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

MOTION OF AURELIUS CAPITAL MANAGEMENT, LP FOR LEAVE TO APPEAL UNDER 28 U.S.C. § 158(a)

Dated: September 27, 2011

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Aurelius Capital Management, LP, on behalf of certain of its managed entities (collectively, "Aurelius") that are creditors of the above-captioned debtors and debtors in possession (collectively, the "Debtors"), hereby submits this motion (the "Motion") pursuant to 28 U.S.C. § 158(a) and Rule 8003 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules") for an order granting leave to appeal the order (the "Order") and related opinion (the "Opinion") (copies of which are attached hereto as Exhibits A and B, respectively) entered by the United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court") on September 13, 2011 denying confirmation of the Debtors' modified sixth amended plan of reorganization (the "Modified Sixth Amended Plan" or the "Plan") and authorizing the Official Committee of Equity Security Holders of Washington Mutual, Inc. (the "Equity Committee") to commence and prosecute an action against Aurelius and certain other creditors on behalf of the Debtors' estates, and in support thereof respectfully states as follows:[1]

PRELIMINARY STATEMENT

1. Aurelius, one of the largest creditors in these bankruptcy cases, appeals from both the Confirmation Order and the Standing Order. The Standing Order radically distorts securities and bankruptcy law and inflicts a gross injustice. It authorizes the Equity Committee, in the name of the Debtors, to bring unprecedented causes of action for alleged insider trading against Aurelius and the other Settlement Noteholders where the trial court found that the estates themselves suffered no harm, where the estates lack standing to bring these claims, and where

[1] While entered as a single order, the Order actually is comprised of two separate orders that resolve two separate and distinct contested matters: (i) an order granting in part a motion filed by the Equity Committee for derivative standing (the "Standing Motion") to pursue certain causes of action on behalf of the Debtors' estates (the "Standing Order") and (ii) an order denying confirmation of the Debtors' Plan (the "Confirmation Order"). As set forth below at ¶¶ 28-31 and ¶ 79, Aurelius asserts that both the Standing Order and the Confirmation Order are final orders under the Third Circuit's "pragmatic" approach to finality in bankruptcy proceedings. *See In re Amatex Corp.*, 755 F.2d 1034, 1039 (3d Cir. 1985). Aurelius nevertheless submits this Motion out of an abundance of caution.

the basic elements of these claims are missing.[2] The Equity Committee represents the general interests of the Debtors' stockholders, who are greatly out of the money, rather than any individual parties that may have traded in the Debtors' securities with Aurelius. The Standing Order inexplicably overrides the judgment of the Debtors and the Official Committee of Unsecured Creditors (the "Creditors' Committee") that these causes of action are meritless and uneconomic to pursue and subjects all creditors (including Aurelius) to yet more delay and expense in these three-year-old bankruptcy cases. Moreover, the Standing Order wreaks havoc with well-established securities law precedent and practice and will, until overturned, invite a substantial expansion of securities litigation (whether or not bankruptcy-related); turn bankruptcy courts into common forums for bringing securities strike suits and (thanks to liberal discovery procedures) conducting pre-suit fishing expeditions, and severely inhibit the negotiation by major stakeholders of consensual reorganization plans in virtually every major corporate bankruptcy.

2. Aurelius also appeals from the final ruling embodied in the Confirmation Order mandating that postpetition interest in any plan must be paid at the federal judgment rate rather than the contract rates bargained for by the parties – a ruling that disregards governing law, blocked confirmation of the Debtors' Plan, and would deprive creditors in these cases of more than $810 million in postpetition interest claims by the time any new plan can be confirmed.

3. Aurelius submits that both of these aspects of the Order are final and appealable as of right, but in the event the Court disagrees, discretionary appellate review under 28 U.S.C. § 158(a)(3) is appropriate here because the appeal presents several disputed legal issues as to

[2] In addition to Aurelius, the "Settlement Noteholders" are Centerbridge Partners, L.P. ("Centerbridge"), Owl Creek Asset Management, L.P. ("Owl Creek"), and Appaloosa Management L.P. ("Appaloosa"), each of which has appeared in these cases on behalf of its own managed entities that also are substantial creditors of the estates.

which there is *at least* fair ground for disagreement and hearing the appeal would materially advance resolution of the underlying disputes. Aurelius respectfully requests expedited consideration of this Appeal in light of the severe burden and harm that otherwise will be inflicted by the decision below on the estates, the parties, and the bankruptcy process generally.

4. In the September 13 Opinion, the Bankruptcy Court explained its reasons for granting the Equity Committee's motion under *Official Comm. of Unsecured Creditors of Cybergenics Corp. v. Chinery*, 330 F.3d 548 (3d Cir. 2003), for leave to file an adversary complaint (the "Complaint") on behalf of the estates. The Bankruptcy Court held that the Complaint stated a "colorable" claim that Aurelius and others violated the federal securities laws by trading while allegedly in possession of material nonpublic information obtained from the Debtors, and authorized the Equity Committee to seek equitable disallowance of the purported defendants' multi-hundred-million dollar holdings in the Debtors' debt securities. The Opinion has already set off shock-waves because (among other things) it premises potential insider trading liability on facts mirroring settlement negotiation procedures relied on and used in virtually all large bankruptcy cases:

- Aurelius participated in settlement negotiations only during two brief periods – one nearly a year and the other more than three months before an agreement in principle was announced. On both occasions, Aurelius (and other creditors) entered into customary confidentiality agreements with the Debtors under which they were temporarily restricted from trading in the Debtors' securities while privy to confidential information.
- These agreements required *the Debtors*, at the conclusion of each confidentiality period, to publicly disclose any material nonpublic information shared with Aurelius,

for the express purpose of allowing Aurelius to resume unrestricted trading. Accordingly, at the end of each of these two periods, the Debtors made material public disclosures regarding the multi-billion dollar tax refunds that the Debtors expected to receive, and the Debtors certified to Aurelius that it was free to resume trading. The Debtors correctly determined at the time, with the advice of experienced securities law counsel, that the stale details of unsuccessful settlement negotiations were not material and did *not* need to be disclosed.

- It was undisputed that Aurelius did not engage in any improper trading during the confidentiality periods.

This approach was modeled on procedures that have been widely accepted and successfully employed for decades to facilitate consensual resolutions in large bankruptcies, as well as in other settings. Until now, it would have been unthinkable that parties carefully following such procedures in good faith could be exposed to a lawsuit for insider trading. But the Opinion rewrote the rules for these cases retroactively – invoking a series of new legal standards that would radically remake federal securities and bankruptcy law. The court essentially declared that (1) *any* creditor privy to confidential settlement negotiations at any time during a bankruptcy case must remain *permanently* restricted or maintain an ethical wall for the duration of the case; (2) *any* creditor receiving confidential information by participating in consensual plan negotiations may thereby be treated as a "temporary insider" with fiduciary duties to the estate; and (3) *any* creditor that holds, or is part of an ad hoc creditor group holding, more than one third of a class of securities (referred to in the Opinion as a "blocking position") may without more be deemed a fiduciary for all creditors in the class *and* a "non-statutory insider" of the estates.

5. The Bankruptcy Court used the questionable doctrine of equitable disallowance to transform any insider trading violation (and presumably any violation of any law by any creditor) into a bankruptcy matter, despite well-established mechanisms for such violations to be rectified by the Securities and Exchange Commission (the "SEC") or the injured parties. The Opinion effectively declares open season for creative and aggressive bankruptcy litigation by allowing a deeply out-of-the-money constituency to bring a derivative suit found meritless by both the Debtors and the Creditors' Committee, despite the court *expressly finding* that the putative defendants had not harmed the estates, but rather actually *helped* the Debtors increase the size of the estates to the benefit of all stakeholders. Opinion at 71, 73.

6. This remarkable new paradigm, if sustained, would radically change modern bankruptcy practice – turning the members of every ad hoc group in these and other cases into fiduciaries with potentially wide-ranging duties and legal exposure, and making it prohibitively burdensome for major economic stakeholders to participate in plan negotiations. This would in turn not just chill but freeze out from plan negotiations the very institutional creditors whose votes will be needed to accept a plan, leaving debtors to propose plans that lack creditor support and may be doomed to rejection, and inviting reorganizations to be resolved through litigation rather than negotiation. This effect is already being felt, as law firm publications have been issued warning clients of the new open-ended duties they may be assuming simply by stepping forward constructively to participate in arm's-length negotiations.[3] The Bankruptcy Court's suggestion that multi-year trading restrictions would not be burdensome since official creditors' committees are already subject to such restrictions (Opinion at 137-38) in fact proves the

[3] For example, attached hereto as Exhibits G, H, I and J are client alerts released in the past two weeks by Davis Polk & Wardwell LLP, Bracewell & Giuliani LLP, Ropes & Gray LLP and Willkie Farr & Gallagher LLP, respectively.

opposite: it is precisely because of such prolonged restrictions that major bondholders in most cases do not sit on official creditors committees, as is so in these cases. That is why the practice evolved of a non-fiduciary ad hoc creditor group; but the Opinion, if not reversed, may destroy this useful and important mechanism for fostering consensual resolution of complex reorganizations.

7. Aurelius will demonstrate upon full briefing that the Standing Order represents an abuse of discretion as a matter of law because it is based on multiple legal errors, *any one of which* would warrant discretionary appellate review under 28 U.S.C. § 158(a)(3):

- The Bankruptcy Court's finding that Aurelius (and the other Settlement Noteholders) did not harm but actually *helped* the estates extinguishes any potential claim for equitable disallowance. Regardless of the availability of any particular remedy, the Debtors (and the Equity Committee standing in their shoes) have standing *only* to seek redress for *harm to the estates*. None has been articulated here.

- Similarly, the Debtors (and therefore the Equity Committee) have no standing to sue for alleged insider trading in their own securities. That claim (to the extent one exists) belongs to the parties with whom Aurelius traded, who would not benefit from the proposed action. The Bankruptcy Court's suggestion that the Debtors would have a defense outside of bankruptcy to the payment of their debt obligations based on insider trading by the claimant with third parties is a radical concept with no legal support.

