UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
RICHMOND DIVISION

In re: PATRIOT COAL CORPORATION, et al., Debtors.	Case No. 15-32450(KLP) Chapter 11 (Jointly Administered)

UNITED STATES TRUSTEE'S OBJECTION TO DEBTORS' MOTION FOR ENTRY OF AN ORDER APPROVING BIDDING PROCEDURES AND BID PROTECTIONS IN CONNECTION WITH THE SALES OF CERTAIN OF THE DEBTORS' ASSETS

The United States Trustee for Region 4 (the "UST") objects (the "Objection") to the Debtors' Motion for Entry of (I) An Order (A) Approving Bidding Procedures and Bid Protections In Connection With the Sales of Certain of the Debtors' Assets, (B) Approving the Form and Manner of Notice, (C) Scheduling Auctions and a Sale Hearing, (D) Approving Procedures for the Assumption and Assignment of Contracts, and (E) Granting Related Relief and (II) An Order (A) Approving the Sale of Assets Pursuant to the Bidding Procedures, (B) Authorizing the Sale of Assets Free and Clear of Liens, Claims, Encumbrances, and Interests, (C) Authorizing the Assumption and Assignment of Contracts, and (D) Granting Related Relief (the "Bidding Procedures Motion") filed on June 2, 2015.[1] See ECF Doc. No. 200. This objection is filed pursuant to 28 U.S.C. § 586 and 11 U.S.C. §307. In support of her response, the United States Trustee represents and alleges as follows:

[1] Unless otherwise defined herein, capitalized terms should have the meanings assigned to them in the Bidding Procedures Motion.

Robert B. Van Arsdale, AUST (Va. Bar No. 17483)
Shannon Pecoraro, Esq. (Va. Bar No. 46864)
Office of the United States Trustee
701 East Broad Street - Suite 4304
Richmond, VA 23219
Telephone (804) 771-2310
Facsimile (804) 771-2330

INTRODUCTION

Patriot Coal Corp. and its affiliates (collectively, the "Debtors") have negotiated a deal to sell most of their operating mines to Blackhawk Mining LLC ("Blackhawk") in a transaction that leaves retirees and union contracts behind. Blackhawk will not pay cash for the Debtors' mines. Instead, the transaction will swap out the Debtors' funded debt for new debt securities totaling about $643 million, as well as 30% of the new entity that will be formed out of the bankruptcy buyout. While the Debtors have emphasized the need for a quick sale of the Debtors' business given the Debtors' cash position, the "need for speed" must be balanced with the requirement that the sale process promotes a level playing field for bidders. The bidding procedures the Debtors propose do not accomplish that.

Here, the procedures proposed in the Bidding Procedures Motion should not be approved because they will likely chill the bidding process and discourage potential bidders from participating in the sale process, thus preventing the Debtors from maximizing the value of the estate assets. Specifically, the UST objects to the Bidding Procedures Motion for the following reasons:

- The Blackhawk Bidding Protections (as defined below), which contemplate a Break-Up Fee and Expense Reimbursement of up to $24 million, should not be approved because (i) they are also triggered and become payable for termination events other than the existence of an alternative transaction; (ii) they are excessive and would have the effect of chilling the bidding process; (iii) they contemplate allowing Blackhawk to credit-bid the amount of the protections in any overbid, thus favoring the stalking horse bidder and failing to create a level-playing field for other potential bidders; (iv) they contemplate the reimbursement of up to $5 million in out-of-pocket expenses without providing parties in interest or the Court any review rights; and (v) they chill bidding on individual assets or a partial combination of assets.

- The Bidding Procedures provide the Debtors with too much discretion and the unfettered ability to, among other things, select the "Qualified Bidder", alter bidding procedures as they deem proper, limit or restrict the flow of information, and direct and preside over the auction process – all without any real oversight or consultation except for, in limited circumstances, in consultation with the DIP Lenders.

- The bidding procedures for the sale of the Debtor's Federal Complex and related assets should not be approved because no Federal Stalking Horse Bid is yet proposed or announced and the deadlines proposed for parties in interest to object to the Federal Bid Protections, which will not be announced, if at all, until July 14, 2015, is only three business days after the notice of the stalking horse bid goes out. Moreover, the overbid amounts proposed for the Federal Sale (as defined below) are also excessive and would hamper rather than promote the bidding process.

