IN THE UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re:	Chapter 11
WASHINGTON MUTUAL, INC., et al.,	Case No. 08-12229 (MFW)
Debtors.	Jointly Administered
	Hearing Date: July 5, 2011 at 9:30 a.m. (EST) **Related Dkt. No. 7040**

OBJECTION TO CONFIRMATION OF THE MODIFIED SIXTH AMENDED PLAN OF AFFILIATED DEBTORS BY CLASS REPRESENTATIVES OF DIME LITIGATION TRACKING WARRANTS

TO: THE HONORABLE MARY F. WALRATH,
UNITED STATES BANKRUPTCY JUDGE

Nantahala Capital Partners, LP, Blackwell Capital Partners, LLC, Axicon Partners LLC, Brennus Fund Limited, Costa Brava Partnership III, LP, and Sonterra Capital Master Fund, Ltd. (collectively, the "Claimants"), for themselves and as class representatives of the Dime Litigation Tracking Warrants ("LTWs"), make this Objection ("Objection") to confirmation of the Modified Sixth Amended Plan of Affiliated Debtors dated February 7, 2011 ("Modified Plan"), and represent as follows:

1. On January 7, 2011, the Bankruptcy Court rendered its opinion denying confirmation of the Debtors' Sixth Amended Joint Plan ("Confirmation Opinion"). The Modified Plan purports to address the infirmities raised by the Court in the Confirmation Opinion so as to proffer a confirmable plan of reorganization. The Debtors miss the mark as demonstrated herein.

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2. The Debtors stated at a June 9, 2011 status conference before the Court that they may file a seventh amended plan based on a tentative settlement with the Equity Committee. As a result, the confirmation hearing relating to the Modified Plan was adjourned until July 5, 2011. Because of this development, the Debtors agreed to extend the Claimants' time to object to confirmation to June 17, 2011. This Objection is being filed only to the Modified Plan, and the Claimants expressly reserve the right to modify and supplement the Objection based on the provisions of any seventh amended plan filed.

A. The treatment under the Modified Plan for LTW holders is improperly vague.

3. The Debtors' prior Disclosure Statement, dated October 6, 2010 (at p. 102), provided that if the Claimants establish they hold claims against, rather than equity interests in, Washington Mutual Inc. ("WMI"), they will be treated as Class 12 general unsecured creditors. The Claimants argued at the confirmation hearing that a corresponding change needed to be made in the Debtors' plan of reorganization. In the Confirmation Opinion (Pp. 89-90, n. 42), the Court said the plan needed to be modified to address this point.

4. Section 1.209 of the Modified Plan does not clarify the situation; it makes matters worse. The Modified Plan adds the phrase "or as otherwise determined by the Bankruptcy Court" which suggests that the LTW holders could be put into a class other than Class 12 (General Unsecured) or Class 21 (Dime Warrants). That additional language ("or as otherwise determined by the Bankruptcy Court") leaves open the possibility that LTW holders may be placed in Class 12A (Late Filed Claims) or Class 18 (Debt Subordinated Claims). This ambiguity was raised by counsel for the LTW holders at the March 21, 2011 Disclosure Statement hearing relating to the Modified Plan, and the Debtors refused to clarify the Modified Plan on this issue.

5. It is hard to conceive how the Debtors can fairly argue that the LTW holders are both debt (Class 18) **and** equity (Class 21). It would seem that, by virtue of the Modified Plan, the Debtors would be required to take a position. Further, since the Modified Plan provides for payment of post petition interest, and the Confirmation Order provided that late filed claims get paid ahead of post petition interest claims (Confirmation Opinion at p. 90), it is not clear at all why there is a Class 12A (late filed claims) under the Modified Plan.

6. The plan confirmation time period is when debtors make decisions and parties in interest vote on a proposed treatment. Parties evaluating the merits of a plan of reorganization should not be left to guess as to what is in store for them after the plan is confirmed. As such, the Modified Plan is impermissibly vague as it applies to the LTW holders. Moreover, the Debtors failure to address these concerns have necessitated additional objections (as set forth herein) to confirmation of the Modified Plan.

B. <u>If Claimants establish they hold claims against, rather than equity interests in, WMI, the LTW holders should not have their distributions forfeited because of the Debtors' convoluted scheme relating to elections to be made on the ballots with respect to third party releases</u>.

7. In the Confirmation Opinion, the Court noted that a failure to make an election should not be viewed as a consent to a third party release (page 84).

8. The Confirmation Opinion also noted that it was unfair to ask parties in interest to elect whether to give a third party release when it was unclear if such party in interest would be receiving a distribution under the plan. (Confirmation Opinion at pp 84-85).

9. Claimants and the Debtors are currently litigating the class action Adversary Proceeding, Adv. No. 10-50911 ("Adversary Proceeding") as to whether, among other things, the LTW holders have claims against the Debtors. It is not clear when a Final Order will be rendered on this issue.