- In any event, the entire adversary proceeding is barred because the supposed remedy of "equitable disallowance" is unavailable under modern bankruptcy jurisprudence. While the Third Circuit has reserved judgment on the existence of the remedy, it is at minimum a highly contested, dispositive threshold issue warranting immediate review. Moreover, even if the remedy were theoretically available, the Bankruptcy Court itself recognized that it should be invoked only "in those extreme instances – perhaps very rare – where it is necessary as a remedy." Opinion at 115. Leaving aside the absence of any harm to the estates, the highly developed mechanisms for rectifying insider trading violations belie any suggestion that equitable disallowance could be "necessary as a remedy" here.

8. In addition, the Opinion contains a series of fundamental errors under federal securities law:

- The Bankruptcy Court ignored settled law in holding that Aurelius could be found to be a "temporary insider" subject to liability under the "classical theory" of insider trading merely because it received confidential information pursuant to an arm's-length confidentiality agreement and advanced its own economic interests in negotiations that had the shared goal of reaching a settlement among economically adverse parties.

- The Bankruptcy Court similarly erred in holding that Aurelius could be found both to have fiduciary duties to other creditors and to be a "non-statutory insider" of the Debtors merely because it joined an informal creditor group that collectively may have held more than one third of the securities within a particular class of securities.

- The Bankruptcy Court disregarded the strict standard mandated by Congress for pleading the scienter element of an insider trading claim, which requires particularized facts giving rise to a cogent and compelling inference – at least as powerful as any non-culpable inference – that a defendant knew or recklessly ignored that it was trading improperly while in possession of material nonpublic information. The court eviscerated that requirement by giving no weight to the Debtors' materiality determinations, the good faith of which was unchallenged; by ignoring undisputed testimony regarding Aurelius's own good-faith determinations of materiality; and by sustaining the pleading even though no inference of knowledge (much less a powerful or cogent one) could be drawn from the allegations regarding Aurelius's pattern of trades.

- The Bankruptcy Court further unduly expanded the concept of materiality, essentially creating a new per se rule that any creditor participating in confidential settlement negotiations must permanently halt all trading in the debtors' securities – or establish an ethical wall – for the duration of the case regardless of the state of the negotiations at the conclusion of the confidential period. Like the court's "insider" holdings, this new, retroactively imposed legal rule has no precedent and, if not promptly reversed, will cast a pall over settlement negotiations in virtually every major corporate bankruptcy.

9. Finally, the Bankruptcy Court further erred as a matter of law by granting standing without making the necessary finding that the Debtors *unreasonably* refused to pursue the alleged insider trading claims – a judgment endorsed by the Creditors' Committee. Although it acknowledged that its decision could precipitate a "litigation morass" (Opinion at 138), the Bankruptcy Court never actually weighed the benefits and burdens facing the estates: the remote chance of success and relatively modest upside (potential disgorgement of the limited profits that could conceivably be traced to use of the alleged material nonpublic information) versus the

crushing expense and extended delay that would be associated with litigating the claims to conclusion. *All creditors* (including Aurelius) have a strong interest in avoiding the harm to the estates of incurring many tens of millions of dollars in legal fees to litigate these disputes to conclusion while further complicating the already troubled effort to promulgate a confirmable plan of reorganization. This costly quagmire (and further financial and reputational harm to innocent parties resulting from the mere pendency of these grave but reckless accusations) can be avoided only by entertaining this appeal and reversing the decision after full briefing.

10. Immediate and expedited review of the Opinion is necessary to halt the adverse impact this decision will have on the bankruptcy process, and also to avoid significant harm in these cases to the estates and their constituents. Over the last year, two plans supported by the overwhelming majority of creditors, and embodying a settlement with JP Morgan and the FDIC twice found to be reasonable and proposed in good faith, have both failed. During this period, because of accrued interest that must be turned over to senior classes at the contract rate and mounting administrative expenses, the Debtors' most junior noteholder class (the "PIERS"), of which Aurelius is a significant holder, has gone from a projected near full recovery after subordination on account of their $789 million in claims for prepetition principal and accreted interest to a recovery approaching zero under any eventual plan. Upon release of the Opinion, the market price of the PIERS dropped from $14.50 per share to $4.08 per share. The Order promises only to create more delay, by directing the parties to mediate both outstanding Plan issues and the merits of the insider trading allegations, even after a week-long trial and the Bankruptcy Court's ruling. This mediation has little chance of success, because the equity holders are massively out of the money and could not benefit from any realistic settlement (or, for that matter, from the proposed litigation). Even assuming (contrary to all experience to date)

that the Debtors could exit Chapter 11 by the end of February 2012, the common equity would be out of the money by more than $7.6 billion, and the preferred equity by more than $165 million. For each month of delay beyond February 2012, these deficits would grow by more than $20 million on account of postpetition interest and administrative expenses. And if the Bankruptcy Court's erroneous ruling on postpetition interest is reversed, the above deficits would increase by more than $810 million (so the preferred holders would be nearly $1 billion out of the money) and would grow by more than $42 million per month of delay beyond February 2012. Finally, complications generated by this pending dispute may well hamper a third attempt to confirm a plan of reorganization. Immediate appellate review to correct the errors below provides the surest path to a speedy, just, and comprehensive resolution of these cases.

STATEMENT OF PERTINENT FACTS

A. General Background

11. Founded in 2006, Aurelius Capital Management, LP is a limited partnership that acts as an investment manager for three separate and independent investment funds (collectively, the "Aurelius Funds").[4] Throughout these cases, the Aurelius Funds collectively have, along with the other Settlement Noteholders, been among the largest creditors of the Debtors' estates, holding claims throughout the Debtors' multi-tiered debt structure. As a result, they have had a strong interest in maximizing the value of the Debtors' estates for all stakeholders while minimizing costs and expenses.

12. In the wake of the seizure and sale of certain subsidiaries of Debtor Washington Mutual Inc. ("WMI") by the Federal Deposit Insurance Corporation (the "FDIC") and the

[4] Each Aurelius Fund has its own trading history, and one did not even commence operations until February 2010.

commencement of these bankruptcy cases, myriad disputes involving billions of dollars arose among the Debtors, JPMorgan Chase ("JPMC"), which purchased certain assets and assumed certain liabilities of WMI, and the FDIC (both in its corporate capacity and as receiver for Washington Mutual Bank ("WMB")). Opinion at 2. For example, the parties disputed ownership of such assets as (i) approximately $4 billion that the Debtors had on deposit in accounts held by JPMC and (ii) approximately $5.5 to $5.8 billion in tax refunds.

B. The Global Settlement and First Confirmation Hearing

13. On March 12, 2010, the Debtors announced the material terms of a global settlement resolving the various claims among the Debtors, JPMC, and the FDIC, eventually memorialized, following further negotiations, in an agreement (as subsequently modified, the "Global Settlement Agreement" or "GSA") filed with the Bankruptcy Court on May 21, 2010. Opinion at 3. The settlement was embodied in a plan of reorganization projected to pay unsecured creditors in full but provide no recovery for the Debtors' equity holders. The Bankruptcy Court held an evidentiary hearing on confirmation of the Debtors' Sixth Amended Plan in early December 2010, ruling a month later that the GSA was fair and provided a "reasonable return in light of the possible results of litigation," even though it provided no recovery for equity. *In re Wash. Mut., Inc.*, 442 B.R. 314, 345 (Bankr. D. Del. 2011). The Bankruptcy Court nevertheless concluded that the Sixth Amended Plan could not be confirmed because of several legal deficiencies unrelated to the proposed litigation. *Id*. at 322.

C. The Equity Committee Investigation

14. Following denial of confirmation, and seeking leverage to derail a new plan, the Equity Committee sought – nearly two and one-half years into the case – authority to conduct discovery of the Settlement Noteholders under Bankruptcy Rule 2004 with respect to accusations

about their trading activity that had been raised (with no admissible evidence) by a pro se security holder in connection with one of his objections to confirmation at the first confirmation hearing – an objection that the Bankruptcy Court denied for complete lack of admissible evidence. *Washington Mut.*, 442 B.R. at 349. The Equity Committee neither joined in that objection nor sought discovery regarding those accusations at that time. The Bankruptcy Court nonetheless granted the Equity Committee's discovery request, and the Settlement Noteholders produced tens of thousands of pages of documents and a representative of each sat for a full-day deposition.

D. <u>The Second Confirmation Hearing and *Cybergenics* Standing Motion</u>

15. While the Equity Committee was conducting its investigation, the Debtors filed and solicited votes on its Modified Sixth Amended Plan, which attempted to correct the deficiencies identified by the Bankruptcy Court in the prior plan. Shifting their tactics, the Equity Committee again objected to confirmation, this time contending that the Plan was the product of a flawed process dominated by the Settlement Noteholders and favoring their interests over those of other constituents – in particular, the Debtors' equity holders – and that the Debtors had intentionally facilitated improper trading by the Settlement Noteholders. The Equity Committee then filed the Standing Motion seeking authority to commence and prosecute claims for equitable subordination and equitable disallowance on behalf of the Debtors' estates based on the same claims of domination and insider trading under the federal securities laws.[5] The Equity Committee specifically requested the Bankruptcy Court to assess the colorability of its claims based on the evidence to be presented at the confirmation hearing on the Modified Sixth Amended Plan (the "<u>Second Confirmation Hearing</u>"). Ex. C at ¶ 13.

[5] A copy of the Standing Motion and Complaint are attached hereto as Exhibit C.

16. The Second Confirmation Hearing was held over seven days in July 2011.[6] During the hearing, the Bankruptcy Court heard extensive, consistent, unrefuted testimony from each of the Settlement Noteholders, confirmed by the testimony of the Debtors' chief restructuring officer, William Kosturos, comprehensively refuting the unsupported allegations of improper domination and insider trading.

