPMC's impression was shared by the Settlement Noteholders involved in this stage of the negotiations. (*See, e.g.*, 7/18/2011 Hr'g Tr. 108:13-110:08 (Gropper) (describing these negotiations as "fifty-two card pick-up" and that JPMC's proposal represented a "dramatic, dramatic shift in the risk allocation" and other factors which indicated to him that "the parties were extremely far apart"); 7/20/2011 Hr'g Tr. 70:20-71:4 (Bolin) ("The negotiations - the discussions ended because Mr. McCree had indicated to Mr. Kosturos that he now wanted to go talk to the FDIC. So we were wide and far apart on any kind of an agreement. Now JPMorgan was bringing in another party to the negotiating table, that party was a government agency, which can be particularly unpredictable. And so I had no idea what was going to transpire from that point forward, but our discussions were over with.").)

The Third Non-Restricted Period

On December 30, 2009, the Confidentiality Agreements terminated by agreement of the parties. As before, the Debtors promptly filed their Monthly Operating Report for the month of November and their Form 8-K with the SEC, which attached the Monthly Operating Report, thereby publicly disclosing any material information that had been shared during the negotiations. (DX-428.) The November Monthly Operating Report disclosed that the second tax refund for net operating losses was valued at approximately $2.6 billion. (*See* DX-428 (Nov. 2009 Monthly Operating Report) at 9, n. 5 (disclosing that the Worker, Homeownership, and Business Assistance Act of 2009 "could result in additional refunds of up to approximately $2.6 billion, as to which there are competing claims of ownership").)

As they had at the expiration of the first restricted period, the Debtors also provided the Settlement Noteholders with written confirmation that all MNPI disclosed during the second restricted period had been made public. (*See* AU-31 (Dec. 28, 2009 Email from Brian Rosen to Matthew Roose confirming that the November Monthly Operating Report satisfied their obligation to disclose all MNPI and that the Confidentiality Agreements were terminated); *see also* 7/21/2011 Hr'g Tr. 127:3-11 (Kosturos) ("We determined that we had material nonpublic information and we disclosed it in our November 2009 MOR which was filed on December 30, 2009"); 7/20/2011 Hr'g Tr. 230:22-231:1, 246:25-247-16 (Melwani) (stating that Debtors were obligated by confidentiality agreement to disclose any MNPI and did so via the November 2009 MOR); 7/18/2011 Hr'g Tr. 113:20-24 (Gropper) ("Additionally, we requested and received an e-mail from Mr. Rosen at Weil Gotshal confirming that once the debtors had disclosed the information in the monthly operating report, the debtor's disclosure obligations under the confidentiality agreement would be satisfied"); 7/19/2011 Hr'g Tr. 142:12-143:20 (Krueger) (acknowledging that the Debtors had indicated they had complied with the "cleansing procedures" in the second Confidentiality Agreement); 7/20/2011 Hr'g Tr. 71:18-

72:19 (Bolin) (stating that "[a]ll material nonpublic information had been disclosed with the . . . November operating report which was filed December 30th" and that he made his own determination that all MNPI had been disclosed).)

Furthermore, just as they had after the expiration of the first confidentiality period, the Settlement Noteholders made independent assessments, including by conferring with counsel, that Debtors had publicly disclosed all MNPI and that they were free to resume trading. (7/20/2011 Hr'g Tr. 71:5-13 (Bolin); 7/19/2011 Hr'g Tr. 142:16-143:3 (Krueger); 7/20/2011 Hr'g Tr. 252:17-23 (Melwani); 7/18/2011 Hr'g Tr. 113:25-114:7 (Gropper) ("And lastly, we did our own analysis. I mean, again, the only information we had was a failed back and forth with JPMorgan in which the parties were extremely far apart. There was no semblance of a deal. JPMorgan had quote, reset the bookends in the words of Mr. Kostoros [*sic*], and in the words of Don McCree were very far apart. No one thought a deal was eminent [*sic*], so we concluded independently that we were not in possession of material nonpublic information."). Once the Debtors published the information about their second tax refund, the trading price in the PIERS jumped almost overnight from about $8 per share to about $20. (7/21/2011 Hr'g Tr. 75:1-76:1 (Melwani).) At the conclusion of this confidentiality period, Aurelius and Centerbridge resumed trading in WMI securities by purchasing the Debtors' senior subordinated debt and PIERS. (AOC-54; AU-8.)[5]

In early 2010, settlement negotiations resumed among the Debtors, JPMC and the FDIC, and on March 12, 2010, the Debtors announced in open court that a settlement had been reached, subject to approval of the FDIC and the Court. (7/21/2011 Hr'g Tr. 135:13-136:5 (Kosturos).) Between early March, 2010 and October, 2010, several of the Settlement Noteholders were given access to certain information relating to the Global Settlement

[5] Aurelius' trading records show that it had been purchasing PIERS units throughout the fall. (AU-8.)

Agreement. However, as discussed below, during this period, in each instance when the Settlement Noteholders obtained MNPI, they refrained from trading until such information had been made public.

Between December 30, 2009 and October 6, 2010, Owl Creek did not participate in settlement negotiations, but did receive draft plans and/or disclosure statements. (7/19/2011 Hr'g Tr. 144:11-25 (Krueger).) When in possession of these draft plans and/or statements, Owl Creek voluntarily restricted its trading in WMI securities. (7/19/2011 Hr'g Tr. 145:1-8 (Krueger).) Owl Creek would keep these restrictions in place until after the relevant documents had been released to the public. (*Id.*)

Between December 30, 2009 and March 12, 2010, Aurelius played no role in the settlement negotiations. (7/18/2011 Hr'g Tr. 116:9-17 (Gropper).) To ensure that it did not receive MNPI during this time, Aurelius gave strict instructions to its counsel not to communicate any MNPI that counsel received from the Debtors. (*Id.* at 118:4-15.) After the settlement agreement was publicly announced in March, 2010, the Debtors and JPMC requested that Aurelius become a party to the settlement agreement. (*Id.* at 121:19-122:11.) Under this arrangement, Aurelius received draft plans, draft disclosure statements, and draft settlement agreements on four occasions. (*Id.*) On each of those occasions, Aurelius voluntarily ceased trading in WMI securities until the relevant documents were publicly filed with the Court. (*Id.*) Mr. Gropper testified that the four restricted periods lasted no more than a few days. (7/19/2011 Hr'g Tr. 78:2-5 (Gropper).)

