IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

In Re:	§	**Chapter 11**
	§	
TMT PROCUREMENT CORPORATION, *et al.*,[1]	§	**Case No. 13-33763**
	§	
	§	
Debtors.	§	**Jointly Administered**

DEBTORS' *AMENDED* MEMORANDUM (I) IN FURTHER OPPOSITION TO THE MOTION TO CONVERT AND (II) IN SUPPORT OF GRANTING COMMITTEE STANDING TO COMMENCE CERTAIN ESTATE CLAIMS
[relates to ECF 2415 & 2455]

INTRODUCTION

1. This Court scheduled the initial hearing for June 12, 2015 on Mr. Su's Motion to Convert (ECF 2415) and on the stipulation (the "Standing Stipulation", ECF 2455) proposing to grant standing to the Committee to assert certain estate causes of action, including avoidance actions under Bankruptcy Code § 547 ("Preference Actions"). The hearing on both matters is scheduled to resume on June 19, 2015 (June 12 and June 19, the "Hearing"). Mr. Su has objected (the "Objection", ECF 2465) to the Standing Stipulation, with the Objection focusing on Mr. Su's assertions that the Debtors have failed to make the showing required by *Louisiana World Exposition v. Fed. Ins. Co.*, 864 F.2d 1147, n.10 (5th Cir. 1989) ("*LWE*") (adopting the "cost-benefit analysis" test enunciated in *In re STN Enters.*, 779 F.2d. 901, 905 (2d. Cir. 1985)

[1] The Debtors in these chapter 11 cases are: (1) A Whale Corporation; (2) B Whale Corporation; (3) C Whale Corporation; (4) D Whale Corporation; (5) E Whale Corporation; (6) G Whale Corporation; (7) H Whale Corporation; (8) A Duckling Corporation; (9) F Elephant Inc; (10) A Ladybug Corporation; (11) C Ladybug Corporation; (12) D Ladybug Corporation; (13) A Handy Corporation; (14) B Handy Corporation; (15) C Handy Corporation; (16) B Max Corporation; (17) New Flagship Investment Co., Ltd; (18) RoRo Line Corporation; (19) Ugly Duckling Holding Corporation; (20) Great Elephant Corporation; and (21) TMT Procurement Corporation.

("*STN*")), *cited with approval in In re Digerati Techs., Inc.*, 2014 WL 2123124 (Bankr. S.D. Tex. 2014).

2. At the June 12 hearing, Mr. Su's counsel stated, without qualification, that, "we don't believe there has really been any investigation beyond just doing a summary of what's been in the Statement of Financial Affairs." Hr'g Tr. June 12, 2015 at 34:3-7. The Debtors do not believe that counsel had a reasonable basis for such belief. In fact, Mr. Su *did* know that the Debtors had investigated and pursued potential avoidance actions and that this extended beyond "just doing a summary of what's been in the Statement of Financial Affairs." The specifics of the Debtors' response concerning what Mr. Su and his counsel knew, at a minimum, are set forth in paragraphs 4, 6, 8 at 13 and 14 of the Affidavit, together with Exhibits A, B, C, D, F and J of the Affidavit, all of which knowledge was acquired by Mr. Su and his counsel prior to Mr. Su's filing of the Motion to Convert and his Objection to the Standing Stipulation, and prior to counsel's above-quoted statement at the June 12 hearing.

3. Having heard Mr. Su's counsel's stated belief as just quoted, this Court continued the Hearing and ordered of the appointment of an examiner to present a report at as to whether "Estate causes of action have been preserved for timely prosecution." ECF 2479. The remainder of this Memorandum, as supported by the Affidavit, is to address the *LWE* factors both as to the Debtors' efforts and analyses concerning potential avoidance actions and as to grounds for Committee standing to pursue same.

POINTS AND AUTHORITIES

4. *LWE* requires this Court to examine whether granting the Committee standing to pursue the Preference Actions "is likely to benefit the reorganization estate." *LWE* contemplates that such examination will be based on "affidavit and other submission, by evidentiary hearing or

otherwise." This Memorandum is intended to serve as an "other submission," and the *Affidavit of Evan D. Flaschen in Opposition to Motion to Convert and in Support of Committee Standing Stipulation* (the "Affidavit", ECF 2481-1 through 2481-11) is intended to serve as an "affidavit." Further, while *LWE* does not require an evidentiary hearing, Mr. Flaschen will make himself available telephonically at the second day of the Hearing should the Court decide that it wishes to consider testimony in support of the Affidavit.

5. For convenience of reference, this Memorandum will follow Mr. Su's interpretation of the *LWE* criteria as set forth at 7-8 of the Objection by introducing each section with Mr. Su's statement in **bolded text**, although the Debtors question whether all such criteria are actually required by *LWE*. This Memorandum and the Affidavit will also refer to the stipulation (the "Debtor/Su Stipulation", ECF 2458) introduced into evidence at the first day of the Hearing.

