IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re: WASHINGTON MUTUAL, INC., *et al*.,[1] Debtors.	Chapter 11 Case No. 08-12229 (MFW) Jointly Administered **Re: Dkt. No. 6965** **Objection Deadline (extended by consent of Debtors): June 22, 2011 at 12:00 p.m. (ET)** **Hearing Date: July 13, 2011 at 9:30 a.m. (ET)**

OBJECTION OF AURELIUS CAPITAL MANAGEMENT, LP TO CONFIRMATION OF THE MODIFIED SIXTH AMENDED JOINT PLAN OF AFFILIATED DEBTORS PURSUANT TO CHAPTER 11 OF THE UNITED STATES BANKRUPTCY CODE

Aurelius Capital Management, LP ("Aurelius"), on behalf of certain of its respective managed entities that are creditors of the above-captioned debtors and debtors-in-possession (collectively, the "Debtors"), hereby submits this objection (the "Objection") to confirmation of the Modified Sixth Amended Joint Plan of Affiliated Debtors Pursuant to Chapter 11 of the United States Bankruptcy Code (the "Modified Sixth Amended Plan") (D.I. 6965) and to that certain Amended and Restated Settlement Agreement (the "Amended Global Settlement Agreement" attached as Exhibit H to the Modified Sixth Amended Plan) among the Debtors, JPMorgan Chase Bank, N.A. ("JPMC"), the Federal Deposit Insurance Corporation, both in its corporate capacity and capacity as receiver of Washington Mutual Bank (the "FDIC"), and the official committee of unsecured creditors appointed in these cases (the "Creditors' Committee," together with the Debtors, JPMC, and FDIC, the "Settlement Parties"). In support of this Objection, Aurelius respectfully states as follows:

[1] The Debtors are (i) Washington Mutual, Inc. and (ii) Washington Mutual Investment Corp.

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PRELIMINARY STATEMENT

1. The passage of time has rendered the Amended Global Settlement Agreement with JPMC materially and unacceptably worse for the Debtors, and impermissibly better for JPMC, than the settlement previously considered by the Court last December and January. The settlement previously considered by the Court was to go effective by January 31, 2011 – a date integral to the fairness of the settlement. In fact, the settlement agreement initially negotiated in March 2010 was expected to go effective by the end of July 2010 with a drop dead date of August 31, 2010. Now, however, the Amended Global Settlement Agreement will likely not go effective before the end of July 2011 – one year later – and possibly even later if the holders of the Debtors' out-of-the money equity interests have their way.

2. Every day deprives the Debtors of access to more than $4 billion in cash improperly held by JPMC, which has paid only $20 million (an average of 20 basis points per annum) in interest since the Petition Date through April 30, 2011. Absent the settlement, the Debtors would be entitled to collect prejudgment interest from JPMC in a far greater and ever-increasing amount. Based on the State of Washington's 12% (per annum) prejudgment interest rate, that equates to roughly *$1.36* billion in prejudgment interest from the Petition Date through July 2011.

3. The Debtors have been deprived of that value while incurring mounting costs from the ongoing bankruptcy cases, rendering the settlement materially less valuable for the Debtors today (and more valuable for JPMC) than it was when the Court blessed the deal as fair. Accordingly, at this time, the Amended Global Settlement Agreement should not be approved as fair unless JPMC provides additional value to the Debtors to compensate for the substantial delays.

4. The Modified Sixth Amended Plan cannot be confirmed for other reasons as well. For example, contrary to the Bankruptcy Code, the Modified Sixth Amended Plan provides for distributions to a new Class 12A for late-filed claims, to be paid after all prepetition claims but ahead of postpetition interest. The Debtors added this provision in response to a portion of the Court's January 7, 2011 opinion denying confirmation of the Debtors' previous plan, but Aurelius respectfully submits that the Court did not have the benefit of full briefing on the point. Subsequent research has brought to light Court of Appeals and other caselaw authorities establishing that late-filed claims have no right to any distributions under a chapter 11 plan.[2]

5. In addition, the Equity Committee's recent baseless and burdensome investigation into the trading activity of the Settlement Noteholders compels Aurelius to preserve its potential claims against the Debtors and the Debtors' officers and professionals relating to written post-petition confidentiality agreements that required the Debtors to publicly disclose all material non-public information provided to Aurelius under those agreements. To be clear, Aurelius believes that the Debtors *did* satisfy those obligations. However, the Equity Committee's contentions to the contrary compel Aurelius to object to the Modified Sixth Amended Plan to the extent it releases the Debtors or the Debtors' officers and professionals from any claims arising from the Debtors' confidentiality agreements and fails to reserve for the payment of administrative expenses arising from these claims.

[2] The last day to assert such claims is the commencement of the confirmation hearing, and Aurelius would be prepared to revisit the need for this aspect of the Objection if the claims asserted prove to be immaterial. The Debtors themselves estimate that allowed Late-Filed Claims will be $0. (*See* Footnote 5 to the Debtors' Updated Liquidation Analysis (the "Liquidation Analysis") filed on May 7, 2011 (D.I. 7430).)