FACTS

A. 2012-13 Restructuring

1. On June 9, 2012 (the "First Petition Date"), Patriot Coal Corporation and 98 of its Affiliated companies (collectively, "Patriot Coal") filed voluntary petitions for relief under Chapter 11 of Title 11 in the Bankruptcy Court for the Southern District of New York. On December 19, 2012, Patriot Coal's cases were transferred to the Bankruptcy Court for the Eastern District of Missouri.

2. On December 18, 2013, the Bankruptcy Court for the Eastern District of Missouri confirmed Patriot Coal's plan of reorganization (the "Plan"). The linchpins of Patriot Coal's 2012-13 restructuring were a global settlement among Patriot Coal, the United Mine Workers of America ("UMWA"), and two third parties – Peabody Energy Corporation and Arch Coal, Inc. – and a commitment by a consortium of Patriot Coal's financial creditors, led by certain funds and accounts managed and/or advised by Knighthead Capital Management to backstop rights offerings (the "Rights Offerings") that funded the plan.

B. Current Chapter 11 Case

3. On May 12, 2015 (the "Petition Date"), the Debtors each filed a voluntary petition under Chapter 11 of the Bankruptcy Code. On May 13, 2015, the Court entered an order authorizing joint administration and procedural consolidation of the chapter 11 cases pursuant to Bankruptcy Rule 1015(b).

4. The Debtors remain in possession of their assets and continue to manage their business as

debtors-in-possession pursuant to Bankruptcy Code Section 1107(a) and 1108. To date, no trustee or examiner has been appointed in these Chapter 11 cases.

5. On May 21, 2015, the United States Trustee appointed the Official Committee of Unsecured Creditors pursuant to Section 1102(a)(1) of the Bankruptcy Code (the "Creditors' Committee"). See ECF Docket No. 115.

6. As of the Petition Date, the outstanding balances of the Debtors' secured debt were as follows:

Debt	Balance
ABL Revolving Facility	$38 million
L/C Facility	$200 million
Term Loan Facility	$247 million
Second Lien Notes	$306 million
Total	**$791 million**

C. Debtor-in-Possession Financing

7. On the Petition Date, the Debtors filed a motion seeking debtor-in-possession financing (the "DIP Motion"). See ECF Docket No. 30. The DIP Motion was approved on an interim basis on May 13, 2015 and on a final basis on June 3, 2015 (the "DIP Order"). Pursuant to the DIP Order, the Debtors were authorized to enter into a $100 million post-petition DIP financing facility (the "DIP Facility") from a group of their prepetition lenders holding a majority of the Debtors' prepetition first lien term debt and second lien notes. See ECF Docket Nos. 67 and 230. As set forth below in Paragraph 11, the DIP Order provides certain milestones which, if not met, would constitute an event of default under the DIP Order.

D. **Sale Transaction and Bidding Procedures**

8. On June 2, 2015, the Debtors filed the Bidding Procedures Motion which, among other things, seeks (a) approval of bidding procedures (the "Bidding Procedures") setting forth a comprehensive process for soliciting bids and holding one or more auctions for the sales of

Debtors' assets, and (b) approval of the sale or sales of Debtors' assets. See Bidding Procedures Motion at ¶ 6.

9. The Bidding Procedures contemplate the sale of a substantial majority of Debtors' assets to Blackhawk, which would be accomplished through the creation of a new company (the "Combined Entity") capitalized with a combination of debt, equity, and cash. Id. at 7. In exchange for the release of liens, the Debtors' prepetition secured lenders will be offered take-back debt in the Combined Entity. Id.

10. More specifically, while no proposed asset purchase agreement is yet filed with the Court, the term sheet attached as Exhibit C to the Bidding Procedures Motion contemplates the following transaction:

a. While Blackhawk will acquire a majority of the Debtors' assets (the "Blackhawk Sale"), it would not include the Debtor's Federal Complex (the "Federal Assets," and such sale, the "Federal Sale") as well as other mining assets.

b. Blackhawk would assume liabilities in relation to the purchased assets but, among other liabilities, would not assume (i) liabilities associated with the Debtors' employees not hired by Blackhawk, the Debtors' collective bargaining agreement and Patriot Coal Corp.'s employee benefit plans and (ii) liabilities or obligations of the Debtors for retiree medical or other retiree welfare benefits and liabilities associated with contributions to the UMWA 1974 Pension Plan.

c. Blackhawk would purchase the assets and assume the liabilities for the following consideration:

    i. From the proceeds of new first lien credit facilities of an estimated $634 million incurred by Blackhawk:

        - Replacement in full of Blackhawk's existing funded debt of up to $300 million;

