IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	:	Chapter 11
COLT HOLDING COMPANY LLC, *et al*.,	:	Case No. 15-11296 (LSS) (Jointly Administered)
Debtors.	:	**Hearing Date: July 10, 2015 @ 9:30 a.m. ET** **Re: Dkt. Nos. 12, 60, 61, 78, 100, 101, 102, 103, 114, 124, 126**

LIMITED OBJECTION OF SCIENS CAPITAL MANAGEMENT LLC TO DEBTORS' PROPOSED ALTERNATIVE DIP FINANCING

Sciens Capital Management LLC, for itself and for various affiliated funds in which it and its investors have direct and indirect ownership interests (collectively, "Sciens") in Colt Holding Company LLC and its affiliates (collectively, "Colt" or the "Debtors"), by and through its undersigned counsel, hereby submits this limited objection (this "Limited Objection") to the motion[1] filed by the Debtors for authority to enter into a debtor-in-possession financing agreement and related relief (the "DIP Motion"). In support of this Limited Objection, Sciens respectfully states as follows:

PRELIMINARY STATEMENT

1. Sciens does not dispute the Debtors' need for a DIP facility. The Debtors require funding to continue their operations and complete a sale or chapter 11 process that will save the company and provide a value-maximizing outcome in these cases. As equity sponsor of Colt for over 20 years, Sciens has always been, and remains, committed to ensuring Colt's viability and

[1] See *Debtors' Motion (I) Pursuant to 11 U.S.C. §§ 105, 361, 362, 363, 364, and 507 Authorizing the Debtors to (A) Obtain Post-Petition Financing, (B) Grant Senior Liens and SuperPriority Administrative Expense Status, and (C) Utilize Cash Collateral of Pre-Petition Secured Parties; (II) Granting Adequate Protection to Pre-Petition Secured Parties Pursuant to 11 U.S.C. §§ 361, 362, 363, and 364; (III) Scheduling a Final Hearing; and (III) Granting Related Relief* [Dkt. No. 12] (the "DIP Motion").

success. Accordingly, Sciens generally supports entry of an order providing the Debtors with the financing they seek to fund these cases.

2. Sciens is compelled to object, however, to the coercive and outcome-altering "roll-up" provisions proposed in the current DIP facility driven by the Ad Hoc Consortium Lenders (defined below). There is no support, or need, for these extraordinary provisions which will indisputably limit the Debtors' flexibility and options in attempting to navigate a successful outcome to these cases. Indeed, the Ad Hoc Consortium Lenders themselves objected to the Debtors' initial DIP financing proposal ostensibly because the sale process milestones associated with the Debtors' initial DIP proposal "compel[led] a particular case outcome."[2] The Ad Hoc Consortium Lenders now seek to replace the allegedly coercive provisions of the initial DIP proposal with equally coercive and outcome-determinative roll-up provisions which will allow the Ad Hoc Consortium Lenders to control the cases for the benefit of the Senior Notes (of which the Ad Hoc Consortium Lenders are the largest holders). The Ad Hoc Consortium Lenders' naked attempt to gain control of these cases for their own benefit via the proposed roll-up is an overreach, is not supported by the record of these cases, and should be denied.

BACKGROUND AND BASIS FOR OBJECTION

3. On June 15, 2015, in connection with the commencement of the Debtors' chapter 11 cases, the Debtors requested this Court's approval to obtain $20 million of debtor in possession financing (the "Proposed DIP").[3] The Proposed DIP would have been provided by the Debtors' lenders (the "Prepetition Senior Lenders") under the Debtors' prepetition senior loan (the "Prepetition Senior Loan") and the Debtors' lenders (the "Prepetition Term Loan Lenders")

[2] *Supplemental Objection of Ad Hoc Consortium of Holders of Senior Notes to Debtors' DIP Motion* [Dkt. No. 100] (the "Supplemental Objection"), at ¶ 1.