BACKGROUND[3]

The Prior Settlement Agreements and Prior Plans

6. In the wake of the seizure and sale of the assets of WMI's wholly owned subsidiary, Washington Mutual Bank ("WMB"), a multitude of disputes arose among the Debtors, JPMC, and the FDIC, with each asserting billions of dollars in claims against one or more of the others. Central among those disputes were competing claims between the Debtors and JPMC to approximately $4 billion of the Debtors' funds that were on deposit in accounts (the "Disputed Deposit Accounts") at WMB and WMB's subsidiary Washington Mutual Bank fsb at the time of WMB's seizure.

7. JPMC has been improperly holding those funds since the commencement of these cases and, according to the Debtors' monthly operating reports, appears to be paying interest at an average nominal rate of 0.20% per annum (for a total of roughly $20 million) since the Petition Date through April 30, 2011.[4]

8. On April 27, 2009, the Debtors commenced an action against JPMC seeking the turnover of the $4 billion on deposit in the Disputed Deposit Accounts. On October 22, 2009, the Court heard oral argument on the Debtors' summary judgment motion. While that motion remains *sub judice* today, the Court was prepared to rule in February 2010. Indeed, Aurelius repeatedly stressed the importance of that ruling to the Debtors and urged them to request that the Court issue its ruling.

[3] As the Court is intimately familiar with the history of these Cases and the key terms of the Amended Global Settlement Agreement and previously proposed plans of reorganization, this section discusses only facts relevant to this Objection.

[4] By contrast, JPMC's average rate of return on interest-earning assets was 5.36% for 2008, 4.04% for 2009, 3.83% for 2010, and 3.74% for the first quarter of 2011, suggesting that JPMC could have earned more than $400 million on those deposits since the Petition Date through March 31, 2011. *See* JPMorgan Chase & Co., 2008 Form 10-K, at 222; 2009 Form 10-K, at 246, 2010 Form 10-K, at 306, Form 10-Q (May 6, 2011) at 173. If the Modified Sixth Amended Plan goes effective in July 2011, JPMC will have earned yet another four months of interest.

9. However, at a March 4, 2010 hearing, the Debtors specifically asked the Court not to rule on the summary judgment motion, indicating that there was some momentum among the Debtors, the FDIC and JPMC on a global settlement. At a continued hearing on March 12, 2010, the Debtors announced the material terms of the global settlement (subject to documentation and necessary approvals).

10. Thereafter, negotiations continued among the parties and certain holders of the Debtors' debt securities (the "Settlement Noteholders")[5] which resulted in an unsigned draft settlement agreement being filed with the Court on March 26, 2010 (D.I. 2622, Ex. I) and a signed settlement agreement (the "Initial Global Settlement Agreement") being filed with the Court on May 21, 2010, as Exhibit H to the Debtors' proposed second amended plan of reorganization (the "Second Amended Plan") (D.I. 4241). Among other things, the Initial Settlement Agreement provided that JPMC would waive any and all claims with respect to the Disputed Deposit Accounts (but not pay any additional amounts for prejudgment interest). It was expected that the Second Amended Plan would go effective by July 31, 2010. (*See* Second Amended Plan, Ex. A-1, n.2.) Moreover, the Initial Settlement Agreement terminated by its terms if a confirmation order was not entered by August 31, 2010. (*See* Initial Settlement Agreement § 7.3.)

11. However, on July 28, 2010, the Court appointed an examiner (the "Examiner") to investigate and to prepare a report with respect to the claims being compromised in the Initial Global Settlement Agreement. As a result, it became apparent that a confirmation order would not be entered prior to the Initial Settlement Agreement's August 31, 2010 termination date.

[5] The Settlement Noteholders consist of Aurelius, Appaloosa Management, L.P., Centerbridge Partners, L.P., and Owl Creek Asset Management, L.P.

12. Initially, Aurelius was opposed to extending its support for the settlement any further than August 31, 2010 but reluctantly acquiesced in an effort to be constructive and with the understanding and expectation that a confirmation order would be entered by year's end. Accordingly, the Settlement Parties and the Settlement Noteholders executed an amended settlement agreement (the "Global Settlement Agreement") which was incorporated into the Debtors' sixth amended plan of reorganization (the "Sixth Amended Plan"), filed on October 6, 2010 (D.I. 5548.) The Global Settlement Agreement gave its signatories the right to terminate on December 31, 2010, provided that the Debtors, JPMC and the Creditors' Committee could agree to extend the termination date to January 31, 2011. JPMC continued to enjoy the benefit of the funds on deposit in the Disputed Deposit Account without providing any additional compensation to the Debtors' estates for the costs of delay.

