UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

In re:	)	Chapter 11
	)	
SCHWAB INDUSTRIES, INC., *et al.*,[1]	)	Case No. 10-60702-rk
	)	(Jointly Administered)
Debtors.	)	
	)	Judge Russ Kendig
	)	

OBJECTION OF OFFICIAL COMMITTEE OF UNSECURED CREDITORS TO DEBTORS' MOTION FOR ORDER (1) AUTHORIZING THE SALE OF SUBSTANTIALLY ALL OF THE DEBTORS' ASSETS, FREE AND CLEAR OF LIENS, CLAIMS, INTERESTS AND ENCUMBRANCES, SUBJECT TO HIGHER OR BETTER OFFERS, PURSUANT TO BANKRUPTCY CODE SECTIONS 363 AND 365; (2) APPROVING THE ASSUMPTION AND ASSIGNMENT OF CERTAIN EXECUTORY CONTRACTS AND UNEXPIRED LEASES IN CONNECTION WITH SUCH SALE AND DETERMINING AND ADJUDICATING CURE AMOUNTS WITH RESPECT TO SUCH CONTRACTS AND LEASES; (3) WAIVING THE FOURTEEN-DAY STAY PERIOD PROVIDED BY BANKRUPTCY RULE 6004(H); AND (4) GRANTING RELATED RELIEF

The Official Committee of Unsecured Creditors (the "*Committee*") appointed in the above-captioned, jointly-administered bankruptcy cases, by and through its counsel, hereby submits this objection (the "*Objection*")[2] to the Debtors *Motion For Order (1) Authorizing the Sale of Substantially all of the Debtors' Assets, Free and Clear of Liens, Claims, Interests and Encumbrances, Subject to Higher or Better Offers, Pursuant to Bankruptcy Code Sections 363 and 365; (2) Approving the Assumption and Assignment of Certain Executory Contracts and*

[1] The Debtors in these chapter 11 cases, along with the last four digits of each Debtor's tax identification number are: Schwab Industries, Inc. (2467); Medina Cartage Co. (9373); Medina Supply Company (3995); Quality Block & Supply, Inc. (2186); O.I.S. Tire, Inc. (7525), Twin Cities Concrete Company (9196); Schwab Ready-Mix, Inc. (8801); Schwab Materials, Inc. (8957); and Eastern Cement Corp. (7232).

[2] In this Objection, the Committee raises each of the objections to the Motion that are known to the Committee as of the date of this Objection. However, additional objections may become known to the Committee following this Objection, but prior to the hearing on the Motion, based upon events that have yet to occur – including the qualification of competing bids and the auction. Accordingly, the Committee reserves the right to raise additional objections to the sale – whether in a supplemental objection filed with the Court or at the hearing itself.

Unexpired Leases in Connection with Such Sale and Determining and Adjudicating Cure Amounts with Respect to Such Contracts and Leases; (3) Waiving the Fourteen-Day Stay Period Provided by Bankruptcy Rule 6004(h); and (4) Granting Related Relief (the "*Motion*"), and states:

INTRODUCTION

1. Despite the promising amount of interest potential purchasers have expressed in the Debtors' assets, and the several competing bids received for those assets, the Committee remains doubtful of the legitimacy of the sale process. These doubts are largely based on the Debtors' promotion of their stalking horse bidder, Cement Resources, LLC ("*Cement Resources*") at the expense of better and less tainted bids.

2. As an initial matter, the Committee is befuddled, on purely economic terms, as to why the Debtors have thrown their full support at the Cement Resources bid. As this Court is aware, two competing "basket" bids for the Debtors' assets are collectively valued at more than ten percent higher than the Cement Resources bid, yet the Debtors seemingly have ignored this fact. That these bids have not been given priority at auction stands at conflict with the Debtors' fiduciary duties to the estates and creditors, and violates the spirit and intent of section 363 of the Bankruptcy Code. Additionally, the failure of the Debtors to give proper credence to the competing basket bids takes us right back to where Cement Resources and the Debtors originally wanted the sale process to go – with a sham auction process and a virtually guaranteed sale to Cement Resources. The result of this sham process will be that value will not be maximized for the benefit of unsecured creditors – which is something that the Committee cannot abide by.