17. The evidence overwhelmingly demonstrated that Aurelius and the other Settlement Noteholders in no way dominated or controlled the Debtors during the course of these cases, but rather were relegated to discrete and intermittent roles in settlement negotiations and the plan process. Ex. D at 48, 78, 116-17; Ex. F at 137. Aurelius was included in confidential settlement negotiations only twice, for limited periods in these nearly three year old cases (the "Confidentiality Periods"), with each period governed by a formal written agreement (the "Confidentiality Agreements"). Opinion at 66. The first Confidentiality Period lasted for only 60 days, from March 9 through May 8, 2009. *Id*. The second Confidentiality Period occurred six months later and lasted for only 45 days, from November 16 through December 30, 2009. *Id*. at 67. Outside of these two periods (and at times even during these two periods), Aurelius was *not* included in the Debtors' settlement negotiations with JPMC, the FDIC, and other parties. The Debtors reached a first, tentative settlement in March 2010, some ten months after the first Confidentiality Period, and three months after the second. Even that agreement required months of additional negotiation and significant further modifications to result in a plan definite enough to take to confirmation.

18. The evidence established that Aurelius received material nonpublic information from the Debtors prior to the announcement of the March 2010 settlement only during the two

[6] Relevant excerpts from the transcripts of the proceedings on July 18, 19, and 21 are attached hereto as Exhibits D, E and F, respectively.

Confidentiality Periods and subject to the terms of the applicable Confidentiality Agreements. The Confidentiality Agreements required Aurelius either to refrain from trading in the Debtors' securities during the Confidentiality Period or to erect an ethical wall between the employee receiving any material nonpublic information and all Aurelius employees trading in the Debtors' securities. Opinion at 66. Aurelius chose to erect an ethical wall during the first period and to shut down trading during the second period. *Id*. at 66-67. There has been no allegation, much less evidence, that Aurelius breached either obligation. To ensure that Aurelius and other creditors that signed similar agreements would be permitted to resume unrestricted trading in the Debtors' securities at the termination of each Confidentiality Period, both Confidentiality Agreements required the Debtors to disclose "within the meaning of Rule 101 of Regulation FD . . . a fair summary, as reasonably determined by the Debtors, of any Confidential Information that constitutes material nonpublic information under U.S. federal securities law."

19. During each Confidentiality Period, Aurelius and the other Settlement Noteholders learned certain material nonpublic business information, including the estimated ranges of the Debtors' tax refunds. Ex. D at 65, 105. This information was publicly disclosed through the Debtors' monthly operating reports published at the end of each Confidentiality Period. *Id*. at 79; Ex. F at 127-28. The Debtors determined, in consultation with their securities law counsel, that the details of settlement negotiations, which ended each time with the parties billions of dollars apart, were not material and therefore did not have to be disclosed. Ex. F. at 127-28, 153. The Debtors explicitly confirmed orally and in writing to the Settlement Noteholders in May and December 2009 that their disclosures satisfied the Debtors' obligations

under the Confidentiality Agreements and that the Settlement Noteholders were free to resume unrestricted trading.[7]

E. The Standing Order and Confirmation Order

20. In its September 13, 2011 Opinion, the Bankruptcy Court recognized that the basic facts regarding Aurelius's conduct during the two confidentiality periods – as recited in the Complaint and presented in court – were largely undisputed. However, the court disregarded the clear legal consequences of these facts, distorting, misapplying, or simply ignoring the law governing federal insider trading claims.

21. Significantly, the Bankruptcy Court *rejected* the Equity Committee's allegations that Aurelius and the other Settlement Noteholders dominated or controlled the Debtors, dictated the course of settlement negotiations, or inflicted *any* harm on the estates:

> Despite the allegations of insider trading by the Settlement Noteholders, the Court is unconvinced that their actions had a negative impact on the Plan or tainted the GSA.
>
> *Rather, the actions of the Settlement Noteholders appear to have helped increase the Debtors' estates*. During the First Confidentiality Period, the Settlement Noteholders, together with other creditors persuaded the Debtors to submit a term sheet to JPMC that was more "aggressive" than the one the Debtors had initially contemplated.

Opinion at 71 (emphasis added). The Bankruptcy Court went on to note that "[i]f the Settlement Noteholders had improperly dominated the case . . . , the Modified Plan would have elevated the treatment of the PIERS class (in which they hold the bulk of their claims); instead the PIERS are receiving the treatment warranted by their subordinated status." *Id.* at 73.

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[7] Other creditors beyond the Settlement Noteholders similarly relied upon this type of temporary restriction to participate in many of the same settlement negotiations and later resume trading following termination of the confidentiality periods – and indeed an even wider circle of creditors (including the large number of senior noteholders represented by White & Case LLP) were aware that negotiations were occurring. Ex. D at 64-65, 79, 81, 114; Ex. E at 137; Ex. F at 152-53.

22. The Bankruptcy Court further concluded that one of the two remedies sought in the Complaint – equitable subordination pursuant to 11 U.S.C. § 510(c) – "is not a remedy available to (or of much help in redressing any injury to) the shareholders" because the plain language of the statute "only permits a creditor's claim to be subordinated to another claim and not to equity." *Id.* at 111. However, the Bankruptcy Court upheld the Equity Committee's alternative proposed remedy – equitable *disallowance* (*see id.* at 115) – even though most cases hold that it is not even available under the Bankruptcy Code and the few that recognize the doctrine stress that it must be reserved for the most extreme misconduct.

23. The Bankruptcy Court then held that the Equity Committee stated a colorable claim for insider trading under the federal securities laws based on the Settlement Noteholders' knowledge of unsuccessful settlement offers, upholding the pleading of materiality by substituting its hindsight judgment for the Debtors' and the parties' own informed and good faith contemporaneous assessments. *Id.* at 118-28. The court further held that Aurelius could be regarded as an "insider" subject to insider trading liability under the "classical theory" based solely on having received confidential information pursuant to an arm's-length confidentiality agreement with the Debtors in order to participate in negotiations aimed at reaching a consensual resolution of the cases, and its membership in an ad hoc group with a "blocking position" in one or more classes of the Debtors' securities. *Id.* at 128-32. And the court held that the scienter requirement of an insider trading claim was satisfied despite uncontroverted evidence of the Settlement Noteholders' good faith reliance on the Debtors' own materiality determinations and the inconclusive inferences to be drawn from their trading patterns. *Id.* at 132-34.[8]

[8] In addition to liability under the "classical theory" of insider trading discussed above, the Bankruptcy Court sustained an allegation that a single noteholder may have violated the "misappropriation" theory by trading after receiving a chart from counsel that included stale details of settlement negotiations from months earlier. *Opinion* at 136. The Bankruptcy Court appears to have extended that holding to the other Settlement Noteholders based solely

24. Ultimately, the Bankruptcy Court left little doubt of its own policy preference to tighten the restrictions on claims trading during bankruptcy cases by retroactively imposing on *all* creditors participating, even fleetingly, in negotiations restrictions previously applied only to members of official creditors committees:

> [C]reditors who want to participate in settlement discussions in which they receive material nonpublic information about the debtor *must* either restrict their trading or establish an ethical wall between traders and participants in the bankruptcy case. . . . The Court does not believe that a requirement to restrict trading or create an ethical wall in exchange for a seat at the negotiating table places an undue burden on creditors who wish to receive confidential information and give their input.

Id. at 137-38 (emphasis added).

25. Finally, the Bankruptcy Court acknowledged that it was "required . . . to balance the probability of success on the claim against the burden on the estate that would result from its prosecution." *Id.* at 138. However, the court inexplicably granted the *Cybergenics* Standing Motion without even attempting to quantify any potential benefits for the estates, providing no basis to question the reasonableness of the Debtors' refusal to embroil the estates in what even the court recognized would be "a litigation morass" that would threaten existing creditor recoveries. *Id.* The Bankruptcy Court stayed the Equity Committee's action pending mediation. *See* Ex. A.

26. In addition, although it reaffirmed the fairness of the GSA, the Bankruptcy Court again denied confirmation of the Plan, principally because it concluded that the Plan improperly contemplated the payment of postpetition interest to unsecured creditors at the applicable contract rate. The court held that the plain language of the Bankruptcy Code mandated interest

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on the Equity Committee's unspecified and unsubstantiated allegation – contradicted by all the evidence in the record, including the testimony of every witness – that counsel may have shared material nonpublic information about negotiations with the Settlement Noteholders after the conclusion of the second Confidentiality Period. *Id.* at 137.

at the federal judgment rate, despite recognizing and validating subordination agreements that mandate turnover from subordinated to senior creditors of the Debtors at the contract rate. Opinion at 81, 83.

ARGUMENT

I.

LEAVE TO APPEAL THE STANDING ORDER SHOULD BE GRANTED, IF NECESSARY, TO PREVENT A WASTEFUL AND DESTRUCTIVE QUAGMIRE AND PUT THESE CASES BACK ON TRACK TOWARDS RESOLUTION

27. Leave to appeal should be granted here, if necessary, to prevent the delay, expense, and injustice of protracted litigation over facially invalid claims that are barred by decades of settled governing law.

28. At the outset, Aurelius submits that the Standing Order is final and appealable as of right under 28 U.S.C. § 158(a). Appellate courts take a more "pragmatic and less technical" approach to finality in bankruptcy cases "[t]o avoid the waste of time and resources that might result from reviewing discrete portions of the action only after a plan of reorganization is approved." *In re Amatex Corp.*, 755 F.2d 1034, 1039 (3d Cir. 1985). This approach is informed by such factors as the impact of the matter on the assets of the estate, the necessity for further fact-finding on remand, the preclusive effect of a decision on the merits, and the interests of judicial economy. *See, e.g., Se. Sprinkler Co. v. Meyertech Corp. (In re Meyertech Corp.)*, 831 F.2d 410, 414 (3d Cir. 1987); *In re F/S Airlease II Inc. v. Simon*, 844 F.2d 99, 104 (3d Cir. 1988); *In re Marvel Entm't Group, Inc.*, 140 F.3d 463, 470 (3d Cir. 1998).

29. All these factors favor a finding of finality here. The Standing Order will most certainly have an impact on the assets of the Debtors' estates since, absent reversal, the parties will plunge into what even the Bankruptcy Court has acknowledged would be a "litigation

morass" that will deplete the assets of the estates and dilute creditor recoveries. Opinion at 138; *see also* below at ¶ 76. An order that will have the effect of increasing administrative expenses or otherwise depleting estate assets is more likely to be treated as final. *See In re Market Square Inn, Inc.*, 978 F.2d 116, 120-21 (3d Cir. 1992) (order finding lease was not terminated was final because of impact on debtor's estate); *In re BH&P, Inc.*, 949 F.2d 1300, 1307 (3d Cir. 1991) (order removing trustee and counsel was final where court's ruling had "the more remote but no less real effect of increasing the estate's administrative costs"); *F/S Airlease*, 844 F.2d at 104 (order authorizing estates' retention of broker was final where broker's fee would impact assets available to creditors).

