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IN RE THQ INC.
“GAME OVER”

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Introduction

Videogames have come a long way since PONG for Atari was introduced in 1972.¹ The industry has advanced from simplistic 8-bit geometric shapes descending from players' screens (*Tetris*)² and a side-scrolling, overall-clad plumber saving a princess in a faraway land (*Super Mario Bros.*).³ Today, the global videogame industry is a \$67 billion enterprise, consisting of hardware (gaming consoles like Nintendo and Playstation), software (the actual videogames themselves), and secondary markets (online games, mobile phones, and other devices).⁴ The major players in this enterprise are few—the “AAA” game developers.⁵ In the videogame industry, an AAA game is analogous to a Hollywood Blockbuster: big budgets, big special effects, and big profits.⁶

For videogame developers, AAA game development is a risky undertaking; according to one industry case study, “developing a AAA game is rapidly becoming one of the most expensive enterprises humans can undertake, outside of building battleships, launching space vehicles, or making movies.”⁷ The typical cash flow cycle for a AAA game is defined by a heavy front-end period of negative cash flow, wherein resources are spent and debts are incurred, and a back-end period of positive cash flow, wherein revenues are collected.⁸

AAA game developers invest millions of dollars over long periods of time to design and build games for the various hardware platforms, requiring large budgets and teams to

¹ Mary Bellis, *Computer and Video Game History*, ABOUT, http://inventors.about.com/library/inventors/blcomputer_videogames.htm (last visited April 8, 2013).

² TETRIS, <http://www.tetris.com/> (last visited April 8, 2013).

³ MARIO, <http://mario.nintendo.com/> (last visited April 8, 2013).

⁴ John Gaudiosi, *New Reports Forecast Global Video Game Industry Will Reach \$82 Billion By 2017*, FORBES (Jul. 18, 2012, 11:35 AM), <http://www.forbes.com/sites/johngaudiosi/2012/07/18/new-reportsforecasts-global-video-game-industry-will-reach-82-billion-by-2017/> (last visited April 8, 2013).

⁵ Polygon Staff, *The State of Games: State of AAA*, POLYGON (Jul. 2, 2012, 5:03 PM), <http://www.polygon.com/2012/10/1/3439738/the-state-of-games-state-of-aaa> (last visited April 8, 2013).

⁶ Juuso, *What Are AAA Titles?*, GAME PRODUCER BLOG (May 26, 2006), <http://www.gameproducer.net/2006/05/26/what-are-aaa-titles/> (last visited April 8, 2013).

⁷ Polygon Staff, *The State of Games: State of AAA*, POLYGON (Jul. 2, 2012, 5:03 PM), <http://www.polygon.com/2012/10/1/3439738/the-state-of-games-state-of-aaa> (last visited April 8, 2013).

⁸ Declaration of Brian Farrell Paragraph 37.

successfully complete the task.⁹ After months, and possibly years, these developers hope (and, in fact, require) that their hard work results in big sales—otherwise, they may find themselves in a situation like that of former powerhouse, THQ Inc. (THQ), once a premiere developer of videogames for the global market.¹⁰

⁹ Declaration of Brian Farrell Paragraph 37.

¹⁰ Marc Graser, *Vidgame publishers see profit despite slump*, VARIETY (May 15, 2012, 5:48 PM), <http://variety.com/2012/digital/news/vidgame-publishers-see-profit-gains-despite-slump-1118054077/> (last visited April 8, 2013).

The Structure and Operations of THQ

THQ,¹¹ founded in 1989, was a conglomerate in the videogame industry.¹² It operated in tandem with a network of domestic subsidiaries and foreign affiliates, as well as other important players in the industry, to develop, market, and distribute AAA games. Since its inception,¹³ THQ had been relatively successful in producing many popular titles, generating large revenues, and functioning internationally; however, over the last few years it saw its financial condition deteriorate.

Organizational Structure

Domestic Subsidiaries and Foreign Affiliates

THQ employed a complex organizational structure to facilitate its business operations and international dealings.¹⁴ Domestically, it was the parent of four subsidiary corporations: Volition, Inc. (Volition),¹⁵ THQ Digital Studios Phoenix, Inc. (THQ Phoenix),¹⁶ THQ Wireless, Inc. (THQ Wireless),¹⁷ and THQ Vigil Games, Inc. (Vigil);¹⁸ all of which THQ wholly owned.¹⁹

¹¹ Voluntary Petition - Page 1 (Principal Place of Business: 29903 Agoura Road, Agoura Hills, California 91301, Los Angeles County).

¹² Voluntary Petition - Annex 1 (Aliases: Heavy Iron Studios; Helixe; Sandblast Games, fka Cranky Pants Games; ValuSoft; Concrete Games; Kaos Studios; Incinerator Studios; ValuSoftArcade.com, fka SlingDot; Paradigm Entertainment; Elephant Entertainment; THQ San Diego).

¹³ THQ was a Delaware corporation formed in 1997. (THQ - Delaware Division of Corporations - Entity Details; Voluntary Petition - Page 1 and Voluntary Petition - Exhibit 1). Prior to January 6th 1998, THQ was a wholly owned subsidiary of a predecessor corporation named T-HQ, Inc. (T-HQI) a.k.a. T.HQ, Inc. (T-HQ, Inc. FORM POS AM POS 01/09/1998 – Page 3). T-HQI created THQ for the purpose of changing its state of incorporation from New York to Delaware. (T-HQ, Inc. FORM 8-K 01/09/1998 – Page 2). T-HQI solicited proxies from its shareholders and a merger was approved on its July 22nd 1997 Annual Meeting. (T-HQ, Inc. FORM POS AM POS 01/09/1998 – Page 3). On January 6, 1998, pursuant to the terms of an Agreement and Plan of Merger, T-HQI merged into THQ; THQ became the successor of T-HQI, thereby, acquiring all of the assets and assuming all of the debts, liabilities and duties of T-HQI. (T-HQ, Inc. FORM POS AM POS 01/09/1998 – Page 3).

¹⁴ See *infra* Exhibit A for THQ's Organizational Chart.

¹⁵ Declaration of Brian Farrell Paragraph 5 (Incorporated under the laws of Delaware; Operations are being Terminated during December of 2012).

¹⁶ Declaration of Brian Farrell Paragraph 5 (Incorporated under the laws of Arizona).

¹⁷ Declaration of Brian Farrell Paragraph 5 (Incorporated under the laws of Delaware; no current operations).

¹⁸ Declaration of Brian Farrell Paragraph 5 (Incorporated under the laws of Texas).

Internationally, THQ owned three foreign affiliates: Relic Entertainment (Relic),²⁰ THQ Montreal Inc. (THQ Montreal), and THQ International GmbH (TGH).²¹

Through TGH, THQ also controlled three TGH subsidiaries operating outside of North America: THQ (UK) Ltd. (THQUK), THQ (Holdings), Ltd. (THQH),²² and THQ Software Development–Shanghai (THQ Shanghai).²³ THQH,²⁴ like its parent TGH, was a holding company for two of its own subsidiaries: THQ Entertainment GmbH (TGHE)²⁵ and THQ France S.a.r.l. (THQ France).²⁶

Development Subsidiaries

THQ largely conducted its international business operations, e.g., its AAA game development, marketing, product distribution, and related services, through its subsidiaries. For purposes of software development, THQ used an internal development team known as the Development Subsidiaries, composed of its domestic subsidiaries Volition, THQ Phoenix, and Vigil; THQ’s foreign affiliates Relic and THQ Montreal; and THQ Shanghai.²⁷ The Development Subsidiaries operated development studios across the United States in Champaign,

¹⁹ Voluntary Petition - Consolidated List of Equity Security Holders; Voluntary Petition - Consolidated List of Equity Security Holders (THQ owns 100% of the equity in these subsidiaries).

²⁰ Declaration of Brian Farrell Paragraph 6 (Relic has done business as THQ Canada, Inc.).

²¹ Declaration of Brian Farrell Paragraph 6 (A Swiss company).

²² Declaration of Brian Farrell Paragraph 7 (THQUK and THQH are both incorporated under the laws of the United Kingdom); Declaration of Brian Farrell Paragraph 7, 9 (THQUK, THQH and TGH are the “European Subsidiaries” of THQ).

²³ Declaration of Brian Farrell Paragraph 7-9 (TGH owned 100% of the equity in these three subsidiaries).

²⁴ Declaration of Brian Farrell Paragraph 7; Declaration of Brian Farrell Paragraph 9 (From THQ’s perspective, both TGHE and THQ France are second-tier European Subsidiaries).

²⁵ Declaration of Brian Farrell Paragraph 7 (Incorporated under the laws of Germany).

²⁶ Declaration of Brian Farrell Paragraph 7 (Incorporated under the laws of France).

²⁷ Declaration of Brian Farrell Paragraph 63.

Illinois; Phoenix, Arizona;²⁸ Austin, Texas; Vancouver, British Columbia; Montreal, Quebec; and Shanghai, China.²⁹

Product Distribution Subsidiaries

For purposes of marketing, product distribution, and related services, THQ used its foreign affiliates and their subsidiaries. For example, Relic collected payments from THQ's customers in Canada;³⁰ TGH administered, on a consolidated basis, a "cash pooling" arrangement between the European subsidiaries;³¹ THQUK distributed THQ's software in the U.K. and functioned as the contracting party for THQ distribution agreements in multiple countries;³² TGHE distributed THQ's software in Germany, Austria, and Switzerland;³³ and THQ France distributed THQ's software in France and directed marketing for the Netherlands through its subsidiary, THQ Benelux (a third-tier European Subsidiary).³⁴

Business Operations

Software Development

THQ operated principally in the videogame industry developing, marketing, and distributing AAA games for a broad range of gaming platforms: videogame consoles for the home; hand-held consoles; wireless devices (e.g., mobile phones, mobile media players, tablet computers, etc.); and personal computers.³⁵ Throughout its existence, THQ generated large revenues from popular titles that it created or acquired,³⁶ e.g., the *Saints Row Series*,³⁷ *Company*

²⁸ Declaration of Brian Farrell Paragraph 5 (THQ Phoenix closed the Phoenix, Arizona development studio in August of 2011).

²⁹ Declaration of Brian Farrell Paragraph 5-6, 8.

³⁰ Declaration of Brian Farrell Paragraph 64.

³¹ Declaration of Brian Farrell Paragraph 7.

³² Declaration of Brian Farrell Paragraph 7.

³³ Declaration of Brian Farrell Paragraph 7.

³⁴ Declaration of Brian Farrell Paragraph 7.

³⁵ Declaration of Brian Farrell Paragraph 10.

³⁶ Declaration of Brian Farrell Paragraph 10.

³⁷ SAINT'S ROW, <http://www.saintsrow.com/> (last visited Apr. 8, 2013) (an action-adventure game featuring the exploits of gang members including acts of violence and the use of weapons when completing tasks).

of *Heroes*,³⁸ *Homefront*,³⁹ and *Darksiders*.⁴⁰ THQ also generated revenues from licensing agreements with World Wrestling Entertainment, Inc. (WWE), related to the *World Wrestling Entertainment* title;⁴¹ *Games Workshops PLC*, related to the *Warhammer 40,000* title;⁴² and 4A Ltd. and Dmitry Glukhovskiy, related to the *Metro: Last Light* title.⁴³

THQ developed AAA games using its Development Subsidiaries, as well as outside game developers and vendors.⁴⁴ The Development Subsidiaries developed these games at various studios in the United States, Canada, and China. To supplement the work of the Development Subsidiaries, THQ also contracted with third-party entities for work it could not efficiently or effectively perform on its own.⁴⁵

Product Distribution and Related Services

To disseminate its products in the global videogame market, THQ's business operations included product distribution and other related services. For tangible products in the United States, Canada, and Mexico, THQ and Relic employed a simple distribution tree structure; they sold directly to primary distributors, which included mass merchandisers, consumer electronic stores, discount warehouses, and national retail chain stores. These primary distributors

³⁸ COMPANY OF HEROES, <http://www.relic.com/games/company-of-heroes/> (last visited April 8, 2013) (a war-strategy videogame set in WWII Europe featuring first-person shooter style gameplay).

³⁹ HOMEFRONT, <http://www.ign.com/games/homefront-2/pc-118311> (last visited April 8, 2013) (a firstperson shooter videogame set in a near-future North Korean military occupation of the United States).

⁴⁰ DARKSIDERS, <http://www.thq.com/us/darksiders2/360> (last visited April 8, 2013) (an apocalyptic action videogame featuring fantasy storylines and battles).

⁴¹ Declaration in Support of Deal with WWE and Take Two Paragraph 4 (THQ's exclusive licensing agreement with WWE requires that it develop videogames for WWE through 2017).

⁴² WWE, <http://wwe.thq.com/> (last visited April 8, 2013) (the official videogame for the *World Wrestling Entertainment* group where gamers play as their favorite *WWE* athlete and compete in entertainment-style wrestling competitions).

⁴³ Declaration of Brian Farrell Paragraph 10.

⁴⁴ Declaration of Brian Farrell Paragraph 63, 152.

⁴⁵ THQ retains the services of programming specialists responsible for creating technical features, addressing technical issues, and providing related support for THQ products. (Declaration of Brian Farrell Paragraph 152). THQ retains separate vendors for animations and videos, known as cinematics; visual and aesthetic components; audio production; and key software components. (Declaration of Brian Farrell Paragraph 153). Outside game developers assume such a unique role in the development process that they become difficult to replace. (Declaration of Brian Farrell Paragraph 152).

subsequently sold to smaller regional retailers and secondary distributors; the secondary distributors sold to clients of their own, like grocery and drug stores.⁴⁶ For tangible products in Europe and Asia,⁴⁷ THQ relied on its European Subsidiaries to handle international publishing and distribution activities.⁴⁸

For non-tangible products, i.e., products that were available only for digital download, THQ used digital distribution methods. For example, THQ relied on the digital distribution services provided by major gaming system entities, e.g., Sony Computer Entertainment Playstation Network, Microsoft's Xbox Live, Xbox Live Arcade, and Apple's App Store.⁴⁹ Consumers could download the games from these services directly to their gaming platforms. THQ similarly provided third-party digital distribution of its software through services like Amazon.com, Electronic Arts' Origin, and Valve Software's Steam.⁵⁰

Marketing

Despite principally operating to produce and distribute videogames, marketing was a major part of THQ's business operations. THQ employed two major marketing operations: first, marketing directly to consumers through independent service providers, and second, marketing indirectly to consumers through THQ's primary distributors.

For its direct marketing operations, THQ relied on independent service providers. These independent service providers created a variety of marketing schemes; some created and maintained THQ's corporate websites, some created and maintained brand specific websites for specific titles, others maintained and operated social media channels and forums. THQ took advantage of these direct-to-consumer schemes to distribute updates and other information about its games, provide links to retailers that carry its products, and provide social forums where users could communicate with one another and with THQ's management.⁵¹ Other independent service providers operated in more traditional marketing capacities; they created promotional videos,

⁴⁶ Declaration of Brian Farrell Paragraph 11, 83.

⁴⁷ Declaration of Brian Farrell Paragraph 12 (Over 80 different territories).

⁴⁸ Declaration of Brian Farrell Paragraph 12.

⁴⁹ Declaration of Brian Farrell Paragraph 13 (Each manufacturer delivers videogame content as digital information, predominantly through broadband internet).

⁵⁰ Declaration of Brian Farrell Paragraph 13.

⁵¹ Declaration of Brian Farrell Paragraph 156.

trailers, and television commercials, as well as tangible advertising content and promotional materials, like printed advertisements and cardboard cut-outs.⁵²

For its indirect marketing operations, THQ negotiated a system of incentives for its primary distributors with the goal of driving consumer sales, developing and sustaining its positive reputation, engendering customer loyalty, ensuring customer satisfaction, meeting competitive pressures, and generating goodwill.⁵³ THQ's incentive system was made up of price protection plans, co-operative advertising, back-end rebates, defective product credits, freight rebates, and special circumstance discounts, among other programs.⁵⁴

Workforce and Compensation

For software development, product distribution, marketing, and related services, THQ required a workforce that was skilled and experienced with the nuances of the videogame industry; it also needed a workforce that could satisfy consumer preferences. Consequently, THQ relied on the service of numerous employees and independent contractors that were skilled with management, marketing, sales, technical support, and software programming.⁵⁵ In the highly competitive videogame industry, THQ retained the service of this workforce by offering them fair compensation and industry standard benefits, depending on whether they were full-time or part-time, permanent or seasonal, salaried or hourly.

THQ's Pending Bankruptcy

THQ's Fall from Grace

For over twenty years, THQ balanced its various business operations: software development, product distribution, marketing, and related services. It established a complex organizational structure, developed popular AAA games, created a vast supply chain in over eighty territories, conducted international marketing campaigns, and developed a skilled and experienced workforce. Unfortunately, between 2007 and 2012, THQ suffered significant operating losses resulting from the shifting tastes of the average gamer (i.e., those of middle-

⁵² Declaration of Brian Farrell Paragraph 157 (These promotions started more than a year before the release of a title).

⁵³ Declaration of Brian Farrell Paragraph 83; Declaration of Brian Farrell Paragraph 84, 95 (Marketing programs of this sort have become customary in the interactive entertainments software industry).

⁵⁴ See *infra* notes 249-54 and accompanying text.

⁵⁵ Declaration of Brian Farrell Paragraph 99.

aged men)⁵⁶ from kid-friendly fare to the violent “shoot ’em up” style games popular today, unsuccessful business ventures,⁵⁷ and an operating model that was unable to adapt to unplanned cash flow conditions. To combat its financial woes and to stave off its creditors, THQ undertook a massive restructuring of its business operations, personnel, and capital structure.

Shifting Tastes

On a macro level, the markets that THQ previously dominated—children’s games and other movie-based titles acquired through licensing—became increasingly less profitable as their popularity fell.⁵⁸ Gamers’ attention instead turned to more “mature” titles, including games featuring violence, gun-usage, and other adult content.⁵⁹ For example, in 2012, seven of the top ten best-selling titles were sports or realistic, first-person shooter games, in short, titles positioning themselves for more mature audiences compared to the types of games that THQ traditionally produced.⁶⁰

The popularity of violent videogames has long been controversial, and in late-2012 and early-2013, the topic again became part of the national conversation in light of the shootings at Sandy Hook Elementary in Newtown, Connecticut.⁶¹ Invariably, social scientists, the media, and the gaming industry rehashed the nexus between the rise in popularity of violent videogames and real life violence. Although the question “Why have violent videogames become so popular?” is well beyond the scope of this case study, it should be acknowledged that the top-selling game of

⁵⁶ ENTERTAINMENT SOFTWARE ASSOCIATION, *Essential Facts About the Computer and Video Game Industry* (2011) (the average gamer is male, 37 years old; approximately 75% of the gaming population is under the age of 50).