Between December 30, 2009 and March 12, 2010, Centerbridge was not involved in the settlement discussions and first learned the terms of the settlement agreement when it was publicly announced on March 12, 2010. (7/20/2011 Hr'g Tr. 260:3-13 (Melwani).) On March 23, 2010, the Debtors asked Centerbridge to review the plan and sign a plan support agreement. (*Id.* at 260:14-262:11.) Accordingly, Centerbridge restricted its trading from March 23 to March

26, 2010, when the plan was publicly disclosed. (*Id.*) Again on May 15, 2010, Centerbridge received the Debtors' plan and restricted its trading until the plan was filed on May 16, 2010. (*Id.*) Although it did not receive any non-public information, Centerbridge also restricted trading from May 18 through May 21, 2010 because it had participated in an update call. (*Id.*)

Between February 1, 2010 and the announcement of the settlement in open court on March 12, 2010, Appaloosa did not trade in WMI securities. (7/20/2011 Hr'g Tr. 76:12-15 (Bolin); AOC-62.) Appaloosa voluntarily restricted trading from February 1, 2010 until just prior to March 4, 2010. (*Id.* at 43:4-11, 75:18-76:1.) Mr. Bolin explained that, during this period, Appaloosa "became aware that discussions between JPMorgan and the FDIC and the debtor may have gotten some traction, and for that reason, we thought it prudent not to trade during that time." (*Id.* at 44:7-17.) Appaloosa, however, did not think it possessed MNPI at that time. (*Id.* at 44:18-23.) Appaloosa did not participate in negotiating the terms of the March 4, 2010 settlement proposal. (*Id.* at 75:9-11, 82:7-12.) However, Appaloosa restricted trading in WMI securities from March 4, 2010 until March 12, 2010. (*Id.* at 76:2-15.) Because it had received an advance draft of the Debtors' proposed disclosure statement, Appaloosa also restricted trading in WMI securities from the evening of March 22, 2010 until the filing of the first disclosure statement on March 26, 2010. (*Id.* at 43:4-11; 77:4-78:4.) Throughout the month of May, 2010, Appaloosa did not trade in WMI securities because it was to be a party to the Global Settlement Agreement and was privy to discussions between the Debtors and the FDIC on the reconstituted plan. (*Id.* at 102:1-3; 157:11-19.)

<u>Efforts To Avoid Trading On MNPI Throughout The Chapter 11 Case</u>

The evidence presented at the confirmation hearing reveals that throughout all of the restricted and non-restricted periods, and throughout the chapter 11 process in general, the Settlement Noteholders and the Debtors endeavored to shield settlement negotiations and to limit the extent of informational exchange so as to prevent improper trading in WMI securities. The evidence shows that such efforts included that certain of the Settlement Noteholders voluntarily restricted trading in WMI securities during various periods. For example, Appaloosa voluntarily refrained from trading from July, 2009 through September 2, 2009, from January 28, 2010 through March 12, 2010. (7/20/2011 Hr'g Tr. 42:3-44:23 (Bolin); AOC-62.) Likewise, Centerbridge restricted itself upon receiving one of JPMC's proposals on August 18, 2009, even absent a governing Confidentiality Agreement. (7/21/2011 Hr'g Tr. 41:23-42:11 (Melwani).)

Similarly, in certain instances the Settlement Noteholders prefaced meetings by making clear that they were engaged in trading, and therefore did not want and would not accept MNPI. (7/21/2011 Hr'g Tr. 117:6-8 (Kosturos); 7/18/2011 Hr'g Tr. 77:9-78:12, 78:22-79:10 (Gropper) (stating that during the May 6, 2009 meeting, the Debtors were "in a listening mode at this meeting and allowing us to transmit to them our view" and stating that during such meeting "it was made very clear that the debtor wasn't going to provide us material nonpublic information. We confirmed that we did not want any material nonpublic information.").)

Further, there was some information that the Debtors refused to share with the Settlement Noteholders *because* the Debtors did not want to disclose such information publicly. That is, cognizant of their obligation to make public all MNPI shared during negotiations, the Debtors opted not to share some confidential information with the Settlement Noteholders. (7/21/2011 Hr'g Tr. 104:8-23 (Kosturos).)

Finally, the Settlement Noteholders utilized Fried Frank as a screen during the non-restricted periods, to further insulate the Settlement Noteholders from MNPI. (7/20/2011 Hr'g Tr. 78:8-19 (Bolin); 7/19/2011 Hr'g Tr. 145:9-18 (Krueger); 7/20/2011 Hr'g Tr. 228:13-21 (Melwani); 7/18/2011 Hr'g Tr. 121:23-122:11 (Gropper).) When Confidentiality Agreements were not in place and Fried Frank received material, nonpublic documents from the Debtors, Fried Frank would advise the Settlement Noteholders that it had received certain documents and that if they wanted to receive the documents they would have to restrict trading. (*See, e.g.*, *id.*)

ARGUMENT

I. THE EVIDENCE ADDUCED AT THE CONFIRMATION HEARING DOES NOT SUPPORT THE ALLEGATION THAT THE SETTLEMENT NOTEHOLDERS ENGAGED IN INSIDER TRADING.

Under the well developed standards for insider trading, not all informational advantages are prohibited. Rather, in order for there to be a violation of the insider trading laws, the evidence must satisfy four elements: (i) a purchase or sale of a security; (ii) while in possession of material non-public information; (iii) in breach of a duty of trust or confidence; and (iv) done with scienter, or a knowing state of mind. *See United States v. Corbin*, 729 F. Supp. 2d 607, 611-12 (S.D.N.Y. 2010). The Creditors' Committee submits that the evidence presented at the confirmation hearing does not establish that the Settlement Noteholders traded in breach of any duty or possessed the requisite scienter as to any of the trades at issue, or that any non-public information the Settlement Noteholders possessed during the non-restricted times was material.[6]

A. Applicable Standard.

Liability for insider trading is governed by Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder. The United States Supreme Court has held that trading on MNPI alone does not constitute securities fraud. *See United States v. O'Hagan*, 521 U.S. 642, 661 (1997) ("There is under § 10(b) . . . no 'general duty between all participants in market transactions to forego actions based on material, nonpublic information.'") (quoting *Chiarella v. United States*, 445 U.S. 222, 233 (1980)); *Dirks v. Sec. & Exch. Comm'n*, 463 U.S. 646, 654 (1983) (to violate § 10(b) and Rule 10b-5 in the insider trading context, "[t]here must also be manipulation or deception") (quotation marks omitted); *Chiarella*, 445 U.S. at 234-35 ("Section 10(b) is aptly described as a catchall provision, but what it catches must be

[6] The Court need not address whether information is material if it finds that there is insufficient evidence to conclude that the Settlement Noteholders breached any duty or acted with scienter.

fraud. . . . [A] duty to disclose under §10(b) does not arise from the mere possession of nonpublic market information.”). For such fraud in the form of manipulation or deception to exist, in turn, there must be a breach of a duty to another in connection with the purchase or sale of a security. *See O’Hagan*, 521 U.S. at 661; *United States v. Chestman*, 947 F.2d 551, 564-65 (2d Cir. 1991).

B. “Classical Theory” of Insider Trading.

An individual may be held liable under the traditional or “classical” theory of insider trading under Section 10(b) and Rule 10b-5 when a “corporate insider trades in the securities of his corporation on the basis of material, nonpublic information.” *O’Hagan*, 521 U.S. at 651-52. This is because “a relationship of trust and confidence [exists] between the shareholders of a corporation and those insiders who have obtained confidential information by reason of their position with that corporation.” *Id.* at 652 (quoting *Chiarella*, 445 U.S. at 228). This relationship of trust “gives rise to a duty to disclose [or to abstain from trading] because of the necessity of preventing a corporate insider from . . . taking unfair advantage of . . . uninformed . . . stockholders.” *Id.* (citation and quotation marks omitted). As such, in a classical insider trading case, the deceiving party owes a duty to the corporation or its shareholders because they are officers, directors, or some other traditional insider of the company. Here, there is no evidence that the Settlement Noteholders were insiders of the Debtors.