        - Replacement of up to $109 million of indebtedness under Patriot's DIP Facility;

        - Replacement of approximately $237 million of existing drawn and undrawn L/Cs.

ii. The Combined Entity will issue the holders of the Debtors' Term Loan Facility (up to $247 million) and the Debtors' Second Lien Notes (up to $50 million), up to $297 million of a second lien PIK loan ("Second Lien PIK Loans"); and

iii. The Combined Entity will issue Class B membership interests to the holders of Debtors' Second Lien Notes.

d. The reorganization shall also include a rights offering to raise cash on the balance sheet for the Combined Entity.

e. Key conditions to closing include, among other things: (i) certain milestones as set forth below being met; (ii) the Combined Entity having received at least $50 million of cash from the proceeds of the rights offering; and (iii) with respect to each of the Debtors' existing collective bargaining agreements (the "CBAs") that cover the employees at the purchased complexes either the Bankruptcy Court shall have entered orders permitting the rejection of the CBAs or retiree benefit plans pursuant to sections 1113 and 1114 or Blackhawk shall have entered into new CBAs on terms and conditions acceptable to Blackhawk in its sole discretion.

11. The milestones that are contemplated for such transaction are fast-paced. The chart below sets forth a comparison of the milestones proposed in the Bidding Procedures with the milestones under the DIP Facility:

Milestones	Deadline Under DIP	Deadline Under Bidding Procedures
Filing of final form APA in connection with Blackhawk Sale	June 30, 2015	June 25, 2015
Approval of Bidding Protections/Procedures	July 31, 2015	June 30, 2015
File Plan and Disclosure Statement and either: - Debtors reach agreement with UMWA for modification of CBA necessary to implement APA or - Debtors file motion for relief under 11 U.S.C. §§ 1113 and 1114	August 1, 2015	N/A
Approval of Disclosure Statement	October 15, 2015	July 21, 2015
Federal Stalking Horse Notice Deadline	N/A	July 14, 2014
Bid Deadline	September 21, 2015	August 7, 2015
Notice of Qualified Bids	N/A	August 11, 2015
Auction (if any)	N/A	August 13, 2015
Hearing to Designate Winning Bidder	N/A	August 18, 2015
Entry of Confirmation Order	November 23, 2015	September 11, 2015
Closing of Blackhawk Sale	November 30, 2015	September 25, 2015

See DIP Order at Exhibit 3 (Schedule 4.03); Bidding Procedures Motion at ¶¶ 17 and 18.

12. The Bidding Procedures further contemplate that anyone submitting a bid must comply, with the following, among other things:

a. Deposit: Each bid must be accompanied by a cash deposit in an amount acceptable to the Debtors (after consultation with the DIP Lenders) which amount shall not exceed 10% of the purchase price. See Bidding Procedures (Exhibit 1 to Proposed Bidding Procedures Order) at p. 3.

b. Blackhawk Sale Overbid: Each overbid for the Blackhawk Sale must be equal or exceed the sum of: (a) cash or non-cash consideration in an amount equal to the Blackhawk Bid; (b) cash in an amount equal to the Blackhawk Bid Protections (as defined below); and (c) $5 million in cash or cash equivalents (with a party entitled to do so having the possibility to credit bid in an amount equal to the Blackhawk Initial Overbid). See Bidding Procedures at p. 4.

c. Federal Sale and Sale Overbid; If the Debtors identify a Federal Stalking Horse Bidder, the Debtors will file a notice (the "Federal Bid") by July 14, 2015 identifying the bidder, the terms of the bid, and the bid protections proposed for the Federal Stalking Horse Bidder (the "Federal Bid Protections"). See Proposed Bidding Procedures Order at ¶ 16; Bidding Procedures Motion at ¶ 26. Any entity wishing to object to the Federal Bid Protections should have until July 19, 2015 to object. See Bidding Procedures Motion at ¶ 27. Any initial overbid to the Federal Stalking Horse Bid must be equal or exceed: (a) cash or non-cash consideration in an amount equal to the Federal Bid; (b) cash in an amount equal to the Federal Bid Protections (as defined below); and (c) $2 million in cash or cash equivalents (with a party entitled to do so having the possibility to credit bid in an amount equal to the Federal Initial Overbid). See Bidding Procedures at pp. 4-5.

d. Minimum Overbid Increment: With respect to any of the sales, any overbid after the baseline bid shall be in cash in increments of at least $1,000,000. See Bidding Procedures at p. 10.