3. The sale to Cement Resources becomes even more suspect when considering that it may be coupled with self-dealing by the Debtors' insiders. The Debtors previously made public that Cement Resources has been engaged in negotiations with the Debtors' insiders to

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give them a continuing management role post-sale, as well as the opportunity to take an equity stake in Cement Resources post-closing. What does this mean? Only that the Debtors' insiders have a strong incentive to support the Cement Resources bid notwithstanding the fact that it may cause significant harm to unsecured creditors, and that their business judgment is hopelessly conflicted.

4. As detailed in prior pleadings filed by the Committee, these cases have been fraught with instances in which the Debtors' management have put their personal interests ahead of those to whom they owe a fiduciary duty – the unsecured creditors of their estates. As with their failure to terminate life insurance policies and their entering into a post-petition financing agreement that encumbered assets that could have been used to provide distributions to the unsecured creditors, the Debtors' management has lightly tossed their fiduciary obligations to the side to try and gain where everyone else will lose. The Court should not condone such conduct and should instead hold the Debtors to the standards required of all debtors in possession.

5. The coupling of the Cement Resources bid with the potential Schwab insider transaction also leads the Committee to conclude that the sale to Cement Resources would amount to an impermissible chapter 11 *sub rosa* plan. Even worse is that this *sub rosa* plan would directly violate the absolute priority rule of section 1129(b)(2) of the Bankruptcy Code, in that the Debtors' equity holders would derive a substantial benefit from the sale while unsecured creditors would stand to receive nothing.

6. Accordingly, the Court should not approve the sale to Cement Resources absent (1) granting competing bidders unfettered participation in the sale and auction process; (2) attributing appropriate value to the competing bids of the basket bidders; and (3) rejecting the efforts of the Debtors' insiders to derive value from the sale process at the expense of unsecured

creditors. These protections are necessary to ensure that value is maximized for the benefit of the Debtors' estates and not solely the Debtors' insiders.

BACKGROUND

A. The Chapter 11 Cases

7. On February 28, 2010 (the "*Petition Date*"), Schwab Industries, Inc. and its affiliated debtors and debtors-in-possession (collectively, the "*Debtors*") filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code (the "*Bankruptcy Code*") in the United States Bankruptcy Court for the Northern District of Ohio (the "*Court*").

8. The Debtors are currently operating and managing their businesses as debtors-in-possession pursuant to sections 1107 and 1108 of the Bankruptcy Code. The Committee was appointed on March 9, 2010.

B. The Sale Motion

9. Pursuant to the Motion, the Debtors seek authority, pursuant to section 363 of the Bankruptcy Code, to sell their "core" assets, including substantially all of their real property, machinery and equipment, the Port Manatee deep water port facility, and its potential aggregates quarry located in Florida currently operated as an orange grove.

10. Pursuant to the Motion, the Debtors proposed to sell the assets through a competitive auction process ("*Auction*").

C. Status of Sale Process

11. Since the entry of the order approving the original bid procedures on April 16, 2010, the Debtors (as well as the Committee) engaged in discussions with dozens of potential bidders for all or portions of the Debtors' assets. The results of these discussions have been quite encouraging – parties have expressed serious interest in placing bids and have conducted detailed

due diligence and, by the initial stalking horse bid deadline of April 28, 2010, several parties submitted non-binding letters of intent to the Debtors.

12. The Debtors chose one of those bids, from Cement Resources, as its stalking horse bidder, despite the Committee's belief that other offers promised more value for the Debtors' estates. Cement Resources' bid includes the following key terms:

- *Purchase Price*: $48,350,000 cash, plus a reimbursement to the Debtors' pre-petition lenders (the "*Pre-Petition Lenders*") of up to $2,000,000 in additional debtor-in-possession financing through the closing of the sale.

- *Excluded Assets*: Certain "non-core" assets having an estimated approximate value of $1,300,000; all other assets to be sold to Cement Resources pursuant to the sale agreement.

- *Assumption of 503(b)(9) Claims and Trade Payables*: Cement Resources has agreed to assume approximately $602,000 worth of section 503(b)(9) claims, as well as up to $750,000 in post-petition trade payables of the Debtors.