13. In support of confirmation of the Sixth Amended Plan and approval of the Global Settlement Agreement, the Debtors impressed upon the Court the benefits of the Global Settlement, including the "immediate" value that would be realized by the Debtors' estates:

> First, the Global Settlement Agreement represents *immediate*, known and certain value, estimated at approximately $6.1 to $6.8 billion, in large part because it secures for the Debtors' estates free and clear title to approximately $3.8 billion of Deposits and an additional $2.49 billion to $2.55 billion in funds that represent the Debtors' allocated share of the Tax Refunds. Thus, approximately $7.5 billion of total funds will be available for distribution to the Debtors' creditors and, potentially, certain equity interest holders, virtually all of which will *immediately* benefit the Debtors' stakeholders as it will largely be available on the Effective Date of the Plan.[6]

14. Likewise, the Debtors impressed upon the Court the costs of delay:

[6] (*See* Memorandum of Law in Support of Confirmation of the Sixth Amended Joint Plan of Affiliated Debtors Pursuant to the Chapter 11 of the United States Bankruptcy Code at 41 (D.I. 6085) (the "Debtors' Confirmation Brief") (emphasis added) (citing Declaration of William C. Kosturos in Support of Entry of an Order Confirming the Sixth Amended Joint Plan of Affiliated Debtors Pursuant to Chapter 11 of the United States Bankruptcy Code ¶ 45 (D.I. 6083) (the "Kosturos Decl.")).)

> Specifically, the Debtors estimate that final resolution of the Actions, through all appeals may last approximately 3 to 4 years, although others consider such a time frame to be optimistic. During such period, the Debtors will continue to accrue substantial litigation and administrative expenses and the Debtors' unsecured claims will continue to accrue postpetition interest, all at a rate of approximately $30 million per month (or $360 million per year), and which, in the aggregate will erode the value of any potential litigation recoveries.

(Debtors' Confirmation Brief at 42 (citing Kosturos Decl. ¶ 46) (emphasis added).)

15. The Court held a four-day evidentiary hearing on confirmation of the Sixth Amended Plan in December 2010, during which it heard evidence on the reasonableness of the Global Settlement. On January 7, 2011, the Court issued an opinion (the "Opinion") (D.I. 6528) holding that the Sixth Amended Plan could not be confirmed but nevertheless concluding that the Global Settlement provided a "reasonable return in light of the possible results of litigation." (Opinion at 60.) The Court identified certain modifications that, if made, would render the Sixth Amended Plan confirmable.

16. In particular, certain holders of WMI's litigation tracking warrants (the "LTW Holders"), which the Debtors had not classified as claims, litigated to have their instruments allowed as claims rather than equity and contended that postpetition interest should not be paid on general unsecured creditors' claims until late-filed claims were paid in full. (Opinion at 90.) The Court agreed with the LTW Holders and concluded that the Sixth Amended Plan should be modified accordingly. (*Id.*)[7]

[7] The Court based its holding on Section 726(a) of the Bankruptcy Code, which provides that, in a chapter 7 case, late-filed claims are paid ahead of postpetition interest on general unsecured claims. (Opinion at 90 (citing 11 U.S.C. § 726(a)(3) and (5)).) However, other parties had opposed the LTW Holders not on the ground that they held late-filed claims but on the ground that they did not hold claims at all, and that issue was resolved by an agreement to classify LTW Holders with other general unsecured creditors if their claims were allowed and not subordinated. The parties never briefed the issue as to whether late-filed claims had the right to receive distributions under the Sixth Amended Plan.

17. In addition, the Court noted in its Opinion that certain creditors had objected to the Sixth Amended Plan on the grounds that postpetition interest should be paid at the federal judgment rate, rather than the applicable contract rate (if any), as the Sixth Amended Plan required. (Opinion at 90.) The Court noted that postpetition interest should be paid at the applicable contract rate unless the equities require otherwise. (*Id*. at 94.) The Court also noted that while there were allegations that the Settlement Noteholders used material non-public information to trade in claims, such allegations were not supported by any admissible evidence that would justify awarding postpetition interest at the lower federal judgment rate. (*Id*.)[8] Nevertheless, the Court concluded that it need not reach the issue because the Sixth Amended Plan as drafted could not otherwise be confirmed. (*Id*.)

The Amended Global Settlement Agreement and Modified Sixth Amended Plan

18. Because the Sixth Amended Plan was not confirmed, the Global Settlement Agreement became terminable on January 31, 2011. The Debtors exercised their rights to terminate and subsequently executed the Amended Global Settlement Agreement. Given the passage of time and the resulting detrimental effect on the Debtors' estates, Aurelius determined that it would not agree to an extension of the Global Settlement Agreement. Accordingly, Aurelius is not a party to the Amended Global Settlement Agreement.

19. On March 16, 2011, the Debtors filed the Modified Sixth Amended Plan along with a revised supplemental disclosure statement (the "Supplemental Disclosure Statement") (D.I. 6966). The Modified Sixth Amended Plan is premised on the Amended Global Settlement Agreement, which, except for modifications to certain release provisions as required by the Court's Opinion, retains the same economic terms as the Global Settlement Agreement.

[8] The lack of admissible evidence reflected that the underlying allegations were merely vague, unsubstantiated, and uninformed musings of a pro se security holder, Mr. Nate Thoma.

(Supplemental Disclosure Statement at 3-4.) Notably, no additional value is being provided by JPMC to the Debtors to compensate them for the additional delay and lost value. Yet, JPMC continues to realize the benefit of the funds on deposit in the Disputed Deposit Account earning a significant spread over the nominal interest that JPMC is currently paying.