C. The Temporary Insider Theory.[7]

In an effort to place a duty on the Settlement Noteholders that would not otherwise exist, the Equity Committee has argued that the Settlement Noteholders acted as “temporary insiders,” but the evidence at the confirmation hearing failed to support this theory.

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[7] See also the discussion of the non-statutory insider issue at pages 34 to 37.

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The temporary insider theory "clothes an outsider with temporary insider status when the outsider obtains access to confidential information solely for corporate purposes in the context of 'a special confidential relationship.'" *Chestman*, 947 F.2d at 565. "The temporary insider thereby acquires a correlative fiduciary duty to the corporation's shareholders." *Id.* Typically, temporary insiders are underwriters, lawyers, or consultants who "'gain[] access to confidential information through [their] relationships with a corporation.'" *Sawant v. Ramsey*, 742 F. Supp. 2d 219, 229 (D. Conn. 2010) (quoting *Chestman*, 947 F.2d at 565). As the Supreme Court explained in *Dirks v. Securities & Exchange Commission*:

> Under certain circumstances, such as where corporate information is revealed legitimately to an underwriter, accountant, lawyer, or consultant working for the corporation, these outsiders may become fiduciaries of the shareholders. The basis for recognizing this fiduciary duty is not simply that such persons acquired nonpublic corporate information, but rather that they have entered into a <u>special confidential relationship in the conduct of the business of the enterprise</u> and are given access to information solely for corporate purposes . . . . For such a duty to be imposed, however, the corporation must expect the outsider to keep the disclosed nonpublic information confidential, and the relationship at least must imply such a duty.

463 U.S. at 655 n.14 (citations omitted) (emphasis added).

During the course of the bankruptcy proceedings there were limited periods ("restricted times") in which the Settlement Noteholders took on a duty to disclose or not to trade by receiving certain material confidential information. These restricted times were only those periods during which the Confidentiality Agreements were in effect, as well as certain limited periods during which the Settlement Noteholders possessed advance copies of certain soon-to-be-filed documents. The evidence shows that during these restricted times the Settlement Noteholders either refrained from trading or, in the case of Aurelius during the first confidentiality period, erected an ethical wall.

The Creditors' Committee has seen no evidence that the Settlement Noteholders acted as temporary insiders at any point in this chapter 11 proceeding. There is no evidence that they acted as lawyers, advisors, or consultants and there is no evidence that they entered into a special confidential relationship with the Debtors in the conduct of the Debtors' business. *See, e.g.*, *Sawant v. Ramsey*, 742 F. Supp. 2d at 238 (court rejected temporary insider status because outsider, who was a major shareholder of the company, was not a professional advisor or consultant to the company, was not employed by the company, did not act as an advisor or consultant to the company, nor did he receive access to confidential information "'solely for corporate purposes in the context of a special confidential relationship;'" rather, the court found that the outsider used the discussions in his capacity as a shareholder) (quoting *Chestman*, 947 F.2d at 565).

The Equity Committee alleged in the Equity Committee Objection that "[e]ven during the non-restricted periods, the evidence will show that the Settlement Noteholders, and their counsel, received information that was not shared with other creditors or the public, in furtherance of the special confidential relationship between them that pervaded the case." (Equity Committee Objection at 25.) However, this argument seeks to relieve the Equity Committee of the burden of demonstrating ***all*** the elements of an insider trading claim in the non-classical setting. That is, not only must the information at issue be ***material***, but the recipient must be a temporary insider who is under a duty not to trade. In this case, none of the evidence at the confirmation hearing indicates that the Settlement Noteholders possessed a relationship of trust and confidence with any alleged source of any MNPI. In fact, the evidence adduced at the confirmation hearing shows that on a number of occasions, the Debtors acted without consulting the Settlement Noteholders in trying to forge a settlement with JPMC, the FDIC, and others. (7/21/2011 Hr'g Tr. 132:9-12 (Kosturos) ("There were many meetings throughout this case where we didn't tell the noteholders or anybody in this case what the debtor was doing. So we found it under no obligation to let people know what the debtor was doing.").)

D. **The Settlement Noteholders Did Not Breach A Duty Not To Trade.**

The Equity Committee also produced no evidence to support the inference that MNPI was shared while the Settlement Noteholders were unrestricted. Instead, the uncontroverted testimony shows that the Debtors specifically withheld MNPI during times when the Confidentiality Agreements were not in effect, during which times all parties knew that the Settlement Noteholders were not restricting their trading. (7/21/2011 Hr'g Tr. 104:8-23, 122:8-11, 153:5-7 (Kosturos); *see also* 7/20/2011 Hr'g Tr. 228:13-229:4 (Melwani); 7/18/011 Hr'g Tr. 93:14-94:4, 116:9-14, 118:4-18 (Gropper).) Conversely, when the Settlement Noteholders were under a duty not to trade on MNPI, the evidence shows that they observed that duty by not trading or by establishing an informational screen. The Equity Committee's claims of insider trading therefore cannot withstand the evidence adduced at the confirmation hearing. The "'absence of any expectation of confidentiality or breach of a duty of confidentiality is fatal to the [] claim.'" *Securities & Exch. Comm'n v. Obus*, No. 06 Civ. 3150 (GBD), 2010 U.S. Dist. LEXIS 98895, *44 (S.D.N.Y. Sept. 20, 2010) (quoting *Securities & Exch. Comm'n v. Rorech,* 720 F. Supp. 2d 367 (S.D.N.Y. 2010)).

The Settlement Noteholders only owed a duty to disclose or abstain from trading during the limited periods of time covered by the Confidentiality Agreements and, potentially, brief periods between March, 2010 and May, 2010. However, trading records and the confirmation hearing testimony reflect that during these times (when the Settlement Noteholders had a duty) they either did not trade or established an ethical wall. (*See* 7/18/2011 Hr'g Tr. 54:13-21, 55:25-56:2, 57:1-59:16, 104:18-20, 105:3-5, 121:19-122:11 (Gropper); 7/19/2011 Hr'g Tr. 78:2-16 (Gropper); 7/19/2011 Hr'g Tr. 128:8-129:1, 139:6-140:16, 144:23-145:18 (Krueger); 7/20/2011 Hr'g Tr. 42:3-10, 52:6-9, 42:22-43:2, 66:14-17, 76:2-15, 43:4-11, 102:1-3, 157:11-19

(Bolin); 7/20/2011 Hr'g Tr. 230:10-231:22, 245:21-247:21, 260:19-261:13 (Melwani).) Thus, there is no evidence in the record that the Settlement Noteholders breached any duty with respect to their trading activities when one actually existed.

As detailed above, between March 9, 2009 and April 30, 2009, when the first set of Confidentiality Agreements were in effect, Owl Creek, Appaloosa, and Centerbridge did not trade in WMI securities at all, and Aurelius established an ethical wall to permit the limited trading it conducted. (*See* 7/20/2011 Hr'g Tr. 230:10-231:22 (Melwani); 7/19/2011 Hr'g Tr. 128:8-129:1 (Krueger); 7/20/2011 Hr'g Tr. 42:3-10, 52:6-9 (Bolin); 7/18/2011 Hr'g Tr. 54:13-21, 55:25-56:2, 57:1-59:16(Gropper).)