- *Break-Up Fee and Expense Reimbursement*: Pursuant to the *Agreed Order Approving Motion for a Revised Bidding Procedures Order Approving (1) Executed Stalking Horse Asset Purchase Agreement; (2) Proposed Break-Up Fee and Expense Reimbursement; (3) Revised Bidding Procedures; (4) the Form and Manner of Service of Notice of the Sale Hearing and Auction; and (5) the Form and Manner of Service of Notice of the Assumption and Assignment of Certain Executory Contracts and Unexpired Leases Which Revises Order (1) Approving Auction and Bidding Procedures and an Auction Date; (2) Scheduling Date and Time for Sale Hearing; (3) Approving the Form and Manner of Service of Notice of the Sale Hearing and Auction Pursuant to Bankruptcy Rules 2002, 6004 and 6006; (4) Approving the Form and Manner of Service of Notice of the Assumption and Assignment of Certain Executory Contracts and Unexpired Leases; and (5) Granting Related Relief* (Docket No. 406) (the "*Revised Bid Procedures Order*"), the Court approved of a combined break-up fee and expense reimbursement in the amount of $1,900,000.

- *Mining Rights*: Under the sale agreement, Cement Resources will grant the Debtors the right to receive, on a cumulative basis, annual earn-out payments equal to twenty percent (20%) of cumulative net profits attributable to (i) the mining of the Debtors' orange grove/aggregates quarry, or (ii) the sale of any such validly permitted and approved mining rights on the property.

- *Assignment and Assumption of Executory Contracts*: The sale agreement permits Cement Resources to direct the Debtors to assume and assign the "Acquired

Contracts." Cement Resources is liable for "Cure Costs" incurred with respect to the Acquired Contracts.

13. The Debtors' investment banker, Western Reserve Partners ("*WRP*"), estimates the total value of the proposed Cement Resources transaction (net of the break-up fee and expense reimbursement) to be in the amount of $52,971,022.

14. As noted by the Debtors in their motion seeking approval of the Revised Bid Procedures Order, Cement Resources began negotiations with the Schwab family with respect to a transaction that will allow the Schwabs to continue managing the business post-sale, and may further allow them to receive a minority share of Cement Resources' equity post-closing, in the event that Cement Resources emerges as the successful bidder of the Debtors' assets. Upon information and belief, Cement Resources and the Schwabs are continuing to negotiate the terms of this potential transaction.

15. In addition to the Cement Resources bid, several other binding bids have now been received for portions of the Debtors' assets, which, combined, exceed the Cement Resources offer substantially. Notwithstanding this reality, the Debtors, with the consent of the Pre-Petition Lenders and without consulting with the Committee, selected the Cement Resources bid as the highest and best bid and have granted Cement Resources stalking horse status.

D. Modified Bid Procedures

16. Pursuant to the offer received from Cement Resources, the Debtors sought to modify the bid procedures. The Committee's objections to that motion are set forth in the *Objection of Official Committee of Unsecured Creditors to Debtors' Motion for a Revised Bidding Procedures Order Approving (1) Executed Stalking Horse Asset Purchase Agreement; (2) Proposed Break-Up Fee and Expense Reimbursement; (3) Revised Bidding Procedures; (4) the Form and Manner of Service of Notice of the Sale Hearing and Auction; and (5) the Form*

and Manner of Service of Notice of the Assumption and Assignment of Certain Executory Contracts and Unexpired Leases (the "*Bid Procedures Objection*") (Docket No. 378), and will not be repeated here.

17. The Court partially granted the Debtors' motion to modify the bid procedures in the Revised Bid Procedures Order, based upon a settlement reached between the Debtors, the Committee and the Pre-Petition Lenders. Pursuant to the Revised Bid Procedures Order, the Court approved the Debtors' choice of Cement Resources as the stalking horse bidder, but reduced the requested break-up fee and expense reimbursement to $1,900,000 (from the almost $3,000,000 originally requested by the Debtors). The parties agreed to, and the Court approved, a modified accelerated sale timeframe, providing for the Auction to be held on May 27, 2010 and for the sale approval hearing to be held on May 28, 2010. And perhaps most importantly, the Debtors and Cement Resources backed off of their original request that qualified bids be limited to bids for substantially all of the Debtors' assets, and agreed to entertain bids for various "baskets" of the Debtors' assets.