10. Section 32.6(c) of the Modified Plan provides that if a creditor does not elect to give a third party release within a specified time period, it forfeits its distribution.[1] That provision is unfair to the LTW holders since (a) they don't know whether they will be receiving a distribution under the Modified Plan until the Adversary Proceeding is decided by Final Order, and (b) they don't know whether such Final Order will be issued before the time period specified in Section 32.6 will expire. This provision is contrary to the Confirmation Opinion and must be stricken. LTW holders should have a minimum of 90 days after the Final Order in the Adversary Proceeding to decide whether to give the third party release under the Modified Plan.

C. The Modified Plan should not provide for trading restrictions with respect to the LTW holders.

11. Pages 36-37 of the Revised Supplemental Disclosure Statement dated March 16, 2011 ("Modified Disclosure Statement") contains a provision for returning securities in order "to ensure accurate identification of the Entities entitled to receive distributions pursuant to the Modified Plan…" Once the securities are returned, there can be no further trading in such security.

12. There is a similar provision in the Modified Disclosure Statement (at page 37) relating to LTW holders making an election to take stock in the Reorganized Debtors instead of cash with respect their potential Class 12 distribution under the Modified Plan. If a stock election is made by the LTW holders, LTWs must be tendered, and there can be no further trading of that LTW security.

13. In the Confirmation Opinion (at page 101-102), the Court held that the LTW holders were entitled to get the same type of stock election that other Class 12 creditors received.

[1] This provision has caused great confusion among the LTW holders. The time period to give a release appears to be one year from the Effective Date under the Modified Plan.

14. The Modified Disclosure Statement also provides (at page 37) that once an LTW holder elects to give a Third Party Release, it has to tender the LTW, and there can be no further trading of that LTW security.

15. These provisions should not apply to the LTW holders since it is not clear whether the Modified Plan will provide for a distribution to the Claimants, and the Adversary Proceeding may not be decided by Final Order until years after confirmation.

16. Claimants believe that the afore-cited provisions of the Modified Disclosure Statement were not included for any meaningful administrative convenience of the Debtors. Rather, the LTW holders believe that the Debtors provided for these harsh consequences to discourage LTW holders from taking a stock election, and to disrupt the trading market for LTWs. These offending provisions of the Modified Plan (a) have created serious confusion among many LTW holders, (b) undermine the relief provided to LTW holders under the Confirmation Order, and (c) should be stricken from the Modified Plan.

D. <u>Other infirmities to the Modified Plan need to be rectified.</u>

17. The Debtors have continually reminded the Court that the alleged "burn rate" in these bankruptcy cases is $30 million a month and therefore, there is a pressing to need to confirm their plan on an expedited basis.[2] Conveniently ignored in the "burn rate" reminders is that the delay in getting to confirmation was caused in large part by the Debtors themselves when they proffered a plan containing provisions relating to, among other things, third party releases

[2] The usage of "burn rate" phraseology in these bankruptcy cases is misleading. The so-called "burn rate" is really the impact of the contractual subordination that certain junior creditors agreed to give to senior creditors. That deterioration is not based on meaningful losses to the bankruptcy estate but rather the impact of a prepetition contractual arrangement wherein junior creditors took a greater risk for a greater economic return. The Debtors and Creditors Committee's misleading usage of this terminology is telling.

In addition, the significant overlap between the senior creditors and the subordinated creditors makes this so-called burn rate issue overstated. It is a situation of the dollars being shifted from a creditor's "left pocket" to its "right pocket."

which simply were contrary to established law. The Debtors compounded their self-induced problem by (a) delaying the adjudication of legitimate objections to their plan, that were raised in connection with the prior disclosure statement hearing, on the grounds that such objections were more properly dealt with as part of the confirmation hearing, and (b) not including in their plan, a provision which permitted the Court to modify offending provisions so that a defective plan may otherwise be confirmable. The Debtors' legal strategy was clear: start the confirmation train running even if the plan had infirmities, and give the Court only an "all or nothing" scenario, and hope that the desire to achieve a "confirmation" will trample over legitimate Section 1129 objections to confirmation raised by aggrieved parties in interest. The Confirmation Opinion showed that this legal strategy was not going to prevail in this Court.

18. Unfortunately, the Debtors do not seem to have fully learned their lesson. In proffering the Modified Plan, they seem to be employing the same flawed strategy again. For example:

(a) PIERS "Debt": The Confirmation Opinion raised the question as to whether the PIERS claims are debt or equity (Confirmation Opinion at p. 101). The Court said it was not persuaded by the evidence presented at the prior confirmation hearing on this point. The Equity Committee is taking discovery relating to the validity of the PIERS claims including the trading which may have taken place by the so-called Settlement Noteholders while the Global Settlement was being negotiated. The Modified Plan assumes that the Debtors are right on this point (that being, the PIERS claims are valid indebtedness) and will prevail on the issue. However, if the Debtors are wrong on this issue, the Modified Plan fails.