After the first restricted period expired, the Debtors publicly disclosed all the MNPI that had been shared, with the result that the Settlement Noteholders' duty to abstain from trading terminated. (*See* AU-25 (May 7, 2009 Email from Brian Rosen to Gerard Uzzi) (confirming all MNPI had been disclosed in the April MOR); *see also* 7/21/2011 Hr'g Tr. 113:12-17, 115:14-24 (Kosturos) (stating Debtors complied with Confidentiality Agreement and disclosed all MNPI); 7/20/2011 Hr'g Tr. 233:3-20 (Melwani) (stating Settlement Noteholders confirmed with Debtors and made independent assessments that all MNPI had been publicly disclosed); 7/18/2011 Hr'g Tr. 81:11-82:12 (Gropper) (same); 7/19/2011 Hr'g Tr. 136:22-137:7 (Krueger) (same); 7/20/2011 Hr'g Tr. 52:21-53:8, 53:15-54:19 (Bolin) (same).) There were no facts introduced at the confirmation hearing demonstrating that the Settlement Noteholders had a duty to abstain from trading or to disclose during the first unrestricted period, which lasted from April 30, 2009 to November 16, 2009.

Between November 16, 2009 and December 30, 2009, when the second set of Confidentiality Agreements were in effect, none of the Settlement Noteholders traded WMI securities. (*See* 7/20/2011 Hr'g Tr. 245:21-247:21 (Melwani); 7/18/2011 Hr'g Tr. 104:18-20, 105:3-5 (Gropper); 7/19/2011 Hr'g Tr. 139:6-140:16 (Krueger); 7/20/2011 Hr'g Tr. 42:22-43:2, 66:14-17 (Bolin); AOC-18, 19, 54, 62; AU-8.)

The Debtors confirmed that they publicly disclosed any MNPI shared during the second restricted period, and there is no evidence that the Settlement Noteholders were given any MNPI during the third non-restricted period (*i.e.*, after the agreements terminated until the Debtors announced the Global Settlement Agreement in March 2010). (*See*, *e.g.*, AU-31 (Dec. 28, 2009 Email from Brian Rosen to Matthew Roose); *see also* 7/21/2011 Hr'g Tr. 127:3-11 (Kosturos) (stating Debtors disclosed MNPI in the November 2009 MOR); 7/20/2011 Hr'g Tr. 252:12-23 (Melwani) (same); 7/18/2011 Hr'g Tr. 111:22-112:22, 113:5-114:7 (Gropper) (same); 7/19/2011 Hr'g Tr. 142:12-143:8, 143:20 (Krueger) (same); 7/20/2011 Hr'g Tr. 67:9-20, 71:5-13, 71:16-72:19 (Bolin) (same).) Accordingly, the Settlement Noteholders did not have any duty to abstain from trading or disclose during this third non-restricted time period.

Finally, in the brief periods in which the Settlement Noteholders learned MNPI relating to the Global Settlement Agreement and Modified Plan terms, the Settlement Noteholders refrained from trading in WMI securities until the MNPI was publicly disclosed by the Debtors. (*See* 7/18/2011 Hr'g Tr. 121:19-122:11 (Gropper); 7/19/2011 Hr'g Tr. 78:2-16 (Gropper); 7/19/2011 Hr'g Tr. 144:23-145:18 (Krueger); 7/20/2011 Hr'g Tr. 76:2-15, 43:4-11, 102:1-3, 157:11-19 (Bolin); 7/20/2011 Hr'g Tr. 260:19-261:13 (Melwani).) As such, the Settlement Noteholders only had a duty to refrain from trading in WMI securities during the limited periods while they were in possession of MNPI, and the evidence is that they complied with that duty.

E. No Evidence Of Scienter Has Emerged

Another element of an insider trading claim is that the trader must have acted with "scienter," or a knowing state of mind. *Institutional Investors Grp v. Avaya, Inc.*, 564 F.3d 242, 251 (3d Cir. 2009).[8] Scienter is a mental state that incorporates an "intent to deceive, manipulate, or defraud and necessitates a 'knowing or reckless state of mind.'" *In re Heckmann Corp. Sec. Litig.*, No. 10-378, 2011 U.S. Dist. LEXIS 63830, at *37 (D. Del. June 16, 2011) (quoting *Avaya*, 564 F.3d at 252). To establish scienter, a plaintiff must show that all of the facts, taken collectively, give rise to a strong inference of either reckless or conscious behavior. *Avaya*, 564 F.3d at 267.[9] Courts define reckless conduct as conduct which is "highly unreasonable" and which represents an "extreme departure from the standards of ordinary care." *See In re Heckmann Corp. Sec. Litig.*, 2011 U.S. Dist. LEXIS 63830, at *37 (citation and internal quotation marks omitted). An inference of scienter is strong if it is "'cogent and at least as compelling as any opposing inference of nonfraudulent intent.'" *Avaya*, 564 F.3d at 267 (quoting *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 313 (2007)).

The record shows nothing that suggests to the Creditors' Committee that any of the Settlement Noteholders acted with the requisite state of mind to support an insider trading claim. To the contrary, the Creditors' Committee believes the following evidence adduced at confirmation hearing demonstrates a conscious effort by the Settlement Noteholders to comply with federal securities laws and to avoid trading on MNPI: prior to being exposed to MNPI, when the Settlement Noteholders were asked to participate in settlement discussions and become restricted, they entered into Confidentiality Agreements with the Debtors;[10] during the restricted

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[8] As noted above, at pages 2-25, despite the Equity Committee's attempt to elicit testimony to the contrary, there is insufficient evidence to conclude that the Settlement Noteholders at any point impermissibly traded in the Debtors' securities while in possession of MNPI. In the absence of such evidence, the Equity Committee has failed to establish that essential element of an insider trading claim.

[9] Courts in the Third Circuit have applied the *Tellabs* motion to dismiss standard for establishing scienter on a motion for summary judgment. *See Pennmont Sec. v. Wallace*, No. 06-1646, 2008 U.S. Dist. LEXIS 25832, *20 & n.5 (E.D. Pa. Mar. 27, 2008) (employing *Tellabs* standard at summary judgment stage and explaining that "'this Court believes the *Tellabs* analysis is at least instructive in the summary judgment context.'") (quoting *Feinberg v. Benton*, No. 05-4847, 2007 U.S. Dist. LEXIS 91561 (E.D. Pa. Dec. 13, 2007)).

[10] (7/21/2011 Hr'g Tr. 102:4-21 (Kosturos).)

periods covered by the Confidentiality Agreements, the Settlement Noteholders either refrained from trading in WMI securities or imposed ethical walls that protected the confidential information;[11] the Settlement Noteholders contractually required the Debtors to publicly disclose any MNPI at the conclusion of the restricted periods, which the Debtors did;[12] the Settlement Noteholders sought and received written confirmation from Debtors' counsel that all MNPI had been disclosed ***prior*** to removing WMI trading restrictions;[13] the Settlement Noteholders made independent assessments that they did not possess MNPI (and/or that any material information they had received in confidence had been publicly disclosed) ***prior*** to trading;[14] when the Settlement Noteholders were not subject to Confidentiality Agreements or voluntarily restricted from trading, they made it known to the Debtors that they did not want to discuss or receive MNPI;[15] the Settlement Noteholders each had internal policies designed to avoid insider trading and no evidence has been adduced suggesting that those internal policies were ever violated; the Settlement Noteholders voluntarily refrained from trading during periods when they had

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[11] (*See* 7/20/2011 Hr'g Tr. 230:10-231:22, 245:21-247:21, 260:19-261:13 (Melwani); 7/19/2011 Hr'g Tr. 128:8-129:1, 139:6-140:16, 144:23-145:18 (Krueger); 7/20/2011 Hr'g Tr. 42:3-10, 52:6-9, 42:22-43:2, 66:14-17, 76:2-15, 43:4-11, 102:1-3, 157:11-19 (Bolin); 7/18/2011 Hr'g Tr. 54:13-21, 55:25-56:2, 57:1-59:16, 104:18-20, 105:3-5, 121:19-122:11 (Gropper); 7/19/2011 Hr'g Tr. 78:2-16 (Gropper).)