18. Notwithstanding these important concessions, the proposed sale of the Debtors' assets to Cement Resources continues to cause the Committee significant concern. As an initial matter, bids that, when viewed collectively, are higher and better than that of Cement Resources have yet to be qualified to participate at auction. The proposed Cement Resources transaction appears to be tainted by conflicts of interest, based upon the potential gain – in the form of continued management control and a minority equity stake – to be realized by the Schwab family in the event that Cement Resources' bid is approved. Finally, the Cement Resources transaction, when coupled with the potential Schwab management and equity sharing agreement, may very well constitute an impermissible chapter 11 *sub rosa* plan. For these reasons, as described more

fully below, the Court should deny the sale of the Debtors' assets to Cement Resources unless and until the Committee's concerns are satisfactorily addressed.

ARGUMENT

19. The underlying goal of section 363 of the Bankruptcy Code is to maximize the value of assets for the estates, and to ensure the highest and best aggregate bid(s) for the Debtors' assets. *See In re Trans World Airlines, Inc.*, 2001 WL 1820326, at *11 (Bankr. D. Del. Apr. 2, 2001) ("The purpose of a § 363(b) sale is to transform assets . . . into cash in an effort to maximize value."); *see also In re Gen. Motors Corp.*, 407 B.R. 463, 496-97 (Bankr. S.D.N.Y. 2009) (citing *Trans World Airlines*).

20. The Debtors have a fiduciary duty to maximize value of their estates for all parties in interest, including unsecured creditors. *In re Biderman Indus. U.S.A. Inc.*, 203 B.R. 547, 551 (Bankr. S.D.N.Y. 1997). The concerns raised in this Objection lead the Committee to conclude that, if the sale to Cement Resources is approved rather than the better offers received for the assets, the Debtors will have failed to satisfy their fiduciary duty toward creditors in these cases. In particular, the Committee raises the following objections to the sale: (1) competing bids that, when viewed collectively, are higher and better than that of Cement Resources have not been qualified, and those bidders have not been granted full participation in the auction process; (2) the presence of the potential insider transaction with Cement Resources renders the business judgment of the Debtors tainted; and (3) the Cement Resources bid, when viewed in conjunction with the potential Schwab insider transaction, is arguably a *sub rosa* plan that cannot be approved by this Court. Unless each of these objections are adequately addressed prior to the auction and sale hearing, the Committee requests that the sale to Cement Resources be denied.

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A. The Suppression of Higher and Better Bids for the Debtors' Assets Casts a Pall on the Sale Process.

21. As the Committee discussed at length in the Bid Procedures Objection, two binding bids were received for portions of the Debtors' assets that, when viewed collectively, greatly exceed the Cement Resources stalking horse bid. Indeed, based upon WRP's analysis, these bids have a combined economic value of $58,397,543 – ***thereby exceeding the Cement Resources bid by $5,426,521***.

22. Notwithstanding the fact that these bids exceed the Cement Resources bid by more than ten percent, and have no contingencies that would otherwise render them unacceptable, the Debtors have failed to qualify both such bids to participate at the May 27, 2010 auction, and have continued to throw their full support behind the Cement Resources bid. The Committee simply cannot comprehend why this has not already occurred, and submits that this failure threatens the legitimacy of the sale process as a whole. Indeed, if the Debtors continue to neglect potential competing bidders, causing them to walk away prior to the auction, millions of dollars in potential value – some of which may very well be within the reach of unsecured creditors – may be lost forever.

23. That this tragic outcome is a potential reality should cause this Court great concern, and should call into question whether the Debtors are fully discharging their fiduciary duties to the estates and unsecured creditors by ensuring the highest and best possible price for their assets. If the potential competing bidders are not immediately granted the right to fully participate at the auction, the Committee's view will be that the sale process is hopelessly tainted and that a sale of the Debtors' assets to Cement Resources cannot be approved.

B. The Debtors' Business Judgment in Selling Their Assets to Cement Resources Should Not Be Honored Due to Management's Conflict of Interest.