e. Blackhawk Bidding Protections: Blackhawk can recover a Breakup Fee of up to $19,000,000 (the "Break-Up Fee") to the extent that (i) Blackhawk terminates the APA due to material, uncured breach by the Debtors; (ii) the Debtors propose through a motion or a plan or consummate a transaction for all or a material portion of the assets to a party other than Blackhawk; or (iii) Blackhawk terminates the APA due to the failure of the closing occurring prior to September 25, 2015 other than if such closing occurred as a result of (a) Blackhawk's existing secured creditors failure to agree to exchange their debt obligations for the debt in post-closing Blackhawk and (b) Blackhawk is unable to raise new money financing to satisfy its obligations and thereafter Patriot consummates a superior transaction by December 1, 2015. Moreover, Blackhawk also stands to recover up to $5,000,000 for reasonable and documented out-of-pocket costs and expenses (the "Expense Reimbursement," and, collectively with the Break-Up Fee, the "Blackhawk Bidding Protections"). See Bidding Procedures at pp. 8- 9.

f. Credit Bid of Bidding Protections: In the event of a competing Qualified Bid, Blackhawk and the Federal Stalking Horse Bidder, if any, will be entitled to submit overbids and will be entitled in any such overbid to credit bid the value of their bidding protections. See Proposed Bidding Procedures Order at ¶ 9.

OBJECTION

The purpose and goal of any asset sale is to maximize the recovery of value for the benefit of the bankruptcy estate. To that end, the bidding procedures that are proposed through a sale process must establish a framework for competitive bidding to ensure the maximization of such value. See In re Jon J. Peterson, Inc., 411 B.R. 131, 137 (Bankr. W.D.N.Y. 2009) ("[U]nless the bidding process remains fair and equitable, competitors will refrain from the type of full participation that is needed to assure bids for the highest reasonable value. For those reasons, the court will not approve bidding procedures that undermine principles of fair play."); In re Cormier, 382 B.R. 377, 388 (Bankr. W.D. Mich. 2008) (quotations omitted) ("'The purpose of procedural bidding orders is to facilitate an open and fair public sale designed to maximize value for the estate.")

Here, the Bidding Procedures that the Debtors propose should not be approved because they will likely chill the bidding process and discourage potential bidders from participating in the bidding process.

I. The Blackhawk Bidding Protections Should Not Be Approved

As the Debtors set forth in the Bidding Procedures Motion, break-up fees, expense Reimbursements, and other forms of bidding protections are a normal and, in many cases, necessary component of asset sales. See Bidding Procedures Motion at ¶ 43. While that is true, the general rule "is that if break-up fees encourage bidding, they are enforceable; if they stifle bidding, they are unenforceable." In re Integrated Resources, Inc., 147 B.R. 650, 659 (S.D.N.Y.

1992); In re On-Site Sourcing, Inc., 412 B.R. 817 (Bankr. E.D. Va. 2009) ("Break-up fees can serve a useful purpose in bankruptcy auctions. But merely reciting the theoretical benefits in a motion does not insure that they inure to the benefit of the estate.").

A break-up fee is a type of bidding incentive designed to encourage potential purchasers to bid for assets. "Agreements to provide breakup fees or reimbursement of fees and expenses are meant to compensate the potential acquirer who serves as a catalyst or 'stalking horse' which attracts more favorable offers." In re S.N.A. Nut Co., 186 B.R. 98, 101 (Bankr. N.D. Ill. 1995); In re Integrated Resources, Inc., 147 B.R. 650, 659 (S.D.N.Y. 1992) (break-up fee is "an incentive payment to an unsuccessful bidder who placed the estate property in a sales configuration mode . . . to attract other bidders to the auction."). Break-up fees reimburse two types of expense: "first, the cost of putting together a 'stalking horse" bid; and second, expenses from which all bidders will benefit." In re Jon Peterson, inc., 411 B.R. at 137. Said differently, break-up fees are usually proposed to provide a prospective buyer with "some assurance that they will be compensated if the transaction is not completed because the seller determines to accept an alternative offer." See Thomas J. Salerno, et al., Advanced Chapter 11 Bankruptcy Practice at § 7.137 (2010).