Presentation of a colorable claim

6. A "colorable claim" is a claim "that on appropriate proof would support a recovery." *STN*, 779 F.2d at 905. This does not require a "mini-trial." *Id.* To "successfully demonstrate that it possesses a colorable claim," the committee "is not required to present its proof, the first inquiry is much the same as that undertaken when a defendant moves to dismiss a complaint for failure to state a claim…. When considering a motion to dismiss, a court must accept as true the allegations and facts pleaded in the complaint and any and all reasonable inferences derived from those facts. A complaint should not be dismissed for failure to state a claim 'unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his [or her] claim which would entitle him [or her] to relief.'" *In re G-I Holdings, Inc.*, 313 B.R. 612, 630-31 (Bankr. D.N.J. 2004) (citations omitted) (granting committee standing to pursue

avoidance claims); *see also In re Dewey & Leboeuf LLP*, 2012 WL 5985445 at *6 (Bankr. S.D.N.Y. 2012) ("A committee seeking standing need not lay bare its complete proof, but rather is required only to describe a facially valid claim, which will be evaluated under a standard 'much the same as that undertaken when a defendant moves to dismiss a complaint for failure to state a claim.'") (citations omitted); *In re Adelphia Comms. Corp*, 330 B.R. 364, 376 (Bankr. S.D.N.Y. 2005) ("Caselaw construing requirements for 'colorable' claims has made it clear that the required showing is a relatively easy one to make.").

7. It must also be emphasized that the only party objecting to standing is the owner of a number of Potential Defendants, but the standing criteria are "not for the protection of defendants sued or to be sued by a committee on behalf of an estate…, the purpose of the bankruptcy court's gatekeeper role is to protect the *estate*." *Adelphia*, 330 B.R. at 386 (emphasis in original).

8. Evidence that a defendant received a transfer within the relevant period is sufficient by itself to establish a colorable claim. *In re Enron Corp*., 319 B.R. 128, 132 (Bankr. S.D. Tex. 2004) ("The defendants received transfers within days of the Enron bankruptcy cases. That in and of itself makes the avoidance claims colorable."). To demonstrate "colorable claims" for the Preference Actions here, one need look no further than Attachments 3b and 3c to each Debtor's Statement of Financial Affairs (collectively, the "SOFAs") at Debtor/Su Stipulation ¶ 26.c, which have been "admitted for all purposes of the hearing." Those attachments set forth "payments identified by the Debtors as having been made within 90 days prior to the petition date and to insiders within 90 days and one year prior to the petition date." The SOFAs were prepared by a team consisting of Debtor personnel in Taipei, AlixPartners and Bracewell. *See* Affidavit ¶ 4. The then-President of each of the Debtors, Mr. Hsin Chi Su, signed each of the

SOFAs, stating: "I declare under penalty of perjury that I have read the answers contained in the foregoing statement of financial affairs and any attachments thereto and that they are true and correct to the best of my knowledge, information and belief." *See* each SOFA.

9. Attachments 3b and 3c to the SOFAs establish on a prima facie basis each of the elements set forth in Bankruptcy Code §§ 547(b)(1)-(4). There are various Potential Defendants (defined below) in the Preference Actions. As to Mr. Su's non-Debtor affiliates, their claims are identified as unsecured on each Exhibit F-2 to each of the relevant Debtor's Schedules identified in the Debtor/Su Stipulation at ¶ 26.c (also signed by Mr. Su under penalty of perjury), and KPI is identified as unsecured on each relevant Exhibit F-1. *See* Schedules; Affidavit ¶ 4. Therefore, the fifth element set forth in Bankruptcy Code § 547(b)(5) is also established as to such Potential Defendants. The remaining Potential Defendants are prepetition lenders. As referred to in the Debtor/Su Stipulation at ¶¶ 6 and 27.q, most of such lenders were not repaid in full out of the liquidation of their collateral, thus satisfying the fifth element on a prima facie as to them. The Debtors, the Committee and the DIP Lender continue to conduct a cost-benefit analysis based on Bankruptcy Code § 547(b)(5) as against those lenders who were, in fact, repaid in full. However, as the *Enron* court held, prima facie evidence as to Bankruptcy Code § 547(b)(4) establishes, by itself, a colorable preference claim.

10. The Debtors are not required to disprove any defenses the Potential Defendants might have under Bankruptcy Code § 547(c) or otherwise. *See* Bankruptcy Code § 547(g) (allocating burden of proof); *In re Entringer Bakeries, Inc.*, 548 F.3d 344, 351 (5th Cir. 2008) (noting that "[t]he creditor bears the burden of proving by a preponderance of the evidence" the existing of a § 547(c) defense); *In re El Paso Refinery, L.P.*, 171 F.3d 249, 253 (5th Cir. 1999) ("Once the trustee meets this burden [as to § 547(b)], the defendant must establish one of the

exceptions contained in § 547(c) to prove the nonavoidability of a transfer. See 11 U.S.C. § 547(g).”); *In re Enron Corp.*, 2005 WL 6237551 at *6 (Bankr. S.D. Tex. 2005), *recon. den’d* Feb. 2, 2006 (“Under 11 U.S.C. § 547(g), the trustee has the burden of proving avoidability under § 547(b), and the defendant has the burden of proving non-avoidability of a transfer under § 547(c).”). Therefore, the Debtors have established colorable claims that would survive a motion to dismiss, and Mr. Su is estopped from asserting otherwise given that he signed the relevant documents under penalty of perjury that establish the colorable claims.