[12] (*See*, *e.g.*, AU-16 at ¶ 13 (Confidentiality Agreement (Limited) with Aurelius) (requiring the Debtors to make public disclosure of "any Confidential Information that constitutes material non-public information under U.S. federal securities laws"); *see also* 7/21/2011 Hr'g Tr. 102:4-21 (Kosturos); 7/18/2011 Hr'g Tr. 53:17-54:12 (Gropper); 7/19/2011 Hr'g Tr. 129:2-7 (Krueger); 7/20/2011 Hr'g Tr. 48:6-17 (Bolin).)

[13] (*See*, *e.g.*, AU-25 (May 7, 2009 Email from Brian Rosen to Gerard Uzzi); AU-31 (Dec. 28, 2009 Email from Brian Rosen to Matthew Roose); *see also* 7/21/2011 Hr'g Tr. 113:12-17, 115:14-24, 127:3-11 (Kosturos) (stating Debtor complied with confidentiality agreement and disclosed all MNPI in the March and November MORs).)

[14] (7/20/2011 Hr'g Tr. 233:3-20, 252:12-23 (Melwani); 7/18/2011 Hr'g Tr. 81:11-82:12, 111:22-112:20, 113:5-114:7, 113:25-114:7 (Gropper); 7/19/2011 Hr'g Tr. 136:22-137:7, 142:12-143:8, 143:20 (Krueger); 7/20/2011 Hr'g Tr. 52:21-53:8, 53:15-54:19, 67:9-20, 71:5-13, 71:16-72:19 (Bolin).)

[15] (*See* 7/20/2011 Hr'g Tr. 228:13-229:4 (Melwani); 7/19/2011 Hr'g Tr. 118:4-18 (Gropper); 7/21/2011 Hr'g Tr. 122:8-11 (Kosturos); 7/19/2011 Hr'g Tr. 144:11-14 (Krueger).)

concerns about the perception that could be drawn if they were to trade;[16] the Settlement Noteholders used Fried Frank to screen MNPI;[17] and both Fried Frank and White & Case entered into Confidentiality Agreements with the Debtors that restricted them from sharing confidential information with the Settlement Noteholders.[18] In light of the foregoing, the Creditors' Committee does not believe that evidence sufficient to demonstrate scienter was offered at the confirmation hearing.

F. <u>All Material Information Was Publicly Disclosed By The Debtors Before Settlement Noteholders Traded While In Possession Of Same.</u>

Even if a party seeking to prove an insider trading claim satisfies the "duty" and "scienter" elements, it still must show that the non-public information on which the investor traded was "material." Information is material if there is a "substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the total mix of [available] information." *Sec. & Exch. Comm'n v. Rorech*, 720 F. Supp. 2d 367, 410 (S.D.N.Y. 2010) (citation and quotation marks omitted). "With respect to 'contingent or speculative' information, 'materiality will depend at any given time upon a balancing of both indicated probability that the event will occur and the anticipated magnitude of the event in light of the totality of the company activity.'" *Id.* (quoting *Basic, Inc. v. Levinson*, 485 U.S. 224, 238 (1988)). Thus, information is not material if it merely confirms information that is "fairly obvious" to those knowledgeable in the market. *Id.*

The Equity Committee argues that the Settlement Noteholders traded on MNPI because some of the settlement proposals exchanged between the Debtors and JPMC (of which

[16] (7/18/2011 Hr'g Tr. 121:19-122:11 (Gropper); 7/19/2011 Hr'g Tr. 145:1-8 (Krueger); 7/20/2011 Hr'gTr. 43:4-8, 44:7-23 (Bolin).)

[17] (7/20/2011 Hr'g Tr. 78:8-19 (Bolin); 7/19/2011 Hr'g Tr. 145:9-10 (Krueger); 7/20/2011 Hr'g Tr. 228:13-21 (Melwani); 7/18/2011 Hr'g Tr. 121:23-122:5 (Gropper).)

[18] (7/21/2011 Hr'g Tr. 100:7-13 (Kosturos).)

the Settlement Noteholders were aware) were material. The Equity Committee confuses confidentiality with materiality. Information that is confidential is not necessarily material, because the applicable standard requires the information at issue to be *both* material *and* nonpublic. *Rorech*, 720 F. Supp. 2d at 409. The Settlement Noteholders' possession of non-public information does not necessarily make it material. Under the facts adduced at the confirmation hearing, the Creditors' Committee submits that the term sheets at issue (that were miles apart and which never materialized into a settlement) and the proposals represented thereby were not material, given the enormous disparity between the respective offers and counteroffers, the length of time between, and lapses in, settlement discussions, and in some instances, the lack of involvement by all constituents whose assent would be necessary to make any proposal become an actual agreement.[19]

First, the testimony was extensive and uncontroverted that there was and could be no agreement on any point until there was agreement on all points. Each of five witnesses (four of whom had been sequestered) testified to the same effect. (*See* 7/21/2011 Hr'g Tr. 109:8-18 (Kosturos); 7/20/2011 Hr'g Tr. 238:3-239:9 (Melwani) (stating term sheets here were not material); 7/18/2009 Hr'g Tr. 84:1-17 (Gropper) (same); 7/19/2011 Hr'g Tr. 138:10-21, 143:25-144:4 (Krueger) (same); 7/20/2011 Hr'g Tr. 72:20-73:5, 53:24-54:19 (Bolin) (same); *see also* 7/20/2011 Hr'g Tr. 70:15-71:4 (Bolin) (stating that JPMC would bring FDIC into the negotiations which would make settlement terms even more uncertain).) To say that one term was "agreed" upon during early stages in negotiations ignores the reality that any agreement on that term was <u>*entirely*</u> contingent upon agreement to <u>*the rest*</u> of the terms. The term sheets (which included a large number of moving parts) reflected negotiating positions, not final terms

[19] In this regard, it is worth noting that on several occasions, the Settlement Noteholders were not aware of discussions that were ongoing between the Debtors and JPMC – discussions which superseded, and underscored the immateriality of, the information they did have.

– particularly when the parties took bargaining positions that left them far apart. *See*, *e.g.*, *Rorech*, 720 F. Supp. 2d at 411 (holding that Deutsche Bank's potential recommendation to restructure a bond offering was "speculative information that does not rise to the level of materiality" because, among other things, whether the financial sponsors would follow the recommendation was uncertain because of tax and jurisdictional concerns).