The courts are divided in applying the business judgment rule and an administrative expense analysis to the propriety of break-up fees. See In re 996 Fifth Avenue Associates, L.P., 96 B.R. 24, 28 (Bankr. S.D. N.Y. 1989) and In re O'Brien Environmental Energy, Inc., 181 F.3d 527 (3d Cir. 1999). The courts applying a variation of the business judgment rule usually analyze the following criteria in determining whether to award a break-up fee – whether the fee (i) was tainted by self-dealing or manipulation, (ii) hampered rather than encouraged bidding, and (iii) was reasonable relative to the proposed purchase price. See In re Integrated Resources,

Inc., 147 B.R. at 662; see also In re Hupp Indus., Inc., 140 B.R. 191, 194 (Bankr. N.D. Ohio 1992) (providing additional factors to consider in evaluating a break-up fee request, including, among others, whether the fee requested correlates with a maximization of value to the debtor's estate). The other test which the Third Circuit adopted, applies the general administrative expense jurisprudence of section 503(b) of the Bankruptcy Code and analyzes whether the fee was an actual and necessary cost and expense of preserving the estate. See In re O'Brien Environmental Energy, Inc., 181 F.3d at 535 (" . . . the allowability of break-up fees, like that of other administrative expenses, depends upon the requesting party's ability to show that the fees were actually necessary to preserve the value of the estate."); In re Tropia, 352 B.R. 766, 768 (Bankr. N.D. W. Va. 2006) ("Break-up fees are allowed as an administrative expense claim against the estate if they satisfy the standard of section 503(b)(1). The fee must reflect the actual and necessary cost of preserving the estate."). Regardless of the analytical approach taken here, the break-up fee should not be approved in this case as it chills the bidding process.

a. Certain Triggers for the Blackhawk Bid Protections Are Inappropriate

The Bidding Procedures inappropriately provide for the payment of the Break-Up Fee and Expense Reimbursement upon a variety of circumstances other than the closing of an actual competing transaction. Specifically, the asset purchase agreement (a copy of which will not be available until approximately June 25, 2015) may be terminated by Blackhawk and the Blackhawk Bidding Protections would be payable due to (a) a material, uncured breach by Patriot that would cause the failure of any condition to closing, or (b) a failure of the closing to occur prior to September 25, 2015, other than if the closing did not occur as a result of the failure of Blackhawk's existing secured creditors to agree to exchange their debt and Blackhawk is unable to raise new money, and Patriot subsequently consummates a superior transaction by

December 15, 2015. See Bidding Procedures Motion at Exhibit 3, pp. 8-9. The Debtors are thus obligated to pay Blackhawk the Blackhawk Bidding Protections upon events other than the closing of an alternative transaction and not from the proceeds of another sale.

The Blackhawk Bidding Procedures are at odds with both analyses employed by courts. As currently proposed, the Blackhawk Bidding Procedures currently require payment of the break-up fee and the expense reimbursement for just about any possible termination event that exists under the asset purchase agreement and for failing to meet the tight timeline proposed thereunder. The problems are three-fold: First, the asset purchase agreement is not attached to the Bidding Procedures Motion and apparently will not be filed until on or around June 25, 2015; accordingly, it is not clear what breaches would trigger the payment of the break-up fee or expense reimbursement.

Second, if no alternative transaction closes, or the break-up fee and expense reimbursement becomes payable by reason of a condition other than the existence of an alternative transaction, then the Debtors' estate will have received no benefit from the payment of the break-up fee and would have to pay up to $24 million from estate assets. There simply is no justification for the payment of a break-up fee if, for instance, the sale does not occur because of a breach of a representation and warranty. This provision is tantamount to a liquidated damages provision for breach of contract before there is even a contract.

Third, by making the Blackhawk Bidding Protections payable upon failing to meet any of the milestones set forth in the Bidding Procedures Motion and failing to close prior to September 25, 2015 is in essence guaranteeing that Blackhawk will receive break-up fees and expense reimbursement without guaranteeing any benefit to the estate. The milestones, in fact, are so tight that meeting them is virtually impossible. Under the current deadlines, a plan needs to be

confirmed and the sale closed within approximately three months. The Debtors, however, are also contemplating modifying or rejecting their liabilities to retirees and under collective bargaining agreements. To the extent that an agreement is not reached with the union or retirees, the timelines under sections 1113 and 1114 are triggered, making it unlikely – if not impossible – to meet the milestones that are proposed in the Bidding Procedures Motion.[2] The consequences of such a compressed time schedule not only make the failure to meet them almost a given, but are also a restriction on the time available to bidders to undertake due diligence and formulate bids. Moreover, even if Blackhawk is the successful winner and then fails to close the transaction for failure to get new financing to enable the contemplated transaction, Blackhawk will keep the $24 million ransom.[3]