20. The Amended Global Settlement Agreement further provides that it can be terminated if the Modified Sixth Amended Plan does not go into effect prior to April 30, 2011, and that WMI, JPMC, and the Creditors' Committee can agree to extend the effective date to May 15, 2011 (Amended Global Settlement Agreement § 7.3) – a date that the Settlement Parties have presumably agreed to extend further.

21. In response to the Court's Opinion, the Modified Sixth Amended Plan now provides for a new class 12A consisting of holders of late-filed claims ("Late-Filed Claims"). (Modified Sixth Amended Plan § 16.2.) Late-Filed Claims include claims filed after the applicable bar date but prior to the commencement of the hearing on confirmation of the Modified Sixth Amended Plan (the "Confirmation Hearing"). (*Id.* § 1.123.) As set forth in Section 16.2 of the Modified Sixth Amended Plan and the Waterfall Recovery Matrix attached as Exhibit G thereto, holders of Late-Filed Claims would be paid after all prepetition claims are paid in full, but prior to the payment of postpetition interest on account of prepetition claims.

The Equity Committee Investigation

22. For the last several months, the Official Committee of Equity Security Holders (the "Equity Committee"), jumping off from Mr. Thoma's unsubstantiated speculations, has been conducting an investigation into trading in the Debtors' securities by the Settlement Noteholders during the pendency of these Cases. The Equity Committee has taken extensive

discovery that has burdened the Debtors' estates with substantial administrative expense and the Settlement Noteholders with massive legal bills.

23. As this discovery has amply demonstrated, Aurelius received material non-public information from the Debtors only in limited circumstances while taking appropriate precautions to avoid any improper trading. Indeed, prior to the initial announcement of the global settlement in March 2010, Aurelius's participation in confidential negotiations and receipt of material non-public information was confined to two discrete time periods, both governed by written post-petition confidentiality agreements (the "Confidentiality Agreements") that set forth the respective obligations of Aurelius (and other negotiating creditors) and the Debtors.[9]

24. Notably, both Confidentiality Agreements required the Debtors, at the termination of the agreements, to make public disclosure (within the meaning of Rule 101 of Regulation FD) of a fair summary of any confidential information provided by the Debtors to Aurelius thereunder that constituted material non-public information under U.S. securities laws.

25. During one of those periods, Aurelius erected an elaborate ethical wall, as permitted by the governing Confidentiality Agreement, between the employee receiving the potentially material non-public information and all other employees trading in the Debtors' securities. There have been no allegations that Aurelius breached that ethical wall. During the other confidentiality period, Aurelius suspended all trading in the Debtors' securities and there have been no allegations to the contrary.

26. At the conclusion of both periods, the Debtors filed monthly operating reports disclosing all material non-public information that had been provided to Aurelius under the Confidentiality Agreements. Upon termination of the Confidentiality Agreements and in

[9] After the announcement of the initial settlement, Aurelius was occasionally provided with certain drafts of the settlement agreement and related plan documents. During those times, Aurelius restricted itself from trading until any material non-public information contained therein was publicly disclosed.

light of the Debtors' disclosures, Aurelius determined that it had satisfied its obligations and was free to resume unrestricted trading in the Debtors' securities.

27. Having uncovered no evidence of wrongdoing, the Equity Committee apparently will resort to arguing that Aurelius was disabled from trading based on its exposure to certain limited (and wholly unsuccessful) settlement negotiations during 2009 – information that the Debtors and their securities counsel determined at the time was not material. Indeed, the practice of engaging in settlement negotiations and resuming trading if those negotiations are unsuccessful has been applicable in countless cases for decades.

28. While Aurelius believes that the Debtors complied with their disclosure obligations under the Confidentiality Agreements, the Equity Committee's contentions to the contrary compel Aurelius to object to the Modified Sixth Amended Plan to the extent it releases the Debtors or the Debtors' officers and professionals from claims arising from any breach of the Debtors' obligations under those agreements and fails to reserve cash for the payment of administrative expenses arising from such claims. In addition, there are several other parties who have also entered into written post-petition confidentiality agreements with the Debtors. The reserve may also need to cover potential claims of such other parties to whom the Debtors undertook obligations to disclose confidential information.

OBJECTION

29. For the reasons set forth below, the Modified Sixth Amended Plan cannot be confirmed unless (i) the Amended Global Settlement Agreement is further amended to require JPMC to compensate the Debtors' estates for the delay in consummating the settlement, (ii) the treatment afforded Class 12A Late-Filed Claims is removed from the Modified Sixth Amended Plan, and (iii) the Modified Sixth Amended Plan preserves and appropriately reserves cash for

any and all administrative and other claims held by Aurelius against the Debtors and the Debtors' officers and professionals arising out of, or otherwise related to, the Confidentiality Agreements.

I. The Amended Global Settlement Agreement Should Not Be Approved

30. While the approval of a settlement under Rule 9019 of the Bankruptcy Rules is committed to the discretion of the bankruptcy court, the court must nevertheless conclude that "the compromise is fair, reasonable, and in the best interests of the estate." *In re Louise's Inc*, 211 B.R. 798, 801 (D. Del. 1997). The burden is on the Debtors to persuade the Court that a settlement is reasonable. *Key3Media Group, Inc. v. Pulver.com Inc. (In re Key3Media Group Inc.)*, 336 B.R. 87, 93 (Bankr. Del. 2005) ("While a court generally gives deference to a Debtors' business judgment in deciding whether to settle a matter, the Debtors have the burden of persuading the bankruptcy court that the compromise is fair and equitable and should be approved."). Moreover, "each part of the settlement must be evaluated to determine whether the settlement as a whole is reasonable." (Opinion at 20.)

