Docket #0480 Date Filed: 9/17/2015

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.[1]	**Re: D.I. 406, 407, 417, 456**

REPLY OF THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS IN SUPPORT OF MOTION OF THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS FOR AN ORDER GRANTING THE COMMITTEE: (A) DERIVATIVE STANDING TO ASSERT, PROSECUTE, AND SETTLE CLAIMS ARISING OUT OF THE DEBTORS' LEASE OF THE WEST HARTFORD FACILITY WITH NPA HARTFORD LLC; AND (B) AUTHORIZATION TO HOLD, ASSERT AND, IF NECESSARY, WAIVE PRIVILEGES ON BEHALF OF THE ESTATES

[1] The Debtors in these cases, along with the last four digits of each Debtors' 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); and CDH II Holdco Inc. (1782). The address of the Debtors' corporate headquarters is: 547 New Park Avenue, West Hartford, Connecticut 06110.

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PRELIMINARY STATEMENT[1]

1. As this Court is well aware, the Committee has been and is still very concerned about conflicts of interest and potential claims and defenses relating to the Lease. These concerns resulted in the Committee conducting its own due diligence and legal analysis, identifying the Claims, disclosing the Claims to the Debtors, and now, seeking standing as the only remaining fiduciary willing to pursue the Claims.

2. Notwithstanding the Committee's efforts to preserve the Lease and the value associated therewith, the Debtors' Objection suggests that the Lease issues will be resolved in a yet to be seen plan term sheet. Despite the Committee's request to be part of the plan term sheet process, neither the Debtors, Sciens nor the Landlord have invited the Committee to the negotiating table. Not even once. Rather, the Debtors – the lone objectors to the Standing Motion – propose that the Committee should remain stymied and prohibited from acting to preserve the Lease and await the fabled plan term sheet, which will not only be devoid of *any* input by the Committee and not the product of arms' length negotiations among all stakeholders, but also will no doubt contain a release of the Claims, worth potentially in excess of $100 million, and provide the Committee's constituency with little or no return on its approximate $300 million in claims.[2]

3. In support of their argument, the Debtors suggest that if the Committee were to pursue the Claims, the negotiations concerning the "global settlement" may be jeopardized.

[1] Capitalized terms used but not otherwise defined herein shall have the meanings ascribed to them below or in the Standing Motion or Proposed Complaint, as applicable.

[2] The terms of any plan term sheet that ultimately may be presented will no doubt pale, from the perspective of unsecured creditors, in comparison to the Consortium's prepetition plan proposal, which was flatly rejected by Sciens. Those terms included, among other things, unsecured noteholders receiving 40% of the equity of the reorganized Debtors and their *pro rata* share of new notes in the aggregate principal amount of $125 million. *See Supplemental Objection of Ad Hoc Consortium of Holders of Senior Notes to Debtors' DIP Motion* [D.I. 100] at ¶ 33.

First, absent participation by the Committee, the Debtors' "global settlement" is anything but "global". Second, the reality is that the best settlements are often reached when litigation is already underway. Indeed, absent the prosecution of the Claims, NPA Hartford and Sciens will have no interest in dealing with the Committee because they will achieve victory as the clock runs towards the midnight hour. As such, derivative standing will facilitate a fair and value maximizing "global settlement" as opposed to a settlement to be incorporated in an unconfirmable plan.[3]

4. The Debtors' arguments that the costs of pursuing the Claims will somehow outweigh the potential benefits to these estates ring hollow. The Lease issue is, by the Debtors' own admission, the paramount issue in these cases. Indeed, the resolution of the Lease will form the cornerstone of any plan of reorganization or proposed sale. Permitting the Committee to prosecute the Claims and, among other things, obtain injunctive relief prohibiting the Landlord from evicting or dispossessing the Debtors would be invaluable. For one thing, it would create clarity regarding the valuable Lease asset – something the Debtors have been unable (or unwilling) to do.

5. With respect to the authority to settle claims, the Committee submits that such authority is mandated under the circumstances of these cases. Contrary to the Debtors' position, there is authority supporting the Committee's requested relief to settle the Claims. In *In re Residential Capital, LLC, et al.*, Case No. 12-12020 (MG) (Bankr. S.D.N.Y. 2012) ("*ResCap*"), the court granted a creditors' committee, subject to consultation with the debtor, the exclusive authority to settle estate claims. Yet, the Debtors, who argue that they should be the only party

[3] Unless the plan provides unsecured creditors with the value inherent in the Claims, the plan will not satisfy section 1129(a)(7) of the Bankruptcy Code. Furthermore, it is highly unlikely that the plan will satisfy the "cram down" requirements for confirmation.

that can settle the Claims, have inherent conflicts with *all* of the Proposed Defendants. Furthermore, absent the Committee's authority to settle the Claims, the Proposed Defendants would likely not take the litigation seriously knowing that at any time they could settle with the Debtors (who are conflicted; so essentially settling with themselves) and avoid litigation. Under these circumstances, the Debtors' position is nonsensical and it is wholly appropriate that the Committee – the only estate fiduciary without a conflict vis-à-vis the Claims – be vested with the authority to settle the Claims.