Furthermore, the uncontroverted testimony shows that the term sheets at issue represented negotiating positions that were so far apart that there was no realistic hope of a settlement on those terms. The evidence at the confirmation hearing was that the parties, during the March, 2009 negotiations, were "very far apart. They were nowhere close to an agreement or common ground." (7/20/2011 Hr'g Tr. 237:15-19 (Melwani); *see* 7/18/2011 Hr'g Tr. 84:5-17 (Gropper); 7/19/2011 Hr'g Tr. 138:10-21 (Krueger); 7/20/2011 Hr'g Tr. 51:24-52:2 (Bolin) (stating that the settlement discussions "were clearly over and dead."); 7/21/2011 Hr'g Tr. 112:23-113:1 (Kosturos) (noting that parties were "well over three billion dollars apart" in negotiations).) Likewise, the summer, 2009 discussions were far enough apart that JPMC pulled its offer off the table and walked from the negotiations in September, 2009. (7/20/2011 Hr'g Tr. 58:6-59:13 (Bolin) (describing September 2, 2009 meeting with JPMC at which JPMC withdrew its settlement proposal and rejected counter-proposals from the Settlement Noteholders, and stating that discussions with JPMC "were dead at that point"); 7/20/2011 Hr'g Tr. 244:6-245:13 (Melwani) (describing the failure of the summer 2009 negotiations, and noting that JPMC stated at such meeting that it didn't think "there was anything more to talk about at this point, and they were retracting their proposal from August 18th.").)

The summer 2009 discussions also cannot qualify as MNPI because the information contained therein was not the Debtors' information. It belonged to Centerbridge and Appaloosa, who had entered into the discussions in an attempt to move the settlement talks forward with terms that they would find palatable. (*See* 7/20/2011 Hr'g Tr. 57:22-58:1 (Bolin) (stating that Bolin represented Appaloosa only); 7/20/2011 Hr'g Tr. 242:2-243:8 (Melwani) (explaining that the "proposal was our information").) If JPMC had agreed to these terms, Centerbridge and Appaloosa would have been in no position to effect a settlement because only the Debtors had that right. (*See* 7/20/2011 Hr'g Tr. 55:5-7 (Bolin).) Even if the Debtors had agreed, any settlement would still have remained subject to negotiation and approval of a number of other parties, including the Creditors' Committee, the FDIC, and ultimately the Court. *See, e.g.*, *Rorech*, 720 F. Supp. 2d at 411 (finding potential recommendation to restructure a bond offering was "speculative information that does not rise to the level of materiality" in part because the final decision to restructure the bond offering was up to the financial sponsors, not Deutsche Bank). Thus, the exchange between JPMC and Centerbridge and Appaloosa was no more than two creditors trying to "find a common ground." (7/20/2011 Hr'g Tr. 55:8-18 (Bolin).)

Finally, the Debtors considered the question of what was material and what was not at the end of the two confidentiality periods and did not disclose any of the terms of the settlement discussions. This decision, made in consultation between the Debtors, Alvarez and Marsal, and their counsel at Weil Gotshal & Manges, that the settlement discussions were not material is highly probative of the issue and entitled to considerable weight since the Debtors were the issuer of the securities being traded.

Based on the evidence submitted at the confirmation hearing, the only information that can reasonably be labeled "material," within the meaning of the securities laws, was shared with the Settlement Noteholders during the two short periods (3/10/09 – 5/8/09, and 11/17/09 – 12/30/09) when the Confidentiality Agreements were in effect, and during the brief periods between March, 2010 and May, 2010, when the Settlement Noteholders voluntarily abstained from trading in WMI securities. The "material" information was the expected tax refunds and details about restricted cash, accrued liabilities, and intercompany loans, and documents relating to the announced but not yet filed Global Settlement Agreement. However, consistent with their obligations under the Confidentiality Agreements, the Debtors publicly disclosed this information at the end of each of the two contractual confidentiality periods. (7/21/2011 Hr'g Tr. 113:12-17, 115:14-24, 127:3-128:24 (Kosturos) (stating Debtors complied with confidentiality agreement and disclosed all MNPI in March and November 2009 MORs); s*ee also, e.g.*, AU-25 (May 7, 2009 Email from Brian Rosen to Gerard Uzzi); AU-31 (Dec. 28, 2009 Email from Brian Rosen to Matthew Roose).) The Debtors also disclosed the material information in the March to May, 2010 time period by announcing the terms of the settlement in open court and by filing documents that disclosed the material information.

II. THERE IS NO BASIS FOR DENYING CONFIRMATION OF THE MODIFIED PLAN ON EQUITABLE GROUNDS.

The Creditors' Committee submits that the evidence presented during the confirmation hearing does not support the Equity Committee's request that this Court deny confirmation of the Modified Plan on the grounds of either "bad faith" or "inequitable conduct." As noted above, the Equity Committee's position hinges entirely on the allegation that the Settlement Noteholders' investment activities in this case were improper. However, the Creditors' Committee submits that the evidence at the confirmation hearing is at odds with that allegation, and instead shows that the Settlement Noteholders' trading activities were appropriate under applicable securities laws. As such, this Court should find, as a matter of law, that such activities do not constitute "inequitable conduct" justifying impairment of claims or denial of confirmation of the Modified Plan.

A. The Equity Committee Advocates An Incorrect Standard For Analyzing "Inequitable Conduct".

In what appears to be a tacit admission that there is no insider trading case here, the Equity Committee advocates the adoption and application of a new "equitable" standard for evaluating securities trading in bankruptcies, instead of relying upon the well-developed body of securities laws. The Creditors' Committee respectfully submits that to follow the Equity Committee's approach would be to invent a new and untested legal analysis for evaluating trading in distressed securities in bankruptcies. To do so here would be especially improper, given that the trades attacked by the Equity Committee have already taken place, which means not only that the Court would have to create out of whole cloth a new standard for evaluating the trades, but would have to apply that new standard retroactively.

First, nothing in the Bankruptcy Code (including its grant of certain equitable powers) authorizes the courts to fashion new legal criteria to replace existing standards of non-bankruptcy law. *See, e.g., Amatex Corp. v. The AETNA Cas. & Sur. Co. (In re Amatex Corp.),* 97 B.R. 220, 225-26 (Bankr. E.D. Pa. 1989) (quoting *Southern Ry. Co. v. Johnson Bronze Co.*, 758 F.2d 137, 141 (3d Cir. 1985) ("section 105(a) does not authorize the bankruptcy court to create rights not otherwise available under applicable law."); *Padilla v. GMAC Mortg. Corp. (In re Padilla)*, 389 B.R. 409, 430 n.30 (Bankr. E.D. Pa. 2008) (section 105(a) cannot be used "to override the mandates of applicable nonbankruptcy law."); *In re Vest Assocs.*, 217 B.R. 696, 699 (Bankr. S.D.N.Y. 1998) (bankruptcy court's equitable powers "are circumscribed by limitations contained in the Bankruptcy Code and other applicable federal law.").

Second, as a matter of sound judicial policy, fairness and common sense, it is submitted that the Court should apply the well-established standards of securities law to evaluate the propriety of securities trading in these cases. The law for determining whether insider trading has occurred is based upon Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder. There are decades of federal court precedent interpreting these statutes, including Supreme Court decisions governing what is and is not insider trading. A federal regulatory authority, the Securities and Exchange Commission, is dedicated to the enforcement of these statutes and rules, and it issues additional rules and regulations that provide further clarity as to the boundaries of insider trading and the specific types of conduct that is prohibited.