⁵⁷ Declaration of Brian Farrell Paragraph 30 .

⁵⁸ Declaration of Brian Farrell Paragraph 30.

⁵⁹ Ethan Gach, *There’s No Way Around It: The Most Popular Video Games Are Violent*, VENTURE BEAT (Jan. 16, 2013, 6:10 AM), <http://venturebeat.com/2013/01/16/theres-no-way-around-it-the-most-popular-video-games-are-also-the-most-violent/> (last visited April 8, 2013).

⁶⁰ Chris Morris, *Video Game Sales Down \$2 Billion in 2011*, YAHOO! GAMES (Jan. 12, 2012, 7:03 PM), <http://games.yahoo.com/blogs/plugged-in/video-game-sales-drop-2-billion-2011-000323900.html> (last visited April 8, 2013) (the other three “non-mature games” were Just Dance 2, Just Dance 3, and a title from the Batman franchise).

⁶¹ Sami Yenigun, *Video Game Violence: Why Do We Like It, and What’s It Doing To Us?*, NPR (Jan. 11, 2013, 4:11 PM), <http://www.npr.org/2013/02/11/171698919/video-game-violence-why-do-we-like-it-and-whats-it-doing-to-us> (last visited April 8, 2013).

2012 was *Call of Duty: Black Ops 2* from videogame maker Activision.⁶² *Call of Duty* is a war-themed videogame where the gamer takes on a “first-person shooter” role, i.e., from the eyes of a soldier; complete with guns, grenades, and knives. This format has become increasingly popular (and duplicated by companies like THQ),⁶³ and accordingly, profitable, in recent years.⁶⁴ Researchers are still exploring why this is the case, and what, if any, effect it has on gamers.⁶⁵ In any event, *Call of Duty* represents the quintessential AAA title with regard to its quality, content, and profitability.

Consequently, THQ altered its course, and moved away from its once-popular projects; it was once well known for its licensing deals with the Walt Disney Company and for developing and distributing games targeting a family market.⁶⁶ For example, THQ’s very first game was *Peter Pan and the Pirates*, released back in 1991.⁶⁷ As the popularity of these titles became eclipsed by more mature games, THQ focused on or developed its other core franchises, including *Saint’s Row*,⁶⁸ *Company of Heroes*,⁶⁹ *Warhammer*,⁷⁰ and the *WWE* line of games.⁷¹

⁶² *10 Best Selling Videogames in 2012*, WALL STREET JOURNAL MARKET WATCH (Jan. 10, 2013), <http://www.marketwatch.com/story/10-best-selling-videogames-in-2012-2013-01-10> (last visited April 8, 2013) (*Call of Duty* has been a top-selling game since 2008).

⁶³ See, e.g. SAINT’S ROW, <http://www.saintsrow.com/> (last visited Apr. 8, 2013); RED FACTION, <http://rfg.redfaction.com/index.php> (last visited April 8, 2013).

⁶⁴ Wesley Yin-Poole, *Call of Duty: Black Ops 2 makes \$1bn a day quicker than Modern Warfare 3*, EUROGAMER (Dec. 5, 2012), <http://www.eurogamer.net/articles/2012-12-05-call-of-duty-black-ops-2-makes-USD1bn-a-day-quicker-than-modern-warfare-3> (last visited April 8, 2013) (*Call of Duty: Black Ops 2* made \$1 billion for Activision, worldwide, in just fifteen days).

⁶⁵ Benedict Carey, *Shooting in the Dark*, NEW YORK TIMES (Feb. 11, 2013), <http://www.nytimes.com/2013/02/12/science/studying-the-effects-of-playing-violent-video-games.html>. (last visited April 8, 2013).

⁶⁶ Luke Plunkett, *How THQ Went From Bad to Very Bad*, KOTAKU (Feb. 1, 2012, 10:00 PM), <http://kotaku.com/5881479/how-thq-went-from-bad-to-very-bad> (last visited April 8, 2013).

⁶⁷ Luke Plunkett, *A History of THQ, 1989-2013*, KOTAKU (Jan. 23, 2013, 10:00 PM), <http://kotaku.com/5978508/a-history-of-thq-1989+2013> (last visited April 8, 2013).

⁶⁸ SAINT’S ROW, <http://www.saintsrow.com/> (last visited Apr. 8, 2013) (an action-adventure game featuring the exploits of gang members including acts of violence and the use of weapons when completing tasks).

⁶⁹ COMPANY OF HEROES, <http://www.relic.com/games/company-of-heroes/> (last visited April 8, 2013) (a war-strategy game set in WWII featuring first-person shooter style gameplay).

⁷⁰ WARHAMMER, <http://www.dawnofwargame.com/uk/faq/index/catId/1> (last visited April 8, 2013) (a science-fiction battle game with an online component).

However, it failed to produce top-selling titles under its existing stable.⁷² Some industry commentators noted that this was the case because THQ both failed to conceive its own cutting-edge games or genres (instead following in the wake of bigger studios like EA, Ubisoft, and Activision)⁷³ and of those games that were produced, many received only middling reviews from industry professionals and online reviewers, even if the game quality was relatively comparable to the “brand name” titles put forth by the bigger studios.⁷⁴ As a result of its failed refocusing efforts, THQ was forced to close two of its international studios and lay off hundreds of employees.⁷⁵

Unprofitable Participation in New Markets

During the two years prior to its bankruptcy filing, THQ rolled out a new multi-pronged strategy, identifying possible new business initiatives around its core franchises to bolster its flagging profits.⁷⁶ Generally, the company sought to increase its footprint and reinforce its videogame sales efforts by developing its presence in existing (and expanding) online and mobile markets. Additionally, THQ pursued an entry into otherwise uncharted market for the company (gaming hardware), believing that buzz around other newly-developed technologies would translate to sales of its own products.

In 2011, the company planned to increase its online and mobile presence in conjunction with each terrestrial videogame release (mostly through advertising and interactive efforts), including heightening activity on social networking websites like Facebook; increasing gamer

⁷¹ WWE, <http://wwe.thq.com/> (last visited April 8, 2013) (the official videogame for the *World Wrestling Entertainment* group where gamers play as their favorite *WWE* athlete and compete in entertainment-style wrestling competitions).

⁷² *THQ Announces Internal Studios Realignment to Focus on Key Strategic Initiatives*, THQ INVESTOR RELATIONS (Aug. 9, 2011), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irolnewsArticle&ID=1594938> (last visited April 8, 2013).

⁷³ Ryan McCaffrey, *Where Will THQ's Games and Studios Go?*, IGN (Jan. 7, 2013), <http://www.ign.com/articles/2013/01/07/where-will-thqs-games-and-studios-go> (last visited April 8, 2013).

⁷⁴ GameCentral, *Why THQ Went Bust—Reader's Feature*, METRO UK (Feb. 2, 2013, 1:00 AM), <http://metro.co.uk/2013/02/02/why-thq-went-bust-readers-feature-3377962/> (last visited April 8, 2013).

⁷⁵ *THQ Announces Internal Studios Realignment to Focus on Key Strategic Initiatives*, THQ INVESTOR RELATIONS (Aug. 9, 2011), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irolnewsArticle&ID=1594938> (last visited April 8, 2013).

⁷⁶ *THQ Announces Internal Studios Realignment to Focus on Key Strategic Initiatives*, THQ INVESTOR RELATIONS (Aug. 9, 2011), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irolnewsArticle&ID=1594938> (last visited April 8, 2013).

accessibility on mobile videogame platforms (i.e., through the creation of new or conversion of existing videogames for smartphones like Apple's iPhone); and revamping THQ.com, the company's official website.⁷⁷

THQ pursued entry into the videogame hardware market in 2010. Four years prior, Nintendo, a premier platform manufacturer and videogame development company,⁷⁸ introduced the Wii console.⁷⁹ The Wii was revolutionary for its time; it uniquely mixed (full-body) motion-controlled videogaming (compared to traditional handheld joysticks) with online connectivity in a way that had not been seen before.⁸⁰ The Wii would go on to sell over eighty-six million units within five years of its release.⁸¹ Given the immense popularity of the Wii system, THQ introduced the uDraw, a gaming tablet intended to compliment Nintendo's Wii, as well as Sony's PlayStation 3 and Microsoft's Xbox 360.⁸²

The uDraw was a digital tablet and stylus that can be used by gamers to draw and view their work on their television screen.⁸³ It paired with the joysticks of Nintendo's Wii, Sony's Playstation 3, or Microsoft's Xbox 360, by docking each controller into the uDraw tablet.⁸⁴ Each

⁷⁷ *THQ Announces Internal Studios Realignment to Focus on Key Strategic Initiatives*, THQ INVESTOR RELATIONS (Aug. 9, 2011), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irolnewsArticle&ID=1594938> (last visited April 8, 2013).

⁷⁸ *Company History*, NINTENDO (last visited April 8, 2013), <http://www.nintendo.com/corp/history.jsp>.

⁷⁹ *Wii*, NINTENDO (last visited April 8, 2013), <http://www.nintendo.com/wii>.

⁸⁰ *What is Wii: Overview*, NINTENDO (last visited April 8, 2013), <http://www.nintendo.com/wii/whatis-wii/#/overview>; *What is Wii: Controls*, NINTENDO (last visited April 8, 2013), <http://www.nintendo.com/wii/what-is-wii/#/controls>; *What is Wii: FAQ*, NINTENDO (last visited April 8, 2013), <http://www.nintendo.com/wii/faq/#/faq-1>.

⁸¹ *Annual Report 2011*, NINTENDO, available at <http://www.nintendo.co.jp/ir/pdf/2011/annual1103e.pdf> (last visited April 8, 2013).

⁸² Declaration of Brian Farrell Paragraph 30; the PS3 and Xbox 360 are two other modern videogame platforms that extensively feature games with high-quality graphics and online connectivity, like Wii.

⁸³ *uDraw Game Tablet*, WORLD OF UDRAW (last visited April 8, 2013), <http://www.worldofudraw.com/tablet>.

⁸⁴ *uDraw Game Tablet*, WORLD OF UDRAW (last visited April 8, 2013), <http://www.worldofudraw.com/tablet>; *uDraw Game Tablet: Xbox*, WORLD OF UDRAW (last visited April 8, 2013), http://www.worldofudraw.com/tablet_ps3; *uDraw Game Tablet PS3*, WORLD OF UDRAW (last visited April 8, 2013), http://www.worldofudraw.com/tablet_xbox.

platform offered various games that could be used in conjunction with the uDraw.⁸⁵ Most of the games, however, were targeted toward a younger audience rather than to the money-making 18-49 demographic,⁸⁶ an operational decision that was directly at odds with THQ's realignment toward adult titles.

THQ's foray into this new line of gaming hardware proved disastrous, significantly failing to meet the company's expectations—estimated revenues fell approximately \$100 million short of THQ's projections,⁸⁷ leaving nearly 1.5 million units unsold.⁸⁸ THQ Chief Financial Officer Paul Pucino noted that those numbers represented “something in excess of \$30 million in operating loss” for the company.⁸⁹ The uDraw was discontinued as of the time of THQ's bankruptcy filing.⁹⁰ In 2012, THQ's failed device, accompanied by overly optimistic projections and pronouncements about the success of the uDraw, resulted in a class-action shareholder suit against the company.⁹¹ That case is still pending.

THQ's attempt to enter or further establish itself in these markets represented a common shortcoming of the company. It was simply behind the times with regard to innovation and unable to compete with the industry's giants, EA, Ubisoft, and Activision. Throwing money behind initiatives dominated by the top players was a losing bet for THQ.

Changes in Management

⁸⁵ *uDraw Games*, WORLD OF UDRAW (last visited April 8, 2013), <http://www.worldofudraw.com/udrawgames>.

⁸⁶ *uDraw Games*, WORLD OF UDRAW (last visited April 8, 2013), <http://www.worldofudraw.com/udrawgames>.

⁸⁷ Fred Dutton, *THQ Details full extent of uDraw disaster*, EUROGAMER (Feb. 2, 2012), <http://www.eurogamer.net/articles/2012-02-02-thq-details-full-extent-of-udraw-disaster> (last visited April 8, 2013).

⁸⁸ Alex Culafi, *THQ Explains the Proportions of uDraw's Collapse*, NINTENDO WORLD REPORT (Feb. 3, 2012, 3:20 PM), <http://www.nintendoworldreport.com/news/29179> (last visited April 8, 2013).

⁸⁹ Fred Dutton, *THQ Details full extent of uDraw disaster*, EUROGAMER (Feb. 2, 2012), <http://www.eurogamer.net/articles/2012-02-02-thq-details-full-extent-of-udraw-disaster> (last visited April 8, 2013).

⁹⁰ Declaration of Brian Farrell Paragraph 31.

⁹¹ Rachel Weber, *THQ faces second uDraw class-action lawsuit*, GAMES INDUSTRY INTERNATIONAL (Jul. 19, 2012, 7:55 AM), <http://www.gamesindustry.biz/articles/2012-07-18-thq-faces-udraw-class-actionlawsuit> (last visited April 8, 2013).; LEVI KORINSKY, LLP, <http://zlkdocs.com/THQ-Info-Request-Form-196> (last visited April 8, 2013).

In June 2012, THQ brought in new officers to restructure its operations, moving away from its failed initiatives around mobile applications and hardware. Instead, management would refocus the company on its core franchises, namely *Saint's Row*,⁹² *Company of Heroes*,⁹³ *Warhammer*,⁹⁴ and the *WWE*⁹⁵ line of games.

Jason Rubin was hired as THQ's new President. Rubin was a former principal at Naughty Dog, a videogame developer responsible for hit titles such as *Crash Bandicoot*, *Jak and Daxter*, and *Uncharted*; each a cartoon or adventure-based children's game popular in the late 1990s and early 2000s—essentially the very type of game that THQ was attempting to distance itself from.⁹⁶ Rubin also co-founded media company Flektor, launched in 2007 and purchased by Fox Interactive Media in 2009.⁹⁷ While at Flektor, Rubin worked closely with business partner, industry executive, and serial entrepreneur Jason Kay. Kay was hired as THQ's new Chief Strategy Officer and brought to the table a background in media, entertainment, and technology, having years of experience at videogame developer Activision, advising at IGN (a technology and videogame website) and media powerhouses News Corp. and HBO.⁹⁸

Rubin and Kay were charged with turning THQ around in a short timeframe; realigning the company's strategy to focus on its more popular franchises, eliminating unprofitable

⁹² SAINT'S ROW, <http://www.saintsrow.com/> (last visited April 8, 2013) (an action-adventure game featuring the exploits of gang members including acts of violence and the use of weapons when completing tasks).

⁹³ COMPANY OF HEROES, <http://www.relic.com/games/company-of-heroes/> (last visited April 8, 2013) (a war-strategy game set in WWII featuring first-person shooter style gameplay).

⁹⁴ WARHAMMER, <http://www.dawnofwargame.com/uk/faq/index/catId/1> (last visited April 8, 2013) (a science-fiction battle game with an online component).

⁹⁵ WWE, <http://wwe.thq.com/> (last visited April 8, 2013) (the official videogame for the *World Wrestling Entertainment* group where gamers play as their favorite *WWE* athlete and compete in entertainment-style wrestling competitions); Declaration of Brian Farrell Paragraph 33; Evan Narcisse, *THQ's New Boss Says No More uDraw, Primary Focus Will Be AAA Games*, KOTAKU (Jun. 18, 2012, 2:30 PM), <http://kotaku.com/5919322/thqs-new-boss-says-no-more-udraw-primary-focus-will-be-aaa-games> (last visited April 8, 2013).

⁹⁶ Declaration of Brian Farrell Paragraph 33; NAUGHTY DOG, <http://www.naughtydog.com/games/> (last visited April. 8, 2013).

⁹⁷ Joseph Menn, *2 amateur video sites snapped up*, L.A. TIMES (May 31, 2007), http://msl1.mit.edu/furdlog/docs/latimes/2007-05-31_latimes_newscorp_acquisitions.pdf (last visited April 8, 2013).

⁹⁸ Declaration of Brian Farrell Paragraph 33; *Jason Kay, Chief Strategy Officer at THQ*, LINKEDIN, <http://www.linkedin.com/in/flektor> (last visited April. 8, 2013).

operations, and reducing its workforce.⁹⁹ Between December 2011 and June 2012, THQ shed approximately 650 employees; down from 1,400 persons before the massive layoffs.¹⁰⁰ THQ's CEO, Brian Farrell, also announced that he would voluntarily halve his salary to save costs.¹⁰¹ His salary was reduced for a one-year period from \$718,500 to just under \$359,250,¹⁰² although his total listed income as a result of stock awards, options, and other compensation remained nearly \$1.3 million in 2011 alone.¹⁰³ Farrell's employment contract was also amended, "chang[ing] the compensation that Mr. Farrell would receive if he were terminated without 'Cause' or resigned for 'Good Reason' . . . by reducing the lump sum payment component that is tied to bonus compensation"¹⁰⁴ Effectively, THQ signaled to Farrell that this would be his last chance to turn THQ's prospects around or face termination.

Recapitalization of THQ

THQ also announced that it would undertake a reverse stock split in July 2012 in an effort to avoid having its common stock delisted by the NASDAQ.¹⁰⁵ The NASDAQ listing

⁹⁹ Declaration of Brian Farrell Paragraphs 32-34.

¹⁰⁰ Declaration of Brian Farrell; Form 8-K, United States Securities and Exchange Commission (Jan. 26, 2012), <http://www.sec.gov/Archives/edgar/data/865570/000086557012000005/a1-26x128xklayoffscompensa.htm> (last visited April 8, 2013); Deborah Crowe, *THQ Imposes Layoffs in Wake of Slow uDraw Sales*, L.A. BUSINESS JOURNAL (Dec. 12, 2011), <http://labusinessjournal.com/news/2011/dec/12/thq-imposes-layoffs-wake-slow-udraw-sales/> (last visited April 8, 2013); Ben Gilbert, *THQ Confirms layoffs of up to 240 employees*, JOYSTIQ (Feb. 1, 2012, 5:47 PM), <http://www.joystiq.com/2012/02/01/thq-confirms-layoffs-of-240-employees-across-nine-months/> (last visited April 8, 2013).

¹⁰¹ Brendan Sinclair, *THQ layoffs hit 240, CEO takes 50% pay cut*, GAMESPOT (Feb. 1, 2012, 2:38 PM), <http://www.gamespot.com/news/thq-layoffs-hit-240-ceo-takes-50-pay-cut-6349587> (last visited April 8, 2013).