6. As discussed in further detail below, all of the legal requirements for granting the Committee derivative standing to pursue and settle the Claims have been satisfied. The Committee has also demonstrated that it is appropriate for it to hold, assert and if necessary, waive the Privileges. As such, the Committee respectfully requests that this Court grant it derivative standing and the related relief set forth in the Standing Motion.

BACKGROUND

7. The Committee incorporates by reference the averments in paragraphs 1-103 of the proposed complaint (the "Proposed Complaint") attached to the Motion of the Official Committee of Unsecured Creditors for an Order Granting the Committee: (A) Derivative Standing to Assert, Prosecute, and Settle Claims Arising Out of the Debtors' Lease of the West Hartford Facility with NPA Hartford LLC; and (B) Authorization to Hold, Assert and, if Necessary, Waive Privileges on Behalf of the Estates (the "Standing Motion") [D.I. 406].

8. On September 10, 2015, the Debtors filed their opposition to the Derivative Standing Motion (the "Objection") [D.I. 456].

REPLY

I. THE COMMITTEE HAS SATISFIED THE STANDARD FOR DERIVATIVE STANDING

9. In the Objection, the Debtors argue that the Committee fails to satisfy the standard for derivative standing because: (a) it has not established that the benefit of pursuing the Claims would outweigh the costs; (b) it has not established that the Claims are colorable; and (c) the Debtors did not unjustifiably refuse a demand to pursue the Claims. The Debtors are wrong on all counts.

A. The Benefit of Pursuing the Claims Undoubtedly Outweighs the Costs

10. The benefits of pursuing the Claims related to the Lease – which is the marquee issue in these cases whether the Debtors pursue a sale or a plan – undoubtedly outweigh the costs of litigation. Indeed, even if a contentious litigation were to ensue, the cost of prosecution will be relatively modest given the amount at stake. *Adelphia Commc'ns Corp. v. Bank of Am. (In re Adelphia Commc'ns Corp.)*, 330 B.R. 364, 384 (Bankr. S.D.N.Y. 2005). The importance of what is at stake has been underscored by the Debtors themselves, who state that, "a relocation of the Debtors' manufacturing operations out of the West Hartford Facility would take a minimum of two to three years and could require tens of millions of dollars of incremental capital investment." *Maib Decl*. at ¶ 53. As a result, the potential benefit of litigating the Claims is invaluable in that it would provide, in addition to monetary relief, certainty concerning the Lease. This certainty, which the Debtors have been unable (or unwilling) to obtain, will undoubtedly enhance the Debtors' enterprise value and at a bare minimum, avoid the "tens of millions of dollars" required to relocate the Debtors' operations. Clarity concerning the Lease will also enhance the prospects of a robust asset auction or plan sponsor process as potential bidders/sponsors can rest assured that the specially designed and regulatory permitted West

Hartford Facility, a facility where the "vast majority" of the Debtors' production takes place, will remain intact. *Id.*

11. The Debtors also argue that the Committee's proposed litigation would be messy and costly. That conclusory statement is without merit. First, the Committee has already investigated and analyzed the *bona fides* of the Claims. Second, the Committee has already prepared the Proposed Complaint. Third, documentary discovery is already underway with much of it already being produced and analyzed by the Committee. Thus, the Debtors' characterization of the costs of moving forward with the Claims are overstated and, in any event, are dwarfed by the potential benefits of litigating the Claims.

B. <u>The Claims That the Committee Seeks to Bring are Colorable</u>

12. The "threshold for stating a colorable claim is low[,]" *see In re Washington Mutual, Inc.*, 461 B.R. 200, 255 (Bankr. D. Del. 2011) and "a relatively easy one" to meet. *See In re Adelphia Commc'ns Corp.*, 330 B.R. at 376; *see also In re Am.'s Hobby Ctr., Inc.*, 223 B.R. 275, 288 (Bankr. S.D.N.Y. 1998) (observing that standing should be denied only if the claim is "facially defective"); *In re Colfor, Inc.*, No. 96-60306, 1998 WL 70718, *2 (Bankr. N.D. Ohio Jan. 5, 1998) (stating that consistent with the common meaning of "colorable", the claims to be asserted need only be "plausible" or "not without some merit"). In deciding whether there is a colorable claim, courts typically undertake the same analysis as when a defendant moves to dismiss a complaint for failure to state a claim. *In re Centaur, LLC*, No. 10-10799 (KJC) 2010 WL 4624910, at *4 (Bankr. D. Del. Nov. 5, 2010). Under that analysis, the plaintiff (the Committee) "gets the benefit of the doubt" with respect to the factual allegations in its complaint in connection with a motion to dismiss. *In re Pitt Penn Holding Co.*, 484 B.R. 25, 34 (Bankr. D. Del. 2012).

