IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	)	
	)	Case No. 15-11296 (LSS)
	)	
COLT HOLDING COMPANY, LLC, *et al.*[1],	)	Chapter 11
	)	
Debtors.	)	(Jointly Administered)
	)	
	)	Hearing Date: August 13, 2015, at 10:30
	)	A.M. (prevailing Eastern time)
	)	
	)	Re: D.I. 213, 307
	)	

REPLY TO THE OBJECTION OF THE AD HOC CONSORTIUM OF HOLDERS OF 8.75% SENIOR NOTES DUE 2017 TO APPLICATION PURSUANT TO FED. R. BANKR. P. 2014(a) FOR ORDER UNDER SECTION 1103 OF THE BANKRUPTCY CODE AUTHORIZING THE EMPLOYMENT AND RETENTION OF FTI CONSULTING, INC. AS FINANCIAL ADVISOR TO THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS NUNC PRO TUNC TO JUNE 25, 2015

The Official Committee of Unsecured Creditors (the "Committee") of the above-captioned debtors and debtors in possession (collectively, the "Debtors") hereby submits its reply (the "Reply") to the *Objection of the Ad Hoc Consortium of Holders of 8.75% Senior Notes due 2017 to the Application Pursuant to Fed. R. Bankr. P. 2014(a) for Order Under Section 1103 of the Bankruptcy Code Authorizing the Employment and Retention of FTI Consulting, Inc. as Financial Advisor to the Official Committee of Unsecured Creditors Nunc Pro Tunc to June 25, 2015* [D.I. 307] (the "Objection"). In support of its Reply, the Committee respectfully states as follows:

[1] The Debtors in these cases, along with the last four digits of each Debtor's federal tax identification number, are Colt Holding Company LLC (0094); Colt Security LLC (4276); Colt Defense LLC (1950); Colt Finance Corp. (7687); New Colt Holding Corp. (6913); Colt's Manufacturing Company LLC (9139); Colt Defense Technical Services LLC (8809); Colt Canada Corporation (5534); Colt International Coöperatief U.A. (6822); CDH II Holdco Inc. (1782). The address of the Debtors' corporate headquarters is: 547 New Park Avenue, West Hartford, Connecticut 06110.

JURISDICTION AND VENUE

1. The Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334. Venue of this proceeding and this matter is proper in this district pursuant to 28 U.S.C. §§ 1408 and 1409. The statutory predicates for the relief sought herein are sections 328(a) and 1103 of the Bankruptcy Code.

BACKGROUND

2. On July 14, 2015, the Committee filed the *Application Pursuant to Fed. R. Bankr. P. 2014(a) for Order Under Section 1103 of the Bankruptcy Code Authorizing the Employment and Retention of FTI Consulting, Inc. as Financial Advisor to the Official Committee of Unsecured Creditors Nunc Pro Tunc to June 25, 2015* [D.I. 213] (the "Application"), including the supporting declaration of Matthew Diaz.

3. On August 5, 2015, the Ad Hoc Consortium of Holders of 8.75% Senior Notes due 2017 (the "Consortium") filed the Objection.

REPLY

4. In its Objection, the Consortium argues that FTI's[2] proposed fee structure is "unreasonable" under the circumstances of these cases. Distilled to its essence, the Objection asks this Court to deny approval of FTI's compensation structure because, in the view of the Consortium (a non-estate fiduciary), the Debtors' restructuring efforts began pre-petition and considerable work regarding plan concepts, DIP financing, and causes of action was completed before these chapter 11 cases filed. For the reasons set forth below, the Objection misses the mark.

I. The Consortium Mischaracterizes the Circumstances of These Cases.

5. In a chapter 11 case, it is virtually always the case that the debtor's restructuring

[2] Capitalized terms used but not defined herein shall have the meanings ascribed to them in the Application.

efforts, encompassing many of the tasks listed by the Consortium in its Objection, would have commenced pre-petition. The unremarkable fact that this occurred in these cases has no bearing on the relief requested in the Application. To the extent that the pre-petition restructuring efforts here were extraordinary or atypical, an assessment the Committee does not necessarily share, they were performed largely by *non-estate fiduciaries – some of whom are now DIP Lenders*. The fact that the Consortium, in its own self-interest, negotiated pre-petition and ultimately obtained post-petition approval of a DIP financing package is simply irrelevant to the terms under which the Committee, an estate professional with a fiduciary duty to all unsecured creditors, may retain a financial advisor.