¹⁰² Form 8-K, United States Securities and Exchange Commission (Jan. 26, 2012), <http://www.sec.gov/Archives/edgar/data/865570/000086557012000005/a1-26x128xklayoffscompensa.htm> (last visited April 8, 2013).

¹⁰³ *Profile: Brian Farrell*, FORBES, <http://www.forbes.com/profile/brian-farrell/> (last visited April 8, 2013).

¹⁰⁴ Form 8-K, United States Securities and Exchange Commission (Jan. 26, 2012), <http://www.sec.gov/Archives/edgar/data/865570/000086557012000005/a1-26x128xklayoffscompensa.htm> (last visited April 8, 2013).

¹⁰⁵ *THQ Announces 1-for-10 Reverse Stock Split*, THQ INVESTOR RELATIONS (Jul. 9, 2012), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irol-newsArticle&id=1711030> (last visited April 8, 2013); Andrew Goldfarb, *How THQ is Protecting Its Future*, IGN (Jul. 2, 2012), <http://www.ign.com/articles/2012/07/03/how-thq-is-protecting-its-future> (last visited April 8, 2013). Note that a company's listing on a national exchange such as NASDAQ carries with it intrinsic benefits, such

rules require that a public company maintain a minimum share price of \$1 or higher for a period of ten consecutive days to remain listed.¹⁰⁶ Thus, in order to continue listing its stock on the national exchange, THQ effectuated a one-for-ten split.¹⁰⁷ Undertaking the reverse split would convert THQ's 68.5 million outstanding shares of common stock to 6.9 million shares, and bring the company back into compliance with NASDAQ's rules by boosting the price per share tenfold, from approximately \$0.60 to \$6.¹⁰⁸ The maneuver was nothing but smoke and mirrors intended to impress THQ's strength on investors; however, the split did nothing but artificially inflate the price of the company's stock, and was devoid of any actual change in THQ's financial position.

THQ's Cash Flow Condition Worsens

THQ's financial and operational maneuvering would be for naught, because it was unable to extract itself from its fiscal slump. THQ had simply become too bloated, unable to adapt its business model to a diminished cash flow condition. As described in detail above, THQ's management decisions failed to effectively anticipate and sufficiently synchronize the cash flow cycles for past, present, and future THQ products. The company misjudged its core audiences' preference for its traditional fare, failed to fully appreciate and cash in on the first-person shooter videogame craze, the uDraw fiasco had left it with few sources of up-coming positive cash flows.¹⁰⁹ These poor business decisions, alongside the following internal business conditions, resulted in THQ hemorrhaging capital resources¹¹⁰:

as an active, open market for the company's securities. Accordingly, delisting THQ's stock would result in serious consequences for the company's value if its stock could not be readily traded.

¹⁰⁶ 5001. *NASDAQ Listing Rules*, NASDAQ OMX, <http://nasdaq.cchwallstreet.com/NASDAQTools/PlatformViewer.asp?selectednode=chp1143&manual=%2Fnasdaq%2Fmain%2Fnasdaq-equityrules%2F> (last visited April 8, 2013).

¹⁰⁷ *THQ Announces 1-for-10 Reverse Stock Split*, THQ INVESTOR RELATIONS (Jul. 9, 2012), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irol-newsArticle&id=1711030> (last visited April 8, 2013).

¹⁰⁸ THQ Stock Price, <https://www.google.com/finance?client=ob&q=NASDAQ:THQ> (restrict search to 2012 to see spike in THQ stock price as result of reverse split) (last visited May 28, 2013).

¹⁰⁹ See *supra* notes 58-108 and accompanying text.

¹¹⁰ Declaration of Brian Farrell Paragraph 10 (THQ's is next scheduled to release *South Park Universe* by the end of 2013).

- THQ relied too heavily on its Development Subsidiaries and from retaining the services of specialized outside game developers, vendors, and programming specialists, leaving it highly leveraged for long periods of time.¹¹¹
- THQ experienced a resource drain associated with its complex supply chain for order processing and return services, including the services of common, rail, freight, and parcel carriers.¹¹²
- Despite falling revenues, THQ poured money into its direct and indirect marketing operations in connection with its publicity websites and promotional materials, as well as various incentive programs price protection plans,¹¹³ co-operative advertising,¹¹⁴ back-

¹¹¹ Declaration of Brian Farrell Paragraph 10.

¹¹² Declaration of Brian Farrell Paragraph 141-142.

¹¹³ Declaration of Brian Farrell Paragraph 85 (Under the price protection plan, THQ issued credits to the primary distributors for the difference in price between the initial price and the new price of any remaining inventory. The primary distributors then used these credits to lessen any outstanding invoices they owe to THQ).

¹¹⁴ Declaration of Brian Farrell Paragraph 87 (THQ's primary distributors, like consumer electronic stores and national retail chain stores, had direct access to a captive audience of patrons at their local brick and mortar stores. These patrons were prime candidates for targeted advertisement because they were already consumers of THQ-like products. As such, THQ attempted to take advantage of this captive audience by reimbursing its primary distributors for advertising THQ products).

end rebates,¹¹⁵ defective product credits,¹¹⁶ freight rebates,¹¹⁷ and special circumstance discounts.¹¹⁸

- Despite its dire financial condition, the company continued to offer its employees fair compensation and industry standard benefits, including reimbursable expenses;¹¹⁹ sale incentive bonuses;¹²⁰ product development profit sharing bonuses;¹²¹ health benefits;¹²²

¹¹⁵ Declaration of Brian Farrell Paragraph 89 (THQ had agreements with certain primary distributors allowing them to temporarily reduce the retail price of THQ products. Like the price protection plan with other primary distributors, THQ's goal with this incentive program was to lessen the primary distributor's market risk. By promising to reimburse in the future up to 80% of the primary distributor's reduction in price, THQ incentivized the primary distributor to make bulk orders of products before their public release date).

¹¹⁶ Declaration of Brian Farrell Paragraph 91-92 (THQ understood that sometimes its products would be defective. Upon receiving a claim for defective inventory from the primary distributor, THQ issued the primary distributor a credit and these credits were used to lessen any outstanding invoices the primary distributor owes to THQ).

¹¹⁷ Declaration of Brian Farrell Paragraph 93 (THQ attempted to incentive primary distributors to use its complex distribution supply chain. For certain primary distributors, THQ issued a per shipment rebate, between \$0.05 - \$0.30, each time an eligible primary distributor selected an authorized common carrier to deliver THQ products).

¹¹⁸ Declaration of Brian Farrell Paragraph 94 (THQ gave certain primary distributors discounts on its products for special circumstances with the hope that these incentives would be mutually beneficial. For example, THQ offered certain primary distributors discounted prices on its products if the primary distributor was opening a new brick and mortar store. Moreover, THQ offered some primary distributors discounted prices for certain titles if the distributor agreed to purchase a different title, or if the distributor purchased a certain quantity of a particular title).

¹¹⁹ Declaration of Brian Farrell Paragraph 109-111 (THQ reimbursed employees for legitimate business expenses incurred within the scope of employment. The types of expenses that qualified for this incentive included: air travel, meals, parking, automobile mileage, office supplies, cellular telephones, related business development expenses).

¹²⁰ Declaration of Brian Farrell Paragraph 114-115 (THQ supplemented the base compensation of its U.S. sales employees for its quarterly and annual sales. The bonus functioned exactly as it sounds; when a sales employee surpasses a certain level of sales within the quarter or year that employee was eligible for additional compensation).

¹²¹ Declaration of Brian Farrell Paragraph 117 (THQ shared its profits for a specific period of time with its Development Subsidiaries; the goal being that the Development Subsidiaries would trickle down the bonuses to their workforce).

¹²² Declaration of Brian Farrell Paragraph 121-122; Motion to Pay EE Benefits Paragraph 41-42, 44 (THQ offered its employees, and their eligible dependents, medical and prescription drug benefits; dental benefits; and vision benefits. For all of these different health plans, THQ also offered its employees a

insurance benefits;¹²³ vacation and paid-time-off (PTO) benefits;¹²⁴ 401(K) plans;¹²⁵ and flexible spending account plans.¹²⁶

THQ's Debt Financing Comes Due and DIP Financing Offered

Overextended and under-performing, THQ announced that it would enter into a multi-year Credit Facility with Wells Fargo Capital Finance, LLC (Wells Fargo)¹²⁷ in September 2011. Wells Fargo would extend nearly \$50 million in financing to the company, increasing its borrowing power by \$15 million from its previous Credit Facility.¹²⁸ Unfortunately, by

premium cost sharing plan wherein THQ paid a portion of the insurance premiums incurred by its employees under their basic health benefit plans).

¹²³ Motion to Pay EE Benefits Paragraph 44; Motion to Pay EE Benefits Paragraph 45 (THQ offered a variety of insurance plans: basic life, accidental death, dismemberment, supplemental life, short-term, and long-term disability, and other voluntary insurance plans. These insurance plans were packaged in different combinations and made available to employees based on their employment level).

¹²⁴ Declaration of Brian Farrell Paragraph 126 (THQ provided all its employees with a certain amount of paid vacation time per year, and a certain amount of paid-time-off (PTO) per year. PTO time is intended to cover sick days, personal days, and to supplement vacation time when needed. The amount of time the employees receive depended on their employment level and their length of employment).

¹²⁵ Declaration of Brian Farrell Paragraph 127-128; Motion to Pay EE Benefits Paragraph 53 (THQ maintained a retirement savings plan for all its eligible employees pursuant to section 401 of the Internal Revenue Code. THQ's policy was to always make matching contributions to its employee's savings pursuant to the 401(K) rules).

¹²⁶ Motion to Pay EE Benefits Paragraph 57-58; Declaration of Brian Farrell Paragraph 129 (THQ offered its employees a flexible spending account, e.g., an account wherein employees save a portion of their pretax compensation to pay for eligible out-of-pocket healthcare and dependent-care insurance premiums, as well as healthcare and dependent-care expenses. Employees realized the benefit of the plan by seeking reimbursements for expenses incurred, or by having the account pay healthcare providers directly).

¹²⁷ Wells Fargo secured the credit facility with first priority security interests in nearly all of THQ's eligible collateral (including inventory and accounts receivable and liens on THQ's real property. Declaration of Brian Farrell Paragraph 165. As additional security, Wells Fargo had THQ's domestic subsidiaries Volition, THQ Wireless, and Vigil as guarantors for the credit facility. Declaration of Brian Farrell Paragraph 26). Similar to the Well Fargo's asset-based revolving credit facility, THQ had financed its business operations by issuing \$100 million in 5% convertible unsecured senior notes to various investment entities, i.e., Silverback Asset Management, LLC, Third Avenue Focused Credit Fund, and Wolverine Flagship Fund Trading Limited. (Objection to Motion for DIP Financing Footnote 1; Declaration of Brian Farrell Paragraph 28). The notes were due August 2014. (Declaration of Brian Farrell Paragraph 28).

¹²⁸ *THQ Announces New Credit Facility with Wells Fargo*, THQ INVESTOR RELATIONS (Sept. 28, 2011), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irol-newsArticle&id=1610682> (last visited April 8, 2013).

November 2012, Wells Fargo informed THQ that it was in default under the terms of the Credit Facility.¹²⁹ Wells Fargo notified the company that it had reached its maximum excess availability amount,¹³⁰ which in turn triggered a fixed charge coverage covenant;¹³¹ ultimately, THQ was unable to pay.¹³² Wells Fargo and THQ subsequently entered into a forbearance agreement in order to avoid a complete default under the Credit Facility.¹³³ Wells Fargo agreed to forbear on THQ's loan through January 15, 2013, and would continue to make its revolving loans to the company.¹³⁴

The forbearance agreement also stipulated that Wells Fargo would continually "sweep the Debtor's depository accounts,"¹³⁵ effectively leaving THQ without operating capital. Simultaneously, Wells Fargo required that THQ "request new advances to pay expenses"

¹²⁹ Declaration of Brian Farrell Paragraph 35.

¹³⁰ In a secured loan agreement, the debtor is permitted to borrow the lesser of the amount of the lender's commitments and the amount of the debtor's eligible assets (as agreed upon by the parties). When the debtor's outstanding loans fall below the maximum amount it may borrow, that unused amount constitutes the "excess." If the excess reaches a certain amount, certain covenants may be triggered under the terms of the agreement. This keeps debtors assuming additional debt under the contract and creditors in business.

¹³¹ Fixed charge coverage is a ratio used to gauge the ability of the debtor to meet its debt obligations. In a loan agreement, a fixed charge coverage covenant sets a limit on how far that ratio can fall. When the debtor's financial position falters and the ratio falls below the contracted for limit, the covenant is triggered, requiring payment to the creditor.

¹³² Declaration of Brian Farrell Paragraph 35.

¹³³ Declaration of Brian Farrell Paragraph 35; *THQ Provides Update on Its Credit Facility and Announces Exclusive Negotiations with Financial Sponsor for Potential Financing Alternatives*, THQ INVESTOR RELATIONS (Nov. 20, 2012), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irolnewsArticle&id=1760963> (last visited April 8, 2013).

¹³⁴ *THQ Provides Update on Its Credit Facility and Announces Exclusive Negotiations with Financial Sponsor for Potential Financing Alternatives*, THQ INVESTOR RELATIONS (Nov. 20, 2012), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irol-newsArticle&id=1760963> (last visited April 8, 2013).

¹³⁵ THQ maintained four depository accounts with Union Bank. THQ used these accounts primarily for the collection of cash receipts. THQ only deposited cash originating from a particular business line into one of the four Union Bank accounts: general customer cash receipts (Declaration of Brian Farrell Paragraph 58(a)(1)), Valusoft customer cash receipts, THQ Wireless customer cash receipts, and Paypal customer cash receipts. (Declaration of Brian Farrell Paragraph 58(a)). The majority of cash receipts received by THQ are general customer cash receipts. (Declaration of Brian Farrell Paragraph 58(a)(1)). The four Union Bank accounts were subject to control agreements by Wells Fargo. (Declaration of Brian Farrell Paragraph 58(a)).

through the Credit Facility.¹³⁶ Wells Fargo was draining THQ dry (as creditors exercising their remedies under the terms of a loan document are wont to do), exhausting all of its capital resources, and forcing it closer to bankruptcy. Internally, it was clear that the company would soon fail; the nearest new game was not scheduled to be released until March 2013 and THQ was without sufficient funds to continue its operations.¹³⁷ An out-of-court restructuring would not be possible at this point.¹³⁸

Around this time, Wells Fargo and investment firm Clearlake Capital Group (Clearlake) agreed to provide debtor in possession (DIP) financing to THQ as needed.¹³⁹ Clearlake was an “investment firm focused on private equity and special situation transactions,” meaning that it focused on distressed companies preparing to collapse under the weight of their pending insolvency.¹⁴⁰ The firm prides itself on “partner[ing] with world-class management teams” of presumably distressed or bankrupt companies “to provide . . . patient, long-term capital and operational expertise.”¹⁴¹ In time, Clearlake would prove to be not only a creditor of THQ during its bankruptcy, but also the architect behind its eventual sale.

During this time, Farrell remained (publicly) optimistic, reiterating THQ’s focus on its reformed business operations and to continue “bringing [its] games in development to market.”¹⁴² Despite the rosy announcement to its investors, THQ continued to hemorrhage capital resources and key personnel, including its CFO, Paul Pucino.¹⁴³ At the time of the forbearance, industry watchdogs noted that THQ’s stock was trading at only “\$1.25 [despite the reverse stock split just four months prior], market capitalization [was] at \$8.5 million, and

¹³⁶ Declaration of Brian Farrell Paragraph 35.

¹³⁷ Declaration of Brian Farrell Paragraph 38.

¹³⁸ Declaration of Brian Farrell Paragraph 38.

¹³⁹ Declaration of Brian Farrell Paragraph 38.

¹⁴⁰ CLEARLAKE CAPITAL, <http://www.clearlakecapital.com/overview.html> (last visited April 8, 2013).

¹⁴¹ CLEARLAKE CAPITAL, <http://www.clearlakecapital.com/overview.html> (last visited April 8, 2013).

¹⁴² *THQ Provides Update on Its Credit Facility and Announces Exclusive Negotiations with Financial Sponsor for Potential Financing Alternatives*, THQ INVESTOR RELATIONS (Nov. 20, 2012), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irol-newsArticle&id=1760963> (last visited April 8, 2013).

¹⁴³ *THQ Provides Update on Its Credit Facility and Announces Exclusive Negotiations with Financial Sponsor for Potential Financing Alternatives*, THQ INVESTOR RELATIONS (Nov. 20, 2012), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irol-newsArticle&id=1760963> (last visited April 8, 2013).

corporate heads [were] exploring financial strategies with a private equity broker.”¹⁴⁴ THQ’s situation was dire.

Pre-Bankruptcy Marketing Efforts

Upon THQ’s determination that its financial condition was unsustainable and bankruptcy was on the horizon, and in an effort to preserve what value remained in the corporation, the company sought the assistance of an investment management, consulting, and monitoring institution in order to maximize its going-concern value.¹⁴⁵ THQ, now on the bankruptcy track, began actively searching for a potential “stalking horse bidder” in its Section 363 sale (a purchaser who typically generates “greater value than an open auction [by setting] a bidding floor, [where] all bids must be greater than the [stalking horse] bid in certain increments”).¹⁴⁶

As a general matter, a stalking horse bidder provides several key functions. First, they provide due diligence for the debtor’s assets and establish the terms and conditions of the auction itself.¹⁴⁷ Second, and as a result of their negotiation with the debtor, they act as the base bid for the auction.¹⁴⁸ Third, the existence and legwork of the stalking horse bidder will (hopefully) attract other bidders to the auction in order to obtain a “higher and better” price for the debtor in bankruptcy.¹⁴⁹ However, the stalking horse bidder may impede the sale process, e.g., if the bid increments are undesirable to other prospective purchasers, or because the breakup fee is too high.¹⁵⁰

THQ first engaged Citibank Global Markets, Inc. to raise capital or sell THQ’s assets during a three-month period between December 2011 and February 2012.¹⁵¹ As a result of this pre-plan marketing push, Citibank identified twenty-six potential bidders and twenty-nine

¹⁴⁴ Joystiq, *THQ in forbearance agreement with Wells Fargo, CFO resigns*, TECH INVESTOR NEWS (Nov. 20, 2012), <http://www.techinvestornews.com/Gaming/Gaming-User-News/thq-in-forbearance-agreement-with-wells-fargo-cfo-resigns> (last visited April 8, 2013).

¹⁴⁵ Declaration of Brian Farrell Paragraph 39.

¹⁴⁶ Michael J. Davis, *363 Sales in Bankruptcy*, 22 DBCA Brief 27, 28 (2009).