13. Thus, the Committee is only required to establish the existence of a plausible claim and that its contentions are not frivolous. *Id.* at 36. The Committee has unquestionably done that by way of the Standing Motion and Proposed Complaint. The Debtors seek to elevate the standard, without citing any precedent, by stating that the evaluation of colorability should be deferred until discovery is complete. The completion of discovery is not a prerequisite under the Third Circuit standard for determining colorability. As discussed below, the Claims are legally cognizable, plausible and genuine and as a result, colorable.[4]

i. Claims for Breach of Fiduciary Duties (Count I)

14. Sciens, as ultimate equity owner of the Debtors, has owed, and continues to owe, to the Debtors, the fiduciary duties of loyalty, care and good faith. *See Pepper v. Litton*, 308 U.S. 295, 306 (1939) (internal citation omitted) ("A director is a fiduciary. So is a dominant or controlling stockholder or group of stockholders."). Standen and Rigas, as members of the Governing Board of Colt Defense, owed Colt Defense and the other Debtors the same fiduciary duties. *Id.*

15. A claim for breach of the duty of care requires a showing of gross negligence and that showing generally "requires directors and officers to fail to inform themselves fully and in a deliberate manner." *In re Fedders N. Am., Inc.*, 405 B.R. 527, 539 (Bankr. D. Del. 2009). The duty of loyalty "mandates that the best interest of the corporation and its shareholders takes precedence over any interest possessed by a director, officer or controlling shareholder and not shared by the stockholders generally." *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993). When a conflict of interest exists, the conflicted fiduciary bears the burden of

[4] Notably, the Debtors rely entirely on the bald, general assertion that the Claims are not colorable. The fact that they have made no effort to address the Claims on an individual basis and assert with specificity alleged deficiencies in the Claims is a tacit acknowledgment that the Claims are colorable.

establishing the entire fairness of the transaction to the corporation. *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710 (Del. 1983). A claim for breach of the duty of good faith may be established in several ways.

> A failure to act in good faith may be shown, for instance, where the fiduciary intentionally acts with a purpose other than that of advancing the best interests of the corporation, where the fiduciary acts with the intent to violate applicable positive law, or where the fiduciary intentionally fails to act in the face of a known duty to act, demonstrating a conscious disregard for his duties.

In re Walt Disney Co. Derivative Litig., 906 A.2d 27, 67 (Del. Ch. 2005).

16. The Claims for the breach of fiduciary duties against Sciens are colorable. During all relevant times, Sciens acted in its own self-interest by, among other things: (a) causing the Landlord to refuse to extend the Lease unless Sciens remained in control of Colt Defense; (b) failing to alert members of management, on a timely basis, that there might be impediments to obtaining a Lease extension from an entity it controlled; and (c) failing to exercise its best effort to procure the Landlord's timely consent to a Lease extension that would accommodate the needs of the Company. Sciens' purpose was and still is clear: to further its own self-interest and remain in control of the Company – a purpose that has devalued the Company and frustrated the prospects for creating a fair and level playing field during the chapter 11 process. In fact, Sciens has acted as an impediment to the Debtors' efforts to effectuate an extension of the Lease – conduct in clear violation of its duties as a fiduciary that threatens the very survival of the Company.

17. Standen and Rigas, as members of the Governing Board of Colt Defense, similarly acted in their self-interest (and the interests of Sciens, which they control). Indeed, just like Sciens, rather than using their best efforts to obtain a life-preserving Lease extension, they

used the Lease as a bargaining chip to further their and Sciens' interests at the expense of the Debtors and their unsecured creditors.

18. These actions, which have significantly devalued the Company and its assets by impeding the extension of the Lease, demonstrate that the Claims against Sciens, Standen and Rigas (collectively, the "Fiduciaries") for the breach of their fiduciary duties are colorable and *bona fide.*

ii. Claims for Aiding and Abetting Breaches of Fiduciary Duties (Count II)

19. A claim for aiding and abetting a breach of fiduciary duties requires "(1) the existence of a fiduciary relationship; (2) proof that the fiduciary breached its duty; (3) proof that a defendant, who is not a fiduciary, knowingly participated in a breach; and (4) a showing that damages to the plaintiff resulted from the concerted action of the fiduciary and the nonfiduciary." *Fedders*, 405 B.R. at 543-44.