[3] See DIP Motion; see also *Declaration of Nikhil Menon in Support of DIP Motion* [Dkt. No. 14].

under the Debtors' prepetition term loan (the "Prepetition Term Loan" and, together with the Prepetition Senior Loan, the "Prepetition Facilities").[4]

4. Hours prior to the first day hearing (the "First Day Hearing") of the Debtors' cases, on June 16, 2015, an ad hoc consortium of holders (the "Ad Hoc Consortium") of the 8.75% Senior Notes Due 2017 (the "Senior Notes") issued by certain of the Debtors filed an alternative debtor in possession financing proposal [Dkt. No. 61] (the "First Alternative DIP"). The First Alternative DIP consisted of a $55 million debtor in possession financing package, with up to $35 million of the proceeds to be used to pay down all amounts outstanding under the Prepetition Senior Loan.[5] On the same day, this Court entered an order approving the Proposed DIP on an interim basis and scheduling a hearing (the "DIP Hearing") to determine whether the Proposed DIP or the First Alternative DIP would be entered on a final basis.[6]

5. Prior to the DIP Hearing, however, certain members of the Ad Hoc Consortium (the "Ad Hoc Consortium Lenders") purchased the Prepetition Senior Loan in its entirety from the Prepetition Senior Lenders and negotiated a second alternative debtor in possession financing proposal (the "Second Alternative DIP") with the Prepetition Term Loan Lenders and the Debtors. The Second Alternative DIP consists of a $75 million financing package, with $41,666,667 to be provided by the Ad Hoc Consortium Lenders and $33,333,333 to be provided by certain of the Prepetition Term Loan Lenders (the "Term DIP Lenders" and, together with the

---

4 See *Id.*

5 See First Alternative DIP, Exhibit A.

6 See *Interim Order: (I) Pursuant to 11 U.S.C. §§ 105, 361, 362, 363, 364, and 507 Authorizing the Debtors to (A) Obtain Postpetition Financing, (B) Grant Senior Liens and Superpriority Administrative Expense Status, (C) Use Cash Collateral of Prepetition Secured Parties, and (D) Grant Adequate Protection to Prepetition Secured Parties; (II) Scheduling a Final Hearing; and (III) Granting Related Relief* [Dkt. No. 78].

Ad Hoc Consortium Lenders, the "DIP Lenders").[7] But only $20 million of the Second Alternative DIP would be made available to the Debtors. The remaining $55 million would not be paid at all. Instead, pursuant to the Second Alternative DIP $55 million of prepetition secured debt would simply be elevated in priority, among other things (i.e., "rolled-up").[8]

6. Sciens submits this Limited Objection because it does not believe that the roll-up feature of the Second Alternative DIP is appropriate. In particular, despite boasting a loan amount of nearly four times the amount initially contemplated by the original Proposed DIP, only the same $20 million would actually be available to the Debtors. Instead of providing working capital or otherwise alleviating the Debtors' liquidity constraints, the remaining $55 million constitutes a roll-up whereby the entire amount of the Prepetition Senior Loan and $20 million of the Prepetition Term Loan would be deemed to be obligations under the Second Alternative DIP facilities.[9]

7. The roll-up is inappropriate for several reasons. *First*, it places the Ad Hoc Consortium in a position to dictate the outcome of the Debtors' chapter 11 cases. It does so because the Ad Hoc Consortium Lenders will be immune from a plan of reorganization cram down on account of the Prepetition Senior Loan. This is precisely the type of outcome determinative measure that the Ad Hoc Consortium itself excoriated at the First Day Hearing.[10] *Second*, it is inappropriate for the Ad Hoc Consortium Lenders – having now positioned themselves as the DIP lenders – to condition the Second Alternative DIP on terms more onerous

---

[7] See *Interim Order: (I) Pursuant to 11 U.S.C. §§ 105, 361, 362, 363, 364, and 507 Authorizing the Debtors to (A) Obtain Postpetition Financing, (B) Grant Senior Liens and Superpriority Administrative Expense Status, (C) Use Cash Collateral of Prepetition Secured Parties, and (D) Grant Adequate Protection to Prepetition Secured Parties; (II) Scheduling a Final Hearing; and (III) Granting Related Relief* [Dkt. No. 126].

[8] See *Id.*

[9] See *Id.*

[10] See Supplemental Objection at ¶ 1.

than previously offered and neither necessary nor supported by the record in these cases.[11] *Third*, as further described below, the Debtors have not satisfied their substantial burden to justify the roll-up of prepetition debt or the superpriority liens that would be created under the Second Alternative DIP. Accordingly, Sciens requests that the Court deny the Second Alternative DIP until the roll-up feature has been removed.