¹⁴⁷ *Id.*

¹⁴⁸ *Id.*

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

¹⁵¹ Declaration of Brian Farrell Paragraph 40.

potential financial backers.¹⁵² Unfortunately for THQ, only six potential bidders and seven potential financial backers entered into Non-Disclosure Agreements with Citibank.¹⁵³ And by the end of the marketing process, none of those entities displayed an interest in purchasing THQ either as a going concern or piecemeal (asset-by-asset or “studio-by-studio”).¹⁵⁴

Undeterred by its first failed effort to market itself, THQ subsequently engaged Centerview Partners, LLC in June 2012 to find an investor to provide liquidity for its business operations or alternatively to purchase all or substantially all its assets.¹⁵⁵ Rubin aligned with Centerview because he had previously worked with the investment company’s senior advisor, Skip Paul, when Paul was an investor in Rubin’s Flektor venture some years prior.¹⁵⁶ Building from the marketing efforts of Citibank, Centerview reviewed THQ’s prospects in the context of a bankruptcy sale.¹⁵⁷ Ultimately, however, Centerview did not continue its pre-bankruptcy marketing efforts with THQ,¹⁵⁸ although it remained an advisor to THQ throughout the duration of its bankruptcy and eventual sale.¹⁵⁹

During this time, industry analysts were also reporting that THQ’s prospects looked grim, and that the company’s bankruptcy was looming.¹⁶⁰ One commentator posited that “[s]hould [THQ’s] financial position continue to deteriorate . . . we expect THQ to raise financing through an equity sale that could lead to dilution of existing shareholders. We expect creditors to be

¹⁵² Declaration of Brian Farrell Paragraph 40.

¹⁵³ Declaration of Brian Farrell Paragraph 40.

¹⁵⁴ Declaration of Brian Farrell Paragraph 40.

¹⁵⁵ Declaration of Brian Farrell Paragraph 41.

¹⁵⁶ Ben Fritz, *THQ delays games, looks to raise capital*, L.A. TIMES (Nov. 5, 2012), <http://articles.latimes.com/2012/nov/05/entertainment/la-et-ct-thq-delays-games-raise-capital-20121105> (last visited April 8, 2013).

¹⁵⁷ Declaration of Brian Farrell Paragraph 41.

¹⁵⁸ Declaration of Brian Farrell Paragraph 41.

¹⁵⁹ *THQ Receives Court Approval for Amended Sale Calendar*, United States Securities and Exchange Commission (Jan. 8, 2013), <http://www.sec.gov/Archives/edgar/data/865570/000086557013000002/a1-8x12pressrelease.htm> (last visited April 8, 2013).

¹⁶⁰ Adam Gauntlett, *THQ Earnings Call Gives Little Reason for Confidence*, THE ESCAPIST (Nov. 6, 2012), <http://www.escapistmagazine.com/news/view/120512-THQ-Earnings-Call-Gives-Little-Reason-for-Confidence> (last visited April 8, 2013).

asked to renegotiate terms at a discount; if they are unwilling, bankruptcy is possible.”¹⁶¹ On a November 5 investor conference call, Rubin did little to encourage THQ’s shareholders, acknowledging that THQ would “no longer provid[e] net sales and earnings guidance.”¹⁶² Further, the company would “withdraw[] [its] previous guidance for [FY‘13] in [its] projected operating model,”¹⁶³ signaling to investors and analysts that the THQ was on its last legs financially.

In November 2012, THQ consulted with Houlihan Lokey, LLC, as a result of pressure from its unsecured note holders, to undertake a marketing process.¹⁶⁴ That marketing was ultimately terminated prior to its commencement and the record is otherwise silent regarding THQ’s subsequent interactions with Houlihan with respect to its pre-bankruptcy marketing efforts.¹⁶⁵

THQ and Clearlake Begin Negotiations

Regardless of the marketing efforts put forth by Centerview and others, THQ independently began formal talks with Clearlake on October 26, 2012, entering into an exclusive forty-five day negotiation period, which later was extended to December 17, 2012.¹⁶⁶ With its options running low and time running out, THQ seemed poised to enter into an agreement with Clearlake, its then DIP lender and soon-to-be stalking horse bidder, unless a better offer materialized¹⁶⁷—an offer that was becoming increasingly unlikely to appear the longer THQ devalued in the market.

¹⁶¹ Adam Gauntlett, *THQ Earnings Call Gives Little Reason for Confidence*, THE ESCAPIST (Nov. 6, 2012), <http://www.escapistmagazine.com/news/view/120512-THQ-Earnings-Call-Gives-Little-Reason-for-Confidence> (last visited April 8, 2013).

¹⁶² *THQ Management Discusses Q2 2013 Results – Earnings Call Transcript*, SEEKING ALPHA (Nov. 5, 2012, 6:00 PM), <http://seekingalpha.com/article/980111-thq-management-discusses-q2-2013-results-earnings-call-transcript?page=1> (last visited April 8, 2013).

¹⁶³ *THQ Management Discusses Q2 2013 Results – Earnings Call Transcript*, SEEKING ALPHA (Nov. 5, 2012, 6:00 PM), <http://seekingalpha.com/article/980111-thq-management-discusses-q2-2013-results-earnings-call-transcript?page=1> (last visited April 8, 2013).

¹⁶⁴ Declaration of Brian Farrell Paragraph 41 Footnote 2.

¹⁶⁵ Declaration of Brian Farrell Paragraph 41.

¹⁶⁶ Declaration of Brian Farrell Paragraph 41 (This is not entirely consistent with the Houlihan Lokey consultation, but any inconsistency is derived solely from the Farrell First Day Motion).

¹⁶⁷ Declaration of Brian Farrell Paragraph 38.

The Asset Purchase Agreement and Sale Procedures

As a result of their negotiations, Space Investors LLC (Space Investors), a newly-formed entity and affiliate of Clearlake, would serve as the stalking horse bidder for THQ's 363 sale, and THQ would be permitted to solicit competing bids from other prospective purchasers.¹⁶⁸ Although discussed more in depth *infra*, under the pertinent terms of the Agreement, Space Investors would pay off Wells Fargo's secured debt (of which approximately \$20 million was outstanding), pay THQ \$6.65 million in cash (ostensibly used for urgent operating expenses), assume another \$15 million in THQ's liabilities, and deliver to THQ a \$10 million seven-year unsecured note,¹⁶⁹ payable by Space Investors.¹⁷⁰

In its initial filings, THQ asserted that the sale of assets to Space Investors (or a higher bidder) in conjunction with Wells Fargo and Clearlake's DIP financing was the best possible option to retain the going concern value of the company and obtain maximum value for THQ's assets.¹⁷¹ The assets would be sold on an "as is" and "where is" basis, with THQ making no representations or warranties of any kind, nature, or description.¹⁷² In the event that Space Investors was not the successful bidder, THQ would pay to Space Investors a \$1.75 million break-up fee plus expense reimbursements pursuant to the Asset Purchase Agreement.¹⁷³

On December 19, 2012, THQ and Space Investors formalized and executed the Asset Purchase Agreement and Bidding Procedures (collectively, the APA), whereby Space Investors would "acquire all right, title and interest of [THQ] in, to or under substantially all of the [company's] properties and assets."¹⁷⁴ The APA provided that any person seeking to bid on

¹⁶⁸ Declaration of Brian Farrell Paragraph 42; Form 8-K, United States Securities and Exchange Commission (Dec. 19, 2012), <http://www.sec.gov/Archives/edgar/data/865570/000086557012000066/a12-19x128xk.htm> (last visited Apr. 8, 2013) (While the First Day Motion states that Clearlake was the stalking horse bidder, THQ's SEC filings indicate that Space Investors (clearly a shell entity controlled by Clearlake) would act as an affiliate).

¹⁶⁹ The Note provided that Space Investors would deliver to THQ a 7-year subordinated, unsecured note, payable by Space Investors to THQ's unsecured creditors, in the amount of \$10M, 2% interest, which did not require an earn-out provision.

¹⁷⁰ Declaration of Brian Farrell Paragraph 43.

¹⁷¹ Declaration of Brian Farrell Paragraph 44.

¹⁷² Declaration of Brian Farrell Paragraph 47.

¹⁷³ Proposed Asset Purchase Agreement Paragraph 7.5(a).

¹⁷⁴ Proposed Asset Purchase Agreement Paragraph 2.1(a).

THQ's assets meet certain bid requirements.¹⁷⁵ For example, a prospective bidder was required under the APA's procedures to submit bids to "the Committee," which included THQ and its counsel, DIP lenders (Wells Fargo and Clearlake), Centerview, and the Official Committee of Unsecured Creditors.¹⁷⁶ Additionally, bidders were required to provide other documentation including confidentiality agreements and proof of financial ability to "close the contemplated transaction and provide adequate assurance of future performance" of any successful bids for THQ's assets.¹⁷⁷ The APA also provided that bidders must seek to purchase *all* of THQ's assets on an "as is, where is" basis and free of any and all encumbrances.¹⁷⁸ Bidders who were deemed qualified under the agreement's terms were also permitted to credit bid their secured claims, if any, under Section 363(k) of the Code.¹⁷⁹

The auction was scheduled, pursuant to the bidding procedures of the APA, to take place on January 9, 2013 at the offices of THQ's counsel in New York, New York.¹⁸⁰ In the event that Space Investors, the Stalking Horse Bidder, was the only qualified bid, no auction would be held.¹⁸¹ At the auction itself, THQ and its counsel would conduct the auction.¹⁸² THQ would set the opening bid as the highest received bid prior to the auction, here the Stalking Horse Bid of \$2.75 million by Space Investors, and continue accepting bids in increments of \$500,000 thereafter (the overbid).¹⁸³ After all the bids were received, THQ would consult with the remaining members of the Committee and determine the winner of the auction by considering the "financial and contractual terms and the factors relevant to the sale process," and the bidder's

¹⁷⁵ Proposed Bidding Procedures Order Part II.

¹⁷⁶ Proposed Bidding Procedures Order Bid Deadline Paragraph.

¹⁷⁷ Proposed Bidding Procedures Order Participant Requirements Paragraph, Part d.

¹⁷⁸ Proposed Bidding Procedures Order Bid Requirements Paragraph, Part i; Proposed Bidding Procedures Order "As Is, Where Is" Paragraph ("The sale of the Assets shall be on an 'as is, where is' basis and without representations or warranties of any kind, nature, or description by the Debtors."); Proposed Bidding Procedures Order Free of Any and All Encumbrances Paragraph (the Assets "shall be sold free and clear of all pledges, liens, security interests, encumbrances, claims, charges, options, and interests thereon and there against . . .").

¹⁷⁹ Proposed Bidding Procedures Order Credit Bidding Paragraph; 11 U.S.C. § 363(k).

¹⁸⁰ Proposed Bidding Procedures Order Auction Paragraph (THQ's lead counsel, Gibson Dunn, is introduced in the subsequent section of this case study).

¹⁸¹ Proposed Bidding Procedures Order Auction Paragraph.

¹⁸² Proposed Bidding Procedures Order Auction Paragraph, Part b.

¹⁸³ Proposed Bidding Procedures Order Auction Paragraph, Part a; Proposed Bidding Procedures Order Auction Paragraph, Part c.

“highest, best, and/or otherwise financially superior offer” for THQ’s assets, which would bring the greatest value to its estate.¹⁸⁴

In any event, a sale hearing would take in the Bankruptcy Court in Wilmington, Delaware the following day to confirm the results of the auction.¹⁸⁵ The winner of the auction would then be required to consummate the sale no later than January 24, 2013.¹⁸⁶ If the winner of the auction failed to consummate the sale, THQ could then accept any lesser (a Back-up Bid) without notice or order from the Court.¹⁸⁷ Although THQ and Space Investors agreed upon these provisions, some details of the APA would later raise concerns among THQ’s creditors and the Court.

THQ Retains Counsel

Around the time the APA was executed, THQ entered into an engagement agreement with Young Conaway Stargatt & Taylor, LLP (Young Conaway).¹⁸⁸ Young Conaway would act as THQ’s counsel in all aspects of its chapter 11 restructuring and proposed asset sale with Clearlake.¹⁸⁹ At that time, THQ also sought to retain Gibson, Dunn & Crutcher, LLP (Gibson Dunn) to serve as lead counsel.¹⁹⁰

THQ would later file an application *nunc pro tunc*¹⁹¹ to the petition date because Young Conaway was retained prior to THQ’s bankruptcy filing, but did not gain the Court’s approval until over a month later.¹⁹² Much of the basis for that motion was supported by the declaration of Michael Nestor, lead counsel for Young Conaway on the THQ case.¹⁹³ Both THQ’s application and Nestor’s declaration provided that Young Conaway was an experienced firm

¹⁸⁴ Proposed Bidding Procedures Order Auction Paragraph, Part e.

¹⁸⁵ Proposed Bidding Procedures Order Sale Hearing Paragraph.

¹⁸⁶ Proposed Bidding Procedures Order Sale Hearing Paragraph.

¹⁸⁷ Proposed Bidding Procedures Order Sale Hearing Paragraph.

¹⁸⁸ THQ’s Application to Retain and Employ Counsel Paragraph 7.

¹⁸⁹ THQ’s Application to Retain and Employ Counsel.

¹⁹⁰ THQ’s Application to Retain and Employ Counsel Paragraph 8.

¹⁹¹ Translated to “Now for then,” and used to retroactively validate a party’s actions.

¹⁹² THQ’s Application to Retain and Employ Counsel.

¹⁹³ THQ’s Application to Retain and Employ Counsel Exhibit A.

with regard to bankruptcy and corporate restructuring and it had intimate knowledge of THQ's business and affairs.¹⁹⁴ Young Conaway would provide services at standard rates (e.g., \$675 per hour for Nestor's services down to \$185 per hour for a paralegal)¹⁹⁵ and received an initial retainer of \$100,000 in order to be paid for work completed in connection with preparing and filing THQ's first day motions and any post-filing representation of the company.¹⁹⁶

THQ Files for Bankruptcy

On December 19, 2012, THQ filed for chapter 11 bankruptcy.¹⁹⁷ The news came as no surprise to investors and industry analysts, who noted that the filing was "long anticipated."¹⁹⁸ Despite the bleak news, Farrell (publicly, at least) seemed optimistic that THQ's agreement with Clearlake would benefit the struggling videogame company. In a press release to investors, he stated that "[t]he sale and filing [we]re necessary next steps to complete THQ's transformation and position the company for the future, as we remain confident in our existing pipeline of games, the strength of our studios and THQ's deep bench of talent."¹⁹⁹ Rubin echoed this hopeful sentiment: "We look forward to partnering with experienced investors for a new start as we will continue to use our intellectual property assets to develop high-quality core games, create new franchise titles, and drive demand through both traditional and digital channels."²⁰⁰ Although Farrell and Rubin appeared hopeful that Clearlake would turn THQ around, they failed to disclose to investors or the public the (very real) possibility that the company could ultimately be dismantled, game by game.

¹⁹⁴ THQ's Application to Retain and Employ Counsel Paragraph 9.

¹⁹⁵ THQ's Application to Retain and Employ Counsel Paragraph 10.

¹⁹⁶ THQ's Application to Retain and Employ Counsel Paragraph 13.

¹⁹⁷ Declaration of Brian Farrell.

¹⁹⁸ Daniel Nye Griffiths, *THQ Files for Bankruptcy – Promises No Disruption*, FORBES (Dec. 19, 2012, 3:16 PM), <http://www.forbes.com/sites/danielnyegriffiths/2012/12/19/thq-files-for-bankruptcy-promises-no-disruption/> (last visited April 8, 2013).

¹⁹⁹ *THQ Inc. Secures Assets Purchase Agreement with Affiliates of Clearlake Capital Group, L.P.*, THQ INVESTOR RELATIONS (Dec. 19, 2012), <http://investor.thq.com/phoenix.zhtml?c=96376&p=iroNewsArticle> (last visited April 8, 2013).

²⁰⁰ *THQ Inc. Secures Assets Purchase Agreement with Affiliates of Clearlake Capital Group, L.P.*, THQ INVESTOR RELATIONS (Dec. 19, 2012), <http://investor.thq.com/phoenix.zhtml?c=96376&p=iroNewsArticle> (last visited April 8, 2013).

Clearly both Farrell and Rubin, along with Clearlake, felt that THQ was worth more alive than dead, but only time would tell; at the time of its filing, THQ's market capitalization had fallen to somewhere between \$11.3 and \$8.5 million, down from a high of \$2 billion just five years prior.²⁰¹ Despite the consistently positive spin, THQ's downward spiral was evident: its stock price had fallen 84% during 2012,²⁰² NASDAQ delisted its shares from the exchange,²⁰³ and at least one commentator questioned whether the company could successfully emerge from bankruptcy.²⁰⁴

Operations and First Day Motions

THQ, as debtor-in-possession²⁰⁵ pursuant to the Bankruptcy Code,²⁰⁶ filed several emergency petitions and requests for first day relief (the First Day Motions). Among them were motions for joint administration of the bankruptcy proceedings among THQ and its domestic subsidiaries, to maintain its bank and internal accounts, to pay critical vendors, to pay employee benefits, and to honor prepetition obligations under certain customer incentive programs. The underlying rationale of each motion was to preserve THQ as a going-concern in order to maximize its value during the bankruptcy and to achieve the highest value in the forthcoming 363 auction. The legal arguments contained in the First Day Motions were substantially the same: the "doctrine of necessity"²⁰⁷ empowered the Court to issue any order necessary to carry out the Code's purpose, i.e., to preserve and protect the value of corporations, with regard to

²⁰¹ Daniel Nye Griffiths, *THQ Files for Bankruptcy – Promises No Disruption*, FORBES (Dec. 19, 2012, 3:16 PM), <http://www.forbes.com/sites/danielnyegriffiths/2012/12/19/thq-files-for-bankruptcy-promises-no-disruption/> (last visited April 8, 2013); Ben Fritz, *THQ Files for Bankruptcy, will seek buyer*, L.A. TIMES (Dec. 19, 2012), <http://articles.latimes.com/2012/dec/19/entertainment/la-et-ct-thq-bankruptcy-20121219> (last visited April 8, 2013).

²⁰² Kristin Jones, *Game Maker THQ Files for Bankruptcy*, WALL ST. JOURNAL (Dec. 19, 2012, 2:45 PM), <http://online.wsj.com/article/SB10001424127887323277504578189612319581942.html> (last visited April 8, 2013).

²⁰³ *THQ Inc. Secures Assets Purchase Agreement with Affiliates of Clearlake Capital Group, L.P.*, THQ INVESTOR RELATIONS (Dec. 19, 2012), <http://investor.thq.com/phoenix.zhtml?c=96376&p=irolnewsArticle> (last visited April 8, 2013) (this in spite of THQ's July 2012 reverse stock split).