20. NPA Hartford, NPA Management, Valnic and Smallman (collectively, the "Aiding and Abetting Defendants") are each aware of the respective capacities in which Sciens (controlling equity holder), Standen (board member) and Rigas (board member) are related to the Company and the duties they each owed to the Company. Given each of the Aiding and Abetting Defendants' roles with respect to matters pertaining to the Lease and their relationship with the Fiduciaries, the inference is inescapable that the Aiding and Abetting Defendants were aware that the Fiduciaries were exploiting the purported termination of the Lease as a bargaining chip to further their self-interests. Moreover, by furthering the Fiduciaries' scheme, the Aiding and Abetting Defendants knowingly participated in the breach of the fiduciary duties of Sciens, Standen and Rigas. As a result, the Claims for aiding and abetting as against NPA Hartford, NPA Management, Valnic and Smallman are, at a minimum, colorable and *bona fide.*

iii. Claim for Avoidance of LLC Agreement Amendment (Count III)

21. Until April 9, 2015, Sciens, Standen, and Rigas unquestionably owed fiduciary duties to Colt Defense. Colt Defense's rights to enforce these fiduciary duties had value and constituted property within the meaning of section 548 of the Bankruptcy Code. Approximately two months before placing Colt Defense into bankruptcy, Sciens, and, on information and belief, Standen and Rigas, caused the LLC Agreement to be amended pursuant to the LLC Agreement Amendment in an effort to eliminate their fiduciary duties.

22. Execution of the LLC Agreement Amendment effected a transfer of property within the meaning of section 101(54)(D) of the Bankruptcy Code (the "Transfer"), which was made with actual intent to hinder or delay creditors of Colt Defense; or for which Colt Defense did not receive reasonably equivalent value (or any value for that matter), and was made at a time when Colt Defense was insolvent or engaged in business or a transaction, or was about to engage in business or a transaction, for which any property remaining with Colt Defense was an unreasonably small capital, as evidenced by Colt Defense's bankruptcy filing approximately two months after the Transfer. As a result, the Claim for avoidance of the LLC Agreement Amendment is colorable and *bona fide.*

iv. Claims for Tortious Interference with Business Relations with Landlord (Count IV)

23. The elements of tortious interference with business relations are: (a) the existence of a business relationship; (b) an intentional and improper interference with that relationship; and (c) a resulting loss of benefits of the relationship. *DiNapoli v. Cooke*, 682 A.2d 603, 608 (Conn. App. Ct. 1996), *cert. denied*, 686 A.2d 124 (Conn. 1996); *G.J. Swanson, LLC v. Cehovsky*, No. FBTCV126027498S, 2013 WL 2278767 (Conn. Super. Ct. Apr. 25, 2013).

24. The Debtors cannot seriously contest that matters pertaining to the Lease constitute a very important business relationship between Colt Defense as tenant and NPA Hartford as landlord. Furthermore, Sciens, NPA Management, Valnic, Standen, Rigas and Smallman (collectively, the "Tortious Interference Defendants") have all had, and continue to have, knowledge of that business relationship. As detailed in the Proposed Complaint, commencing on or after January 1, 2015, the Tortious Interference Defendants intentionally interfered with the existing business relationship between Colt Defense and the Landlord by causing the Landlord to refrain from discussing with, or offering to, Colt Defense an extension of the Lease on terms not tainted by a bad faith ulterior motive to assist Sciens in retaining a controlling interest in the Company This tortious and intentional interference was without just cause or excuse and driven by an improper motive.

25. As a direct and proximate cause of this interference, the Debtors are now faced with the prospect of a forced, value-diminishing section 363 sale or insider controlled plan, or cessation of business operations. Indeed, the harm caused by this interference is part and parcel of the Lease overhang issue that has plagued the Debtors. Accordingly, the Claims for tortious interference of business relations as against Sciens, NPA Management, Valnic, Standen, Rigas and Smallman are colorable and *bona fide*.

v. Claims for Injunctive Relief (Count V and Count VI)

26. The Committee seeks injunctive relief against the Landlord on two separate bases: (a) equitable estoppel; and (b) the breach of the implied obligations of good faith and fair dealing. In the Third Circuit, courts consider the following factors to determine whether injunctive relief should be issued under section 105(a) of the Bankruptcy Code: (a) whether the movant has shown a reasonable likelihood of success on the merits; (b) whether the movant has

shown a likelihood that it will suffer irreparable harm if relief is denied; (c) whether the balance of equities tips in the movant's favor; and (d) whether the public interest favors the relief requested by the movant. *Groupe SEB USA, Inc. v. Euro-Pro Operating LLC*, 774 F.3d 192, 197 (3d Cir. 2014) (citing *Winter v. Natural Res. Def. Council, Inc.*, 555 U.S. 7, 24 (2008)). "In deciding whether to issue an injunction, the court must engage in 'a delicate balancing of the probabilities of ultimate success at final hearing with the consequences of immediate irreparable injury.'" *In re Broadstripe, LLC*, 402 B.R. 646, 655 (Bankr. D. Del. 2009) (quoting *GlaxoSmithKline Consumer Healthcare, L.P. v. Merix Pharm. Corp.*, 197 F. App'x 120, 124 (3d Cir. 2006)). "Such a 'delicate balancing' requires that the above-listed factors be weighed, rather than mechanically applied." *Id.*