30. Moreover, immediate appellate review of the Standing Order will further the interests of judicial economy and protect both the estates and the parties from irretrievable loss. The Standing Order is premised upon legal errors that, if reversed, will end the Equity Committee's proposed litigation. This factor weighs heavily in favor of finality. *See BH&P*, 949 F.2d at 1307 (order final where "[r]esolution of the issues raised on appeal will eliminate the need for further consideration of conflict of interest issues, freeing the bankruptcy court to adjudicate the more substantive issues relating to the estates in question."); *F/S Airlease*, 844 F.2d at 104 (order final where "[a] resolution of this discrete dispute at this time would further the goal of judicial economy because it could obviate the need for further action by the bankruptcy court."); *Meyertech*, 931 F.2d at 414 (order final where "[a] decision now will . . . preclude the necessity of further activity by the fact-finding tribunal, will obliterate the need for more litigation and serves the ever-prevailing interest of judicial economy").

31. Finally, immediate appellate review of the Standing Order is the only meaningful way in which that order can be reviewed by an appellate court. Review of the Bankruptcy

Court's legal errors after discovery and trial would simply be too late to protect the estates from massive expense and delay. *See Marvel*, 140 F.3d at 470 (treating order as final and noting that "[w]ere we not to take jurisdiction at this juncture, no meaningful review of the order . . . could ever take place as a practical matter").

32. If the Court determines that the Standing Order is not a final order, Aurelius respectfully seeks leave to appeal, which the Court may grant in its discretion under 28 U.S.C. § 158(a)(3). Courts generally grant leave to appeal decisions of a bankruptcy court where the criteria of 28 U.S.C. § 1292(b) are present – *i.e.,* where (i) a controlling question of law is involved; (ii) the question is one as to which there is a substantial ground for difference of opinion; and (iii) an immediate appeal would materially advance the ultimate termination of the litigation. *See, e.g., Nat'l Cable Television Coop., Inc. v. Broadstripe, LLC (In re Broadstripe, LLC)*, No. 09-39, 2009 U.S. Dist. LEXIS 25690, at *5 (D. Del. Mar. 25, 2009). Immediate appeal from an interlocutory order is further appropriate to avoid "'harm to a party *pendente lite* from a possibly erroneous interlocutory order and the avoidance of possible wasted trial time and litigation expense.'" *First Am. Bank of N.Y. v. Sw. Gloves & Safety Equip., Inc.*, 64 B.R. 963, 967 (D. Del. 1986) (quoting *Katz v. Carte Blanche Corp.*, 496 F.2d 747, 755 (3d Cir. 1974)); *see also Broadstripe*, 2009 U.S. Dist LEXIS 25690, at *6.[9]

33. With respect to the merits, while the Bankruptcy Code contains no explicit authority for a committee or other party-in-interest to prosecute a derivative suit on behalf of a

[9] Moreover, there can be no doubt that Aurelius qualifies as a "person aggrieved" by the Order with standing to appeal it under *In re Combustion Eng'g, Inc.*, 391 F.3d 190, 214 (3d Cir. 2004). A party is aggrieved by a bankruptcy court order that "diminishes their property, increases their burdens, or impairs their rights." *Id.* (internal quotation marks omitted). Here, Aurelius (along with all creditors) will suffer significant pecuniary harm if the estates are required to pay tens of millions of dollars in attorneys fees to fund the "litigation morass" predicted by the Bankruptcy Court and if related delay causes further diminution in the value of its claims. *See Licensing by Paolo, Inc. v. Sinatra (In re Gucci)*, 126 F.3d 380, 388 (2d Cir. 1997) (creditors have standing to appeal orders that affect assets available to pay claims); *Kane v. Johns-Manville Corp.*, 843 F.2d 636, 642 (2d Cir. 1988) (same).

debtor's estate, the Third Circuit has recognized a qualified right to derivative standing where (i) the claim that the party is seeking to prosecute is "colorable" and (2) the debtor has unjustifiably refused to prosecute it. *See Official Comm. of Unsecured Creditors of Cybergenics Corp. v. Chinery*, 330 F.3d 548, 566-67 (3d Cir. 2003); *Infinity Investors Ltd. v. Kingsborough (In re Yes! Entm't Corp.)*, 316 B.R. 141, 145 (D. Del. 2004); *see also Unsecured Creditors Comm. of Debtor STN Enters. v. Noyes (In re STN Enters.)*, 779 F.2d 901, 905 (2d Cir. 1985). The party seeking standing (here, the Equity Committee) bears the burden of showing that it has met these derivative standing requirements. *G-I Holdings, Inc. v. Those Parties Listed on Exhibit A (In re G-I Holdings, Inc.)*, 313 B.R. 612, 629 (Bankr. D.N.J. 2004).

34. The determination by a bankruptcy court to grant standing to pursue a derivative cause of action on behalf of a debtor's estate is an exercise of its equitable powers, *Cybergenics*, 330 F.3d at 568, reviewable for abuse of discretion, *see Interface Group-Nevada, Inc. v. Trans World Airlines, Inc. (In re Trans World Airlines, Inc.)*, 145 F.3d 124, 131 (3d Cir. 1998). However, as was the case here, "[a] bankruptcy court abuses its discretion when its ruling is founded on an error of law or a misapplication of law to the facts." *Manus Corp. v. NRG Energy, Inc. (In re O'Brien Envtl. Energy, Inc.)*, 188 F.3d 116, 122 (3d Cir. 1999).

A. The Appeal Presents Controlling Questions of Law on Which There are Substantial Grounds for a Difference of Opinion

35. A "question of law" is "controlling" when, if decided erroneously, it would lead to reversal upon appeal. *See Broadstripe*, 2009 U.S. Dist. LEXIS 25690, at *5 n.3; *Stanziale v. Sun Nat'l Bank (In re Dwek)*, No. 09-5046 2010 U.S. Dist. LEXIS 3203, at *4-5 (D.N.J. Jan. 15, 2010). This appeal presents several such questions, any one of which would warrant granting leave to appeal.

1. The Finding that Aurelius Helped Rather Than Harmed the Estates Bars Any Claim for Equitable Disallowance

36. For several different reasons, the Debtors would lack standing to bring the claims that the Equity Committee seeks to bring on their behalf, and each of these grounds turns on threshold legal issues that satisfy the standard for interlocutory review. Most basically, the Bankruptcy Court's finding that Aurelius and the other Settlement Noteholders *helped* rather than *harmed* the estates is an absolute bar to the proposed Complaint.

37. It is well-settled that a debtor in bankruptcy lacks standing to pursue claims based on harm to individual creditors or equity holders, but rather can only pursue claims based on *harm to the debtor's estate*. *See Caplin v. Marine Midland Grace Trust Co. of N.Y.*, 406 U.S. 416, 434 (1972) (bankruptcy trustees lack standing to pursue claims of individual creditors); *Hirsch v. Arthur Andersen & Co.*, 72 F.3d 1085, 1093-94 (2d Cir. 1995) (same); *E.F. Hutton & Co. v. Hadley*, 901 F.2d 979, 986-87 (11th Cir. 1990) (same); *see also Citicorp Venture Capital, Ltd. v. Comm. of Creditors Holding Unsecured Claims*, 160 F.3d 982, 991 (3d Cir. 1998) (holding that injury caused to creditors who sold claims to insider "must play no role in determining the extent of any [equitable] subordination").

38. Official committees, similarly, can only bring claims based on general harm to the estate – *not* based on particularized harm to specific individuals. *Official Comm. of Unsecured Creditors v. Halifax Fund L.P. (In re AppliedTheory Corp.)*, 493 F.3d 82, 87 (2d Cir. 2007) (committee lacks standing to pursue equitable subordination based on injury to particular creditors); *Official Comm. of Unsecured Creditors v. Foss (In re Felt Mfg. Co.)*, No. 06-1171, 2007 Bankr. LEXIS 2569, at *24 (Bankr. D.N.H. July 27, 2007) (committee has no standing to bring claims belonging to individual creditors) (citing *Caplin*, 406 U.S. at 434).

39. The Complaint alleges only two injuries – neither of which can give rise to Equity Committee standing: (i) injury caused by the Settlement Noteholders' participation in a settlement with the Debtors and JPMC that did not provide for a return to equity investors (Complaint ¶ 56) and (ii) injury caused by their alleged insider trading (*id.* at ¶ 60). The Bankruptcy Court's reaffirmation of the fairness of the Global Settlement Agreement, and its related conclusion that the Settlement Noteholders did not harm the estates and actually *helped improve* the JPMC settlement, conclusively defeats the first allegation – the only one that even *attempted* to link the Settlement Noteholders' conduct to any actual harm to the estates.

40. With respect to the alleged "insider trading," the Complaint does not plead any plausible basis upon which a court could conclude that the *Debtors' estates* were harmed – even assuming that Aurelius violated the federal securities laws (which it most assuredly did not). The Settlement Noteholders traded with other individual securities holders, not with the Debtors. Even if individual trading counter-parties were harmed by any such trading, the Debtors themselves (and by extension, the Equity Committee as an estate representative) lack standing to seek redress of those harms. Any individual parties that believe they were injured by Aurelius's trading may pursue their non-bankruptcy remedies in an appropriate forum. *See Viking Assocs., L.L.C. v. Drewes (In re Olson)*, 120 F.3d 98, 102 & n.4 (8th Cir. 1997) (debtor lacked standing to challenge transfer of claims despite evidence that fiduciary had bought claims by misleading sellers for purpose of gaining control of estate's primary asset; parties who considered themselves wronged could individually object or pursue non-bankruptcy remedies). The Plan proposed in these cases would not release such claims.