31. While the Court previously concluded that the Global Settlement Agreement was reasonable and could be approved under the standards of Bankruptcy Rule 9019, the Court must reconsider that ruling in light of the significant delays affecting these Cases. The settlement agreement as originally negotiated in March 2010 was expected to be implemented by July 2010 with a drop dead date of August 31, 2010. Aurelius's reluctant consent to an extension was provided with the expectation and understanding that a confirmation order would be entered by year's end and no later than January 31, 2011. But that has not occurred. In fact, it appears that the earliest the Modified Sixth Amended Plan will even be presented to the Court for confirmation is July 13, 2011 and not likely to go effective until at least the end of July 2011

at best – one year after the settlement was intended to be implemented – and potentially longer if the holders of the Debtors' equity interests continue to engender delay. (*See* Notice of Confirmation Hearing (D.I. 7921).) That delay has had detrimental consequences to the Debtors' estates and concomitant benefits to JPMC.

32. *First and foremost*, as the Court noted in its Opinion, there is a "strong likelihood of success" on the merits of the Debtors' claims to the roughly $4 billion in the Disputed Deposited Accounts. (Opinion at 26.) As a result, not only would the Debtors be entitled to the return of those funds, but they would also be entitled to recover prejudgment interest from JPMC. *See, e.g., Black Diamond Mining Co. v. Hazard Coal Sales, LLC (In re Black Diamond Mining Co.),* Adv. Pro. No. 08-7005, 2009 Bankr. LEXIS 4639, at *22 (Bankr. E.D. Ky. June 11, 2009) (awarding of prejudgment interest at applicable state rate in turnover action); *Grauman v. Smith (In re U.S. Physicians, Inc.),* Adv. Pro. No. 00-138, 2001 U.S. Dist. LEXIS 9707, at *22 (E.D. Pa. July 12, 2001) (same).

33. However, the Amended Global Settlement Agreement releases JPMC from any claims for prejudgment interest, which, outside of any settlement, would continue to accrue until a judgment is entered against JPMC. Under Washington State law (the law of the State in which WMI is incorporated and has its principal place of business), judgments for liquidated amounts owed by a defendant accrue prejudgment interest at 12% per annum. Rev. Code. Wash. § 19.52.010; *see also Smith v. Olympic Bank*, 693 P.2d 92, 96 (Wash. 1985) (awarding prejudgment interest at 12% per annum where bank failed to turn over a liquidated amount); *Unigard Sec. Ins. Co. v. Kansa Gen. Ins. Co.*, Case No. 90-1693, 1992 U.S. Dist. LEXIS 20677, at *26 (W.D. Wash. Nov. 9, 1992) (awarding prejudgment interest at 12% per

annum where amount owed was liquidated); *Jenner v. De Los Santos Constr., Inc.*, Case No. 07-0550, 2008 U.S. Dist. LEXIS 90080, at * 3 (W.D. Wash. Aug. 27, 2008) (same).

34. Accordingly, assuming that Washington State law applies, JPMC's prejudgment interest liability has accrued at approximately $40 million per month. That equates to roughly *$1.36 billion* since the Petition Date through July 30, 2011. Those are amounts to which the Debtors would be entitled were the Court to grant judgment in favor of the Debtors – a prospect that the Court already considered to be a "strong likelihood." (Opinion at 26.) Yet the Debtors' claims to those amounts are completely released under the Amended Global Settlement Agreement. Meanwhile, JPMC has continued to enjoy the benefit of, and has earned an interest spread on, the $4 billion while paying only $20 million in interest during the period between the Petition Date and April 30, 2011. (*See supra* ¶ 7 and n.4.)

35. *Second*, as the Court is aware, each month of delay in these cases results in the Debtors' incurrence of what has recently been estimated as $40 million in professional fees and postpetition interest expense. (*See also* Opinion at 58.) This has a material adverse effect in particular on the holders of PIERS claims, whose projected recovery has already been reduced through delay from approximately 100%, as projected in the disclosure statement filed in May 2010 (D.I. 4242 at 25), to only 32% under the current timetable. (*See* Liquidation Analysis.)

36. In sum, the "immediate" cash benefits of the global settlement trumpeted by the Debtors in December 2010 no longer exist. Following the Court's consideration of the global settlement on the facts in evidence as of January 2011, the Debtors will have incurred an estimated $280 million of additional postpetition interest and administrative expenses.

37. As a result, the Amended Global Settlement Agreement is no longer fair and equitable to the Debtors' estates and will continue to get worse as the Debtors' out-of-the

money equity holders continue to cause delay. Unless JPMC provides additional consideration to the Debtors' estates to compensate for the delay in implementing the settlement and the concomitant loss in value, the Amended Global Settlement Agreement must not be approved and the Modified Sixth Amended Plan cannot be confirmed.