The Modified Disclosure Statement (at page 9) states that the holders of the Preferred Securities of the PIERS received an equity warrant for the Debtors' common stock and

that the value of the equity warrant was reflected in the original issue discount ("OID") related to the issuance of the PIERS. The Disclosure Statement also states that the PIERS claims increased in value since its issuance in 2001, for the seven year period through 2008, based on the reduction of the OID, and that the PIERS claim in these bankruptcy cases as of September 2008 (approximately $756 million in principal amount) reflects such reduced OID. That should mean that the PIERS claim includes a value for the equity warrant given to the PIERS in 2001, and the Debtors propose to pay the PIERS such value, plus post petition interest on such equity warrant value.[3] The impact of the equity warrant value in the PIERS "debt" claim is estimated to be between $16-$21 million dollars.

The Modified Disclosure Statement (at page 12) also states that the holder of the Common Securities of the PIERS is WMI, and there will be no distribution on this aspect of the PIERS claim, **except** to the extent such distribution is made to the Preferred Securities holders of the PIERS on account of a contractual subordination provision. Modified Plan, §20.1. The principal amount of the PIERS Common Securities is approximately $24 million, and with post petition interest, is approximately $30 million. To the extent that part of the distribution to the PIERS Preferred Securities includes an amount referable to the PIERS Common Securities distribution made by the Debtors to themselves, that would seem to be improper.

(b) <u>Rate of Post-Petition Interest</u>: In the Confirmation Opinion, the Court left open the issue as to whether post-petition interest should accrue at the contract rate for the benefit of unsecured creditors or whether the federal judgment rate should apply to all creditors. (Confirmation Opinion at p. 94). In the Confirmation Opinion, the Court raised the question as to whether certain "conflicts of interest" may impact which interest rate should apply. The

[3] The Modified Disclosure Statement states a contrary position at p.12. It states that no value is being distributed to PIERS Preferred Securities on account of the equity warrant given to them.

Equity Committee has taken some discovery on the "conflicts of interest" issue. The Court also raised the *additional* issue whether there were other "equitable reasons" why the lower federal judgment rate should be used but indicated the issue need not be decided since confirmation of the plan was being denied. The Modified Plan takes the position that the contract rate applies which unquestionably redounds to the detriment of the junior classes who are receiving nothing under the Modified Plan. Again, if the Debtors are wrong on the federal judgment rate issue, the Modified Plan simply fails because the Debtors have not accounted for the possibility they could be wrong on this issue. There clearly is ample law to suggest the Debtors are wrong on this issue. The Confirmation Opinion has an entire section referring to cases on both sides of the "post-petition interest" spectrum. The Confirmation Opinion suggests that there is no clear black and white answer, and the matter may lie in the discretion of the Court (Confirmation Opinion at pp. 90-93). In a situation where so many innocent junior constituencies are being wiped out under the Modified Plan as a result of the greatest financial crisis that this country has experienced since the Great Depression, a credible argument can certainly be made that the equities of the case warrant using the lower federal judgment rate.

One of the PIERS holders has stated in a Court pleading relating to the Modified Disclosure Statement that they bargained for a contract interest rate during negotiations relating to the Global Settlement and it is a large number which impacts their otherwise **sizeable** recovery. (Response of Aurelius Capital Management, LP, dated March 16, 2011 to Supplemental Disclosure Statement at paragraphs 7 and 9. "PIERS Statement") Seemingly lost in the PIERS argument is that it is indeed a large number as well to the lower classes (including long term, individual, good faith investors) who are otherwise getting **no** recovery if the higher contract interest rate is used.

Moreover, the PIERS Statement calls into question the bona fides of the Global Settlement. There was testimony at the Confirmation Hearing that the Settlement Noteholders (which include the PIERS holders) made settlement proposals directly to JP Morgan. The PIERS Statement strongly suggests that the Global Settlement amount was reached in order for the PIERS to get a threshold rate of return and, once that was done, there was no need to bargain for the true value that should be paid to the Debtors by JPMorgan, which would have redounded for the benefit of junior creditors, otherwise getting nothing under the Modified Plan. That is the only conclusion that can be drawn from the PIERS Statement since it concludes that if it did not get a post petition contract interest rate, it would have objected to the Global Settlement -- presumably because the amount to be paid by JP Morgan was too low.