41. Invocation of equitable remedies does not change the basic rule that a derivative action may *only* be based on actual harm to the estates. For instance, it is well-settled that the

remedy of equitable subordination under 11 U.S.C. § 510(b) (which the Bankruptcy Court held is unavailable here) is remedial, not penal, and may be invoked even by individual creditors "only to the extent necessary to offset *specific harm that creditors have suffered on account of the inequitable conduct*." *Cohen v. KB Mezzanine Fund II, LP (In re Submicron Sys. Corp.)*, 432 F.3d 448, 462 (3d Cir. 2006) (emphasis added; citation omitted). The same must be true for a claim for equitable disallowance – assuming such a claim is even legally cognizable. *Official Comm. of Unsecured Creditors of Sunbeam Corp. v. Morgan Stanley & Co. (In re Sunbeam Corp.)*, 284 B.R. 355, 364, 369 n.3 (Bankr. S.D.N.Y. 2002) (equitable disallowance, if still viable, "would be based on the same principles as equitable subordination"). Since the Debtors, and therefore the Equity Committee, have standing to sue only for harm to the *estates* and *not* harm to individual creditors, the rejection of allegations that Aurelius harmed the estates required denial of the *Cybergenics* motion as a matter of law – presenting a threshold legal issue for review as to which there is at least a good faith basis for a difference of opinion.

2. The Bankruptcy Court Erred by Granting Standing to Pursue Insider Trading Claims that the Debtors Themselves Would Lack Standing to Pursue

42. A closely related threshold legal issue requiring reversal is the clear rule that the Debtors, who were not contemporaneous traders in the securities, would lack standing to sue Aurelius for violating the federal insider trading laws with respect to the Debtors' own securities. It is well-settled that only parties to the relevant trades have standing to bring private suits for federal securities fraud. *See Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 732-33 (1975) (only purchasers or sellers have standing); *Wilson v. Comtech Telecomm. Corp.*, 648 F.2d 88, 94-95 (2d Cir. 1981) (only parties trading contemporaneously with defendant have standing

to sue for insider trading). As a result, the Equity Committee lacks standing to bring these claims on behalf of the Debtors.

43. The Bankruptcy Court ignored this authority, which dooms the entire Complaint. The court stated only that "[b]ecause the Equity Committee seeks to disallow the claims of the Settlement Noteholders under facts that suggest they violated the securities laws, the Court believes that the Debtors would have a defense to those claims outside of the bankruptcy context as well." Opinion at 116. But the Bankruptcy Court's speculation that an issuer has a defense to paying a debt claim if it can show that a portion of the claim was acquired from a third party through insider trading is utterly unsupported in the law. The authorities cited by the Bankruptcy Court – which discuss the remedies of disgorgement, interest, and civil penalties available *in an SEC enforcement action* (Opinion at 116-17) – are obviously irrelevant to the putative standing of an *issuer* either to bring an insider trading claim or to invoke securities law violations as a defense to paying a debt. The Debtors simply lack standing to sue Aurelius for insider trading; and as a result, so does the Equity Committee.[10]

3. The Bankruptcy Court Erred in Sustaining a Claim for Equitable Disallowance Because Such a Remedy Is Not Recognized Under the Bankruptcy Code

44. A third independent threshold legal issue is whether equitable disallowance is even available as a remedy under the Bankruptcy Code. If it is not, the Complaint as limited by

[10] Even if such a defense were theoretically available, it could never be enforced by the Debtors here, because the Debtors themselves were contractually obligated to publicly disclose all material nonpublic information that they provided to Aurelius during the Confidentiality Periods. If the Debtors breached that obligation by failing to publicly disclose material information and, as a result, the Settlement Noteholders traded while in possession of material nonpublic information, equitable principles of unclean hands and/or *in pari delicto* would preclude the Debtors from refusing to pay the underlying debt claims of the Settlement Noteholders on the basis of such trading. *See, e.g., Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 310-11 (1985) (private right of action under securities law may be barred based on plaintiff's own culpable conduct); *OHC Liquidation Trust v. Credit Suisse (In re Oakwood Homes Corp.)*, 356 F. App'x 622, 627 (3d Cir. 2009) (*pari delicto* bars claims by equally culpable plaintiffs) (unpublished); *Official Comm. of Unsecured Creditors v. R.F. Lafferty & Co.*, 267 F.3d 340, 358-60 (3d Cir. 2001) (*pari delicto* barred committee from prosecuting claims on debtor's behalf). Indeed, if the Settlement Noteholders suffer any harm as a result of any breach by the Debtors' of their obligations under the Confidentiality Agreements, the Settlement Noteholders will have administrative claims against the Debtors' estates.

the Bankruptcy Court, does not state a colorable claim for relief.

45. Most courts that have addressed the issue have found that equitable disallowance simply does not exist as a remedy. *See, e.g.*, *Benjamin v. Diamond (In re Mobile Steel Co.)*, 563 F.2d 692, 699 (5th Cir. 1977) ("Equitable considerations can justify only the subordination of claims, not their disallowance."); *see also In re Mid-American Waste Sys., Inc.*, 284 B.R. 53, 68 (Bankr. D. Del. 2002) (Walsh, J.) (quoting *Mobile Steel* for proposition that equitable considerations cannot justify claim disallowance); *American Cigar Co. v. MNC Commercial Corp. (In re M. Paolella & Sons, Inc.)*, Adv. Pro. No. 87-1007F, 1991 Bankr. LEXIS 1181, at *38 (Bankr. E.D. Pa. April 15, 1991) (same).

46. This conclusion is mandated by limitations on the power of the bankruptcy courts to create new remedies through the exercise of equitable discretion. As the Third Circuit held in *In re Combustion Engineering, Inc.*, 391 F.3d 190, 236 (3d Cir. 2004), "[t]he general grant of equitable power contained in § 105(a) cannot trump specific provisions of the Bankruptcy Code, and must be exercised within the parameters of the Code itself." *See also Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 206 (1988) ("[W]hatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code."). Here, Section 510(c) of the Bankruptcy Code expressly creates an equitable remedy – equitable subordination – that addresses creditor misconduct, and neither that section nor any other in the Bankruptcy Code contemplates the use of the court's equitable powers to *disallow* a claim. Indeed, Section 502(b) of the Bankruptcy Code enumerates the nine grounds upon which a claim may be subject to disallowance. Notably, those grounds do *not* include any equitable considerations. The Supreme Court has confirmed that these constitute the *only permissible*

grounds on which a court may disallow a claim. *Travelers Cas. & Sur. Co. of Am. v. PG&E*, 549 U.S. 443, 449 (2007).

47. Despite the absence of a single reported case applying the doctrine of equitable disallowance, the Bankruptcy Court nevertheless upheld the potential availability of the doctrine, citing a footnote in *Citicorp Venture Capital, Ltd. v. Comm. of Creditors Holding Unsecured Claims*, 160 F.3d 982 (3d Cir. 1998), in which the Third Circuit declined to address the issue. Opinion at 112. The Bankruptcy Court also relied on decisions in the *Adelphia* bankruptcy upholding the theoretical availability of equitable disallowance. *See id.* at 112-15. While the *Travelers* case appears to close the door left open in *Citicorp*, that debate may await full briefing. It suffices for present purposes to note that this is yet another dispositive threshold legal issue as to which there is *at the very least* substantial ground for difference of opinion – warranting immediate review by an appellate court.

48. A closely related question is whether this remedy, even if theoretically available, could ever be imposed based on the facts alleged in these cases. The Bankruptcy Court noted Judge Gerber's observation in *Adelphia* that the severe step of actually disallowing, rather than merely subordinating, a claim on equitable grounds could be taken only "in those extreme instances – perhaps very rare – where it is *necessary* as a remedy." *See Adelphia Commc'ns Corp. v. Bank of Am., N.A. (In re Adelphia Commc'ns Corp.)*, 365 B.R. 24, 73 (Bankr. S.D.N.Y. 2007) (emphasis added); *see also* Opinion at 115.

49. Here, the Bankruptcy Court has already found that Aurelius did not harm but actually *helped* the estates by urging the Debtors to seek and obtain a *larger* settlement from JPMC, which redounded to the benefit of all stakeholders in the cases. Opinion at 71. The only remaining "injury" even theoretically requiring a "remedy" is the supposed harm to creditors that

sold securities to Aurelius based on Aurelius's supposed possession of material nonpublic information. Even assuming that any such harm could be established (along with all of the other elements of an insider trading claim), the federal securities laws provide a well-developed set of standards and potential remedies that may be pursued by the parties actually claiming injury, as well as by the SEC. The draconian remedy of equitable disallowance clearly is not appropriate, much less *necessary*, in such circumstances.

50. Accordingly, there is substantial ground for difference of opinion both as to the existence of equitable disallowance as a remedy and whether, as a matter of law, it could ever be imposed in this context. Immediate appellate review is warranted to answer these questions.

4. The Bankruptcy Court Distorted and Misapplied the Law Governing Each Element of an Insider Trading Claim

51. The Bankruptcy Court misstated or ignored well-settled legal principles governing each of the elements of an insider trading claim. Again, any *one* of these legal issues, properly decided, would mandate reversal of the *Cybergenics* ruling.

a) The Bankruptcy Court ignored settled law in holding that Aurelius could be found to be an "insider" of the Debtors subject to potential insider trading liability under the "classical theory"

52. First, the Bankruptcy Court erred in upholding the allegations that Aurelius was an "insider" of the Debtors, a necessary step in alleging a breach of duty since there is no allegation that Aurelius breached any contractual duty. For an individual or entity to become liable for insider trading under Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5, it must trade on material, nonpublic information in violation of a fiduciary duty and while employing "manipulation or deception." *See Dirks v. S.E.C.*, 463 U.S. 646, 653-54 (1983). Trading by a non-fiduciary does not violate the securities laws unless done *in breach of a duty to*

the source of the information. *See id.* at 657. The need for a breach of duty flows from the requirement of deception or manipulation as an element of securities fraud. The party misappropriating inside information must be guilty of "deception of those who entrusted him with access to confidential information." *United States v. O'Hagan*, 521 U.S. 642, 652 (1997). It is well settled that where the recipient of information discloses to the source that he plans to trade on it, "there is no 'deceptive device' and thus no section 10(b) violation." *Id.* at 655.