Accordingly, if the Court is inclined to permit payment of the Blackhawk Bidding Protections at all, then payment of the Break-up Fee should at least be triggered only if the Debtors consummate and close a competing sale transaction. Furthermore, the Break-Up Fee should not be tied to any milestones that are so tight as to be in essence a guarantee that Blackhawk will receive a windfall with no equivalent benefit to the estate.

b. The Amount of the Blackhawk Bidding Protections Is Excessive

[2] Under § 1113, the court shall approve an application for rejection of a collective bargaining agreement within 30 days after the date of the commencement of the hearing, unless further extended. 11 U.S.C. § 1113(d)(2). Under §1114, the court shall rule on an application for modifying retiree benefits within 90 days after the date of the commencement of the hearing. 11 U.S.C. § 1114(j)(2).

[3] The term sheet currently provides that Blackhawk will be entitled to the bidding protections if Blackhawk terminates the APA due to a failure of the closing to occur prior to September 25, 2015 other than "if such closing failed to occur primarily as a result of the failure of Blackhawk's existing secured creditors (other than holders of Patriot debt or their affiliate transferees that also hold Blackhawk debt) to agree to exchange their debt obligations for the debt in Post-Closing Blackhawk contemplated by the Asset Purchase Agreement **and** Blackhawk is unable to raise new money financing elsewhere to satisfy its obligations thereunder) and thereafter Patriot consummates a superior transaction . . . on or prior to December 1, 2015." See Bidding Procedures Motion at Exhibit C, p. 8 (emphasis added). Accordingly, the way the provision is currently drafted provides that even if the Blackhawk's existing creditors consent to exchange their debt but Blackhawk is not able to raise new financing, and the sale does not occur prior to September 25, 2015 but an alternate transaction occurs by December 1, 2015, then Blackhawk would still stand to recover $24 million.

To compensate Blackhawk for serving as the "stalking horse," thereby subjecting its bid to higher or better offer, the Debtors seek authority to pay Blackhawk a Break-Up Fee of $19,000,000, and up to $5,000,000 in out-of-pocket costs and expenses. While Blackhawk stands to earn a maximum of $24,000,000 in bidding protections, the proposed transaction is not a cash transaction. Rather, the Blackhawk sale contemplates the assumption of the Debtors' secured liabilities, with no cash being provided in consideration by Blackhawk. In this case, the Break-Up Fee contained in the Blackhawk Bid Protections represents approximately 3.0% of the $643 million of new debt securities that Blackhawk would issue to the Debtors' secured lenders in connection with the transactions. When the maximum of the Expense Reimbursements is also taken in consideration, the percentage of the Blackhawk Bid Protections rises to approximately 3.7%.

While the UST does not dispute the fact that a 3.0% range for break-up fees is generally within the norm, bankruptcy courts maintain discretion not only to approve or deny a proposed break-up fee entirely, but also to limit the amount of the fee approved. The aggregate amount of the bidding protections must "constitute a fair and reasonable percentage of the proposed purchase price [and must be] reasonably related to the risk, effort, and expenses of the prospective purchaser." In re Integrated, 147 B.R. at 662; see also In re O'Brien Envt'l Energy, Inc., 181 F.3d at 537. Thus, even if the Debtors could establish that the Blackhawk Bidding Protections preserve value for their estates – which they cannot – they must also show that the amount of the proposed fees are fair and reasonable, and serve as a catalyst to other higher bids. Here, they simply do not.

While the transaction with Blackhawk is not a cash transaction – but rather a swap out of funded debt with new debt liability – any other bidder would be required to pay a minimum of

$19,000,000 in cash for the Break-Up Fee, plus up to an additional $5,000,000 in Expense Reimbursement. That is in addition to the $5 million in cash or cash equivalents for the initial overbid amount. For a potential purchaser to be required to come up with up to $29,000,000 million, when Blackhawk does not have to provide any cash up-front, does not enhance the bidding process but rather creates an unfair barrier to *bona fide* bidding. In the context of the transaction as a whole, the Blackhawk Bidding Protections appear unreasonable and should not be approved in the proposed amounts.

c. Blackhawk Should Not Be Allowed to Credit Bid Its Break-Up Fee

The Proposed Bidding Procedures Order contemplates that in the event of a competing Qualified Bid, Blackhawk and the Federal Stalking Horse Bidder, if any, will be entitled to submit overbids and will be entitled in any such overbid to credit bid the value of their bidding protections. See Proposed Bidding Procedures Order at ¶ 9. Allowing a stalking horse bidder to "credit bid" its break-up fee gives it an unreasonable and unwarranted advantage to its sole windfall.