The Claimants are aware that other objectors to the Modified Plan have fully briefed the post-petition interest rate issue and the Claimants reserve the right to weigh in on the argument at the Confirmation Hearing.

c. Priority of Post-Petition Interest Ahead of Subordinated Claims

The Modified Plan assumes that post petition interest gets paid to unsecured creditors ahead of subordinated debt claims (Class 18). The Modified Plan has no flexibility if the Debtors are wrong. This issue was raised in the Confirmation Opinion but not decided. Again, for no good reason (which raises Section 1129(a)(3) good faith concerns relating to the Modified Plan proponent) the Modified Plan does not provide flexibility on this issue in the event the Debtors are wrong. Claimants are aware that this issue has been fully briefed by other objectors to the Modified Plan. And, since the Debtors have kept open the possibility that the Claimants could be subordinated debt claims, the Claimants reserve the right to weigh in on this issue at the Confirmation Hearing.

E. The Debtors Have Not Maximized the Value of their Substantial Net Operating Loss

19. Aside from the concerns relating to the "inflexibility" of the Modified Plan which will hinder the ability of the Court to promptly confirm a "fair and equitable" plan, the Claimants have a concern regarding the new provision in the Modified Plan which withdraws the Registration Rights Offering. That action means that the Reorganized Debtors may not have any additional capital to better utilize their multi-billion net operating loss and thus, this "reorganization" is nothing more than the preservation of a relatively small, non-filed liquidating entity, with a self liquidating insurance portfolio, which may be sold at any time. In a circumstance where there are so many long term public investors getting nothing, that clearly is not the best alternative for this valuable asset (net operating loss).[4]

20. As noted, the Confirmation Opinion required all creditors to have a stock election for the Reorganized Debtors. This would have allowed such electing creditors to get the benefit of the value of the huge net operating loss. The Modified Plan addressed this concern by (a) as previously stated, creating artificial obstacles for the LTW holders in making the stock election, (b) removing the Registration Rights agreement which would have infused capital into the Reorganized Debtor in order to maximize usage of the net operating loss, and (c) creating a gaping hole as to how the Reorganized Debtors would get capital to maximize the net operating loss value. This important asset was never exploited and seems to have been skewed for the stealth benefit of the electing stock holders. These actions illustrate the lack of good faith relating to the Modified Plan proponent.

[4] It remains to be seen how the seventh amended plan will address the issue. The Debtors prior valuations have put a negligible value of its huge net operating loss. It will be interesting to see if the Debtors reverse position on this issue when it becomes convenient to make a contrary argument.

21. The lack of good faith is also illustrated by the Debtors failure --until it was compelled to-- to disclose the fees they wanted to pay to professionals of certain creditors without disclosure or Court approval. That amount of a minimum of $36 million is staggering and the effort to "hide the ball" illustrates the Debtors lack of good faith.

F. Late Filed Claims

22. The Liquidation Analysis (Exhibit D to the Modified Disclosure Statement) assumes that Late Filed Claims are paid, since the Analysis provides for post-petition interest being paid to unsecured creditors. As noted, the Confirmation Opinion states that late filed claims get paid ahead of post petition interest claims.

23. The Debtors have kept open the possibility that some of the Claimants have late filed claims. Therefore this issue remains relevant for the Claimants. It should be noted that the Claimants are not late filed since, among other things, (a) a class claim was timely filed by one of the LTW holders on behalf of all Claimants, and (b) LTW holders never got notice of the claims bar date. The chief restructuring officer of the Debtors testified at his deposition that the LTW holders should have gotten notice of the claims bar date if their identities were known to the Debtors. The names of the LTW holders were maintained by the so-called Warrant Agent and the Warrant Agent acts under the direction of the Debtors. Therefore, the names of the LTW holders were fully known to the Debtors.

24. The definition of Late Filed Claims under the Modified Plan does not include claims that are allowable based on the “excusable neglect” standard. Such claims are no different than a timely filed claim. Thus, the definition in the Modified Plan as to Late Filed Claims is wrong, and improperly discriminates against Late Filed Claims which are deemed timely filed under the "excusable neglect” standard.

CONCLUSION

The Adversary Proceeding is intended to decide whether LTW holders are in Class 12 (Unsecured Claims) or not. In a variety of ways, the Modified Plan seeks to undermine the rights of LTW holders before the Adversary Proceeding is decided. Based on the foregoing arguments, the Claimants urge the Court not to confirm the Modified Plan.

WHEREFORE, the Claimants request that the Court deny approval of the confirmation of the Modified Plan, and that they be granted such other and further relief as is just under the circumstances.

Dated: June 16, 2011
Wilmington, Delaware

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Debtors.	)	Jointly Administered
	)	
	)	

CERTIFICATE OF SERVICE

I, Scott J. Leonhardt, hereby certify that on or before the 16h day of June 2011, I served a copy of the foregoing, *Objection to Confirmation of the Modified Sixth Amended Plan of Affiliated Debtors by Class Representatives of Dime Litigation Tracking Warrants* upon the following parties in the manner listed below:

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