a. There is a Reasonable Likelihood of Success on the Merits

27. Equitable estoppel is established if: (a) a party to a contract does or says something which is intended or calculated to induce another to believe in the existence of certain facts and to act upon that belief; and (b) the other party, influenced thereby, actually changes his position or does something to his injury which he otherwise would not have done. *W. v. W.*, 248 Conn. 487, 496, 728 A.2d 1076, 1082 (1999).[5] Indeed, silence by a fiduciary may also give rise to estoppel. *See Duguay v. Great Atl. & Pac. Tea Co.*, No. 391344, 2003 WL 21149855, at *2 (Conn. Super. Ct. Apr. 28, 2003) (citing *Macomber v. Travelers Prop. & Cas. Corp.*, 261 Conn. 620, 640, 804 A.2d 180 (2002)) ("A duty to speak is imposed when there is a fiduciary or confidential relationship between the parties."). Moreover, a plaintiff is not required to show "actual intention to mislead or a deceitful purpose", rather, "[i]t is enough if the circumstances are such that the party is fairly chargeable with knowledge that his declaration may induce the

[5] The Lease is governed by Connecticut law.

action taken." *Steinegger v. Fields*, 37 Conn. Supp. 534, 538, 425 A.2d 597, 599 (Conn. Supp. 1980).

28. The Proposed Complaint has ample detail to make this Claim colorable and highly likely to succeed. For example:

- as a fiduciary of Colt Defense, Sciens had a duty to inform Colt Defense, with enough lead time for Colt Defense to take effective protective action, if there was any prospect that the Lease might not be extended beyond its scheduled termination date;
- Sciens made no such disclosure to Colt Defense in time for Colt Defense to take effective protective action, thereby utilizing silence to lull Colt Defense into a false sense of security regarding the Lease; and
- Colt Defense reasonably relied on the fact that its controlling equity holder, who also controlled the Landlord, had the ability to ensure that an acceptable Lease extension would be forthcoming.

Sciens' conduct is imputed to NPA Hartford for estoppel purposes based on Sciens' control of NPA Hartford and NPA Hartford's active participation in whipsawing Colt Defense on the Lease extension issue.

29. Establishing a breach of the implied obligation of good faith and fair dealing requires that the Committee demonstrate that the defendant (NPA Hartford), in bad faith, impeded the plaintiff's right to receive benefits that he or she reasonably expected to receive under a contract. *De La Concha of Hartford, Inc. v. Aetna Life Ins. Co.*, 269 Conn. 424, 432, 849 A.2d 382, 433 (2004). This duty applies with equal force to landlords. *See, e.g.*, *Warner v. Konover*, 210 Conn. 150, 154, 553 A.2d 1138, 1140 (1989); *Savin Gasoline Props., LLC v. CCO, LLC*, Nos. CV094046741S, CV094045586, 2011 WL 726110 (Conn. Super. Ct. Jan. 31, 2011). In deciding whether to grant a Lease extension to Colt Defense, NPA Hartford is subject to an implied obligation of good faith and fair dealing and does not have unfettered discretion to withhold a Lease extension based on an ulterior motive to enhance Sciens' bargaining position in the Debtors' bankruptcy cases. However, as detailed in the Proposed Complaint, NPA Hartford

has been unwilling to grant Colt Defense a Lease extension in a context other than one in which Sciens, which controls NPA Hartford, retains ownership and control of the Debtors. In fact, even the most recent thirty (30) day extension of the Lease is suspect because that extension was granted only after Sciens resurfaced as the potential plan sponsor.

30. NPA Hartford's exercise of its discretion in withholding a Lease extension to provide leverage to Sciens constitutes bad faith and a breach of NPA Hartford's implied obligation of good faith and fair dealing under the Lease. *See Warner*, 210 Conn. at 156 (holding that plaintiff-tenant stated a claim for breach of duty of good faith and fair dealing where commercial landlord retained discretion to withhold consent to assignment of lease, lease did not clearly establish parameters of such discretion, and landlord refused to consent to assignment, without renegotiation of rent payments).

31. For these reasons, the Committee has demonstrated that its Claims for injunctive relief have a reasonable likelihood of success on the merits.

b. Absent Injunctive Relief, the Debtors will Suffer Irreparable Harm

32. If the Debtors are evicted from the West Hartford Facility, tens if not hundreds of millions of dollars in value will be destroyed and the continuation of the Debtors' business operations will be in jeopardy. *Truglia v. KFC Corp.*, 692 F. Supp. 271, 279 (S.D.N.Y. 1988), *aff'd*, 875 F.2d 308 (2d Cir. 1989) ("loss or destruction of an entire business has also widely been held to constitute irreparable harm, at least when the business has been in operation for some time") (citations omitted). Indeed, even if Colt Defense and the other Debtors operating at the West Hartford Facility were able to find a new facility with the required regulatory approvals shortly after eviction – a scenario the Committee believes is highly unlikely – the lost time and productivity would likely still irreparably harm the Debtors' enterprise. *See Drakes Bay Oyster*

Co. v. Salazar, 921 F. Supp. 2d 972, 995 (N.D. Cal. 2013) (noting that, in absence of injunctive relief, plaintiffs would suffer "gap in production" and inability to effectively resume operations, factors that supported a finding that irreparable harm was likely).