6. Second, the Objection appears to rest on the faulty premise that the trajectory and likely outcome of these cases is, at least to some extent, a *fait accompli*. Based on this premise and the fact the Consortium analyzed certain issues pre-petition, the Consortium suggests that the terms of FTI's retention are not "tailored to the task at hand." This argument ignores the true state of affairs here: the Debtors are developing their business plan, the parties are at odds over the propriety of the Debtors' proposed sale process and no stalking horse has been identified, the Debtors' access to their primary manufacturing facility is in question, no plan has been filed, no plan support agreements with any constituents are in place, and extensive discovery is ongoing. Simply put, these cases are complex and in flux, rather than straightforward and pre-baked, as the Consortium would suggest. Indeed, the Consortium's own pleadings recognize as much: "*[T]he case dynamic has changed. The Debtors' secured and unsecured creditors prefer a plan strategy*." [D.I. 258], at ¶1 (emphasis added). Likewise, although the Consortium alludes to its efforts in investigating matters relating to the Debtors' landlord pre-petition, the Consortium has since filed a Rule 2004 motion seeking discovery of that landlord. [D.I. 225]. Thus, not only

has the Consortium not teed up the issues for the Committee, it is actually continuing in its own right to investigate. Viewed from this perspective, the very premise of the Consortium's argument falls away, and the Objection loses any force it otherwise theoretically might have had. In order to navigate these complex and fluid cases, the Committee requires the services of a skilled financial advisor and has chosen FTI to serve this role. Nothing in the Objection provides a basis for questioning this decision.

7. The Committee also notes that, while the Committee has worked well with the Consortium to date, the members of that group and the Committee's constituents are not the same. Nor are the two parties' interests necessarily aligned on all matters in these cases. This is particularly true now that certain of the Consortium's members are secured DIP lenders to the Debtors. The Committee requires an *independent* advisor to assist it in these cases and is entitled to retain FTI to act in this role.

II. The FTI Fee Structure is Appropriate.

8. The Committee is surprised that the Consortium would question the structure of FTI's fees when (a) the Consortium's own financial advisor is charging similar monthly fees and nearly *double* the completion fee ($650,000 versus $1.25 million)[3], and (b) the Debtors' financial advisor is likewise charging a similar monthly fee and, in all likelihood, a significantly higher completion fee ($650,000 versus $1.9 million, less $100,000 of each monthly fee received).[4] Under any scenario, FTI's fees will be substantially less of a burden to the Debtors' estates than those of the Consortium's or the Debtors' financial advisors, both of which will be

[3] Email from Andrew Carty to Todd C. Meyers, et al. (July 23, 2015, 7:30 PM), Exhibit A hereto (setting forth compensation structure for Consortium's financial advisor: $125,000 monthly fees and $1.25 million transaction fee).

[4] *See* D.I. 297, ¶12. It should be noted that the Debtors have also hired Mackinac Partners, who are budgeted to charge $275K per month.

paid from the estates.[5] The structure of the fee arrangement will not change this fact. Moreover, the Committee's fees in total are reasonable for cases of this magnitude and complexity and represent only 10% of the Debtors' restructuring budget for all case professionals. Against this background, the Objection rings particularly hollow.[6]

9. The Consortium's arguments regarding what it terms FTI's "success" fee are similarly misguided. As an initial matter, FTI's back-end fee is unequivocally not a "success" fee. The fee is a completion fee that was agreed to in an effort by FTI to defer its fees and to relieve some of the tension on the Debtors' currently cash-strapped estates, not to reward FTI for any particular outcome. In the Committee's view, such a proposal was more advantageous to the estates in the initial months of these cases because the time commitment early in cases such as these can be (and has already been) substantial, resulting in correspondingly high hourly fees and potentially lower fees near the plan stage, when the Debtors may have greater access to funding. The proposed structure also forces FTI to absorb considerable risk based upon the terms of Final DIP Order. Specifically, under the Final DIP Order, and subject to certain conditions, fees incurred by the Committee's and the Debtors' professionals following delivery of a Carve-Out Trigger Notice (as defined in the Final DIP Order) under the DIP facilities are capped at an aggregate of $500,000. *Id.* ¶ 16(a)(iii). Fees incurred, but not paid, as of the same date are not similarly capped and may be payable, so long as they are within the Final DIP

[5] *See* D.I. 202, Ex. C (the "Final DIP Budget") (reflecting fees budgeted for Consortium's financial advisor, GLC, and Debtors' financial advisor, Perella Weinberg); D.I. 297, ¶ 12 (reflecting final approved fee structure for Perella Weinberg).

[6] The Committee also notes that it engaged in extensive negotiations with the DIP lenders, certain of which are also members of the Consortium, regarding the terms of the final order approving DIP financing [D.I. 202] (the "Final DIP Order"). The consideration received by the Committee under the Final DIP Order in exchange for withdrawing its various objections thereto included, among other things, a monthly allocation under the Final DIP Budget of $600,000 for the Committee's professionals, including FTI. In agreeing to this amount (which, for avoidance of doubt, does not constitute a cap), the Committee considered FTI's fee structure and determined that the budgeted amount would, among other things, allow for FTI to perform the services required to act as the Committee's financial advisor. From the Committee's perspective, the filing of the Objection could be construed as an effort to limit FTI's ability to perform these tasks or to revisit the heavily negotiated bargain embodied in the Final DIP Order, neither of which is appropriate here.

Budget and ultimately approved by the Court. *Id.* By back-loading its fee structure, FTI has simultaneously (i) eased the Debtors' cash flow concerns, and (ii) put at risk its larger back-end fees, which could in theory go unpaid if a default occurs under either of the DIP facilities.