Those engaged in the business of trading in public securities – including many creditors in this case – universally rely upon this well developed body of law in determining what they can and cannot do.

As explained *supra*, the record made during the confirmation hearing reflects that the Settlement Noteholders' trading activities were at all times well within the boundaries of acceptable conduct under the laws governing insider trading. As such, the Creditors' Committee respectfully submits that the Court should conclude that those trading activities provide no basis for a finding of inequitable conduct or of bad faith for purposes of plan confirmation.

B. <u>There Is No Basis For Finding Inequitable Conduct.</u>

Even if the Court were to look outside the well-established body of securities laws to evaluate the propriety of trading activities in this case, the Creditors' Committee submits that the evidence at the confirmation hearing reflects no basis for "equitable disallowance" or "equitable subordination" of the Settlement Noteholders' claims. Subordination or disallowance of claims based upon equitable grounds, in any setting, is an extraordinary remedy that the Court should apply sparingly. *Bank of N.Y. v. Epic Resorts-Palm Springs Marquis Villas, LLC (In re Epic Capital Corp.)*, 307 B.R. 767, 773 (D. Del. 2004). However, with respect to the claims of non-insider creditors (such as the Settlement Noteholders), a party seeking equitable impairment must go further and prove an even "more egregious level of misconduct". *Rosener v. Majestic Mgmt., Inc. (In re OODC, LLC)*, 321 B.R. 128, 146 (Bankr. D. Del. 2005) (quoting *Century Glove, Inc. v. Iselin (In re Century Glove, Inc.)*, 151 B.R. 327, 333 (Bankr. D. Del. 1993)).

In an attempt to escape this exacting burden, the Equity Committee asserts that the Settlement Noteholders are insiders and/or fiduciaries of the Debtors. (Equity Committee Objection at 24-29.) However, no evidence was adduced at the confirmation hearing that supports either of these assertions. Thus, the burden of demonstrating inequitable conduct remains exceedingly high. *Cf. Schubert v. Lucent Techs. (In re Winstar Commc'ns., Inc.)*, 554

F.3d 382, 412 (3d Cir. 2009) (*quoting Fabricators, Inc. v. Technical Fabricators, Inc. (In re Fabricators, Inc.)*, 926 F.3d 1458, 1465 (5th Cir. 1991)) (holding that "[i]f the claimant is not an insider, then evidence of more egregious conduct such as fraud, spoliation or overreaching is necessary"). The record at the confirmation hearing does not sustain that burden.

1. <u>The Settlement Noteholders are not insiders.</u>

Only those entities having a close relationship with a debtor, and who engage in transactions with a debtor that are *not* negotiated at arm's length, can qualify as non-statutory insiders. *Winstar*, 554 F.3d at 396-97. In *Official Unsecured Creditors' Comm. of Broadstripe, LLC v. Highland Capital Mgmt., L.P. (In re Broadstripe LLC)*, 444 B.R. 51 (Bankr. D. Del. 2010), this Court identified eight factors courts will consider to determine whether a creditor qualifies as a non-statutory insider, including whether the creditor: (i) attempted to influence decisions made by the debtor; (ii) selected new management for the debtor; (iii) had special access to the debtor's premises and personnel; (iv) was the debtor's sole source of financial support; (v) generally acted as a joint venture or prospective partner with the debtor rather than an arm's length creditor; (vi) controlled the debtor's voting stock; (vii) controlled the debtor's management, including personnel and payment decisions; as well as (viii) whether the relationship was the result of an arm's length transaction. *Id.* at 79-80.

None of the testimony or exhibits at the confirmation hearing contradicts the view that the Debtors and the Settlement Noteholders operated throughout these cases (and negotiations) independently and with competing interests. There is no evidence that the Settlement Noteholders controlled the Debtors' management, litigation decisions, personnel decisions, finances, payments to creditors or voting stock. They did not share offices or personnel, they were not engaged in a joint venture with Debtors, nor were they the source of financial support to the Debtors and they did not control the Debtors' settlement decisions. To the contrary, representatives of both the Debtors and the Settlement Noteholders offered the uncontradicted testimony at the confirmation hearing that the Settlement Noteholders exercised no control over the Debtors' negotiations or managerial decisions. In a nutshell, the Creditors' Committee believes there is nothing in the record to support the Equity Committee's allegation that the Settlement Noteholders were non-statutory insiders.

Specifically, Mr. Kosturos testified that the Settlement Noteholders had no role whatsoever in making decisions on behalf of the Debtors with respect to settlement negotiations. (7/21/2011 Hr'g Tr. 96:9-12 (Kosturos); *see also id.* at 137:2-17 ("there's been numerous instances . . . where the settlement noteholders wanted the debtor to do something and we rejected their ideas and did what we thought was best for the estate. We led the negotiations; the settlement noteholders did not. The unsecured creditors' committee participated with us throughout this case. And ultimately the debtor exercised its judgment, its sole judgment in entering into the global settlement agreement."); *id.* at 132:9-12 ("[t]here were many meetings throughout this case where we didn't tell the noteholders or anybody in this case what the debtor was doing. So we found it under no obligation to let people know what the debtor was doing.").) Likewise, Mr. Krueger stated unequivocally that Owl Creek did not dominate such negotiations. (7/19/2011 Hr'g Tr. 116:17-117:22 (Krueger).) Indeed, there was extensive testimony by Mr. Gropper regarding his frustration over the degree to which the Settlement Noteholders were excluded from certain settlement negotiations. (7/18/2011 Hr'g Tr. 72:24-75:19 (Gropper).) Mr. Bolin, of Appaloosa, described the assertion that the Settlement Noteholders dominated the settlement negotiations as "naïve." (7/20/2011 Hr'g Tr. 79:5-80:23 (Bolin) (also stating that "if you look at the facts of the case, we were not bashful in expressing our opinions to the debtor. More often than not, fortunately or unfortunately, they did what they wanted . . . So if we dominated the debtor and controlled the case, frankly we did a lousy job of it.").)

The Equity Committee has presented no evidence to contradict these statements and cannot satisfy the applicable standard for imposing "non-statutory insider" status on any of the Settlement Noteholders. *Broadstripe*, 444 B.R. at 80.

In its pre-Confirmation Hearing objection to confirmation, the Equity Committee made similarly baseless allegations regarding the effectiveness and independence of the Creditors' Committee. The Equity Committee alleged that the Settlement Noteholders dominated the Creditors' Committee, "robbed the Creditors['] Committee of its watchdog function," excluded the Creditors' Committee from the negotiation process, and "held great power over the Creditors' Committee itself, through their influence over two of the indenture trustees who sit on the Creditors['] Committee." (Equity Committee Objection at ¶¶ 35, 54.) Unquestionably, no evidence or testimony elicited during the confirmation hearing support any of these allegations. In fact, at no time during the seven-day confirmation hearing did the Equity Committee even attempt to introduce any evidence or ask any witness any questions to support the Equity Committee's false accusations. Instead, this is merely another example of the Equity Committee's all-too-common practice during these cases of throwing any allegation it can imagine against the wall and hoping it sticks.