33. The irreparable nature of the harm to the Debtors is further supported by the fact that the Lease rights, which are a real property right, are unique and cannot be readily substituted or replaced. *See Drakes Bay Oyster Co.*, 921 F. Supp. 2d at 994 ("Loss of an interest in real property may also be considered irreparable harm since the unique nature of real property makes a damages remedy inadequate."); *Patriot-BSP City Ctr. II v. U.S. Bank Nat'l Ass'n*, 715 F. Supp. 2d 91, 96 (D.D.C. 2010) ("[i]t is settled beyond the need for citation . . . that a given piece of property is considered to be unique, and its loss is always an irreparable injury") (quotations and citations omitted). As such, absent the injunctive relief requested in the Proposed Complaint, the Debtors and their estates will suffer irreparable harm.

c. The Balance of the Equities Favors the Committee[6]

34. Even if the Committee could not demonstrate a likelihood of success on the merits (which it has), the Court may still issue injunctive relief because the Committee has raised a sufficiently serious question regarding the merits to make it a fair ground for litigation, and a balance of the equities tips decidedly in the Committee's favor. *See, e.g.*, *In re Netia Holdings S.A.*, 278 B.R. 344, 357 (Bankr. S.D.N.Y. 2002) (holding that even if the court had not found a likelihood of success on the merits, the balance of hardships would weigh sharply in favor of issuing preliminary injunction).

35. As discussed above, denial of immediate injunctive relief would be potentially catastrophic for the Debtors. The same cannot be said of NPA Hartford. In fact, there would be

[6] In reality, the Committee and the Debtors should be aligned on this issue because the real balance is between the interests of the Debtors' estates and NPA Hartford, who has not opposed the Standing Motion.

little or no harm to NPA Hartford because it would continue to receive the substantial rent payments owing under the Lease on terms that it was prepared to accept from Sciens. Therefore, the balance of equities decidedly favors the Committee. *See Aim Int'l Trading, LLC v. Valcucine SpA., IBI LLC*, 188 F. Supp. 2d 384, 388 (S.D.N.Y. 2002) (determining that "balance of equities tip[ped] firmly in plaintiffs' favor" where, if the status quo was not preserved, the plaintiffs' business would be destroyed, while the defendants failed to make a showing as to how they would be damaged).

d. The Injunction is in the Public Interest

36. "As a practical matter, if a plaintiff demonstrates both a likelihood of success on the merits and irreparable injury, it almost always will be the case that the public interest will favor the plaintiff." *See Am. Tel. & Tel. Co., v. Winback & Conserve Program, Inc.*, 42 F.3d 1421, 1427 & n.8 (3d Cir. 1994), *cert. denied*, 514 U.S. 1103 (1995). In the context of a bankruptcy case, promoting a successful reorganization is one of the most important public interests. *In re R & G Fin. Corp.*, 441 B.R. 401, 412 (Bankr. D.P.R. 2010) ("[T]he fourth prong of the test, the public interest in the context of a bankruptcy proceeding, consists in promoting a successful reorganization."); *In re Broadstripe*, 402 B.R. at 658 ("In the face of the potential for significant injury to the Debtors' business value and reorganization efforts and the potential loss of service to its customers, the public interest favors granting the requested injunctive relief to enable the Debtors to attempt to reorganize in chapter 11.").

37. Here, absent a meaningful extension, renewal, or court-ordered injunctive relief, the Debtors would be forced to hastily vacate the leased premises and tens if not hundreds of millions of dollars in value could be destroyed. *See In re Nurses' Registry & Home Health Corp.*, 533 B.R. 590, 599 (Bankr. E.D. Ky. 2015) (referencing prior ruling that "the public

interest was served by … the rehabilitation of a troubled company"); *Allied Home Mortg. Corp. v. Donovan*, 830 F. Supp. 2d 223, 234 (S.D. Tex. 2011) (public interest would be served by preserving plaintiff's business). Thus, a preliminary injunction is in the public interest.

C. The Committee Has Satisfied the Demand Requirement Because Demand Would be Futile Given the Debtors' Myriad of Conflicts

38. Given the Debtors' myriad of conflicts with each of the Proposed Defendants, demand would be futile, and for the Debtors to suggest otherwise strains credulity. Case law makes clear that a committee is not required to demand formally that a debtor take action where it is "plain from the record that no action on the part of the debtor would have been forthcoming." *See In re Nat'l Forge Co.*, 326 B.R. 532, 544 (W.D. Pa. 2005) (affirming the bankruptcy court's excusal of the committee's failure to petition the debtor on the ground that any request to file suit, under the facts of the case, would have been futile); *see also In re La. World Exposition, Inc.* 832 F.2d 1391, 1397-98 (5th Cir. 1987); *In re First Capital Holdings Corp.*, 146 B.R. 7, 13 (Bankr. C.D. Cal. 1992).