II. Late-Filed Claims Are Not Entitled to Distributions

38. The Modified Sixth Amended Plan provides for the establishment of a Class 12A consisting of Late-Filed Claims that would be paid after all prepetition claims are paid in full, but prior to the payment of postpetition interest on account of general unsecured claims. As we demonstrate below, that classification and treatment of Late-Filed Claims violates applicable bankruptcy law.

39. Bankruptcy Rule 3003(c) governs the filing of proofs of claim in a chapter 11 case. That rule provides that the bankruptcy court "shall fix and for cause shown may extend the time within which proofs of claim . . . may be filed." Fed. R. Bankr. P. 3003(c)(3). The rule further provides that any creditor that fails to timely file a proof of claim "*shall not be treated as a creditor with respect to such claim for the purposes of voting and distribution*." Fed. R. Bankr. P. 3003(c)(2) (emphasis added). The Rule allows no exceptions.

40. Bankruptcy Rule 9006(b) governs the enlargement of time in which a creditor may file a proof of claim. That rule provides that, where an extension of time to file a claim is sought after the bar date has passed, the court may enlarge the time to file that claim only "where the failure to act was the result of excusable neglect." Fed. R. Bankr. P. 9006(b).

41. Where a creditor in a chapter 11 case fails to establish excusable neglect, the consequence under Bankruptcy Rule 3003(c)(2) is that the claim is disallowed – it is not simply subordinated:

> If a scheduled creditor does not file a timely proof of claim when it is required to do so, that creditor is in the worst of all worlds: it cannot participate in plan voting, will receive no distributions under the plan, and will have its claim discharged, should the debtor receive a discharge. *Unlike in a Chapter 7 case, a creditor that fails to file a required proof of claim in a Chapter 11 case does not even get a subordinated claim against the debtor. Instead, in effect the late claim simply no longer exists for purposes of the Chapter 11 case.*

In re Dartmoor Homes, Inc., 175 B.R. 659, 664 (Bankr. N.D. Ill. 1994) (emphasis added, internal citations omitted); *see also Burgio v. Protected Vehicles, Inc. (In re Protected Vehicles, Inc.)*, 397 B.R. 339, 346 (Bankr. D.S.C. 2008) (non-scheduled claims for which proofs of claim not filed are not allowable under Rule 3003(c)(2) for purposes of voting or distribution).

42. In fact, the bar date order (the "Bar Date Order") (D.I. 632) entered by the Court in these Cases confirms this result:

> ORDERED that any holder of a claim against the Debtors who receives notice of the Bar Date (whether such notice was actually or constructively received) and is required, but fails, to file a Proof of Claim in accordance with this Order on or before the Bar Date, *shall not be permitted to vote to accept or reject any chapter 11 plan filed in these chapter 11 cases, or participate in any distribution in Debtors' chapter 11 cases on account of such claim* or to receive further notices regarding such claim . . .

(Bar Date Order at 7-8.)

43. Nevertheless, the Court held in its Opinion that the priorities set forth in Section 726 of the Bankruptcy Code mandate that late-filed claims be paid after timely filed claims are paid in full but before postpetition interest is paid. (Opinion at 90.) Aurelius respectfully submits that the Court should revisit this issue because it was not provided with the relevant legal authorities establishing that Section 726 does not overrule the clear language of Bankruptcy Rule 3003.

44. The Bankruptcy Code is clear on its face that the priority scheme set forth in Section 726 does not apply in chapter 11. Section 103(b) of the Bankruptcy Code expressly

provides that subchapters I and II of chapter 7 (which includes Section 726) apply only in chapter 7. 11 U.S.C. § 103(b).

45. The Eleventh Circuit addressed this precise issue in *In re Banco Latino Int'l*, 404 F.3d 1295 (11th Cir. 2005) ("*Banco Latino III*"). There, the debtor had already confirmed a liquidating chapter 11 plan, paid all timely filed claims in full (with post-petition interest), and begun making distributions to equity when certain of the debtor's former directors and officers filed motions seeking allowance and payment of indemnification claims. *In re Banco Latino Int'l*, Case No. 94-10202, 2003 Bankr. LEXIS 2139, at *9-10 (Bankr. S.D. Fla. Jan. 23, 2003) ("*Banco Latino I*"). The former directors and officers argued that such claims should be paid out of reserves set aside for disputed claims. *Id.*

46. While the bankruptcy court concluded that these indemnification claims could not be deemed timely filed, it nevertheless held that they should be allowed under Section 726 of the Bankruptcy Code. *Banco Latino I*, 2003 Bankr. LEXIS 2139, at *21-22. The bankruptcy court reasoned that, while not directly applicable in chapter 11 cases, the equitable principles underlying Section 726 are subsumed within Section 1129 of the Bankruptcy Code – in particular, the best interests of creditors test and the absolute priority rule. *Id.* at *22-29. As a result, the bankruptcy court modified the plan to permit the late-filed claims to be paid out of the post-confirmation reserves before any further distributions would be made.