24. A sale pursuant to section 363 of the Bankruptcy Code must be justified by a debtor's business judgment. *See, e.g.*, *In re Gulf Coast Oil Corp.*, 404 B.R. 407, 416 (Bankr. S.D. Tex. 2009) ("[I]t is implicit in § 363(b) that the sale must be justified by the debtor in possession or trustee, and that the debtor in possession or trustee has a fiduciary duty to parties in interest."); *In re Psychrometric Sys., Inc.*, 367 B.R. 670, 674 (Bankr. D. Colo. 2007) ("[T]he court must always scrutinize whether the trustee has fulfilled his duty to 'maximize the value obtained from a sale, particularly in liquidation cases.'"); *In re Global Crossing Ltd.*, 295 B.R. 726, 743 (Bankr. S.D.N.Y. 2003) ("The business judgment rule is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.") (citation and internal quotation marks omitted).

25. The business judgment rule comes into play based on the fiduciary duties owed by the Debtors' officers and directors to the Debtors' creditors. In a bankruptcy case, a debtor owes fiduciary duties to the bankruptcy estate. As such, the operators of the debtor's business, "acting as a debtor in possession, must run the business as agents of the bankruptcy estate, and not for their own personal gain. The fiduciary obligations consists of two duties: the duty of care and the duty of loyalty." *Lange v. Schropp (In re Brook Valley VII, Joint Venture)*, 496 F.3d 892, 900 (8th Cir. 2007); *see also In re Penick Pharmaceutical, Inc.*, 227 B.R. 229 (Bankr. S.D.N.Y. 1998) (holding that a chapter 11 debtor-in-possession's fiduciary duties fall on the debtor's directors, officers and managing employees, who have an obligation to maximize the value of the estate, and who are burdened to ensure that resources that flow through the debtor's

hands are used to benefit the unsecured creditors and other parties in interest). As further held by the *Brook Valley VII Joint Venture* court:

> The duty of loyalty comes into play when there appears to be a conflict between the interests of the fiduciary and the entity to which he owes loyalty. *For a debtor in possession, this duty includes an obligation to refrain from self-dealing, to avoid conflicts of interests and the appearance of impropriety, to treat all parties to the case fairly and to maximize the value of the estate*.

In re Brook Valley VII Joint Venture, 496 F.3d at 900-01 (emphasis added); *see also In re Tenn-Fla Partners*, 226 F.3d 746, 748 (6th Cir. 2000) (affirming bankruptcy court decision to revoke confirmation order where the debtor violated its debtor-in-possession obligations and engaged in self-dealing at the expense of the bondholders, who had been induced by the debtor's misrepresentations to give up their elections pursuant to section 1111(b)(2) of the Bankruptcy Code); *In re V Cos.*, 274 B.R. 721 (Bankr. N.D. Ohio 2002) (converting a chapter 11 case based, in part, on the breach of fiduciary duties by the debtor-in-possession's management in engaging in certain questionable transactions and self-dealing).

26. The business judgment rule does not apply where the debtor's insiders are not disinterested, as is the case here, and a proposed transaction is thereby subject to heightened scrutiny. *See, e.g.*, *Marsalis v. Wilson*, 778 N.E.2d 612, 615-16 (Ohio Ct. App. 2002) ("The rule [under Ohio law] is a rebuttable presumption that directors are better equipped than the courts to make business judgments and that the directed *acted without self-dealing or personal interest* and exercised reasonable diligence and acted in good faith."); Robin E. Phelan, et al., *If Their Business Judgment Was So Good How Come They're In Bankruptcy and Other Perplexing Mysteries of the Business Judgment Rule: Corporate Governance Issues for the Financially Troubled Company*, 10 J. Bankr. L. & Prac. 471, 474 (Sept./Oct. 2001) ("The business judgment

rule presupposes that a challenged corporate decision is made by disinterested corporate directors."). As explained by the Fourth Circuit Court of Appeals:

> Under the business judgment rule, courts defer to corporate officers' decisions on matters entrusted to their business judgment absent a showing of bad faith or gross abuse of that judgment, and this rule extends to bankruptcy proceedings. Whether a debtor's decision is so manifestly unreasonable that it could only be based on bad faith, whim, or caprice rather than sound business judgment is a question of fact, and this factual determination is subject to the clearly erroneous standard.