²⁰⁴ Brett Molina, *THQ files for Chapter 11 bankruptcy*, USA TODAY (Dec. 19, 2012, 3:15 PM), <http://www.usatoday.com/story/tech/gaming/2012/12/19/thq-files-for-bankruptcy/1780109/> (last visited April 8, 2013) ("It's going to be difficult for them to keep going as a viable publisher.").

²⁰⁵ See Declaration of Brian Farrell Paragraph.

²⁰⁶ 11 U.S.C. § 1101.

²⁰⁷ See 11 U.S.C. § 105(a); see, e.g., *In re Ionosphere Clubs, Inc.*, 98 B.R. 174 (Bankr. S.D.N.Y. 1989); *In re NVR L.P.*, 147 B.R. 126 (Bankr. E.D. Va. 1992); *In re Just for Feet, Inc.*, 242 B.R. 821 (D. Del. 1999).

maintaining THQ's operations during the chapter 11 process.²⁰⁸ Further, THQ consistently argued, and pointed to relevant authority, throughout its First Day Motions that the Court regularly sought to preserve a company's "going concern" value in chapter 11.²⁰⁹

THQ's Motion for Order Authorizing the Joint Administration of its Related Chapter 11 Cases

Given THQ's organizational structure, a threshold matter to be reached by the Court was the consolidation of the several chapter 11 cases into a single matter.²¹⁰ THQ moved, for procedural purposes, to combine the bankruptcy cases for itself, Volition, THQ Phoenix, THQ Wireless, and Vigil, as well as any later filed chapter 11 cases for THQ's foreign affiliates, as they may arise.²¹¹ THQ appealed to the Court's past precedence of consolidating interrelated bankruptcies between parent and subsidiaries,²¹² as well as notions of efficiency for both debtor and court, to save time, expense, and energy in duplicating efforts with respect to notices, motions, and orders among the many parties.²¹³ Further, THQ argued, no party would be prejudiced or negatively affected by the joint administration of the case, noting that THQ's creditors' rights to the respective estates of each consolidated party would not be substantively affected.²¹⁴ Accordingly, the Court granted such requested relief.²¹⁵

THQ's Motion for Order to Maintain Accounts

²⁰⁸ See Harvey R. Miller & Shai Y. Waisman, *Is Chapter 11 Bankrupt?*, 47 B.C.L. REV. 129, 129-30 (2005).

²⁰⁹ See, e.g., *In re Digital Domain Media Group, Inc.*, Case No. 12-12569 (Bankr. D. Del. Sept. 12, 2012); *In re Pemco World Air Servs., Inc.*, Case No. 12-10799 (Bankr. D. Del. Apr. 3, 2012); *In re Friendly Ice Cream Corp.*, Case No. 12-10799 (Bankr. D. Del. Oct. 6, 2011); *In re Neb. Book Co.*, Case No. 11-12005 (Bankr. Del. Jun. 28, 2011); *In re Ambassadors Int'l, Inc.*, Case No. 11-11022 (Bankr. D. Del. Apr. 5, 2011); *In re Am. Safety Razor Co.*, Case No. 10-12351 (Bankr. D. Del. Aug. 23, 2010); *In re Cooper-Standard Holdings, Inc.* Case No. 09-12743 (Bankr. D. Del. Aug. 5, 2009).

²¹⁰ 11 U.S.C. § 1015(b); Del. Bankr. Local Rule 1015-1.

²¹¹ Motion for Joint Administration Paragraph 4.

²¹² See, e.g., *In re Digital Doman Media Grp., Inc.* Case No. 12-12568 (Bankr. D. Del. Sept. 9, 2012); *In re Pemco World Air Servs., Inc.*, Case No. 12-10799 (Bankr. D. Del. Mar. 6, 2012); *In re Buffets Rests. Holdings, Inc.*, Case No. 12-10237 (Bankr. D. Del. Jan. 19, 2012); *In re AES E. Energy, L.P.*, Case No. 11-14138 (Bankr. D. Del. Jan. 4, 2012); *In re DSI Holdings, Inc.*, Case No. 11-11941 (Bankr. D. Del. Jun. 28, 2011); *In re Elec. Components Int'l, Inc.*, Case No. 10-11054 (Bankr. D. Del. Dec. 22, 2009).

²¹³ Motion for Joint Administration Paragraph 9-10.

²¹⁴ Motion for Joint Administration Paragraph 11.

²¹⁵ Order Approving THQ's Motion for Joint Administration.

THQ, as an ongoing concern, also sought to maintain its bank accounts and other related operational systems, specifically, the continued use of its cash management system, continued use of its existing business forms, the continued performance of intercompany transactions, and limited waivers for deposit and investment requirements under Section 345(b) of the Code.²¹⁶

As a mainstay of its business operations,²¹⁷ THQ utilized an integrated cash management system for the collection, management, and disbursement of funds. THQ used the system to create status reports on the location and amount of funds; track and control corporate funds; ensure cash availability; initiate prompt payment of corporate, employee, and vendor related expenses; reduce administrative costs; and move funds throughout the organization structure.²¹⁸ Moreover, THQ used the cash management system to disburse funds via debit transactions, wire transfers, automated clearing house transfers, and tangible checks.²¹⁹

THQ's cash management system was made up of numerous accounts at various financial institutions, including Union Bank, JP Morgan Chase Bank, N.A. (JP Morgan), and UBS Financial Services, Inc. (UBS).²²⁰ For over fourteen years, THQ maintained accounts with Union Bank.²²¹ The Union Bank accounts were principally used for depository and disbursement purposes, making them the primary bank accounts for the cash management system.²²² Another integral part of THQ's cash management system was its investment function, including money market accounts with Union Bank, UBS, and JP Morgan.²²³

²¹⁶ Motion to Maintain Accounts.

²¹⁷ Declaration of Brian Farrell Paragraph 59.

²¹⁸ Declaration of Brian Farrell Paragraph 55.

²¹⁹ Declaration of Brian Farrell Paragraph 57.

²²⁰ Declaration of Brian Farrell Paragraph 57.

²²¹ Declaration of Brian Farrell Paragraph 59.

²²² Declaration of Brian Farrell Paragraph 58(a), 102 (the key functions of the accounts were to collect cash receipts (Declaration of Brian Farrell Paragraph 58(a)(1)); disburse funds for employee payroll (Motion to Maintain Accounts Paragraph 9(c)); satisfy vendor invoices (Motion to Maintain Accounts Paragraph 9(c)(1)); maintain spending accounts (Motion to Maintain Accounts Paragraph 9(c)(3)); and to transfer funds between THQ and its subsidiaries (Motion to Maintain Accounts Paragraph 9(c)(4); Motion to Maintain Accounts Paragraph 14).

²²³ Declaration of Brian Farrell Paragraph 58(d); Motion to Maintain Accounts Paragraph 9(d)(1); Motion to Maintain Accounts Paragraph 9(d)(2).

Thus, to preserve its going-concern value, THQ would need access to its cash management system and related bank accounts, as it did prepetition, to continue with its day-to-day operations and ongoing financial obligations. THQ asserted in its motion that it was “vital . . . [to] maintain their Cash Management System . . .” as “integral to the Debtor’s business operations . . .” the disruption of which “jeopardizes the Debtor’s ability to continue operating long enough to complete a sale as a going concern and seamlessly pay employees . . .” To freeze the cash management system and related bank accounts would cause an immediate halt to THQ’s ability to effectively operate. The Court agreed and granted THQ’s motion.²²⁴

THQ’s Motion to Pay Critical Vendors

THQ also filed a motion to pay the claims of its critical vendors, arguing that its business required that it purchase certain goods and services from third-party vendors, namely videogame developers hired as contractors and other related professionals.²²⁵ Without continued payment to these vendors, THQ argued, it could not properly operate.²²⁶ To be considered “critical,” THQ submitted that a vendor must be either a vendor providing “unique and specific engineered goods or services crucial to the continued operation of THQ, or provide essential goods and services, for which replacement with alternative vendors would be prohibitively expensive due to lead time required by alternate vendors or alternative vendors’ remote geographic location.”²²⁷ In short, the very type of highly-skilled, rare, and expensive professionals used by THQ and other top videogame makers to develop, market, and sell its big titles.

In its motion, THQ identified certain vendors to its business considered critical.²²⁸ Those vendors included:

- *Product development vendors and service providers:* THQ hired many external videogame developers, programming specialists, animators, visual designers, audio production (voice talent, music, etc.).²²⁹

²²⁴ Order Approving THQ’s Motion to Maintain Accounts.

²²⁵ Motion to Pay Critical Trade Vendors.

²²⁶ Motion to Pay Critical Trade Vendors Paragraph 6.

²²⁷ Motion to Pay Critical Trade Vendors Paragraph 7.

²²⁸ Motion to Pay Critical Trade Vendors Paragraph 8.

²²⁹ Motion to Pay Critical Trade Vendors Paragraph 9-10.

- *Operational vendors and service providers:* THQ entered into license agreements with the various platform developers (e.g., Nintendo (Wii), Sony Computer Entertainment (Playstation), and Microsoft (Xbox)) to develop games that play on each platform; hired replicators (to digitally encode the games onto discs, assemble finished goods, and ship to retail customers and distribution centers); and used other third-party vendors to provide raw materials for game packaging and marketing displays.²³⁰
- *Marketing and Advertising service providers:* THQ relied on third-party marketing vendors to promote its games prior to their release, to create and maintain corporate and brand-specific websites, and to create and maintain its social media presence (Facebook, Twitter, etc.); it also relied on creators of promotional videos and trailers to market its videogames.²³¹

THQ estimated the cost due to its critical vendors was approximately \$6 million, accounting for both pre- and postpetition claims.²³²

THQ requested that the Court permit it to pay, at its discretion, the claims of any identified critical vendor to continue its business operations and maintain value in the company.²³³ The Court granted this motion.²³⁴

THQ's Motion to Pay Employee Benefits

THQ next sought to continue payments for its employees,²³⁵ which included the authority to pay the wages, salaries, other compensation, and taxes related to employee expenses (including salaried, hourly, and temporary employees, as well as independent contractors);²³⁶ pay

²³⁰ Motion to Pay Critical Trade Vendors Paragraph 11-12.

²³¹ Motion to Pay Critical Trade Vendors Paragraph 13-15.

²³² Motion to Pay Critical Trade Vendors Paragraph 17.

²³³ Motion to Pay Critical Trade Vendors Paragraph 20, 22; *see also* 11 U.S.C. § 105(a); *see, e.g., In re TC12 Holdings, LLC* 428 B.R. 117 (Bankr. D.N.J. 2010); *In re NVR L.P.* 147 B.R. 126 (E.D. Va. 1992); *In re Ionosphere Clubs, Inc.* 98 B.R. 174 (Bankr. S.D.N.Y. 1989). Accord Code Section 363(b)(1); *see, e.g., Official Comm. Of Unsecured Creditors of LTV Aerospace & Def. Co. v. LTV Co. (In re Chateaugay Corp.)*, 973 F.2d 141 (2d Cir. 1992); *In re Ionosphere Clubs, Inc.*, 100 B.R. 670 (Bankr. S.D.N.Y. 1989).

²³⁴ Order Approving THQ's Motion to Pay Critical Trade Vendors.

²³⁵ Motion to Pay Employee Benefits Paragraph 7.

²³⁶ Motion to Pay Employee Benefits Paragraph 12-21 (Also related to THQ's cash management system, because such compensation was automatically deposited to employees and contractors).

and honor both pre- and postpetition obligations relating to employee medical, insurance, sales bonus, and other benefit programs;²³⁷ and honor and process checks related to those obligations.²³⁸

THQ argued, successfully, that cause existed for the continued ability to pay compensation, benefits, and reimbursement for its employees.²³⁹ THQ asserted that its employees relied on such compensation for daily living expenses, health, and well-being.²⁴⁰ Additionally, and important for THQ's continued corporate existence, immediate termination of certain employees would result in the hemorrhaging of "unique" operational, management, and development talent, further hindering THQ's ability to preserve going-concern value and creditor confidence.²⁴¹ Lastly, THQ relied on certain statutory authority to compel the Court to grant its motion.²⁴² The Court granted the motion.²⁴³

THQ's Motion to Honor Prepetition Obligations under Customer Marketing Programs

Lastly,²⁴⁴ THQ sought to continue honoring its prepetition obligations under its customer marketing programs, including those related to mass merchandisers, consumer electronic stores,

²³⁷ Motion to Pay Employee Benefits Paragraph 22-59 (As previously discussed, some of THQ's programs included sales incentive bonus plan (yearly and quarterly benchmarks); product development profit sharing bonus plan (profitability thresholds for subsidiary development companies); employee benefit programs (prescription and medical benefits, dental care, vision care, basic life insurance, disability insurance, vacation and PTO plans, 401(k) plans)).

²³⁸ Motion to Pay Employee Benefits Paragraph 22-59.

²³⁹ Order Approving THQ's Motion to Pay Employee Benefits.

²⁴⁰ Motion to Pay Employee Benefits Paragraph 70.

²⁴¹ Motion to Pay Employee Benefits Paragraph 64.

²⁴² Motion to Pay Employee Benefits Paragraph 65-80; *see, e.g.*, 11 U.S.C. § 1129(a)(9)(B) (2012) (requiring payment of allowed unsecured claims for wages, salaries, and commissions); § 507(a)(4)(A) (granting priority treatment to employee claims for wages, salaries, or commissions for up to \$11,725); § 541 (requiring employer withholding and payment to governmental and taxing authorities); § 363(a) (permitting a debtor to pay prepetition obligations where a sound business purpose exists); §§ 1107(a), 1108 (permitting DIP to operate the business for the benefit of creditors and equity owners and preserve going-concern value, *see also* *In re CoServe, LLC*, 273 B.R. 487 (Bankr. N.D. Tex. 2002) establishing DIP's fiduciary duties to protect and preserve estate); Section 105(a) (the doctrine of necessity).

²⁴³ Order Approving THQ's Motion to Pay Employee Benefits.

²⁴⁴ THQ submitted additional first-day motions, but for the sake of brevity, this case study addresses only those identified herein.

discount warehouses, and other national retail stores.²⁴⁵ THQ engaged in these programs to drive sales, develop and maintain a positive reputation in the videogame and consumer industries, build customer loyalty, ensure customer satisfaction, meet competitive pressures,²⁴⁶ and generate goodwill for its brand.²⁴⁷ Moreover, such programs remain customary in the industry, and THQ's customers would expect (and rely) on such programs in the course of business.²⁴⁸ Some examples highlighted by THQ in its motion included:

- *Price protection credits*: THQ provided a credit to retailers who had purchased THQ's products at a higher price than later could be sold for as a result of decreased consumer demand.²⁴⁹
- *Cooperative advertising with retailers*: THQ and retailers cooperated to promote and advertise THQ's upcoming and recently released videogames, and in consideration, THQ credited retailers' invoices.²⁵⁰
- *Back-end rebates*: Retailers would sell THQ products at a reduced price for a short promotional period and THQ would fund the amount of the discount, which would be credited to the retailer after the product was actually purchased.²⁵¹
- *Defective product credits*: THQ accounted for the possibility that its product would be defective, which cost ordinarily would be borne by the retailer. In consideration, THQ provided a small credit to retailers.²⁵²
- *Freight rebates*: THQ reimbursed retailers for the cost of common carriers delivering its product.²⁵³

²⁴⁵ Motion to Honor Prepetition Obligations under Customer Marketing Programs.

²⁴⁶ This point truly cannot be overstated. THQ, as a player in the AAA world of videogame development (and one who was struggling, as discussed throughout this case study) could not afford to give less than other (better) companies.

²⁴⁷ Motion to Honor Prepetition Obligations under Customer Marketing Programs Paragraph 5.

²⁴⁸ Motion to Honor Prepetition Obligations under Customer Marketing Programs Paragraph 6.

²⁴⁹ Motion to Honor Prepetition Obligations under Customer Marketing Programs Paragraphs 7-8.

²⁵⁰ Motion to Honor Prepetition Obligations under Customer Marketing Programs Paragraph 9-10.

²⁵¹ Motion to Honor Prepetition Obligations under Customer Marketing Programs Paragraphs 11-12.

²⁵² Motion to Honor Prepetition Obligations under Customer Marketing Programs Paragraphs 13-14.

²⁵³ Motion to Honor Prepetition Obligations under Customer Marketing Programs Paragraph 15.

- *Miscellaneous rebates and credits:* THQ also offered certain discounts and credits to customers who, for example, wanted to trade out games that were at different price points.²⁵⁴

Arguing that these obligations were standard for the industry and necessary to maintain good retailer and customer relations, THQ asserted it must maintain its prepetition customer programs.²⁵⁵ One major point that THQ made was that without the credits, retailers and customers would instead turn to the company's major competitors, like EA, Ubisoft, or Activision, to get (essentially) the same product accompanied by more favorable programs.²⁵⁶ The Court accepted THQ's argument and granted its motion.²⁵⁷

Objections to the Sale

On January 2, 2013, just days after THQ asked the Court to allow the sale of the entire company to Clearlake Capital, several interested parties filed objections to the proposed 363 sale. The first and most important group that objected to the sale was the Official Committee of Unsecured Creditors (the "Committee").²⁵⁸ The Committee was comprised of a collection of note holders who together held roughly \$100 million in unsecured convertible notes, as well as three of the largest trade creditors.²⁵⁹ The Committee's reason for opposing the sale is unsurprising; they stood to lose essentially everything in the sale plan. According to the terms of the proposed sale, nearly all of the roughly \$60 million purchase price by Clearlake would be

²⁵⁴ Motion to Honor Prepetition Obligations under Customer Marketing Programs Paragraph 16.

²⁵⁵ Motion to Honor Prepetition Obligations under Customer Marketing Programs Paragraph 27.

²⁵⁶ Motion to Honor Prepetition Obligations under Customer Marketing Programs Paragraph 27.

²⁵⁷ Order Approving THQ's Motion to Honor Prepetition Obligations under Customer Marketing Programs.

²⁵⁸ Based on the expedited sale date requested in the motion, the note holders felt it best to form an immediate ad hoc group of 3 of the convertible note holders in order to promptly object to the sale. These three note holders, Silverback Asset Management, Third Avenue Focused Credit Fund, and Wolverine Flagship Fund, collectively held 41% of the principal amount of the convertible notes. Eventually, when the full collection of note holders could successfully form the Official Committee of Unsecured Creditors (the "Committee"), they would issue a separate objection on behalf of the Committee. The Committee, made up of the holders of the convertible notes and certain other trade creditors, was eventually formed on January 3, 2013. They filed their own objection to the sale on January 3, 2013, which was a verbatim copy of the objection filed by the Ad Hoc Committee of Convertible Noteholders.