10. Moreover, the fact that the Committee will not be "providing capital" or, through FTI, "run[ning] an M&A process" is irrelevant here. It is rarely, if ever, the responsibility of a committee to raise capital or lead an M&A process, yet courts routinely approve compensation of financial advisors on terms similar to those proposed in the Application. Indeed, although the Objection seems to imply that FTI always charges on an hourly basis for its engagements as financial advisor to committees, this is simply not the case. FTI has utilized this fee structure (monthly fees plus a completion fee) as financial advisor to committees in countless other cases. *See* First Supplemental Declaration of Matthew Diaz, attached hereto as Exhibit B (the "First Supplemental Declaration"), ¶ 2 (listing cases). And the Committee had an option in these cases and chose this compensation structure. Taken to its logical extreme, the Consortium's argument would dictate that this structure would be unavailable to committees and their financial advisors. The foregoing cases belie this position.

11. Although FTI is not raising capital or running an M&A process, it has committed significant resources to and performed substantial work on the Debtors' cases and will continue to do so throughout these cases. Without limitation, FTI has undertaken or will undertake the following actions on behalf of the Committee:

(a) Investigating pre-petition transactions to which one or more of the Debtors were a party;

(b) Analyzing the Debtors' cash flows and evaluating options for financing to the extent that funds advanced under the DIP facilities are exhausted;

(c) Working, both independently and in concert with the Debtors' financial advisor, to locate potential buyers for the Debtors' assets and otherwise bolster the marketing process therefor;

(d) Evaluating the Debtors' financial results and projections and providing both the Committee and the Debtors with analyses and proposals based upon the same;

(e) In consultation with the firm's real estate group, analyzing matters relating to the Debtors' West Hartford, Connecticut lease and manufacturing facility;

(f) Negotiating the Final DIP Budget;

(g) Evaluating and advising the Committee on the merits of sale and plan structures in these cases;

(h) Assessing go forward capital structures and evaluating the feasibility of any proposed plans;

(i) Challenging proposed plan valuations and developing alternative valuations, if necessary; and

(j) Meeting with the Debtors and professionals of the Debtors and the Consortium regarding the matters set forth above, among others.

See First Supplemental Declaration, ¶ 3.

12. Fundamentally, the Committee has the right to choose its professionals and compensate them reasonably. Section 328(a) of the Bankruptcy Code provides, in relevant part, that a committee "with the court's approval, may employ or authorize the employment of a professional person under section 327 . . . on any reasonable terms and conditions of employment, including on a retainer, on an hourly basis, on a fixed or percentage fee basis, or on a contingent fee basis . . . ." *Id.* § 328(a). In deciding whether to approve the retention of a financial advisor under section 328(a), "the appropriate inquiry is whether taken as a whole, the terms of the retention are fair and reasonable, and the retention is in the [best] interest of the estate." *In re Joan & David Halpern Inc.*, 248 B.R. 43, 47 (Bankr. S.D.N.Y. 2000). In making such a determination, courts consider a non-exhaustive list of factors, including:

(a) whether the terms of engagement reflect normal business terms in the marketplace;

> (b) whether the parties are sophisticated entities with equal bargaining power who engaged in an arm's length negotiation;
>
> (c) whether the retention is in the best interests of the estate;
>
> (d) whether there is creditor opposition to the retention and the compensation procedures; and
>
> (e) whether, given the size, circumstances, and posture of the case, the amount of compensation is reasonable.

See In re Insilco Techs., Inc., 291 B.R. 628, 634 (Bankr. D. Del. 2003). A committee's decision to retain a professional on reasonable terms is entitled to deference under the "business judgment" standard of review. *See In re One2One Commc'ns, LLC*, No. 12-27311 (NLW), 2014 WL 3882467, at *2 (Bankr. D.N.J. Aug. 7, 2014) (referring to "appropriate exercise of [committee's] business judgment"); *In re Grand Eagle Companies, Inc.*, 310 B.R. 79, 85 (Bankr. N.D. Ohio), *report accepted in part, rejected in part sub nom. Official Comm. Unsecured Creditors of Grand Eagle Companies, Inc. v. ASEA Brown Boverie, Inc.*, 313 B.R. 219 (N.D. Ohio 2004) (referring to "the touchstone for assessing the activity of both trustees and official creditors' committee, the business judgment rule"). These tests are met here, and the Objection should be overruled.

13. Additionally, while the Consortium points out that section 328's "improvident" standard limits the ability of parties to object to FTI's fixed fees in the event "there is less work to do", the converse is also true: should FTI be required to perform more work than is anticipated, FTI's fees will remain the same (and FTI will not request additional fees).

CONCLUSION

Based upon the foregoing, the Committee respectfully requests that this Court overrule the Objection, approve the Application and enter an order, substantially in the form attached to the Application as Exhibit 2, authorizing the Committee to employ and retain FTI as its financial

advisor for the purposes set forth in the Application, with such employment being *nunc pro tunc* to June 25, 2015**,** and that the Court grant such further relief as is just and proper.

Dated: August 10, 2015
Wilmington, Delaware

/s/ Domenic E. Pacitti

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