53. A straightforward application of this threshold breach of duty requirement bars insider trading liability here. Neither Aurelius nor the other Settlement Noteholders were fiduciaries; they acted solely on behalf of themselves. *See In re Drexel Burnham Lambert Grp.*, 123 B.R. 702, 706 (Bankr. S.D.N.Y. 1991) (ad hoc groups, "unlike members of officially appointed committees, have no fiduciary obligations under the Bankruptcy Code"); *see also Dixon v. Am. Cmty. Bank & Trust (In re Gluth Bros. Constr.)*, 424 B.R. 379, 390 (Bankr. N.D. Ill. 2009) ("[C]reditors have no fiduciary duty to debtors or other creditors."). Aurelius's obligations to the Debtors were assumed *contractually*, through the Confidentiality Agreements. Under New York law, the existence of an arm's-length contract bars any inference of an additional fiduciary duty. *See LFD Operating, Inc. v. Ames Dep't Stores, Inc. (In re Ames Dep't Stores, Inc.)*, 274 B.R. 600, 626 (Bankr. S.D.N.Y. 2002). Moreover, receipt of confidential information does not by itself create a fiduciary duty, particularly where parties operate under an arm's-length agreement. *See Walton v. Morgan Stanley & Co.*, 623 F.2d 796, 799 (2d Cir. 1980).

54. Aurelius indisputably satisfied all of its contractual duties to the Debtors, and any obligations it had under the Confidentiality Agreements with respect to trading terminated with those agreements. The very structure of the Confidentiality Agreements, requiring the Debtors at

the end of the Confidentiality Periods to publicly disclose any material nonpublic information provided, reflects that the parties understood and expected that the Settlement Noteholders would resume unrestricted trading once those agreements terminated. This understanding was confirmed in undisputed testimony at the Second Confirmation Hearing. Ex. F at 152-53. Aurelius cannot be liable for insider trading based on misappropriation where it breached no duty and deceived no one.

55. Notwithstanding the fundamental failure of this critical element, the Bankruptcy Court remarkably determined that Aurelius could be considered an "insider" of the Debtors with fiduciary duties to shareholders and the estates, making it subject to liability under the "classical theory" of insider trading. Opinion at 128-32. The court illogically held that Aurelius may have assumed fiduciary duties that overrode its expressly limited contractual obligations simply because it was provided with confidential information *pursuant to those very contracts* to facilitate negotiations with the common goal of reaching a consensual resolution. *See id.* at 130. This unprecedented holding stretches beyond recognition the "temporary insider" doctrine under *Dirks*, 463 U.S. at 655 n.14 – which applies only to those who *actually become insiders of a debtor* on a temporary basis, such as accountants, lawyers, and consultants – and ignores the authority cited above (at ¶ 53) holding that receipt of confidential information pursuant to an arm's-length contract does *not* create fiduciary duties. On this theory, anyone negotiating anything confidentially with an issuer would become a temporary insider simply because they share a common goal of reaching a deal, and would retain that status following failed negotiations so long as there was any prospect that negotiations might resume months or even years later.

56. The Bankruptcy Court further held that, based on their mere "status" as alleged "holders of blocking positions in two classes of the Debtors' debt structure," the Settlement Noteholders could be found to have assumed fiduciary duties to all other members of those classes. Opinion at 132.[11] This holding by itself would impose fiduciary duties on most ad hoc creditor groups – a radical concept that would render even the formation of such a group self-defeating and unviable, and thereby disrupt and chill the settlement negotiation process in countless in-court bankruptcy cases and out-of-court restructurings.[12]

57. But the Opinion goes further. The Bankruptcy Court held that based solely on this purported duty to other *creditors*, Aurelius and the other Settlement Noteholders could be viewed as "non-statutory insiders" with even broader fiduciary duties. *Id.* at 132. This holding again completely ignores the governing legal standards; it is well-settled (even in the cases cited by the Bankruptcy Court) that "non-statutory insider" status requires a non-arm's-length relationship and some ability to dominate a debtor or dictate its business decisions. *See, e.g.*, *Schubert v. Lucent Techs. Inc. (In re Winstar Commc'ns, Inc.)*, 554 F.3d 382, 396-97 (3d Cir. 2009) ("non-statutory insider" status found where party controlled important business decisions of debtor and had ability to coerce it into unfavorable contracts and involve its employees in improper transactions); *Official Unsecured Creditors Comm. of Broadstripe, LLC v. Highland*

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[11] The phrase "blocking position" is something of a misnomer. It merely refers to the ability to cause one class of creditors to be considered a "rejecting class" under 11 U.S.C. § 1126(c). But being a rejecting class does not "block" a plan of reorganization, or anything else for that matter. Section 1129(b) of the Bankruptcy Code permits a court to confirm a plan of reorganization over the objection of a rejecting class so long as the plan does not discriminate unfairly and is fair and equitable with respect to that rejecting class. Ex. D at 164-65. In any event, none of the Settlement Noteholders individually held a blocking position in any class, and the undisputed testimony was that there were no voting agreements among the four separate noteholders. *See* Ex. D at 50.

[12] If, as the Bankruptcy Court appears to contemplate, members of ad hoc groups would assume all the duties and restrictions that apply to members of *official* creditors' committees, this would preclude group members from pursuing their own economic interests and bar them from trading for the duration of the case *even if they were not in possession of material nonpublic information*. But these restrictions are precisely what deters most large bondholders from sitting on official committees, as is the case here. Expanding these restrictions to all groups holding a potential blocking position would functionally eliminate ad hoc groups as an important tool in bankruptcy and out-of-court restructuring negotiations.

Capital Mgmt., LP (In re Broadstripe, LLC), 444 B.R. 51, 80 (Bankr. D. Del. 2010) (listing customary indicia of non-statutory insider status, including ability to select management for debtor, control over management decisions, and pre-existing relationship stemming from other than arm's-length transaction).

58. The facts alleged by the Equity Committee fell far short of establishing "insider" status under either of these doctrines. But the Bankruptcy Court's own findings that Aurelius and the other Settlement Noteholders *helped* the estate and did not improperly dominate or skew the Plan process (Opinion at 71-73) rendered the court's "insider" holdings truly inexplicable – particularly since the Bankruptcy Court earlier held that the Settlement Noteholders could not obtain a release under the Sixth Amended Plan because they "were not acting in this case in any fiduciary capacity; their actions were taken solely on their own behalf; not others." *Wash. Mut.*, 442 B.R. at 349. On information and belief, the Bankruptcy Court's "insider" rulings are already having an impact on the willingness of parties in major bankruptcies and out of court to participate in ad hoc groups and engage in confidential negotiations. Immediate appellate review is necessary to prevent these rulings from causing even more widespread damage.

b) The Bankruptcy Court ignored the strict requirement that an insider trading claim include allegations of facts giving rise to a compelling inference of scienter

59. The Bankruptcy Court further compounded its error by ignoring the strict standard for the pleading of scienter in a securities fraud complaint, failing to require that the Equity Committee plead facts giving rise to a "strong inference" that Aurelius acted with fraudulent intent and "knew or recklessly disregarded" that it was trading while in possession of material nonpublic information. The Private Securities Litigation Reform Act of 1995 (PSLRA) set forth stringent new pleading requirements that the Supreme Court construed in *Tellabs, Inc.*

v. Makor Issues & Rights, Ltd., 551 U.S. 308 (2007). *Tellabs* requires that a plaintiff plead *with particularity* facts showing not just that an inference of knowledge or recklessness "rationally could be drawn," but rather facts giving rise to a "powerful or cogent" inference. *Id.* at 323. And a court also "must consider plausible nonculpable explanations for the defendant's conduct," such that a complaint will not be sustained unless "a reasonable person would deem the inference of scienter cogent and at least as compelling as any opposing inference one could draw from the facts alleged." *Id.* at 324; *see also Winer Family Trust v. Queen*, 503 F.3d 319, 328-29 (3d Cir. 2007) (affirming dismissal of scienter pleading under *Tellabs* standard).

60. The Equity Committee's proposed Complaint certainly fails to (and could not even be amended to) satisfy Congress's stringent standard, which the Bankruptcy Court failed even to acknowledge while giving no weight to the plausible, indeed overwhelming, non-culpable explanations for the defendants' conduct. It is undisputed that Aurelius and the Debtors specifically agreed in the confidentiality agreements that *the Debtors would disclose* any material nonpublic information at the end of each Confidentiality Period. It is also factually undisputed that the Debtors, in consultation with their experienced securities counsel, Weil, Gotshal & Manges LLP, actually made informed, good faith judgments about what information did and did not have to be disclosed. Ex. F at 127-28, 153. Aurelius's reasonable, good faith reliance on the Debtors' contractual duties *and* the Debtors' actual judgments in performing those duties undercuts any reasonable inference of scienter, let alone a cogent or compelling one, particularly given the undisputed testimony that Aurelius independently confirmed the Debtors' conclusions based on its own understanding and experience. Ex. D at 113-14.

61. The Bankruptcy Court did not question any of these facts, but merely stated that good faith reliance does not constitute an "exception to the scienter element of insider trading"

(Opinion at 134) – as if the burden were on Aurelius to *disprove* scienter rather than on the Equity Committee to plead scienter with particularity. The Bankruptcy Court circularly suggested that Aurelius cannot use its good faith reliance on the Debtors and their professionals as a "shield" if it violated its own internal insider trading policies (*id.* at 135) – failing to explain how Aurelius's careful conduct (which included its *own* good-faith judgments that information in its possession about settlement negotiations was not material) in any way violated those polices in the first place, much less why the policies themselves could somehow alter Aurelius's legal duties.

62. The Bankruptcy Court's holding comes dangerously close to equating a finding of materiality with a showing of scienter. But as one court aptly observed:

> [I]t would be folly to hold . . . that the knowing failure to disclose a material fact in and of itself necessarily gives rise to a strong inference of fraud. There are far too many circumstances in which a material omission would evidence no such mental state. The person or entity responsible might have held a perfectly reasonable and good faith, if ultimately mistaken, belief that the fact omitted was not material, to name but one.