Quality Inns Int'l, Inc. v. L.B.H. Assocs. Ltd. P'ship, 1990 WL 116761, at *7 (4th Cir. July 26, 1990) (unpublished) (citations omitted); *see also In re W.A. Mallory Co.*, 214 B.R. 834 (Bankr. E.D. Va. 1997) (concluding that where proposed purchasers were insiders of the corporation, it suggested a lack of good faith).

27. And as held in *In re Farmland Industries, Inc.*:

> Under the "business judgment" rule, the management of a corporation's affairs is placed in the hands of its board of directors and officers, and the Court should interfere with their decisions only if it is made clear that those decisions are, *inter alia*, clearly erroneous, made arbitrarily, are in breach of the officers' and directors' fiduciary duty to the corporation, are made on the basis of inadequate information or study, are made in bad faith, or are in violation of the Bankruptcy Code. . . . *Only in circumstances where there are allegations of, and a real potential for, abuse by corporate insiders, should the Court scrutinize the actions of the corporation*.

In re Farmland Indus., Inc., 294 B.R. 855, 881 (Bankr. W.D. Mo. 2003) (citations and internal quotation marks omitted) (emphasis added).

28. Specifically with respect to a sale pursuant to section 363 of the Bankruptcy Code, "[t]he court must be satisfied that (i) notice has been given to all creditors and interested parties; (ii) the sale contemplates a fair and reasonable price; and (iii) the purchaser is proceeding in good faith." *In re Gen. Motors Corp.*, 407 B.R. at 493-94. "When the Court considers

'disinterestedness,' it looks to the disinterestedness of [the debtors'] Board and management, and particularly its Board, which is the ultimate decision maker for any corporation." *Id.* at 495 n.62.

29. As held by one court, "a debtor-in-possession must exercise fiduciary duty in determining whether and how to propose a sale of assets. If entities that control the debtor will benefit, or will potentially benefit, from the sale the court must carefully consider whether it is also appropriate to defer to their business judgment." *In re Gulf Coast Oil Corp.*, 404 B.R. at 424; *see also In re Summit Global Logistics, Inc.*, 2008 Bankr. LEXIS 896, at *27 (Bankr. D.N.J. Mar. 26, 2008) ("[H]eightened scrutiny [is] required . . . for insider transactions.").

30. Here, the Debtors have proposed to sell substantially all of the Debtors' assets to Cement Resources, a bidder that has proposed to include the Debtors' current management in the management of the purchased businesses. In addition, under this proposed deal, the Debtors' current equity holders – the Schwab family – will have the opportunity to obtain equity interests in Cement Resources post-closing. None of the other bidders for the Debtors' assets have offered similar benefits to the Debtors' management. Accordingly, the Committee can only conclude that the Debtors' management and board of directors are hopelessly conflicted, in that they chose the lower Cement Resources bid because of the potential for significant personal benefit. *See, e.g.*, *In re Psychrometric Sys., Inc.*, 367 B.R. at 675 ("[A] Bankruptcy Court . . . does have the power to disapprove a proposed sale recommended by a trustee . . . if it has an awareness there is another proposal in hand which, from the estate's point of view is better or more acceptable.") (citation omitted); *In re Castre, Inc.*, 312 B.R. 426, 430 (Bankr. D. Colo. 2004) (same).

31. Given this reality, the Committee is concerned that the Debtors' desire to enter into the sale agreement with Cement Resources may be motivated by their desire to preserve the Schwab family's role in the Debtors' businesses. To support such a sale, when better offers have

been rejected, may be a breach of the Debtors' fiduciary duties to these estates and creditors. Accordingly, this Court should reject the business judgment of the Debtors in selling the Debtors' assets to Cement Resources.

C. The Proposed Sale to Cement Resources Is an Impermissible *Sub Rosa* Plan.

32. The Committee believes that if the sale to Cement Resources is coupled with a transaction whereby the Debtors' insiders will retain equity interests in the businesses and remain part of management, such a sale is an impermissible *sub rosa* plan that cannot be approved by this Court. *Sub rosa* plans (i) involve significant restructuring of creditors' rights; (ii) change the composition of the debtor's assets; (iii) dictate at least some of the terms of any future reorganization plan; and (iv) call for release of claims against the debtor, all of which occur outside the plan solicitation and approval process set forth in sections 1121 through 1129 of the Bankruptcy Code. *See In re Braniff Airways, Inc.*, 700 F.2d 935, 939-40 (5th Cir. 1983).