2. <u>No evidence was presented that the Settlement Noteholders acted as fiduciaries.</u>

Equally misplaced, in light of the evidence (or the lack thereof) at the confirmation hearing, is the Equity Committee's theory that that the Settlement Noteholders are fiduciaries to the Debtors, other creditors, or even holders of equity interests. As an initial matter, this Court has already concluded that the Settlement Noteholders never attained the status of fiduciaries. *In re Washington Mut., Inc.*, 442 B.R. 314, 349 (Bankr. D. Del. 2011) [D.I. 6528] ("[t]he Settlement Noteholders were not acting in this case in any fiduciary capacity; their actions were taken solely on their own behalf, not others."). The Equity Committee is bound by that finding under the law of the case doctrine. *Bellevue Drug Co. v. Caremarks PCS Inc. (In re Pharmacy Benefit Managers Anti-Trust Litig.)*, 582 F.3d 432, 438 (3d Cir. 2009) (explaining that "'when a court decides upon a rule of law, that decision should continue to govern the same issues in subsequent stages in the same case'") (quoting *Arizona v. California*, 460 U.S. 605, 618 (1983)). Under the law of the case doctrine, there is no justification for revisiting that decision now. *Christianson v. Cold Indus. Operating Corp.*, 486 U.S. 800, 816-17 (1988); *Scheafnocker v. Comm'r. of Internal Revenue Serv.*, No. 08-2655, 2011 WL 1467198, at *3 (3d Cir. Apr. 19, 2011).

In all events, because the Settlement Noteholders are non-insiders in this case, the law is well-settled that they are under no fiduciary obligation to either the Debtors or to other constituencies. *Waslow v. MNC Commercial Corp. (In re M. Paolella & Sons, Inc.)*, 161 B.R. 107, 120 (E.D. Pa. 1993) (*citing Cosoff v. Rodman (In re W.T. Grant Co.)*, 699 F.2d 599, 610 (2d Cir. 1983)). As a matter of law, a debtor-creditor relationship is not a fiduciary relationship. *American Consol. Transp. Cos., Inc. v. RBS Citizens N.A. (In re American Consol. Transp. Cos., Inc.)*, 433 B.R. 242, 253 (Bankr. N.D. Ill. 2010).

It is only possible for a non-insider creditor to acquire a fiduciary duty to other creditors in its class when such creditor "purports to act for the benefit of [the] class." *In re Washington Mut., Inc.*, 419 B.R. 271, 279 (Bankr. D. Del. 2009) (*citing Official Comm. of Equity Sec. Holders of Mirant Corp. v. The Wilson Law Firm, P.C. (In re Mirant Corp.)*, 334 B.R. 787, 793 (Bankr. N.D. Tex. 2003)). As this Court has already determined, there is no evidence that the Settlement Noteholders have acted, nor have they claimed to act, on behalf of other entities. *Wash. Mut.*, 442 B.R. at 349. Further, there was no evidence at the confirmation hearing that the Settlement Noteholders have ever held themselves out as representing others, purported to assert causes of action belonging to the estate, or otherwise asserted positions in this case as a collective.[20] *See Mirant*, 334 B.R. at 800 (providing examples of actions indicative of a creditor's purporting to act on behalf of a class rather than for itself). As such, the Creditors' Committee sees no evidence in the record that the Settlement Noteholders have acted on others' behalf in these cases such that they could be designated "fiduciaries."

3. No evidence has emerged of inequitable conduct.

The Creditors' Committee views the record at the confirmation hearing as devoid of any evidence of inequitable conduct on the part of the Settlement Noteholders, let alone conduct that is so "egregious" as to justify the equitable impairment of claims or denial of confirmation of the Modified Plan. To the contrary, the evidence adduced at the confirmation hearing suggests that the Settlement Noteholders participated constructively in those settlement negotiations to which they were privy and acted with care to avoid trading in WMI securities based upon MNPI.

Impairment of claims on equitable grounds is an extraordinary remedy to be applied only sparingly. *Epic Capital*, 307 B.R. at 773. Indeed, the remedy is permissible only where (i) the claimholder engaged in inequitable conduct; (ii) such misconduct caused injury to the creditors or conferred an unfair advantage on the claimholder; and (iii) the remedy would be consistent with bankruptcy law. *Broadstripe*, 444 B.R. at 78. Where, as here, the claimants at issue are non-insiders, the misconduct must be "egregious", *i.e.*, "very substantial" and involve moral turpitude, misrepresentation, or gross misconduct amounting to fraud, overreaching or spoliation. *Winstar*, 348 B.R. at 234. Generally, only three categories of misconduct will rise to the level of "inequitable conduct" within the meaning of this standard: (i) fraud, illegality and breach of fiduciary duties; (ii) substitution of debt for capital when a company is

[20] While there was testimony that Aurelius at one time was a member of the steering committee of a group of thirty-five creditors represented by White and Case, (7/18/2011 Hr'g Tr. 49:6-16 (Gropper)), there is no evidence in the record that such group purported to represent the interests of creditors outside of that group.

undercapitalized; and (iii) the claimant's use of the debtor as an alter ego or instrumentality. *Official Comm. of Unsecured Creditors of Hydrogen, L.L.C. v. Blomen (In re Hydrogen, L.L.C.)*, 431 B.R. 337, 361 (Bankr. S.D.N.Y. 2010). Certainly, a creditor's efforts to maximize recovery on account of its claims are not inequitable conduct, and in seeking to collect on its claim, a creditor owes no duties to the debtor, other creditors or any other constituency. *Boyd v. Sachs (In re Auto Specialties Mfg. Co.)*, 153 B.R. 457, 480 (Bankr. W.D. Mich. 1993); *Reese v. Lyons Equip. Co., Inc. (In re Lyons Equip. Co., Inc.)*, 436 B.R. 281, 285 (Bankr. W.D.N.Y. 2010).

The Equity Committee argues that the requisite misconduct is present here based upon the Settlement Noteholders' alleged trading while in possession of MNPI. (Equity Committee Objection, 18, 29.) However, as discussed at length above, the evidence at the confirmation hearing shows that the information to which the Equity Committee points was not MNPI. The record also reflects a good faith effort by the Settlement Noteholders to take numerous and reasonable precautions specifically to avoid trading in WMI securities based on MNPI. Given the record established at the confirmation hearing, the Creditors' Committee does not believe that it is credible to argue that the Settlement Noteholders acted in bad faith or inequitably.

Moreover, if the Court were even inclined to consider denial of confirmation of the Modified Plan based upon allegations of inequitable conduct, any such action would need to be based on overwhelming evidence of inequitable conduct, in light of the enormous hardship that would be suffered by scores of creditors in potentially multiple classes if confirmation of the Modified Plan were denied or if certain remedies suggested to the Court relating to interest were imposed. As set forth in the *Post-Confirmation Hearing Brief of the Official Committee of Unsecured Creditors In Support Of Confirmation (Issues Other Than Alleged Insider Trading)*, the consequences of any such rulings, many of which would likely be unintended, would be visited upon creditors that have not been accused of any improper conduct. The foregoing concerns are especially important to bear in mind given what the Creditors' Committee believes is the absence of any evidence of any inequitable conduct.

CONCLUSION

Based upon the documents and testimony adduced at the confirmation hearing, the Creditors' Committee finds no sound basis for the Equity Committee's allegations of insider trading or inequitable conduct, nor is there evidence to support any finding other than that the Modified Plan was proposed in good faith. In all events, the Creditors' Committee submits that the Modified Plan should be confirmed, regardless of the conduct of any particular creditor.

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