Assuming that an initial overbid comes in, according to the Bidding Procedures, it would have to be at a minimum consistent with the assumption of $643 million in debt – as provided by the Blackhawk "stalking horse" bid and, in addition, would have to provide cash in the amount of the Blackhawk Bidding Protections – or a maximum of $24,000,000 in cash plus an additional $5 million in cash or cash equivalents. To the extent that Blackhawk wanted to overbid, it would have to offer at a minimum $5 million in cash or cash equivalents and $1 million in cash over the initial overbid. A subsequent bidder, however, would have to offer, in addition to the minimum amount of the cash overbids, up to an additional $24,000,000 in cash to pay off the Blackhawk Bidding Protections. Said differently, Blackhawk would always be at an advantage over other

bidders because it would be automatically given up to a $24,000,000 cash discount through the credit bidding for fees and expenses that it has not yet earned. This does not foster competitive bidding in that the ability to credit bid the bidding protections would always favor Blackhawk and not create a level playing field for other potential bidders.

d. **The Expense Reimbursement Should Be Subject to Further Review**

The Blackhawk Bidding Protections include, along with the Break-Up Fee, the reimbursement of expenses up to $5 million. Upon certain triggering events, described further above, the Debtors shall reimburse Blackhawk for reasonable and documented out-of-pocket costs and expenses (including legal, accounting, and other consultant fees and expenses other than any success or similar fees payable to financial advisors or consultants) incurred in connection with the transaction. Nothing in the proposed Bidding Procedures, however, contemplates the review of any such expenses being awarded to Blackhawk by the Court or parties in interest, leaving the discretion to pay for such expenses solely to the Debtors. The UST requests that to the extent that the Court is inclined to approve the Expense Reimbursement, a mechanism is established whereby such expenses are further subject to the review of parties in interest as well as the Court through a transparent process.

e. The Blackhawk Bidding Protections Chill Partial Bids

The Bidding Procedures as currently proposed contemplate bidders' ability to submit bids for individual assets or combinations of assets (each, a "Partial Bid"). See Proposed Bidding Procedures at p. 5. Partial Bids must include a mark-up of the Blackhawk APA and "the Debtors, in consultation with the DIP Lenders, must conclude that the Partial Bid, when taken together with other Bids or Partial Bids, satisfies the criteria for being a Qualified Bid." Id. Even though the Bidding Procedures contemplate Partial Bids, the fact that Partial Bids, when

taken together with other Bids or other Partial Bids, must satisfy the requirements of being a "Qualified Bid" – including that it must (a) be in an amount equal to the Blackhawk Bid, (b) must provide cash in an amount of the Blackhawk Bid Protections, and (c) must provide $5 million in cash or cash equivalent do not stimulate bidding. In fact, a potential purchaser who is only interested in bidding on a portion of the assets included in the Blackhawk sale, could be offering on a *pro rata* basis a higher price for the assets yet be subject to the same incremental overbid amounts, including the Blackhawk Bidding Protections, thus not ensuring the maximizing of the value for the Debtors' estate. Accordingly, the Bidding Procedures should be modified so that the Blackhawk Bidding Protections do not chill Partial Bids.

II. The Bidding Procedures Give the Debtors Too Much Discretion

The Bidding Procedures, as proposed, provide the Debtors with the unfettered ability to select Qualified Bidders, alter procedures as they deem proper, determine the financial capacity of bidders, direct and preside over the auction, and limit or restrict the flow of information to certain bidders – all without any Court supervision or input by the Creditors' Committee or any other parties in interest . Said differently, the Bidding Procedures give the Debtors and their advisors *carte blanche* to run the bidding process, allowing for possible bias in selecting a Qualified Bidder and in determining the ultimate winning bid.

More specifically, under the current Bidding Procedures, the Debtors have the following discretion:

- To determine whether a proposal or offer constitutes a "Qualified Bid". See Proposed Bidding Procedures at p. 3.
- To determine the amount of cash deposit (after consultation with the DIP Lenders), which amount shall not exceed 10% of the purchase price of the bid. Id.
- To determine that the executed confidentiality agreement is in a form and substance satisfactory to the Debtors. Id. at p. 2.

- To withhold any diligence materials from any competitors interested in making a bid. Id. at p. 3.