33. As a general matter, *sub rosa* plans have been disapproved by courts as an impermissible circumvention of the standard plan process. *See id.*; *see also In re Iridium Operating LLC*, 478 F.3d 452, 466 (2d Cir. 2007) ("The trustee is prohibited from such use, sale or lease if it would amount to a *sub rosa* plan of reorganization."); *In re Babcock & Wilcox Co.*, 250 F.3d 955, 960 (5th Cir. 2001) (holding that section 363 of the Bankruptcy Code does "not allow a debtor to gut the bankruptcy estate before reorganization or to change the fundamental nature of the estate's assets in such a way that limits a future reorganization plan"); *Institutional Creditors of Cont'l Air Lines, Inc. v. Cont'l Air Lines, Inc. (In re Cont'l Air Lines, Inc.)*, 780 F.2d 1223, 1226 (5th Cir. 1986) (holding that section 363 of the Bankruptcy Code "does not authorize a debtor and the bankruptcy court to 'short circuit the requirements of a reorganization plan by establishing the terms of the plan *sub rosa* in connection' with a proposed transaction") (quoting *Braniff*, 700 F.2d at 940).

34. Sales of substantially all of a debtor's assets outside of the plan process "are extraordinary and should be viewed as an exception to the rule. . . . Because there is some danger that a section 363 sale might deprive parties of substantial rights inherent in the plan confirmation process, sales of substantial portions of a debtor's assets under section 363 must be scrutinized closely by the court." *In re Cloverleaf Enters., Inc.*, 2010 Bankr. LEXIS 1301, at *6-*7 (Bankr. D. Md. Apr. 2, 1010) (citation omitted). In *Cloverleaf*, the bankruptcy court denied approval of the sale of substantially all of the debtor's assets where the debtor's sole stockholder stood to "reap a remarkable dividend should everything fall into place under the [sale agreement]." *Id.* at *11.

35. In the Sixth Circuit, "a bankruptcy court can authorize a sale of all a Chapter 11 debtor's assets under § 363(b)(1) *when a sound business purpose dictates such action*." *Stephens Indus., Inc. v. McClung*, 789 F.2d 386, 390 (6th Cir. 1986) (emphasis added). Here, and as further discussed above, there is no sound business purpose to enter into the sale agreement with Cement Resources over the better bids received by the Debtors. The Debtors' equity holders will receive significant value from the sale to Cement Resources while the Debtors' unsecured creditors (who are ahead of the equity holders with respect to priority under the Bankruptcy Code) will get nothing.

36. This effectively violates the absolute priority rule set forth in section 1129(b)(2)(B)(ii) of the Bankruptcy Code, which requires that junior classes cannot receive anything pursuant to a plan until prior classes are paid in full. *See* 11 U.S.C. § 1129(b)(2)(B)(ii). This is just the type of result that the prohibition against *sub rosa* plans is meant to prevent. *See, e.g.*, *Cont'l Air Lines*, 780 F.2d at 1227 ("[I]f a debtor were allowed to reorganize the estate in some fundamental fashion pursuant to § 363(b), creditor's rights under, for example, 11 U.S.C. §§ 1125, 1126, 1129(a)(7), and 1129(b)(2) might become meaningless."); *Braniff*, 700 F.2d at

940 (noting that section 363(b) of the Bankruptcy Code cannot be utilized to bypass the requirements of, among other things, the absolute priority rule of section 1129(b)(2)(B) of the Bankruptcy Code); *In re Gen. Motors Corp.*, 407 B.R. at 495 ("A 363 plan may also may be objectionable as a *sub rosa* plan if the sale itself seeks to allocate or dictate the distribution of sale proceeds among different classes of creditors.").

37. Accordingly, because the proposed sale to Cement Resources, if approved, will, among other things, result in equity holders receiving substantial benefit ahead of and at the expense of unsecured creditors, this Court should deny the sale to Cement Resources as an impermissible *sub rosa* plan.

WHEREFORE, the Committee respectfully requests entry of an order:

(a) denying the Motion in its entirety; and

(b) granting such other and further relief as is just and proper.

Dated: May 21, 2010

OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF SCHWAB INDUSTRIES, INC., *et al.*

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