L.L. Capital Partners, L.P. v. Rockefeller Ctr. Props., Inc., 939 F. Supp. 294, 299 (S.D.N.Y. 1996). Where, as here, a complaint "does not present facts indicating a *clear* duty to disclose" – in light of Aurelius's reasonable reliance on the scope of its contractual duties – "plaintiff's scienter allegations do not provide *strong* evidence of conscious misbehavior or recklessness." *Kalnit v. Eichler*, 264 F.3d 131, 144 (2d Cir. 2001) (emphasis added). Moreover, contrary to the Bankruptcy Court's statement that "the statute only requires that the Settlement Noteholders have knowledge that they were in possession of material nonpublic information" (Opinion at 134), the scienter element further requires knowing *deception*. *See McLean v. Alexander*, 599 F.2d 1190, 1197 (3d Cir. 1979) (scienter element requires "'conscious deception or . . . a

misrepresentation so recklessly made that the culpability attaching to such reckless conduct closely approaches that which attaches to conscious deception.'") (internal citation omitted).

63. In any event, the dubious materiality of the information in Aurelius's possession itself further undercuts the strength of any inference of scienter. Even the Bankruptcy Court implicitly recognized that the fitful, frustrating, and inconclusive settlement negotiations (established through detailed and uncontradicted testimony) were not material throughout, but only "may have shifted towards the material end of the spectrum" at some unspecified point. Opinion at 128. The undisputed facts simply do not support a strong inference that Aurelius – which participated in those negotiations only during two brief periods that were ten and three months prior to a first, tentative settlement being reached – knew or recklessly ignored that it was improperly trading while in possession of material nonpublic information.

64. The Bankruptcy Court further erred in failing to scrutinize the Equity Committee's allegations regarding Aurelius's trading patterns to ensure that they could support a cogent and compelling inference of guilty knowledge – absent which, allegations regarding trading cannot support a pleading of scienter. *See In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1424 (3d Cir. 1997) (declining to infer fraudulent intent from trading "in the normal course of events"); *see also Zumpano v. Juniper Networks, Inc. (In re Juniper Networks, Inc.)*, 158 F. App'x 899, 901 (9th Cir. 2005) (granting motion to dismiss based on failure to allege that defendants' stock sales were "inconsistent with prior trading histories"). Here, the Complaint alleges only that Aurelius bought certain of the Debtors' securities at the conclusion of the Confidentiality Periods, but offers no reason to infer that this trading was unusual or driven by knowledge of stale settlement offers rather than the contemporaneous public disclosure of material new information about the company (*e.g.*, the size of expected tax refunds) – and thus

no basis to conclude, as *Tellabs* requires, that the facts could support a "powerful or cogent" inference of scienter that is "at least as compelling" as the non-culpable inferences. *See Tellabs*, 551 U.S. at 323-24; *see also Baker v. MBNA Corp.*, No. 05-272, 2007 WL 2009673, at *7 (D. Del. July 6, 2007) (strong inference of scienter may not be based on sale of relatively small proportion of holdings, adopting "30 percent" figure as "useful guide" based on *In re Suprema Specialties, Inc. Sec. Lit.*, 438 F.3d 256, 278 (3d Cir. 2006)).

65. The Bankruptcy Court was unable to draw any conclusions itself from the trading patterns with respect to materiality (*see* Opinion at 127-28), and with respect to scienter, merely recited the Equity Committee's conclusory allegations about the general volume of trades without explaining (in light of the highly material information that *was* disclosed at the conclusion of each Confidentiality Period and undisputed evidence that the trading was consistent with pre-existing patterns) what facts actually gave rise to a compelling inference of scienter (*id.* at 133-34).

66. In this connection, the Bankruptcy Court simply brushed aside as irrelevant many other undisputed facts highly inferential of nonculpability, e.g., that certain Aurelius Funds sold securities – to their substantial detriment – just days before the settlement was publicly announced; that the Aurelius Funds' purchases and sales of PIERS closely corresponded to the Debtors' public announcements regarding billions of dollars of tax refunds, as well as the ebbs and flows of important tax legislation bearing on that issue; that the Settlement Noteholders were frequently trading in opposite directions to each other; and that there were important transcendent factors (such as the tumultuous markets of 2009 and the inflows of capital into the Aurelius Funds) that could plausibly explain why the Aurelius Funds made the purchases they did. Moreover, the trading records that the Bankruptcy Court reviewed plainly reveal that a

significant part of the supposed "buying spree" (Opinion at 126) by two of the Aurelius Funds in May 2009 (the third fund did not yet exist) consisted of simply rotating from low coupon to high coupon bonds of the same class.

67. In essence, the court "punted" on scienter, leaving the issue to be developed through discovery – but that is *precisely* what the stringent facial pleading requirements of the PSLRA are meant to prevent. The entire point of the PSLRA is to *protect* defendants from "abusive practices committed in private securities litigation,"[13] by requiring a heightened and particularized pleading of scienter *before* a plaintiff is permitted to proceed with discovery. Indeed, granting discovery to permit a plaintiff to try to meet this standard – as the Bankruptcy Court appears to have done here – is grounds for mandamus. *See SG Cowen Sec. Corp. v. U.S. Dist. Court for the N. Dist. of Cal.*, 189 F.3d 909, 912-19 (9th Cir. 1999) (granting mandamus to restore discovery stay in insider trading case where district court had rejected pleadings for insufficient particularity, but nonetheless authorized limited discovery). This distortion of Congress's intent requires immediate reversal.

c) The Bankruptcy Court changed the law of materiality to create a new per-se no-trading rule that accorded with its policy preferences

68. The Bankruptcy Court's discussion of materiality focused largely on case law drawn from the merger context, *e.g.*, *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988), where the mere existence, or early progress, of negotiations not known or suspected by the marketplace may be material. *See* Opinion at 119-20. The Bankruptcy Court ignored the reality that brief, intermittent negotiations – often occurring months apart and ultimately spanning a year or more, as was the case here – are part and parcel of the bankruptcy process; that the existence of

[13] Joint Explanatory Statement of the Committee of Conference, H.R. Rep. No. 104-369, at 41 (1995) (Conf. Rep.), reprinted in 1995 U.S.C.C.A.N. 730.

negotiations itself is rarely surprising or material; and that all parties in large, complex bankruptcies understand that until a deal takes shape, intermediate, non-binding bargaining positions of the parties are simply not material. In any event, the record overwhelmingly established that the settlement discussions to which Aurelius was privy during 2009 left the parties billions of dollars apart and could not be used to predict the contours of the multi-party settlement that ultimately emerged, and that the pendency of negotiations was widely known.[14]

69. While the details of that record are beyond the scope of this Motion,[15] what is relevant is that the Bankruptcy Court – despite devoting ten pages of its Opinion to discussing materiality (Opinion at 118-28) – ultimately made clear that it believed the situation should be governed by a per se rule that parties participating in confidential settlement negotiations by definition become permanently restricted. Such parties, the court declared, are required to adopt permanent trading restrictions (either shutting down trading or maintaining an ethical wall for the duration of the case) – a requirement previously imposed only upon members of official bankruptcy committees and other fiduciaries. *See id.* at 137-38.

70. The retroactive imposition of this extreme, per se rule is unfair to the parties in this case, who relied upon customary practice and acted scrupulously and with a high level of care, and will have a destructive effect on the bankruptcy process in other cases, where parties that are not in a position to assume ongoing trading restrictions or the burdens of maintaining an

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[14] Ex. D at 69, 118-19; Ex. E at 129-30, 165.

[15] However, some of the inferences credited by the Bankruptcy Court are facially unreasonable. For example, the court seemed to accept an argument that the Settlement Noteholders' request to terminate the Second Confidentiality Period one day early, on December 30, 2009, is evidence that they wanted to trade based on the details of unsuccessful settlement negotiations from November (Opinion at 126), even though (1) trading was obviously driven at the end of December by highly material tax refund information then being publicly disclosed, and (2) undisputed testimony established that the reason for the request was not to facilitate trading but to allow the market to absorb the tax refund information before year end, so that audited financial statements (which are prepared as of December 31 for the Aurelius Funds and many other institutions) could be valued using the normal marked-to-market method. *See* Ex. E at 52-53.

ethical wall are likely to eschew participation in settlement negotiations – to the detriment of the core purpose of chapter 11 of fostering consensual reorganizations. For this reason as well, immediate appellate review of the Standing Order is warranted.

5. The Bankruptcy Court Failed to Determine whether the Debtors were in Fact Reasonable in Refusing to Pursue the Insider Trading Claims

71. Both the Debtors and the Creditors' Committee reviewed the discovery record promulgated by the Equity Committee and determined that the insider trading charges were wholly without merit and should not be prosecuted. Implicit in that judgment was the conclusion that, even if the claims could be shown to have any merit, the scant likelihood of success was outweighed by the significant costs and burdens of financing and participating in the litigation.

72. Having concluded, contrary to the responsible fiduciaries, that the Equity Committee alleged colorable claims against the Settlement Noteholders, the Bankruptcy Court acknowledged that it was "required . . . to balance the probability of success on the claim against the burden on the estate that would result from its prosecution." Opinion at 138. While recognizing that these cases would likely "devolve into a litigation morass" (*id.*), the Bankruptcy Court inexplicably granted the Standing Motion without engaging in the required analysis. If it had, the conclusion would have been inescapable that the Debtors could and did reasonably decide that the litigation simply was not worth pursuing.

73. On the "benefit" side of the ledger would have to be weighed, first, the highly unlikely prospect (in light of the Complaint's multiple infirmities) that the claims could survive a formal motion to dismiss, summary judgment, or trial. And even if the Equity Committee were to prevail, the damages that it could recover from the Aurelius Funds on behalf of the estates would be quite modest – limited to disgorgement of profits *directly* resulting from use of the

wrongfully acquired material nonpublic information. *See, e.g., S.E.C. v. Cavanagh*, 445 F.3d 105, 116 n.25 (2d Cir. 2006) ("Because the remedy is remedial rather than punitive, the court may not order disgorgement above [the] amount [of money acquired through wrongdoing . . . plus interest.]"). Moreover, the damage calculation would have to *exclude* increases in the value of securities purchased attributable to factors *other than* the alleged material nonpublic information. *See Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 343 (2005) (civil securities fraud damage calculation must consider the "tangle of factors affecting price").