47. On appeal, however, the district and circuit court of appeals reexamined the bankruptcy court's application of Section 726 in the chapter 11 context and concluded that it had been erroneous. The district court held that *Pioneer Inv. Servs. Co. v. Brunswick Assocs. Ltd. P'ship*, 507 U.S. 380 (1993), permits a late proof of claim to be allowed in a chapter 11 case *only* after a showing of excusable neglect. *Banco Latino Int'l v. Gomez-Lopez (In re Banco*

Latino Int'l), 310 B.R. 780, 784-85 (S.D. Fla. 2004) ("*Banco Latino II*"). Because the bankruptcy court concluded that the failure to file a timely proof of claim could not be justified by excusable neglect, the district court held that the late claims could not be allowed. *Id*. The district court expressly rejected the bankruptcy court's reliance on the priorities set forth in Section 726, confirming that "11 U.S.C. § 726 is inapplicable to Chapter 11 proceedings" and noting that the lower court's purported policy analysis "disregarded the policies supporting the excusable neglect standard of Fed. R. Bankr. P. 9006(b)(1) before deviating from the bar date." *Id*. at 785-86 (internal citations omitted).

48. The Eleventh Circuit affirmed the district court, holding and reconfirming that *Pioneer* governs the allowance of late filed claims in a chapter 11 case:

> If Appellants, like anyone else, wish to file claims after the claims bar date in a Chapter 11 bankruptcy, then they must demonstrate that their failure to file timely claims was the result of excusable neglect. As Appellants have not even attempted to argue excusable neglect to this Court, we agree with the district court that the "late filing of the claims should not have been allowed."

Banco Latino III, 404 F.3d at 1296 (citation omitted).

49. *In re Xpedior Inc.*, 354 B.R. 210 (Bankr. N.D. Ill. 2006), further underscores this result. At issue there was the manner in which a chapter 11 liquidating trustee could dispose of surplus funds. *Id*. at 219. Because all creditors had been paid in full plus postpetition interest and all equity interests had been canceled, the trustee petitioned the court for authorization to donate surplus funds to charity. *Id.*

50. Before authorizing the trustee to do so, the bankruptcy court considered whether any other constituents in the case should be entitled to those surplus funds. In particular, the bankruptcy court considered whether creditors who previously had their claims disallowed as

untimely should be entitled to a distribution out of the surplus funds. *Xpedior*, 354 B.R. at 225-26. The court easily rejected this notion:

> Because Section 103(b) of the Bankruptcy Code states that "[s]ubchapters I and II of chapter 7 of this title apply only in a case under such chapter" and Section 726 is included within subchapter II of Chapter 7, Section 726 should only be applied to cases under Chapter 7. *Thus, late-claims heretofore barred should not be entitled to a "subordinated priority" or receive any distribution from the Debtors' Chapter 11 estate pursuant to Section 726.*

Id. at 225 (emphasis added). Accordingly, the court concluded that it was more appropriate to distribute surplus funds to charity than to late-filing creditors. *Id.* at 240. *See also In re Dartmoor Homes, Inc.*, 175 B.R. 659, 664 (Bankr. N.D. Ill. 1994) ("Unlike in a Chapter 7 case, a creditor that fails to file a required proof of claim in a Chapter 11 case does not even get a subordinated claim against the debtor.").

51. Structural differences in the treatment of claims filing between chapter 7 and chapter 11 support the logic of providing special back-up treatment for holders of late-filed claims in a chapter 7 case that is not available in a chapter 11 case. For example, claims filing in chapter 7 cases is governed by Bankruptcy Rule 3002, which generally provides less time to file a proof of claim than in chapter 11 cases. Bankruptcy Rule 3002(c) provides, in relevant part, that general unsecured claims in a chapter 7 case must be filed within 90 days of the first date set for the section 341 meeting of creditors. By contrast, Bankruptcy Rule 3003(c)(3) (which governs claims filing in chapter 11 cases) provides that *the Court* shall fix the time in which proofs of claim must be filed. It is not uncommon in large chapter 11 cases for the bar date to be set much further out than 90 days after the initial Section 341 meeting of creditors.

52. In addition, the permissible reasons for extending the bar date in chapter 7 are more circumscribed than those in chapter 11. In chapter 7, a bar date can be extended only (i) for governmental authorities if a motion is made prior to the expiration of the governmental

bar date, (ii) for an infant or incompetent person if such extension will not unduly delay the administration of the case, or (iii) for certain foreign creditors who received insufficient notice. *See* Bankruptcy Rule 3002(c)(1), (2) and (6). By contrast, as discussed above, a court has discretion to extend the bar date for *any* chapter 11 creditor upon a showing of excusable neglect. *Pioneer*, 507 U.S. at 389 ("The 'excusable neglect' standard of Rule 9006(b)(1) governs late filings of proofs of claim in Chapter 11 cases but not in Chapter 7 cases.") The more rigid rules of chapter 7 justify the safety valve of residual subordinated treatment for late claims.

53. Most importantly, Bankruptcy Rule 3003(c)(3) explicitly sets forth the consequences to a creditor who files a late proof of claim in a chapter 11 case without demonstrating excusable neglect: such a creditor "shall not be treated as a creditor with respect to such claim for the purposes of voting and distribution." Bankruptcy Rule 3002, however, provides no similar express disallowance. Rather, Section 726 provides the late-filing chapter 7 creditor (but not the late-filing chapter 11 creditor) with a subordinated claim.