LIMITED OBJECTION

8. If the Second Alternative DIP is approved, the Debtors would be permitted to pay $55 million in prepetition obligations to the DIP Lenders under the Prepetition Facilities. At the same time, the DIP Lenders would receive superpriority administrative expense claims that are based on the same prepetition obligations paid down under the Prepetition Facilities. By elevating the status of prepetition claims in this manner, the proposed roll-up of prepetition claims is strategically beneficial to the DIP Lenders, and in particular the Ad Hoc Consortium Lenders because 100% of the Ad Hoc Consortium Lenders' prepetition secured claims would be rolled-up. As noted by a leading bankruptcy treatise in the context of roll-up financing:

> The[] protections [available to postpetition lenders] can sometimes ***shift the dynamics of a chapter 11 reorganization dramatically***, because of the increased rights that the holder of an administrative claim may have over the holder of a prepetition secured claim. For example, the holder of a prepetition claim risks cramdown treatment under a chapter 11 plan . . . . By contrast, administrative claims must be paid in cash in full upon confirmation, giving the postpetition lender greater leverage and control over the case.

3 COLLIER ON BANKRUPTCY 364.04(2)(e) (Alan N. Resnick & Henry J. Sommer eds., 15th rev. ed.) (emphasis added).

[11] The First Alternative DIP offered by the Ad Hoc Consortium Lenders contemplated only that $35 million of the DIP proceeds may be used to buy out the Debtors' prepetition ABL facility. The proposed roll-up is objectionable no matter its size.

9. It follows that courts are often circumspect when a prepetition secured lender seeks to roll-up prepetition debt. See, e.g., In re Saybrook Mfg. Co., Inc., 963 F.2d 1490, 1494–96 (11th Cir. 1992) (noting that cross-collateralization is inconsistent with bankruptcy law because it (a) is not authorized as a means of postpetition financing pursuant to Section 364 and (b) is directly contrary to the fundamental priority scheme of the Bankruptcy Code); Official Comm. of Unsecured Creditors of New World Pasta Co. v. New World Pasta Co., 322 B.R. 560, 569 n.4 (M.D. Pa. 2005) (noting that roll-up provisions "have the effect of improving the priority of a prepetition creditor"); In re Tenney Vill. Co., 104 B.R. 562, 570 (Bankr. D.N.H. 1989) (holding that "Section 364(d) speaks only of the granting of liens as security for new credit authorized by the Court"); In re Monach Circuit Indus., Inc., 41 B.R. 859, 862 (Bankr. E.D. Pa. 1984) (stating that cross-collateralization constitutes an unauthorized preference); In re Vanguard Diversified, Inc., 31 B.R. 364, 366 (Bankr. E.D.N.Y. 1983) (noting that cross-collateralization is "a disfavored means of financing").

10. Furthermore, and undoubtedly reflective of the power-shifting concerns noted above, the local rules promulgated in this district reflect the general reluctance to permit prepetition debt from transforming into postpetition debt. Specifically, Local Rule 4001-2(a)(i)(E) requires the disclosure of such provisions, and Local Rule 4001-2(b) prohibits debtors from seeking such relief in interim orders "[i]n the absence of extraordinary circumstances." Similarly, the Bankruptcy Court for the Southern District of New York has adopted guidelines to address the "extraordinary" of roll-up financings. *See* Bankr. S.D.N.Y. General Order No. M-274.

11. As noted above, the proposed roll-up entirely or substantially prevents the Debtors' prepetition lenders from being crammed down under a chapter 11 plan. This is

particularly troubling now that the Ad Hoc Consortium Lenders dominate both the secured and unsecured tiers of the Debtors' capital structure. It is in the best interests of the Debtors' estates and the Debtors' stakeholders as a whole, including the thousands of retail bondholders, that this Court decline to bestow even greater leverage on the DIP Lenders, and particularly the Ad Hoc Consortium Lenders, than they already have. In fact, the roll-up financing contemplated under the Second Alternative DIP must be denied in the absence of evidence demonstrating the extraordinary circumstances that warrant such relief. The Debtors have not met this burden. Neither the Debtors nor the DIP Lenders have provided any justification for the proposed roll-up at all.

[SIGNATURES ON NEXT PAGE]

Dated: Wilmington, Delaware
July 2, 2015

SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP

/s/ Jason M. Liberi

Anthony W. Clark (I.D. No. 2051)
Jason M. Liberi (I.D. No. 4425)
One Rodney Square
P.O. Box 636
Wilmington, Delaware 19899-0636
(302) 651-3000 (telephone)
(302) 651-3001 (facsimile)

- and -

Jay M. Goffman, Esq.
Mark A. McDermott, Esq.
Evan A. Hill, Esq.
Skadden, Arps, Slate, Meagher & Flom LLP
Four Times Square
New York, New York 10036-6522
Telephone: (212) 735-3000
Fax: (212) 735-2000

Counsel for Sciens Capital Management LLC