²⁵⁹ Members of the Official Committee of Unsecured Creditors. The committee was formed on January 3, 2012 and was represented by Landis Rath & Cobb LLP and Andrews Kurth LLP.

used to pay off Wells Fargo, first paying its large secured claim and then paying the DIP credit facility.²⁶⁰ The only consideration paid to the Committee would be a \$10 million unsecured note executed by Clearlake with a maturation date of 2020 and an interest rate of only 2%.²⁶¹ Under this plan, the Committee would receive an estimated 1-3% of their unsecured claim.²⁶² Needless to say, the Committee was not happy with the proposed sale.

The United States Trustee for the region also raised an objection to the proposed sale. The Office of the U.S. Trustee is a division of the Department of Justice tasked with oversight of the national bankruptcy system.²⁶³ The office dispatches officers, known as United States Trustees, to investigate potential fraud and abuse in bankruptcy cases.²⁶⁴ Because bankruptcy is designed to effectuate an orderly distribution of assets to a debtor's creditors, a U.S. Trustee will generally object when he feels that, due to an insider relationship, a debtor is taking a particular action to the detriment of his unsecured creditors.²⁶⁵ Because of this responsibility to protect the interests of unsecured creditors, the U.S. Trustee often has the same interests as the Committee and will object when he feels their rights are threatened.

While sales under Section 363 generally do not provide the unsecured creditors with much of a return on their claim, the sales must nonetheless be fair and equitable to all parties involved.²⁶⁶ However, this sale, according to the Committee and the U.S. Trustee, was anything but fair and equitable.²⁶⁷ In its objection, the U.S. Trustee focused on the expedited timing and the allegedly excessive breakup fee required by the Asset Purchase Agreement in the debtor's 363 sale motion.²⁶⁸ The Committee similarly objected to the expedited timing, but focused the bulk of their objection on the non-piecemeal bidding process required under the sale motion.

²⁶⁰ Objection by the Ad Hoc Committee of Convertible Noteholders Paragraph 2; Objection by the Official Committee of Unsecured Creditors Paragraph 2.

²⁶¹ Objection by the Ad Hoc Committee of Convertible Noteholders Paragraph 20; Objection by the Official Committee of Unsecured Creditors Paragraph 20.

²⁶² Objection by the Ad Hoc Committee of Convertible Noteholders Paragraph 20; Objection by the Official Committee of Unsecured Creditors Paragraph 20.

²⁶³ George W. Kuney et al., CHAPTER 11-101: THE NUTS AND BOLTS OF CHAPTER 11 PRACTICE: A PRIMER 20 (2007).

²⁶⁴ *Id.*

²⁶⁵ *Id.*

²⁶⁶ *Id.* at 232.

²⁶⁷ Objection by the Official Committee of Unsecured Creditors; Objection by the United States Trustee.

²⁶⁸ Objection by the United States Trustee.

Objection to the Expedited Timing

The Committee and the U.S. Trustee each objected to the expedited timeline for the proposed sale, alleging that it would chill competitive bidding and thus unfairly hurt the unsecured creditors.²⁶⁹ THQ filed its motion requesting the going-concern sale on December 19, 2012. Pursuant to the initially submitted APA, prospective bidders were required to submit bids by January 8, 2013 with an auction to take place on January 9, 2013, and a final sale hearing on January 10, 2013.²⁷⁰ However, the Court did not set the hearing date for approval of the sale, including the bidding procedures, until January 4, 2013.²⁷¹ Thus, once all prospective bidders knew the rules of the auction, they would have only four days to perform sufficient due diligence to determine if they wanted to bid.²⁷² Furthermore, because the timing fell within the holiday season, the Committee alleged that any potential bidders would likely be unavailable and thus fail to submit a bid.²⁷³ This deadline, according to the Committee and the U.S. Trustee, would prevent competitive bidding and assure that Clearlake would be the ultimate purchaser under the terms of the APA, much to the detriment of the unsecured creditors, and thus, it was unfair and unreasonable.²⁷⁴

Objection to the Breakup Fee

The U.S. Trustee next targeted the proposed breakup fee in the sale motion.²⁷⁵ In a typical chapter 11 sale of assets outside the ordinary course of business, the stalking horse bidder submits the initial bid to set the floor for other bidders. Accordingly, the stalking horse bidder performs a substantial amount of due diligence to discover the value of the assets, or, as in this case the value of the entire company, before submitting its initial bid. Other bidders, however, can avoid much of this cost by simply relying on the due diligence of the stalking horse bidder. Courts have recognized the disadvantageous position of the stalking horse bidder, and so to protect it, they allow it to require in its asset purchase agreement that, if it is not ultimately the

²⁶⁹ Objection by the United States Trustee, Objection by the Official Committee of Unsecured Creditors.

²⁷⁰ Objection by the United States Trustee Paragraph 7; Objection by the Official Committee of Unsecured Creditors Paragraph 29.

²⁷¹ Objection by the United States Trustee Paragraph 7.

²⁷² Objection by the United States Trustee; Objection by the Official Committee of Unsecured Creditors.

²⁷³ Objection by the Official Committee of Unsecured Creditors Paragraph 30.

²⁷⁴ Objection by the United States Trustee; Objection by the Official Committee of Unsecured Creditors.

²⁷⁵ Objection by the United States Trustee.

winner at the auction, the winner must pay it a “breakup fee.”²⁷⁶ Courts will additionally allow the stalking horse bidder to set a minimum overbid requirement so long as the amount is not unfair or unreasonable.²⁷⁷

In THQ’s proposed sale to Clearlake, the asset purchase agreement included a breakup fee of \$1.75 million and a \$50,000 expense reimbursement.²⁷⁸ Thus, assuming Clearlake was not the winning bidder, the winner would have to pay Clearlake \$2.25 million in addition to their bid amount.²⁷⁹ THQ asserted that a 1-3% breakup fee is appropriate in sales of assets under Section 363(f).²⁸⁰ To comply with this standard, THQ alleged that the fee should be measured against the total amount of consideration to be paid by Clearlake under the APA. Here, Clearlake was to pay a total of roughly \$60 million. Thus, as a percentage of the total purchase price, Clearlake’s requested breakup fee was less than 3% and therefore reasonable.

The U.S. Trustee disagreed with the calculation used by THQ in its sale motion.²⁸¹ Rather than using the total consideration offered in the sale motion, the U.S. Trustee argued that the breakup fee must be measured against only the *cash component* of the sale.²⁸² By using the cash component, \$29 million to satisfy the DIP credit facility and \$6.65 million in additional cash, the breakup fee totaled over 6% of the cash component and was therefore unreasonable.

Objection to the Non-Piecemeal Sale

While the Committee objected to several features of the proposed sale under the initial APA, its strongest objection focused on the debtor’s requirement that the auction only allow bids for the entire company. Under the proposed sale to Clearlake, competing bidders had to submit “qualified bids” for the bid to be considered. According to the APA, a qualified bid required a

²⁷⁶ Kuney, *supra* note 263, at 231.

²⁷⁷ *Id.* at 425.

²⁷⁸ THQ’s Motion for the Sale of Substantially All of its Assets Paragraph 51.

²⁷⁹ THQ’s Motion for the Sale of Substantially All of its Assets Paragraph 51.

²⁸⁰ THQ’s Motion for the Sale of Substantially All of its Assets Paragraph 102.

²⁸¹ Objection by the United States Trustee.

²⁸² Objection by the United States Trustee Paragraph 11 (citing *Calpine Corp. v. O’Brien Env’tl. Energy, Inc.* (In re O’Brien Env’tl. Energy, Inc.), 181 F.2d 527 (3d Cir. 1999) (The amount of the bid protections is excessive when measured against the cash component of the purchase price and does not represent the “actual, necessary” cost of preserving the Debtors’ estate.)).

competing bidder to bid for *all* of THQ's assets; it could not bid for one or several properties without taking the whole lot.²⁸³

This outcome was certainly preferable to THQ. If a buyer had to purchase THQ in its entirety, it would likely wish to rehire the current THQ management and employees to continue operations. By wiping out the liability owed to the note holders, THQ believed that it could regain profitability with relatively few changes to its organizational structure and its relationships with its customers and vendors.²⁸⁴

THQ made this goal clear in a press release posted on its website on December 19, 2012, the same day it filed chapter 11.²⁸⁵ In this release, Rubin explained that Clearlake would purchase all of THQ through a chapter 11 bankruptcy.²⁸⁶ He reassured the public at large that the bankruptcy did not mean the end of THQ, as Clearlake would purchase the entire company and will fund the production of all titles currently in development. Specifically, he states, "Rest assured that the goal throughout this sale process has been to preserve our teams and products Whatever happens, the teams and products look likely to end up together and in good hands." By structuring the APA's bid procedures in such a way that a potential buyer could not bid unless it agreed to purchase all of THQ's assets, THQ could more easily resume operations without substantial changes to its management.

While this may have been great for THQ, it was not the best option for the unsecured creditors. THQ was the sole owner of several different studios, each tasked with producing one or more game franchises. Each of these studios produced a different type of game. For example, Relic was established solely for the creation of *Company of Heroes*, a military-strategy game set

²⁸³ Proposed Bidding Procedures for the Sale of Substantially All of the Debtor's Assets. ("Each Bid must provide for the purchase of all or a substantial portion of the Assets and payment or assumption of all or a substantial portion of the liabilities to be paid or assumed under the Stalking Horse Agreement").

²⁸⁴ This was, in fact, specifically the goal of the sale to Clearlake. The Committee alleged that THQ had engineered the entire sale process to Clearlake to ensure that the key employees and management could retain their jobs, yet had made scant reference to this arrangement in their sale motion. Pursuant to Local Rule 6004, the debtor must include this information in the Bidding Procedures Motion. The Committee alleged that, by failing to disclose this information, THQ was not only in violation of the Local Rules, but also failing to act in the best interest of creditors. As a result, it requested that the sale not be approved as constructed in the debtors' motion.

²⁸⁵ *THQ Community Message From Jason Rubin*, THQ INVESTOR RELATIONS (Dec. 19, 2012), http://www.thq.com/us/go/article/view/homepage_article/261277/thq_community_message_from_jason_rubin (last visited April 23, 2013).

²⁸⁶ *THQ Community Message From Jason Rubin*, THQ INVESTOR RELATIONS (Dec. 19, 2012), http://www.thq.com/us/go/article/view/homepage_article/261277/thq_community_message_from_jason_rubin (last visited April 23, 2013).

during World War II. This contrasted with another other development subsidiary, Volition, which exclusively developed the *Saints Row* franchise, an action game about gang conflict. These two studios make completely different types of games. According to the Committee, a piecemeal sale of each studio would enable other developers to strategically pick certain game studios instead of being forced to purchase all of them in a going concern sale.²⁸⁷ This piecemeal sale approach would, according to the Committee, yield a much higher auction result than a forced going concern sale.²⁸⁸

The Committee's argument was logical. The likely purchasers of the several studios would be other large videogame developers. After all, the games made by each THQ subsidiary studio had an established fan base with several obtaining critical acclaim. A studio without a similar title would certainly be interested in bidding on the subsidiary. However, if a studio had a similar title to just one of THQ's many games, and yet it had to bid for all of THQ's assets in the auction, it would necessarily own duplicative titles if it won the auction. This result would alone discourage competitive bidding. For example, a studio may wish to add *Saints Row* to its collection of properties, but if it already develops its own military strategy game, it will not want to also purchase *Company of Heroes*. The requirement that all bidders bid for the entire company would certainly chill bidding to the detriment of the unsecured creditors.

Court Approves the Auction, But Not Before Making Certain Modifications to the Bidding Procedures

On January 11, 2013, the Bankruptcy Court approved THQ's motion for a sale of its assets under Section 363 of the Code.²⁸⁹ However, acknowledging the concerns of the United States Trustee and the Committee in their respective objections, it made certain changes to the proposed order.

First, the Court addressed the disputed bidding procedures.²⁹⁰ Recognizing the high breakup fee relative to the sale's cash component, the Court ordered that the fee be lowered from \$1.75 million to \$1 million.²⁹¹ This adjustment lowered the ratio of the breakup fee to the cash component to 2-3%, which was, according to the Court, a more fair and reasonable amount.

²⁸⁷ Objection by the Official Committee of Unsecured Creditors Paragraph 32.

²⁸⁸ Objection by the Official Committee of Unsecured Creditors Paragraph 32.

²⁸⁹ Order Approving the Sale of Substantially All of the Debtor's Assets.

²⁹⁰ Order Approving the Sale of Substantially All of the Debtor's Assets Paragraph A; Bidding Procedures for the Sale of Substantially All of the Debtor's Assets.

²⁹¹ Order Approving the Sale of Substantially All of the Debtor's Assets Paragraph B.

Next, the Court adjusted the sale date. Both the United States Trustee and the Committee had objected to the expedited time for the sale, which was to occur only four days after the hearing on the bidding procedures motion.²⁹² Recognizing the need for a quick sale, but still wanting to provide potential bidders with adequate time to conduct the required due diligence, the Court ordered that the sale hearing would be pushed to January 23, 2013.²⁹³ On this date, the Court would award all of the assets to the stalking horse bidder, Clearlake, or any higher bidding party at the auction.²⁹⁴ Any party who objected to the sale would be required to file their objection on January 18, and any reply by THQ would be due on January 21.²⁹⁵ Finally, the Court set the deadline for bidding on January 22 at 9:30 a.m. with the auction to actually take place later that afternoon at 3:00 p.m.²⁹⁶ However, if THQ did not receive any bids other than Clearlake's stalking horse bid, the Court would not hold an auction; Clearlake would simply take the assets at their bid price.²⁹⁷

Finally, much to the dismay of Clearlake and THQ, the Court adjusted the bidding procedures to allow piecemeal bidding.²⁹⁸ In THQ's sale motion, the initial APA defined a "Qualified Bid" as one that included a bid for all or substantially all the assets.²⁹⁹ Thus, pursuant to their requested sale procedures, only buyers of the entire company could actually bid at the auction.³⁰⁰ However, in the bidding procedures, attached as Exhibit 1 to the sale order, the Court defines a "Qualified Bidder" as one who bids for either "all or substantially all of the Debtors' Assets or *any part of the Debtors' Assets (a 'Piecemeal Bid')*."³⁰¹ The order further explains that if the Debtors receive Piecemeal Bids from Qualified Bidders, and such bids, *in the aggregate*,

²⁹² See *supra* note 270 and accompanying text.

²⁹³ Order Approving the Sale of Substantially All of the Debtor's Assets Paragraph 3.

²⁹⁴ Order Approving the Sale of Substantially All of the Debtor's Assets Paragraph 3.

²⁹⁵ Order Approving the Sale of Substantially All of the Debtor's Assets Paragraph 4.

²⁹⁶ Order Approving the Sale of Substantially All of the Debtor's Assets Paragraph 6.

²⁹⁷ Order Approving the Sale of Substantially All of the Debtor's Assets Paragraph 9.

²⁹⁸ Bidding Procedures for the Sale of Substantially All of the Debtor's Assets.

²⁹⁹ THQ's Motion for the Sale of Substantially All of its Assets.

³⁰⁰ THQ's Motion for the Sale of Substantially All of its Assets.

³⁰¹ Bidding Procedures for the Sale of Substantially All of the Debtor's Assets.

would result in greater value to the estate than under Clearlake's stalking horse bid, the assets shall be sold to the various Piecemeal Bidders.³⁰²

The Auction Concludes

Pursuant to the sale order, the auction for the sale of substantially all of THQ's assets occurred on January 22 and 23, 2013.³⁰³ However, because of the Court's allowance of piecemeal bidding for the assets, Clearlake was not the final purchaser. Instead, confirming the belief held by the Committee in its objection, the piecemeal sale encouraged diverse bidding from competing studios, leading to an aggregate sale price in excess of Clearlake's Stalking Horse Bid.³⁰⁴ The results of the auction were as follows:³⁰⁵

1. Relic, whose assets were held primarily for the marketing, development, and sale of the *Company of Heroes* franchise, sold to Sega Corporation for \$26.6 million.³⁰⁶
2. THQ Montreal, whose assets were held primarily for the marketing, development, and sale of the *1666* and *Underdog* franchises, sold to Ubisoft LLC for \$2.5 million.³⁰⁷
3. The assets held primarily for the marketing, development, and sale of *Evolve* sold to Take-Two Interactive Software, Inc. for approximately \$10.9 million.³⁰⁸

³⁰² Bidding Procedures for the Sale of Substantially All of the Debtor's Assets.

³⁰³ Notice of Auction Results.

³⁰⁴ Notice of Auction Results.

³⁰⁵ Notice of Auction Results Exhibit A: THQ, Inc., et al. Auction Summary: January 22-23, 2013.

³⁰⁶ COMPANY OF HEROES, <http://www.relic.com/games/company-of-heroes/> (last visited April 8, 2013) (*Company of Heroes* is a "real-time strategy" game set in World War II Europe. While the original game was released over six years ago, Relic was engaged in the development of *Company of Heroes 2* when it sold its assets to Sega. Sega's expected release date of *Company of Heroes 2* is June 25, 2013).

³⁰⁷ Christopher Dring, *Ubisoft acquires new THQ Montreal IP 1666*, DEVELOP-ONLINE (Jan. 24, 2013), <http://www.develop-online.net/news/43064/Ubisoft-acquires-new-THQ-Montreal-IP-1666> (last visited April 23, 2013) (Little is known about the *1666* game, but industry insiders speculate that the game will be a historical action game focused on the Great Fire of London, which occurred in 1666).

³⁰⁸ Jeffrey Grubb, *Turtle Rock Studios outbid for its own game: Take 2 thinks it's worth \$11M*, VENTUREBEAT (Jan. 23, 2013, 1:13PM), <http://venturebeat.com/2013/01/23/thq-auction-turtle-rock-evolve-11-million/> (last visited April 23, 2013) (Like *1666*, nothing is known about *Evolve*, as it was in the beginning stages of development when Take-Two purchased it at the auction. According to industry authors, based on Take-Two's history of spending large sums of money to develop games as well as the over \$10 million purchase price, *Evolve* should command high sales forecasts).