54. Accordingly, there is no basis for concluding that the priorities of Section 726 of the Bankruptcy Code, as they relate to late-filed claims, have any application to late-filed claims in a chapter 11 case. While Section 726 serves as a benchmark for determining whether a plan complies with the "best interests" test of Section 1129(a)(7), holders of late-filed claims are simply not entitled to distributions under a chapter 11 plan and therefore have no standing to assert an 1129(a)(7) objection.

55. In sum, Section 16.2 of the Modified Sixth Amended Plan does not comply with all the provisions of title 11, as required by Section 1129(a)(1) of the Bankruptcy Code, because it provides for a distribution to a class of creditors that is not entitled to distributions in chapter 11 – those who did not file claims prior to the bar date and cannot

demonstrate that their failure to timely file was the result of excusable neglect. The precise impact, if any, that this provision could have on creditor recoveries cannot currently be ascertained, as potential Class 12A creditors have until July 13, 2011 to file late claims. That impact, however, could be material and could affect creditor recoveries. Accordingly, the Modified Sixth Amended Plan cannot be confirmed unless Section 16.2 of the Modified Sixth Amended Plan and any related provisions are stricken from it.[10]

III. Preservation and Reservation of Post-Petition Claims

56. Aurelius may hold significant administrative expense and other claims against the Debtors and the Debtors' officers and professionals relating to the Confidentiality Agreements. Under the circumstances, these claims must be preserved and reserved for under the Modified Sixth Amended Plan.

57. As discussed in detail above, during the course of settlement and plan negotiations, the Debtors provided information to Aurelius pursuant to Confidentiality Agreements covering certain confidentiality periods that required the Debtors, at the conclusion of those periods, to publicly disclose any and all material non-public information provided by the Debtors thereunder.

58. During those periods, Aurelius either restricted itself from trading in the Debtors' securities or erected an ethical wall between the employee given access to information from the Debtors and employees trading in the Debtors' securities. At the conclusion of those periods all potentially material, non-public information provided by the Debtors to Aurelius during those periods was publicly disclosed by the Debtors through the filing of monthly

[10] Because such a modification would not materially and adversely affect any creditor entitled to a distribution under, or entitled to vote on, the Modified Sixth Amended Plan, no re-solicitation of votes is required to make this modification. *See In re Aleris Int'l, Inc.*, Case No. 09-10478, 2010 Bankr. LEXIS 2997, at *97 (Bankr. D. Del. May 3, 2010) ("Further disclosure and resolicitation of votes on a modified plan is only required, however, when the modification materially *and* adversely affects parties who previously voted for the plan.").

operating reports. Following those disclosures, Aurelius resumed unrestricted trading in the Debtors' securities.

59. While Aurelius believes that the Debtors *did* in fact comply with their disclosure obligations and therefore no claims should arise, the Equity Committee has contended to the contrary. If the Equity Committee were correct, the Debtors would have breached their post-petition obligations to Aurelius under the Confidentiality Agreements to publicly disclose all material non-public information provided to Aurelius thereunder. In that circumstance, Aurelius would hold (and would assert) administrative expense claims against the Debtors. *See* Collier on Bankruptcy ¶ 503.06[6][a] (Alan N. Resnick & Henry J. Sommer eds., 16th ed.) ("If the trustee enters into a contract or lease after entry of the order for relief and subsequently breaches the contract or lease, the other party will have a claim for damages. The amount of those damages will be determined under the contract or lease, and the full amount of the damages arising from the trustee's breach will constitute an administrative expense."). In order to comply with Section 1129(a)(9)(A) of the Bankruptcy Code, the Modified Sixth Amended Plan must not release and must reserve for Aurelius's administrative claims against the Debtors in cash.

60. Moreover, the Modified Sixth Amended Plan must be further amended to provide that the exculpation provisions in Section 43.8 of the Modified Sixth Amended Plan shall not affect the liability of the Debtors and the Debtors' officers and professionals with respect to any claims of Aurelius arising out of, or otherwise relating to, the Confidentiality Agreements and any disclosures related thereto. Indeed, the Court has already required in its Opinion that those exculpation provisions be amended to exclude claims that the LTW Holders

may hold against the Debtors' board of directors. (Opinion at 74.) Aurelius's claims against the Debtors and the Debtors' officers and professionals must similarly be preserved.

CONCLUSION

For the reasons stated above, Aurelius respectfully requests that the Court (i) deny confirmation of the Modified Sixth Amended Plan and (ii) grant such other and further relief as it deems just and proper.

Dated: June 22, 2011

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CERTIFICATE OF SERVICE

I, Victoria Guilfoyle, hereby certify that on June 22, 2011, I caused a copy of the following document to be served upon the parties listed on the attached service list in the manner indicated.

OBJECTION OF AURELIUS CAPITAL MANAGEMENT, LP TO CONFIRMATION OF THE MODIFIED SIXTH AMENDED JOINT PLAN OF AFFILIATED DEBTORS PURSUANT TO CHAPTER 11 OF THE UNITED STATES BANKRUPTCY CODE

Dated: June 22, 2011

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