39. The Debtors argue that the Independent Committee could authorize litigation and no demand was made on it to do so. If that is the case, then why, thirty-one (31) days after delivering the Derivative Standing Letters, has the Independent Committee not authorized the litigation of the Claims? The Debtors argue that negotiations, not litigation, should resolve the Lease overhang issues. Yet, neither the Objection nor the record establishes that (a) the Independent Committee is involved in the plan term sheet negotiations; or (b) that the Lease issues have been delegated to the Independent Committee. Assuming, *arguendo*, that the Independent Committee was involved in plan term sheet negotiations, Sciens has an express veto right over any decision, including those of the Independent Committee, involving "fundamental

transactions" such as a plan of reorganization. Proposed Complaint at ¶ 32. Thus, even the decisions of the Independent Committee may be tainted with conflicts of interest.

40. As further evidence of the Independent Committee being controlled by Sciens, the Committee highlights that after Sciens was no longer the stalking horse bidder for the Debtors' assets, the Debtors – acting under the supposed guidance of the Independent Committee – filed revised bidding procedures that included a proposed sale order granting releases to principals of the Debtors (which includes Sciens) irrespective of whether Sciens was the winning bidder! If the Independent Committee is truly independent, why is it seeking to grant releases to Sciens in the context of a proposed sale order if Sciens is no longer acting as the stalking horse? Thus, no matter how it is dressed up, one thing remains the same: Sciens is in control of the Debtors and not even the Independent Committee can curb such control. Against this backdrop, there can be no serious debate that demand would have been futile.

II. THE AUTHORITY TO HOLD, ASSERT, AND IF NECESSARY, WAIVE THE PRIVILEGES, IS APPROPRIATE

41. The Committee seeks authority to hold, assert and if necessary, waive the Privileges. Contrary to the Debtors' position, that authority is consistent with applicable case law and the facts of these cases. Indeed, the fiduciary exception set forth in *Garner v. Wolfinbarger*, 430 F.2d 1093 (5th Cir. 1970) is squarely on point and the Committee has satisfied each of the factors to determine whether "good cause" exists for applying the *Garner* Doctrine. The Debtors' arguments in opposition to the *Garner* Doctrine are akin to public policy arguments and conveniently ignore: (a) the inherent conflicts of interest that have plagued these estates since the Petition Date; and (b) the relevance of *Official Committee of Asbestos Claimants of G-I Holdings, Inc. v. Heyman*, 342 B.R. 416 (S.D.N.Y. 2006), where a bankruptcy court

applied the *Garner* Doctrine and held that "good cause" existed to set aside the attorney-client privilege.

42. Furthermore, in an attempt to cast the applicability of the *Garner* Doctrine as overreaching, the Debtors exaggerate the scope and extent of the Committee's relief. The fact of the matter is that the Committee is seeking to employ the *Garner* Doctrine only for matters related to past actions concerning the Claims, which are expressly related to the Lease. Moreover, it is highly unlikely that matters pertaining to a lease of a gun manufacturer will implicate trade secrets or other confidential information. Rather, the Committee believes they will implicate documents further evidencing that the Lease was exploited by the Debtors' officers, controlling equity holder and the other Proposed Defendants to the detriment of these estates and its creditors.

43. The Committee submits that absent the authority to hold the Privileges, the Debtors and the Proposed Defendants may utilize their claims of privilege and refuse to produce documents or other information concerning the allegations in the Proposed Complaint. Such a result would directly contravene applicable law. *See In re Bevill, Bresler & Schulman Asset Mgmt Corp.*, 805 F.2d 120, 125 (3d Cir. 1986) ("To provide a blanket privilege regarding all corporate matters on the basis of personal privileges by the officers would prevent the trustee from investigating possible misconduct by the officers and permit the officers to 'use the privilege as a shield against the trustee's efforts.'") (quoting *Commodity Futures Trading Comm'n v. Weintraub*, 471 U.S. 343, 353 (1985)).

III. THE AUTHORITY TO SETTLE THE CLAIMS IS APPROPRIATE

44. The Committee also seeks exclusive authority from this Court to settle the Claims. That authority is wholly appropriate for several reasons. *First*, the Debtors make the