4. Volition, whose assets were held primarily for the marketing, development, and sale of the *Saints Row* franchise, sold to Koch Media GmbH for in excess of \$22 million.³⁰⁹
5. The assets held primarily for the marketing, development, and sale of the *Homefront* franchise sold to Crytek GmbH for \$544,218.³¹⁰
6. The assets held primarily for the marketing, development, and sale of *Metro 2033* and *Metro 2034* sold to Koch Media GmbH for over \$5.8 million.³¹¹
7. The assets held primarily for the marketing, development, and sale of *South Park: The Stick of Truth* sold to Ubisoft LLC for over \$3.2 million.³¹²

Two other studios, Vigil and THQ Agoura Hills, were not sold in the auction.³¹³

Just like that, THQ's dreams of a going concern sale, complete with protections for management and development teams, were gone. Instead of THQ simply ridding itself of the debt held by the unsecured note holders and continuing operations, it sold its assets to competitors, costing management and certain employees their jobs.

While Jason Rubin had expressed his belief that THQ would remain intact following the sale in his press release,³¹⁴ he was forced to tell his employees the hard truth in a letter that

³⁰⁹ SAINT'S ROW, <http://www.saintsrow.com/> (last visited April 8, 2013) (*Saints Row* is an open-world-action-adventure game focused around gang activity in a fictional city. Koch Media, the purchaser of the assets used to develop *Saints Row*, plans to release the fourth installment of the game through its subsidiary, Deep Silver, on August 20, 2013).

³¹⁰ HOMEFRONT, <http://www.ign.com/games/homefront-2/pc-118311> (last visited April 8, 2013) (*Homefront* is a first-person shooter game focused on a fictional invasion of the United States by North Korea. Following its purchase of the *Homefront* assets, Crytek is expected to release a sequel, *Homefront 2*, sometime in 2013).

³¹¹ METRO, <http://www.ign.com/games/metro-last-light/pc-79464> (last visited April 23, 2013) (The *Metro* series is a futuristic, post-apocalyptic first-person shooter game. Koch Media, the purchaser of the *Metro* assets, expects to release *Metro: Last Light* through its subsidiary, Deep Silver, on May 14, 2013).

³¹² SOUTH PARK: THE STICK OF TRUTH, <http://www.ign.com/games/south-park-the-game/ps3-123757> (last visited April 23, 2013) (*South Park: The Stick of Truth* is a role playing game set in the fictional South Park universe. Its purchaser in the auction, Ubisoft LLC, expects to release the game sometime in 2013).

³¹³ Notice of Auction Results; THQ's Motion to Allow a Settlement with the Terminated Employees.

followed the sale.³¹⁵ Specifically, when explaining the employment situation to his former employees, Mr. Rubin stated: “[W]e cannot say what these owners may intend, and there will likely be some positions that will not be needed under the new ownership. . . . If you are an employee of an entity that is not included in the sale, we regret to inform you that your position will end.”³¹⁶

This result, unfortunate as it may be for THQ’s management and employees, reflects the underlying purpose of asset sales under Section 363: to maximize the value of the bankruptcy estate for the benefit of the creditors. By permitting a piecemeal sale, the estate amassed \$12 million more than it would have under the Stalking Horse Bid, allowing a higher yield to the unsecured note holders.³¹⁷

Post-Auction Events

Assumption and Assignment of the Related Executory Contracts

Following the sale, each purchaser listed the contract rights related to its purchase that it wished to acquire as was required under the sale order.³¹⁸ This process of buying and selling rights to executory contracts is a standard practice under the Bankruptcy Code, whether the debtor is reorganizing or selling its assets.³¹⁹ A debtor first decides if it wants to reject or assume each of its executory contracts. If a debtor rejects a contract, any damages suffered by the non-debtor as a result of the rejection shall be treated as a prepetition unsecured claim.³²⁰ However, if the contract is valuable to the debtor, either for its own operations or for its market value, the

³¹⁴ *THQ Community Message From Jason Rubin*, THQ INVESTOR RELATIONS (Dec. 19, 2012), http://www.thq.com/us/go/article/view/homepage_article/261277/thq_community_message_from_jason_rubin (last visited April 23, 2013).

³¹⁵ Jason Schreier, *THQ Is No More. Here’s The Letter The CEO Sent Employees Today*, Kotaku (Jan. 23, 2013, 3:06PM), <http://kotaku.com/5978429/this-is-the-letter-that-thq-sent-to-employees-today> (last visited April 23, 2013).

³¹⁶ Jason Schreier, *THQ Is No More. Here’s The Letter The CEO Sent Employees Today*, Kotaku (Jan. 23, 2013, 3:06PM), <http://kotaku.com/5978429/this-is-the-letter-that-thq-sent-to-employees-today> (last visited April 23, 2013).

³¹⁷ Notice of Auction Results.

³¹⁸ Order Approving the Sale of Substantially All of the Debtor’s Assets Paragraph 14; Bidding Procedures for the Sale of Substantially All of the Debtor’s Assets.

³¹⁹ 11 U.S.C. § 365(f).

³²⁰ 11 U.S.C. § 365(g).

debtor may assume the contract.³²¹ This requires the debtor to cure any defaults, compensate the non-debtor party for any pecuniary loss suffered from the defaults, and provide adequate assurances to the non-debtor party that it will not default again in the future.³²² Once a debtor successfully assumes a contract, it may, if it desires, assign the contract to any other party notwithstanding any “anti-assignment” provision in the underlying agreement, assuming the assignee also provides the non-debtor party with assurances of future compliance.³²³

The assignment of executory contracts to the various buyers was an instrumental part of the asset sale under 363. Under the revised APA in the Sale Order, which dictated the various THQ assets to be sold at the auction, each Qualified Bidder was required to identify which contracts that it wished to take via assignment as a part of its asset purchase.³²⁴ These contracts were critical to each bidder’s asset acquisition, as many of the game studios relied upon certain software and intellectual property licenses to actually produce the games. Thus, in order for each purchaser to successfully continue development of the games after their respective asset purchases, each purchaser listed each executory contract that it wanted to assume. This would allow THQ to properly assume and assign each relevant contract to each buyer.

This process was not uncontested, however. Prior to the sale, THQ filed and distributed a notice of all of its executory contracts to each of the non-debtor parties to each contract.³²⁵ This notice contained the estimated cure amount for each contract in anticipation of the contracts’ assumption and assignment to the ultimate purchaser of the THQ assets. Finding this estimated cure amount insufficient, several of the non-debtor parties filed objections to the assignment of their contracts.³²⁶ Specifically, they alleged that THQ failed to provide a sufficient payment to cure the defaults under the contract and failed to provide adequate assurances of future compliance, both prerequisites to assumption under Section 365.³²⁷

³²¹ 11 U.S.C. § 365(f).

³²² 11 U.S.C. § 365(b).

³²³ 11 U.S.C. § 365(f).

³²⁴ Order Approving the Sale of Substantially All of the Debtor’s Assets Paragraph 14, Section b.

³²⁵ Notice of Auction Results.

³²⁶ Objection and Reservation of Rights of Pipeworks Software (Each of the other non-debtor parties to THQ’s executory contracts filed nearly identical objections).

³²⁷ THQ’s Response to the Objections of the Non-Debtor Parties to the Executory Contracts (Pursuant to 11 U.S.C. § 365(b), all contracts to be assigned must first be assumed, and to assume a contract, the debtor must cure all defaults under the contract.).

In response, because each objection was so similar, THQ filed one omnibus reply covering each objection.³²⁸ However, rather than explain why the estimated cure amount was accurate, THQ instead simply stated either that the contract would not be assumed or that any dispute would be worked out before the sale, likely an insufficient answer for the non-debtor parties to the contracts.³²⁹

The Court ultimately overruled the objections raised by the non-debtor parties.³³⁰ Each of the Court's sale orders to the respective asset purchasers included a section detailing the treatment of each contract that each buyer wished to purchase. In these sections, the Court ordered that each contract be assigned so long as the purchaser paid the "Determined Cure Cost" as defined in the respective asset purchase agreements for each asset sale (the Auction Asset Purchase Agreements).³³¹ Thus, pursuant to the respective sale order and the terms of each Auction Asset Purchase Agreement, each purchaser simply picked which contracts it wanted as a part of its asset purchase, paid the required cure amount, and obtained rights to the contract, notwithstanding the objections of the non-debtor parties.

In addition to the intellectual property contracts, THQ also had to deal with its real property leases. THQ was no longer engaged in the business of videogame development, and most of its offices had been vacated. Because the leases were generating unnecessary administrative expenses each month, THQ made the decision to reject its real property leases under Section 365(a), filing a motion requesting such relief on January 31, 2013.³³² In its motion, THQ indicated three large office space leases that it wished to reject: its leased offices in Champaign, Illinois (the "Champaign Lease"), New York City (the "New York Lease"), and Huixquilucan, Mexico (the "Mexico Lease").³³³ However, while THQ was able to reject the

³²⁸ THQ's Response to the Objections of the Non-Debtor Parties to the Executory Contracts.

³²⁹ THQ's Response to the Objections of the Non-Debtor Parties to the Executory Contracts.

³³⁰ Order Approving the Sale of Substantially All of the Debtor's Assets.

³³¹ Asset Purchase Agreement for the *Evolve Assets* Section 2.5 (Each of the seven asset sales had a separate sale order and asset purchase agreement that provided for, among other things, the executory contracts to be assigned to each purchaser. The Asset Purchase Agreement for the *Evolve Assets* is substantially similar to the Asset Purchase Agreements for the other assets purchased in the sale).

³³² THQ's Motion to Reject Certain Unexpired Non-Residential Real Property Leases; THQ's Second Motion to Reject Certain Unexpired Non-Residential Real Property Leases.

³³³ THQ's Motion to Reject Certain Unexpired Non-Residential Real Property Leases; THQ's Second Motion to Reject Certain Unexpired Non-Residential Real Property Leases.

New York Lease and the Mexico Lease without issue,³³⁴ it ran into trouble with its attempted rejection of the Champaign Lease.³³⁵

The controversy around the Champaign Lease was due primarily to the presence of a subtenant who refused to leave the leased premises.³³⁶ The basic facts are as follows. THQ entered into the Champaign Lease with Church Street Square, LLC (CSS), the lessor, on November 16, 2007.³³⁷ This lease included a six and a half year term, beginning on January 1, 2008 and ending on May 31, 2014.³³⁸ On April 1, 2011, THQ subleased the Champaign Lease to 004 Technologies USA Inc. (004) following CSS's written consent to the sublease as required by the Champaign Lease.³³⁹ As of the date of rejection by THQ, January 31, 2013, 004 had not relinquished the leased property back to CSS; rather, it continued to occupy and conduct business on the premises.³⁴⁰

The issue created by 004's continued occupation is the treatment of the rental payments as a prepetition breach or an administrative expense. Pursuant to Section 365, a rejected non-residential real property lease shall be treated as a prepetition breach, entitling the lessor to a prepetition claim for the lost rent subject to certain limitations.³⁴¹ However, until the lessee properly rejects such lease, the lessor must continue to perform pursuant to the lease terms. If the debtor lessee later rejects the lease, the lessor will be entitled to administrative expense priority for all expenses incurred between the petition date and the date of rejection.³⁴² THQ argued that the date of rejection should be January 31, 2013, the date it filed its motion to reject

³³⁴ Order Authorizing Rejection of Certain Unexpired Non-Residential Real Property Leases.

³³⁵ Objection by Church Street Square, LLC to THQ's Second Motion to Reject Certain Unexpired Non-Residential Real Property Leases.

³³⁶ Objection by Church Street Square, LLC to THQ's Second Motion to Reject Certain Unexpired Non-Residential Real Property Leases.

³³⁷ Objection by Church Street Square, LLC to THQ's Second Motion to Reject Certain Unexpired Non-Residential Real Property Leases Paragraph 2.

³³⁸ Church Street Square, LLC Lease Section 3.

³³⁹ Objection by Church Street Square, LLC to THQ's Second Motion to Reject Certain Unexpired Non-Residential Real Property Leases Paragraph 4.

³⁴⁰ Objection by Church Street Square, LLC to THQ's Second Motion to Reject Certain Unexpired Non-Residential Real Property Leases Paragraph 8.

³⁴¹ 11 U.S.C. § 365(g), § 502(b)(6).

³⁴² 11 U.S.C. § 503(b)(1)(A).

the Champaign Lease.³⁴³ CSS on the other hand contended that the date of rejection should be the date that 004 vacated the leased premises, which was expected to be May 15, 2013, the date of termination on the sublease.³⁴⁴ Because THQ was liable for rent payments on the sublease,³⁴⁵ CSS requested that all rent obligations due from the petition date to May 15, 2013 be treated as administrative expenses.

The Court resolved the issue once and for all on February 19, 2013.³⁴⁶ Siding with THQ, the Court determined that the date of rejection would be January 31, 2013, and CSS would not be entitled to any administrative expenses for unpaid rent after that date regardless of 004's continued occupation of the leased premises.³⁴⁷ However, in consideration of the damages suffered by CSS, the Court ordered THQ to pay CSS \$22,400.³⁴⁸ Following this ruling, THQ had properly rejected nearly all of its real property office leases. It next turned its attention to wrapping up the rest of the loose ends remaining following the sale of its assets at the auction.

The Closing of Vigil and THQ Agoura Hills

While THQ successfully sold most of its valuable game development assets in the asset sale on January 22-23, 2013, it failed to sell two of its studios, Vigil and THQ Agoura Hills (Agoura Hills).³⁴⁹ With no buyer, it became clear to THQ that it would have to cease operations at these studios. Thus, as Jason Rubin warned in his letter to the employees following the sale of assets,³⁵⁰ certain employees would lose their jobs. In total, the closing of the two studios caused the termination of over 200 employees.³⁵¹

³⁴³ THQ's Second Motion to Reject Certain Unexpired Non-Residential Real Property Leases.

³⁴⁴ Objection by Church Street Square, LLC to THQ's Second Motion to Reject Certain Unexpired Non-Residential Real Property Leases Paragraph 9.

³⁴⁵ Sublease Agreement Between THQ, Church Street Square, LLC, and 004 Technologies USA, Inc.

³⁴⁶ Order Authorizing Rejection of Certain Unexpired Non-Residential Real Property Leases.

³⁴⁷ Order Authorizing Rejection of Certain Unexpired Non-Residential Real Property Leases Paragraph 3.

³⁴⁸ Order Authorizing Rejection of Certain Unexpired Non-Residential Real Property Leases Paragraph 11.

³⁴⁹ Notice of Sale of Substantially All of THQ's Assets; THQ's Motion to Allow a Settlement with the Terminated Employees.

³⁵⁰ Jason Rubin Letter to Employees Following the Auction.

³⁵¹ THQ's Motion to Allow a Settlement with the Terminated Employees (noting that THQ had employed approximately 120 employees at Vigil and 88 employees at Agoura Hills).

The termination of these employees concerned THQ and its attorneys for more than its impact on the lives of the now terminated workers. Pursuant to the federal Worker Adjustment and Retraining Notification Act (WARN Act), certain employers are required to provide sixty-days notice of any “mass layoff,” which is defined under the statute as a layoff affecting fifty or more employees during any thirty-day period.³⁵² THQ failed to provide this notice to its employees because it did not anticipate the closing of either Vigil or Agoura Hills. If no competing bidder had outbid Clearlake’s Stalking Horse Bid, Clearlake intended to keep these studios operational, causing no job loss as a result of the sale. However, because of the unexpected piecemeal sale, coupled with the lack of bids on Vigil and Agoura Hills, THQ found itself potentially in violation of federal law.

The WARN Act’s sixty-day notice requirement has certain exceptions. Under the Act, an employer may shut down a site of employment without providing the sixty-day notice if (1) at the time the notice would have been required, the employer was actively seeking capital which, if obtained, would prevent the need to close the site, and (2) the employer reasonably believed that giving the notice would have prevented the employer from obtaining the needed capital.³⁵³ Because these studios would have remained open if Clearlake had been the successful bidder, THQ believed that it fell directly within this exception with regard to its decision to close Vigil and Agoura Hills.

While THQ could have chosen to litigate this issue, incurring attorneys’ fees and court costs to be paid out of the bankruptcy estate, it preferred to settle with the terminated employees.³⁵⁴ Thus, on January 21, 2013, THQ filed a motion to allow it to enter into a settlement agreement with the employees from Vigil and Agoura Hills.³⁵⁵ This settlement would be offered to each employee individually, and would provide each employee with a cash payment representing thirty days of compensation and a cash payment of the value of the benefits that the employee would have received during that thirty-day period.³⁵⁶ In exchange, the employee would agree to waive all claims based upon the WARN Act as well as any other potential claims under THQ’s severance policy.³⁵⁷ In addition, the employee would further agree

³⁵² 21 U.S.C. §§ 2101-2109. THQ’s Motion to Allow a Settlement with the Terminated Employees.

³⁵³ 29 U.S.C. § 2102(b)(1).

³⁵⁴ THQ’s Motion to Allow a Settlement with the Terminated Employees (Noting THQ’s probability of success; the complexity, expense, inconvenience, and delay of litigation involved; the benefit to creditors; and the expected difficulty of collection).

³⁵⁵ THQ’s Motion to Allow a Settlement with the Terminated Employees.

³⁵⁶ THQ’s Motion to Allow a Settlement with the Terminated Employees Paragraph 14, 15.

³⁵⁷ THQ’s Motion to Allow a Settlement with the Terminated Employees Paragraph 15.

to preserve THQ confidentiality and refrain from making any disparaging comments about THQ, its Board of Directors, affiliates, subsidiaries, or any current or former employees.³⁵⁸ On February 19, 2013, finding this settlement reasonable and in the best interest of the estate, the Court approved the settlement agreement, allowing THQ to avoid any uncertainty regarding liability from closing of Vigil and Agoura Hills.³⁵⁹

The WWE Contract

In its sale of substantially all of its assets, THQ also failed to sell one of its most well-known and valuable properties, an exclusive license with WWE to produce an annual *WWE* game based around the wrestling league.³⁶⁰ Professional wrestling is an extraordinarily popular sport in America, and the WWE is the most popular league; its weekly show, “Monday Night Raw,” has been watched by at least 4.2 million viewers per week in 2013.³⁶¹ This popularity extended into videogames, with THQ’s most recent WWE game, *WWE 13*, selling 250,000 copies within one week of release.³⁶²

The terms of the contract between THQ and WWE were relatively straightforward. THQ was required to pay a \$7.5 million annual advance to WWE each year through 2017.³⁶³ Each advance was recoupable against the royalties earned throughout the year.³⁶⁴ To develop the game, THQ employed approximately twenty employees.³⁶⁵ Additionally, it engaged a third-party developer to help with the production of *WWE 13* and *WWE 14*.³⁶⁶ This developer, Yuke’s

³⁵⁸ THQ’s Motion to Allow a Settlement with the Terminated Employees Paragraph 15.

³⁵⁹ Order Authorizing Settlement with the Terminated Employees (The Court modified the automatic stay in conjunction with order and made the settlement binding on all employees who chose to accept it).