- To conclude, in consultation with the DIP Lenders, whether a Partial Bid, when taken together with other bids or Partial Bids, satisfies the criteria for being a Qualified Bid. Id. at p. 5.

- To determine, in consultation with the DIP Lenders, whether any bidder has the necessary financial capacity to consummate the proposed transaction. Id. at p. 6.

- To direct and preside over the auctions and only Qualified Bidder (which are determined in the discretion of the Debtors) should be entitled to make any subsequent bids, make statements on the record, or otherwise participate at the auctions. Id. at p. 9.

- To remove any Qualified Bidder from the auctions if the Debtors determine (after consultation with the DIP Lenders) that the applicable Qualified Bidder is no longer engaged in active bidding. Id. at p. 11.

- To announce additional procedural rules that are reasonably necessary or advisable under the circumstances for conducting the auctions. Id.

- To modify, with the reasonable consent of the DIP Agent, the Bidding Procedures or impose, at or prior to the Auction, additional customary terms and conditions on the sale of the Assets. Id. at p. 14.

While the DIP Lenders have been granted certain oversight or consultation rights under the proposed Bidding Procedures, at a minimum, the Committee should also be granted those rights. The auction process should also be more transparent and, rather than being held at the direction and sole supervision of the Debtors, it should be held in open court so as to prevent any possible bias.

Lastly, the due diligence process contemplated in the Bidding Procedures needs to be modified to ensure that the flow of information is equal to all parties interested in making a bid. Even if a Qualified Bidder executes a confidentiality agreement in substance satisfactory to the Debtors and satisfies all other eligibility requirements, under the Bidding Procedures, the Debtors are not required to give the Qualified Bidder any diligence material that the Debtors, in

their sole discretion, determine are business-sensitive or otherwise inappropriate for disclosure to such bidder. Since (i) it is likely that based on the type of assets being sold the potential bidders would probably fit under the rubric of "competitor," and (ii) the Debtor appears to have unfettered and absolute authority to limit or restrict the flow of important information to a Qualified Bidder, many potential bidders may be discouraged from seeking to participate in the bidding process because they may perceive that the deck has already been stacked against them and the cards will not be in their favor. Accordingly, the Bidding Procedures should make clear that the due diligence the Debtors will provide to each party interested in submitting a bid and who signs a confidentiality agreement will be provided with the same due diligence as that provided to Blackhawk and that Blackhawk will also share any additional due diligence that it may have gathered and that entitles it to the Expense Reimbursement.

III. The Bidding Procedures for the Federal Sale Should Not Be Approved

As set forth above, if the Debtors identify a Federal Stalking Horse Bidder, the Debtors will file a supplemental notice no later than Tuesday, July 14, 2015, which will include possible bidding protections. Any entity wishing to object to the Federal Bid Protections then would have five days – or until Sunday, July 19, 2015 to file an objection. The three-business days objection deadline should be extended to ensure reasonable and sufficient time for a party in interest to analyze the Federal Stalking Horse Bid and the protections sought therein and to respond to it to the extent that the bidding protections are unreasonable. Accordingly, the UST requests that the deadline to object to the Federal Stalking Horse Notice be extended to July 28, 2014.

Moreover, the minimum overbid increments for any sale – including the Federal Sale – is $1,000,000. See Bidding Procedures at p. 10. The Bidding Procedures seek to approve the overbid increments for a sale whose terms are yet to be known. Accordingly, the Proposed

Bidding Procedure Order should clarify that the overbid increment of $1,000,000 does not apply to the Federal Sale and that the overbid increment should be set forth in the Federal Stalking Horse Notice so that parties in interest can evaluate it in connection with the Federal transaction proposed as a whole. To the extent that no Federal Stalking Horse Bidder is found, the overbid amount in excess of the initial bid should be set upon consultation with the Committee and the UST.

CONCLUSION

For the foregoing reasons, the UST respectfully requests that the Bidding Procedures not be approved in their current form and, if approved at all, without the Blackhawk Bidding Protections and with other modifications addressed herein.

Respectfully submitted,

JUDY A. ROBBINS
United States Trustee
Region 4

By: /s/ Robert B. Van Arsdale
Robert B. Van Arsdale
Assistant U.S. Trustee

CERTIFICATE OF SERVICE

I hereby certify that on June 16, 2015, a true copy of the foregoing was delivered via electronic mail pursuant to the Administrative Procedures of the CM/ECF System for the United States Bankruptcy Court for the Eastern District of Virginia to all necessary parties.

/s/ Robert B. Van Arsdale
Robert B. Van Arsdale