74. Here, if a trial court were to find liability, it would be required to calculate the portion of the profits of each of the Aurelius Funds relating *only* to purchases *after* Aurelius was provided with material nonpublic information but before it was publicly disclosed (at most, a period of ten months) and *directly attributable to trading on particular material nonpublic information* – eliminating, for starters value attributable to (1) the passage of legislation in November 2009 that added billions of dollars of value to the estates by expanding the Debtors' eligibility for NOL carry-back tax deductions; (2) the Debtors' public disclosures in April and December 2009 of the likely size of its tax refunds; and (3) the continued accrual of postpetition interest. Moreover, to the extent it is shown that the Aurelius Funds' trades were with other Settlement Noteholders (as appears likely from a comparison of trading records in evidence) or other sophisticated institutional investors, many of which participated in or knew of settlement negotiations, the trial court will have to determine whether, in fact, the Aurelius Funds had a material advantage over its seller in knowledge about the state of settlement negotiations. This inquiry would lead to very limited damages, if any. Regardless, the Equity Committee made no showing on the issue, and the court made no finding on it.

75. Moreover, even if the estates could overcome all of these hurdles and recover *something* on these putative claims, it is virtually impossible for any benefit from such recovery to flow down to the parties on whose ultimate behalf the Equity Committee purports to labor. Common stockholders are more than $7.6 billion out of the money. Even preferred stockholders will be at least $165 million out of the money by February 2012, an extremely optimistic target for the effective date of a new plan. Any delay thereafter pushes equity further out of the money by $20 million per month – or $42 million per month if the Bankruptcy Court's interest rate ruling is reversed (an event that would itself add more than $810 million in postpetition interest claims to be paid before equity holders can receive a recovery).

76. Against this remote and (at most) modest upside, the Debtors could reasonably weigh the grave costs and harms that would flow from full litigation of the insider trading charges. First, the attorneys' fees of this enterprise alone are likely to exceed the ultimate potential damages. The Debtors would be responsible at minimum for the fees and expenses of the Equity Committee in prosecuting the action; their own fees in defending it (since the Debtors' own conduct is at issue and they will be liable to the Settlement Noteholders if it is determined that the Debtors breached the Confidentiality Agreements); the fees of the Creditors' Committee, which participated in the settlement negotiations; and potentially the fees of other parties receiving fee reimbursements that ultimately are required to participate in the litigation. Moreover, the scope of the litigation in which all these parties would have to participate would be massive. Many creditors other than the Settlement Noteholders (including, for example, certain senior noteholders represented by White & Case LLP and holders of Trust Preferred Securities, Litigation Tracking Warrants, and WMB bonds) participated in or have been made privy to the existence and details of confidential negotiations of one type or another and then

resumed unrestricted trading in the Debtors' securities – conduct that may be relevant to many issues touching on liability and damages. Under the Bankruptcy Court's Opinion, many of these parties would be considered estate fiduciaries that should have restricted their trading. Any differential treatment in the bankruptcy between such parties and the Settlement Noteholders would obviously be hotly litigated. The aggregate cost to the estates to litigate all of these intertwined matters to conclusion will be at least many tens of millions of dollars. Beyond that, pendency of the litigation is likely to complicate efforts to confirm a reorganization plan in these cases, imposing further cost and delay on the estates and their creditors.

77. In short, even if it were not so obvious that the Complaint fails to state a colorable claim, the Debtors were entirely reasonable in refusing to pursue claims that could only mire the estates in endless, pointless, fruitless litigation. Immediate, expedited appeal is necessary to prevent these harms and burdens from being imposed on the estates and the parties.

B. Immediate Appeal of the Standing Order Would Materially Advance the Termination of the Litigation and Conserve Resources

78. The final prong of the interlocutory appeal standard under 28 U.S.C. § 1292 is easily satisfied here. An immediate appeal of the Standing Order will lead to reversal and put an end to this baseless, harassing litigation, freeing the Debtors to proceed expeditiously with another revised plan of reorganization. *See Stanziale v. Sun Nat'l Bank (In re Dwek)*, No. 09-5046, 2010 U.S. Dist. LEXIS 3203, at *7 (D.N.J. Jan. 15, 2010) (granting leave to appeal ruling on motion to dismiss where reversal would alleviate need to litigate certain claims). This would avoid a waste of the limited resources of the parties, and more importantly, the judiciary. *See*

Broadstripe, 2009 U.S. Dist. LEXIS 25690, at *7 (granting leave to appeal interlocutory order to "avoid wasted trial time and litigation expense").[16]

II.

LEAVE TO APPEAL THE CONFIRMATION ORDER SHOULD BE GRANTED, IF NECESSARY, TO ENSURE THAT UNSECURED CREDITORS RECEIVE THEIR CONTRACTUAL ENTITLEMENTS UNDER ANY PLAN OF REORGANIZATION

79. Aurelius asserts that the Confirmation Order is a final order appealable as of right under the "pragmatic and less technical" approach to finality in bankruptcy cases. *See* authorities cited above at ¶¶ 28-31. Indeed, in *In re Armstrong World Indus., Inc.*, 432 F.3d 507 (3d Cir. 2005), the Third Circuit held that an order denying confirmation of a plan of reorganization was "final" where (i) the distribution of assets between different creditor classes was affected; (ii) no additional fact-finding was required; (iii) discrete questions of law were presented and (iv) practical considerations of judicial economy were present. *Id*. at 511. So too here. The Bankruptcy Court's denial of confirmation was premised on an erroneous legal conclusion – that a creditor's entitlement to postpetition interest in a solvent estate is limited as a matter of law to the federal judgment rate. *See* Opinion at 81.

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[16] In the event the Court determines that review on appeal is unavailable here, Aurelius respectfully requests in the alternative that the Court exercise its power to treat this application as a petition for a writ of mandamus and issue a writ reversing the Standing Order. *See, e.g., First Fid. Bank, N.A. v. Hooker Invs., Inc. (In re Hooker Invs., Inc.)*, 937 F.2d 833, 837 (2d Cir. 1991) ("Although we do not have jurisdiction over the Bank's attempted appeal as a matter of right from the non-final bar order, we may in appropriate circumstances treat an unsuccessful attempt to appeal as a petition for a writ of mandamus."). Mandamus may be appropriate where (i) the petitioning party has no other means to obtain relief, (ii) the lower court committed clear and indisputable error, and (iii) issuance of the writ is appropriate in the circumstances. *See Cheney v. United States Dist. Ct. for the Dist. of Columbia*, 542 U.S. 367, 380-81 (2004); *United States v. Brunson*, 416 F. App'x 212, 221 (3d Cir. 2011) (unpublished).

Here, absent reversal of the Standing Order, Aurelius will have no other means to prevent the Equity Committee's wasteful and vexatious litigation campaign from inflicting upon Aurelius, the estates, and other parties the massive costs and expenses of this "litigation morass." The pendency of these accusations does not just exact a dollar cost – it leaves a cloud over Aurelius, its honorable and hard-working professionals, and the other Settlement Noteholders. The toll of this reputational damage is likely to be significant even if, as is overwhelmingly likely, the claims are eventually dismissed. As set forth in detail above, the Bankruptcy Court's Standing Order is based on multiple clear errors of law, such that a writ of mandamus would be entirely appropriate in the circumstances of these cases.

80. That conclusion is in direct conflict with case law holding that the contract rate is presumptively *required*. *See, e.g.*, *Official Comm. of Unsecured Creditors v. Dow Corning Corp. (In re Dow Corning Corp.)*, 456 F.3d 668, 679 (6th Cir. 2006) (holding that absent compelling equitable considerations, the bankruptcy court's role is to enforce contractual rights of parties with respect to postpetition interest); *Ruskin v. Griffiths*, 269 F.2d 827, 832 (2d Cir. 1959) (awarding post-petition interest at contract rate and noting that "where there is no showing that the creditor entitled to the increased interest caused any unjust delay in the proceedings, it seems to us the opposite of equity to allow the debtor to escape the expressly-bargained-for result of its act"); *see also FSLIC v. Moneymaker (In re A&L Props.)*, 96 B.R. 287, 290 (C.D. Cal. 1988) (awarding post-petition interest at contract rate); *In re Smith*, Case No. 03-10666, 2008 Bankr. LEXIS 7, at *2 (Bankr. W.D. Ky. Jan. 7, 2008) (same); *In re Schoenberg*, 156 B.R. 963, 972 (Bankr. W.D. Tex. 1993) (same); *In re Beck*, 128 B.R. 571, 573 (Bankr. E.D. Okla. 1991) (same).

81. Indeed, the Bankruptcy Court *twice* recognized that enforcement of bargained-for contract rates was permissible under the Bankruptcy Code and appropriate if supported by the equities in a particular case – first in *In re Coram Healthcare Corp.*, 315 B.R. 321, 346 (Bankr. D. Del. 2004) (holding that contract rate may be payable depending on specific facts dictating which rate is "fair and equitable"), and more recently in its January opinion in these cases, *Wash. Mut.*, 442 B.R. at 358-59. The Bankruptcy Court departed sharply from these prior holdings in concluding now that the federal judgment rate is legally *mandated*. That conclusion could have a significant impact on the distribution of estate assets as it results in the improper elimination of more than $810 million of postpetition interest claims. Resolution of this discrete legal issue requires no further fact-finding and will expedite resolution of these cases as it will obviate the

need for further appeals in connection with any alternative plan that does not respect creditors' contractual rights to postpetition interest.

82. In the event the Court concludes that the Confirmation Order is not final, the Court should nevertheless grant leave to appeal as the appeal would undoubtedly involve a controlling question of law for which there is a substantial ground for difference of opinion – namely, whether the Debtors' creditors are entitled to postpetition interest at the applicable contract rate. Resolution of this issue now will expedite the resolution of these cases by correcting a legal error that will otherwise render any subsequently confirmed plan subject to reversal on appeal.

WHEREFORE, Aurelius respectfully requests that the Court enter an Order substantially in the form attached hereto as Exhibit K or in the alternative grant vacatur through the issuance of a writ of mandamus; set an expedited schedule for the briefing of this appeal; and grant such further and other relief as the Court deems appropriate.

Dated: Wilmington, Delaware
September 27, 2011

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