³⁶⁰ Motion to Allow Settlement with WWE.

³⁶¹ Elliott Binks, *WWE News: Raw Continues to Post Impressive Ratings, We Take a Closer Look*, BLEACHER REPORT (Mar. 13, 2013), <http://bleacherreport.com/articles/1565594-wwe-news-raw-continues-to-post-impressive-ratings-we-take-a-closer-look> (last visited April 23, 2013).

³⁶² Bill Pritchard, *WWE ’13 First Week, Total Sales Numbers Are In, Wrestle Zone* (Nov. 15, 2012), <http://www.wrestlezone.com/news/264031-wwe-13-first-week-total-sales-numbers-in> (last visited April 23, 2013).

³⁶³ Motion to Allow Settlement with WWE Paragraph 8.

³⁶⁴ Motion to Allow Settlement with WWE Paragraph 8.

³⁶⁵ Motion to Allow Settlement with WWE Paragraph 9.

³⁶⁶ Motion to Allow Settlement with WWE Paragraph 10.

Co., Ltd. (Yuke's), is a publically traded company in which THQ owned 14% of the outstanding stock.³⁶⁷ As of the petition date, THQ owed the WWE \$7.6 million in royalties and owed Yuke's between \$15 million and \$20 million for its services in developing *WWE 13* and *WWE 14*.³⁶⁸

Despite the seemingly profitable relationship, no party entered a Qualified Bid for THQ's rights to develop the WWE games pursuant to the exclusive license.³⁶⁹ This was problematic for both THQ and its unsecured creditors. If THQ terminated the license via rejection under Section 365, WWE would suffer an estimated \$45 million in additional damages.³⁷⁰ Because damages from a rejected executory contract are treated as a prepetition unsecured claim, WWE and Yuke's would eat away at the already limited portion of the estate intended for unsecured creditors.³⁷¹

Though it did not sell at the auction, the WWE license still had value to certain developers. After the auction, game developer Take-Two expressed interest in entering a relationship with the WWE, but it was unwilling to assume THQ's obligations under the license. Instead, Take-Two wanted to create a new agreement with WWE and Yuke's to develop the WWE games going forward. To facilitate this transaction, THQ filed a motion on February 12, 2013 requesting that the Court allow it to terminate its relationship with WWE and Yuke's, enabling Take-Two to enter new contracts with these entities.³⁷²

THQ's request had three distinct components. First, it requested approval of an agreement with the WWE to terminate the exclusive license.³⁷³ Under the terms of this agreement, THQ would stop all development of future WWE games and all sales of past WWE games.³⁷⁴ Additionally, it would pay WWE approximately \$650,000 in royalties accrued during

³⁶⁷ Motion to Allow Settlement with WWE Paragraph 11.

³⁶⁸ Motion to Allow Settlement with WWE Paragraph 18 (Each game is developed for release in October of the previous year of release. For example, *WWE 13* is released in October 2012, and *WWE 14* is expected to be released in October 2013).

³⁶⁹ Motion to Allow Settlement with WWE Paragraph 14.

³⁷⁰ Motion to Allow Settlement with WWE Paragraph 14 (WWE claimed that, because no bidder had an interest, it would likely not be able to mitigate by finding another licensee).

³⁷¹ 11 U.S.C. § 365(g).

³⁷² Motion to Allow Settlement with WWE Paragraph 21.

³⁷³ Motion to Allow Settlement with WWE Paragraph 22(d).

³⁷⁴ Motion to Allow Settlement with WWE Paragraph 22(d).

the bankruptcy.³⁷⁵ In exchange, the WWE would release all prepetition claims against THQ, including any claims that might arise from the rejection or termination of the WWE license.³⁷⁶ Next, the motion requested approval of a termination of the development agreement between Yuke's and THQ. According to this termination agreement, THQ would transfer all of its 1,552,000 shares of Yuke's, worth an estimated \$4.485 million, plus an additional \$250,000 in exchange for a release from Yuke's of any prepetition claims against THQ.³⁷⁷ Finally, the motion requested that THQ be allowed to sell its assets related to the development of the WWE games to Take-Two.³⁷⁸

This agreement would benefit all parties involved. THQ would substantially reduce the amount of unsecured claims against the bankruptcy estate, which would allow the other unsecured creditors to obtain a greater dividend on their claims. Furthermore, it provided WWE and Yuke's with the assurance that the *WWE* franchise would continue to be developed. The Court agreed with this and, finding the agreements reasonable and in the best interest of the bankruptcy estate, it approved the termination and sale agreements on February 19, 2013.³⁷⁹

Remaining Issues

Although THQ's case is still ongoing, most of the action has settled down tremendously. THQ sold most of its major assets in the 363 auction, but it still possessed certain miscellaneous personal property that no longer benefitted the estate. THQ continued to try to sell the personal property that it owned,³⁸⁰ reject the contracts for the personal property that it leased,³⁸¹ and take

³⁷⁵ Motion to Allow Settlement with WWE Paragraph 22(f).

³⁷⁶ Motion to Allow Settlement with WWE Paragraph 22(e).

³⁷⁷ Motion to Allow Settlement with WWE Paragraph 22(g), (h), (i).

³⁷⁸ Motion to Allow Settlement with WWE Paragraph 22(j) (In addition to the equipment, Take-Two also indicated its willingness to hire the entire THQ team involved in the development of the WWE games).

³⁷⁹ Order Authorizing the Termination Agreement with WWE (Note that since this transaction, Take-Two has announced via its parent company, 2K Games, that it plans on releasing *WWE 14* on schedule, promising a "commitment to authenticity," and assuring the fans that it will contain the "signature gameplay" to which they have become accustomed).

³⁸⁰ THQ's Motion to Allow the Sale or Abandonment of Certain Miscellaneous Property; Order Establishing Procedures for the Sale or Abandonment of Certain Miscellaneous Property.

³⁸¹ Motion to Reject Certain Unexpired Leases of Personal Property; Order Authorizing Rejection of Certain Unexpired Leases of Personal Property.

further action to reduce its holdings of property to cash.³⁸² As this case involved a pre-planned sale of THQ as a going concern, much of the action in the case took place in just two months, from December 19, 2012, the date of filing, to February, 19, 2013, the date in which the Court ordered the rejection of the real property leases, the settlement with the terminated employees, and the termination of the WWE contract. Today, much of the work in the case involves wrapping up the remaining odds and ends.

Attorney Compensation

To the dismay of the unsecured creditors, a quick case does not necessarily mean a cheap one. This case required extensive legal work on behalf of, among others, THQ and the Committee, and the lawyers were handsomely compensated for their efforts. Gibson Dunn was approved for \$1,137,169.75 in fees and \$20,766.50 in expenses for the period from December 19, 2012 to January 31, 2013 alone.³⁸³ Additionally, the firm has filed a request for \$473,160.00 in additional fees to cover work done in the month of February.³⁸⁴ THQ's other firm, Young Conaway, also requested \$403,639 in fees and \$33,892.28 in expenses for work done from December 19, 2012 to February 28, 2013.³⁸⁵

In addition to the work completed by THQ's counsel, the lawyers representing the Committee have also sought compensation. Two separate law firms, Andrews Kurth and Landis Rath & Cobb, represented the Committee following its formation on January 3, 2013. As of January 31, a period of less than one month, Andrews Kurth had amassed fees of \$432,194.50 and expenses of \$9,474.19 for which it sought payment out of the estate.³⁸⁶ Over the same period, Landis Rath & Cobb accrued fees of \$138,655 and expenses of \$4,826.23 for work done on behalf of the Committee.³⁸⁷ In sum, attorneys' fees totaled approximately \$2.65 million as of March, 2013.

³⁸² Order Authorizing Retention of a Liquidating Consultant.

³⁸³ Application of Gibson, Dunn & Crutcher, LLP for Compensation for Services Rendered and Reimbursement of Expenses.

³⁸⁴ Application of Gibson, Dunn & Crutcher, LLP for Compensation for Services Rendered and Reimbursement of Expenses.

³⁸⁵ Application of Young Conaway Stargatt & Taylor for Allowances of Compensation and Reimbursement.

³⁸⁶ Application of Andrews Kurth LLP for Compensation for Services Rendered and Reimbursement of Expenses.

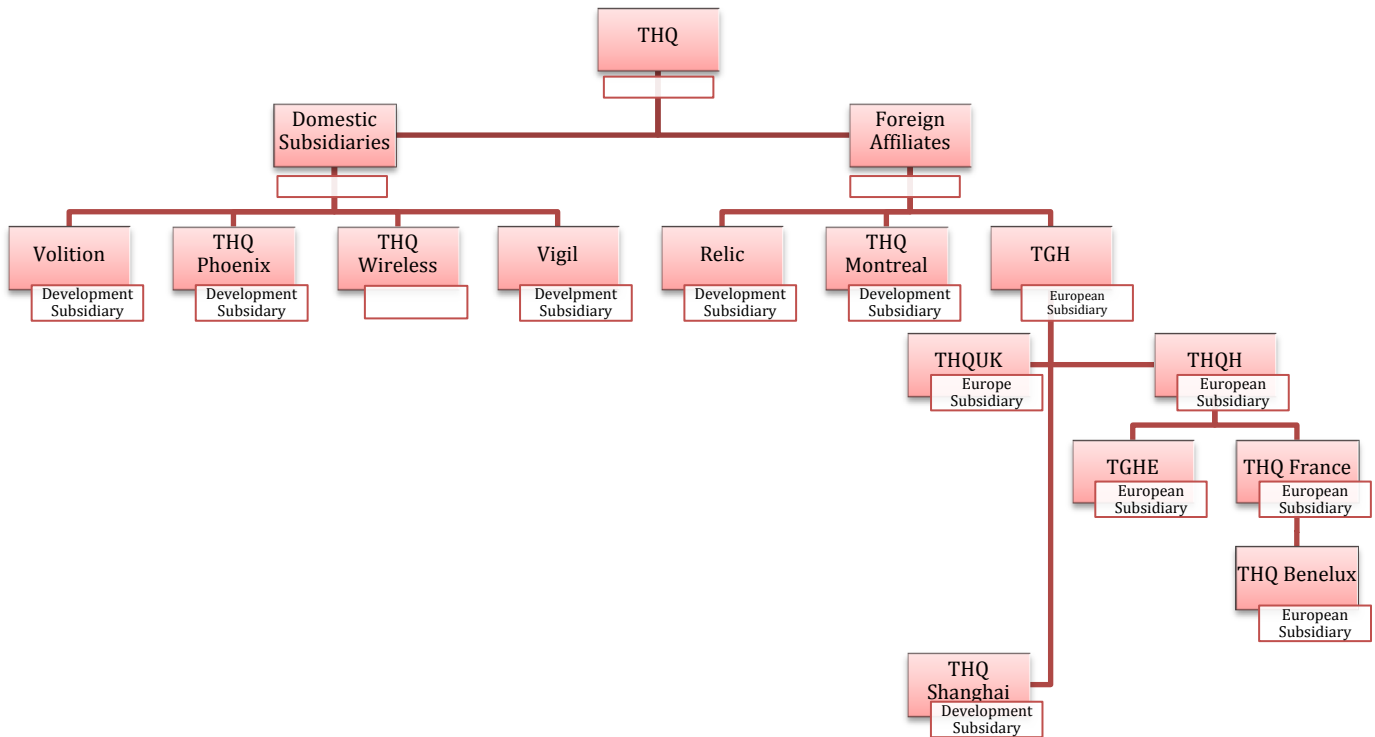
³⁸⁷ Application of Landis Rath & Cobb LLP for Compensation and Reimbursement of Expenses.

Conclusion

In just over two months, the bulk of the case is complete. THQ, once a AAA studio responsible for some of the world's most popular videogame franchises, is now essentially nonexistent, save for some miscellaneous property that it still retains. Onlookers may view this as an unfortunate solution, as this formerly powerful company now sits gutted of its assets. Although a reorganization may have been more socially palatable, the public is arguably better off as a result of the bankruptcy. The purchasing studios have given every indication that all games that THQ intended to release prior to the bankruptcy will, in fact, be released. Additionally, with the backing of financially solvent studios with proven success, which each of the buyers at the auction are, the quality of the THQ franchises should continue to improve over time. Furthermore, with the exception of Vigil and THQ Agoura Hills, nearly all of the employees of THQ's various studios were able to retain their jobs following the respective studio's purchase.

The benefits are significant: jobs retained, game studios preserved, and new games to be released with minor delay. With the exception of the unsecured note holders and certain senior management, the consequences of THQ's bankruptcy are relatively minor considering the size and scope of the company. The bankruptcy process is complex and stressful for all parties involved. However, as the THQ bankruptcy has demonstrated, it can be an effective tool for a company to restructure or eliminate debt while simultaneously preserving its day-to-day operations, even in the case of a going concern sale. In this case, THQ managed to achieve this goal, and though it is now merely a shell of its former self, fans can still count on the release of their favorite THQ games from studios with a solid financial backing. THQ will always have an important place in the history of videogames, and while its demise may be tragic to some, the fact remains that through bankruptcy, the company was able to provide its fans with their greatest want: the assurance that the quality games that it has produced for years will continue to reach the screens of fans across the world. Thus, while it may have been "game over" for THQ as a company, its games, at least for now, have an extra life.

Exhibit A
THQ's Organizational Chart



Appendix A



In re THQ Inc.

Ned Hildebrand

Carlo Salas

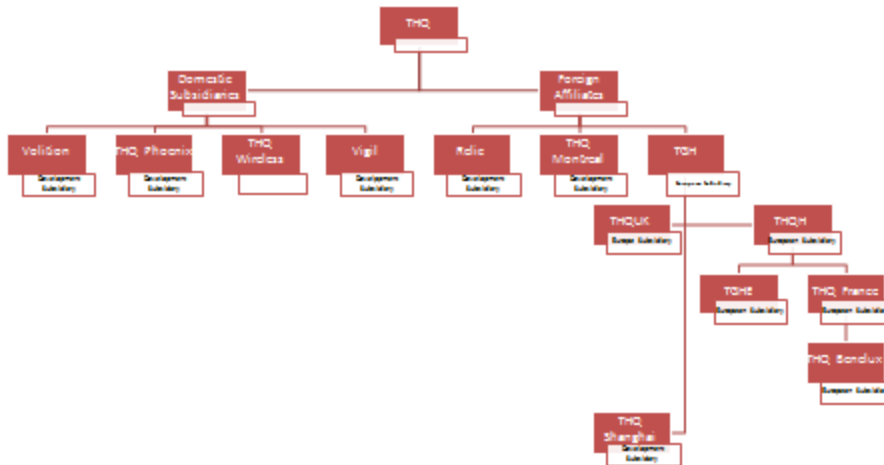
Taylor Wirth

Introduction

- What is THQ?
 - The videogame industry and THQ



THQ's Structure and Organization



THQ's Pending Bankruptcy

- Shifting tastes in gaming
- Unprofitable entry into new markets
- Unsuccessful changes in management
- Recapitalization of the company
- THQ's worsening cash flow
- Default of Wells Fargo loan

Pre-Bankruptcy Efforts

- Negotiation of DIP Financing
- Marketing of THQ as Going-Concern
- Retention of Stalking Horse Bidder



THQ's Asset Purchase Agreement

- Key Features of APA
 - Assumption of THQ debts and liabilities
 - Cash payment to THQ
 - Delivery of unsecured Note
- Questionable provisions
 - “All or substantially all” versus Piecemeal sale
 - Break up fee
 - Expedited auction date

THQ Files for Bankruptcy

- Counsel
 - THQ: Young Conaway Stargatt & Taylor, and Gibson Dunn & Crutcher
- First Day Motions
 - Declaration
 - Joint Administration of Related Cases
 - § 363 Motions: Maintain Accounts, Pay Critical Vendors, Pay Employee Benefits, Honor Prepetition Obligations

Objections

- Objection by Ad Hoc Committee of Convertible Noteholders / Unsecured Creditors Committee
 - Counsel: Landis Rath & Cobb, and Andrews Kurth
 - Specific objections
 - Expedited date of auction
 - Non-piecemeal auction
- Objection by US Trustee
 - Specific Objections
 - Expedited date of auction
 - Break up fee



Court's Decision

- Modifications to APA Bidding Procedures
 - Reduced break up fee
 - Delayed auction date
 - Piecemeal sale



Results of Auction

Studio	Purchaser	Game Produced	Sale Price
Relic	Sega Corp.	<i>Company of Heroes</i>	\$26.6mm
THQ Montreal	Ubisoft, LLC	<i>1666</i> <i>Underdog</i>	\$2.5mm
THQI	Take-Two Interactive	<i>Evolve</i>	\$10.9mm
Volition	Koch Media GmbH	<i>Saint's Row</i>	\$22mm
THQI	Crytek GmbH	<i>Homefront</i>	\$544k
THQI	Koch Media GmbH	<i>Metro 2033</i> <i>Metro 2034</i>	\$5.8mm
THQI	Ubisoft, LLC	<i>South Park: The Stick of Truth</i>	\$3.2mm
Vigil	Unsold	<i>Warhammer: 40,000</i>	
THQ Agoura Hills	Unsold		

Post-Auction Events

- Assumption and Assignment of Executory Contracts
 - Procedure under APA
 - Objections
 - Debtor's Reply
 - Court's Ruling

Post-Auction Events

- Rejection of Real Property Leases
 - New York lease
 - Mexico lease
 - Champaign Lease
 - Objections
 - Debtor's Response
 - Court's Ruling

Post-Auction Events

- Closing of Vigil and THQ Agoura Hills
 - WARN Act Violation
 - Settlement Procedures
 - Approval by Court



Post-Auction Events

- *World Wrestling Entertainment (WWE) Contract*
 - Development Relationship
 - No Qualified Bid at Auction
 - Requested Rejection
 - Court's Ruling



Remaining Issues

- Abandonment of Personal Property
 - Rejection of Personal Property Leases
 - Sale of Miscellaneous Personal Property without Court Approval

Attorney Compensation

- **THQ**
 - Gibson Dunn: \$1,137,169 in fees, \$20,766 in expenses (Dec. 19, 2012 – Jan. 31, 2013); \$473,160 (Feb. 1, 2013 – Feb. 28, 2013)
 - Young Conaway: \$403, 639 in fees, \$33,892 in expenses (Dec. 19, 2012 – Feb. 28, 2013)
- **Unsecured Creditors**
 - Andrews Kurth: \$432,194 in fees, \$9,474 in expenses (Jan. 3, 2013 – Feb. 28, 2013)
 - Landis Rath & Cobb: \$138,655 in fees, \$4,826 in expenses (Jan. 3, 2013 – Feb. 28, 2013)
- **TOTAL: \$2.65 million as of March, 2013**



Questions?