false assertion that no law supports the Committee's request for authority to settle claims. In circumstances where a debtor cannot bring claims and the committee is entitled to derivative standing (such as here), courts have granted a committee exclusive authority to settle claims, subject to consultation with the debtor. *See, e.g.*, *ResCap* [Docket No. 2518] (ordering that the committee shall have, in consultation with the debtor, the "***exclusive right and authority***" to enter into settlements on behalf of the debtors' estates (emphasis added)); *see In re Evergreen Solar, Inc.*, No. 11-12590 (MFW) (Bankr. D. Del. Oct. 28, 2011) [D.I. 382]; *In re Dewey & LeBouef LLP*, No. 12-12321 (MG), 2012 WL 5985445, at *9 (Bankr. S.D.N.Y. Nov. 29, 2012); *In re Majestic Capital, Ltd.*, No. 11-36225 (CGM) (Bankr. S.D.N.Y. Dec. 12, 2011) [D.I. 211]; *In re Old Carco LLC*, No. 09-50002 (AG) (Bankr. S.D.N.Y. Aug. 13, 2009) [D.I. 5151]; *In re The Standard Register Company*, No. 15-10541 (BLS) (Bankr. D. Del. June 10, 2015) [D.I. 648]. The Committee submits that incorporating the same terms as in *ResCap* would fairly and appropriately balance the Committee's right to prosecute and negotiate a settlement of the Claims with the Debtors' ability to propose a "global settlement" in these cases. The Debtors, however, are proposing to do precisely what the *ResCap* court sought to avoid: compromise claims that a debtor is inherently conflicted from pursuing without *any* consent (or consultation) from a creditors' committee. Such a result would effectively render the concept of derivative standing meaningless because it would permit a disabled and conflicted debtor, who could not bring suit in the first instance, to unilaterally settle an estate claim out from under a committee. The Court should not permit such a result.

45. *Second*, the Committee's ability to litigate the Claims will be hindered if the Debtors retain the right to propose a settlement because, among other things: (a) it will reduce the incentive for the Proposed Defendants to enter into settlement negotiations with the

Committee; and (b) it will create an improper settlement dynamic which may be exploited by the Proposed Defendants to the detriment of all unsecured creditors and these estates.

46. *Third*, the Objection suggests that if the Committee is vested with sole settlement authority, the Committee may obstruct the Debtors' efforts towards confirmation of a plan. That statement is baseless and self-serving. As discussed above, the leverage of litigation will facilitate and maximize the value of a "global settlement".

47. *Fourth*, contrary to the Debtors' assertions, the lack of a debtor objection does not make the cases cited in the Standing Motion inapplicable. Rather, it demonstrates that the request for exclusive authority to settle estate claims when a debtor is otherwise conflicted from pursuing such claims is rather uncontroversial and, is in fact, routinely granted. Furthermore, in *ResCap*, where the creditors' committee was vested with exclusive settlement authority for certain estate claims, such authority was granted over objections from, among other parties in interest, the debtors. *See ResCap* [D.I. 1864 and 1865].

48. *Fifth*, contrary to the Debtors' assertion, *Smart World Techs., LLC v. Juno Online Servs., Inc. (In re Smart World Technologies, LLC)*, 423 F.3d 166 (2d Cir. 2005) does not stand for the iron clad proposition that only a debtor may settle estate claims pursuant to Bankruptcy Rule 9019. In *Smart World*, the Second Circuit addressed the efforts of creditors to *settle*, over the debtors' objection, estate claims that the *debtor* had brought and was actively seeking to prosecute. *Smart World*, 423 F.3d at 168. It was in this context that the Secord Circuit held that only debtors may settle estate claims pursuant to Bankruptcy Rule 9019. *Id.* In so ruling, however, the Second Circuit expressly distinguished cases like this one, where the debtor would not or could not pursue a certain cause of action. *Id*. at 176-77 ("We do not rule out that in certain, rare cases, unjustifiable behavior by the debtor-in-possession may warrant a settlement

over the debtor's objection, but this is not such a case."). Given the inherent conflicts of interest by and among the Debtors, each of the Proposed Defendants and even the Independent Committee, the Committee submits that this is the type of "rare case" that was expressly carved out of *Smart World*.

CONCLUSION

WHEREFORE, the Committee respectfully requests that this Court (a) grant the Standing Motion; and (b) grant such other and further relief to the Committee as is appropriate under the circumstances.

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/s/ Domenic E. Pacitti

KLEHR HARRISON HARVEY BRANZBURG LLP
Domenic E. Pacitti, Esq. (DE Bar No. 3989)
Richard M. Beck, Esq. (DE Bar No. 3370)
919 Market Street, Suite 1000
Wilmington, Delaware 19801-3062
Telephone: (302) 426-1189
Facsimile: (302) 426-9193
Email: dpacitti@klehr.com
rbeck@klehr.com

-and-

KILPATRICK TOWNSEND & STOCKTON LLP
David M. Posner, Esq. (admitted *pro hac vice*)
Shane G. Ramsey, Esq. (admitted *pro hac vice*)
The Grace Building
1114 Avenue of the Americas
New York, New York 10036-7703
Telephone: (212) 775-8764
Facsimile: (212) 658-9523
Email: dposner@kilpatricktownsend.com
sramsey@kilpatricktownsend.com

-and-

Todd C. Meyers, Esq. (admitted *pro hac vice*)
1100 Peachtree Street NE, Suite 2800
Atlanta, Georgia 30309-4528
Telephone: (404) 815-6482
Facsimile: (404) 541-3307
Email: tmeyers@kilpatricktownsend.com

Co-Counsel for the Official Committee of Unsecured Creditors