That upon appropriate proof would support recovery

11. Mr. Su asserts that the Debtors have not met this criteria because “[m]any of the potential Chapter 5 defendants also have proof of claims which could support defenses or offset any such claim.” As noted, the Debtors are not required to disprove defenses in order to establish a colorable claim. For example, even if a particular defendant does have a valid defense or right of offset, unless such defendant meets its burden of proving same in accordance with Bankruptcy Code § 547(g), the Debtors would be entitled to judgment as a matter of law upon meeting their burden of proof as to the five elements under Bankruptcy Code § 547(b). *See, e.g.*, *In re Brooke Corp.*, 515 B.R. 632, 634 (Bankr. D. Kan. 2014) (noting that default judgment was entered against preference defendants for failure to respond to trustee’s prima facie case); *In re Oldco M Corp.*, 484 B.R. 598 (Bankr. S.D.N.Y. 2012) (defendant’s failure to respond to a properly-noticed preference claim merited default judgment, which *Stern v. Marshall* did not prevent the bankruptcy court from entering).

Court examination, by affidavit or live evidence, of whether action on such claim is “likely to benefit the reorganization estate”

12. As noted above, this Memorandum and the Affidavit satisfy this criteria. Mr. Su asserts that the Debtors’ action in declining to pursue the Preference Actions should be construed

as a presumption "that the Debtors did not believe the benefits outweighed the risks." As noted at the first day of the Hearing, Mr. Su's own Objection identifies at least two reasons for the Debtors' decision. *See* Objection ¶ 8 (third and fourth sentences); Affidavit ¶¶ 15 & 16. Thus, whatever Mr. Su would like this Court to presume, such presumption has been overcome by Mr. Su's own allegations of Debtors' counsel's alleged conflicts. *See In re Louisiana World Exposition, Inc.*, 832 F.2d 1391, 1397 (5th Cir. 1987) (committee standing was appropriate where the debtor declined to commence the requested actions, "apparently being unable to act because of the conflict of interest presented to its decision makers"); *In re Enron Corp*., 319 B.R. at 132 ("Where a debtor in possession consents to suit by a committee, the test is met. The bankruptcy court found that Enron determined not to prosecute the claims but instead agreed to assign the prosecution to the committee. That constitutes the functional equivalent of the unjustifiable refusal test. The test protects the trustee, deferring to the trustee to act for the estate. Consent by the trustee accomplishes that objective.").

"a determination of probabilities of legal success"

13. As noted above, the Debtors' documents sworn to by Mr. Su establish the elements of Bankruptcy Code § 547(b). This means that, *per se*, the Preference Actions have a probability of success unless the Potential Defendants file a response, *see Brooke* and *Oldco M*, *supra*, and then meet their burden of proof as to any potential defenses.

"determination of ….financial recovery in event of success"

14. On April 6, 2015, the Debtors provided to counsel for all potential defendants, including Mr. Su on behalf of his non-Debtor affiliates, a list of the potential defendants ("Potential Defendants") and transfer amounts (the "Potential Preferences"). *See* Affidavit ¶ 8 and Exhibit F. The aggregate amount of Potential Preferences is approximately $33 million.

Even if the aggregate recoveries on all Potential Preferences after settlement or litigation is, hypothetically, only 10%, this would still result in a financial recovery to the estates of more than $3 million.

[four criteria relevant to whether it would be preferable to appoint a trustee]

15. As the Court itself noted at the first day of the Hearing, neither Mr. Su nor anyone else disputes that it would be more expensive to appoint a chapter 11 trustee or to convert to chapter 7 and appoint a chapter 7 trustee. To the extent the Debtors even arguably have conflicts, the Debtors have declined to pursue the Preference Actions but have an available remedy far less expensive than bringing in a trustee. The Debtors do not believe that Committee counsel has a conflict because it represents the Committee, not its members. As to the "wishes of the parties," no party-in-interest other than Mr. Su support the appointment of a trustee.

[two criteria relevant to attorneys' fees]

16. The DIP Lender and the Debtors have agreed to increase the "carve-out" under the Final DIP Order to pay the Committee's professionals on a current basis up to $25,000, plus costs (such as filing fees) and expenses, to preserve the Preference Actions. This amount may be increased modestly upon consent of the DIP Lender and the Debtors given the bifurcation of the Hearing and the need for additional presentations as a result of Mr. Su's allegations. The parties have not yet discussed a fee arrangement or budget, or any potential increase to the carve-out to permit current payment, if Preference Actions are required to be pursued beyond the initial activity of either entering into tolling agreements or filing "placeholder" complaints against Potential Defendants who decline to enter into tolling agreements. While contingency fee arrangements are not unusual in these circumstances, the Debtors and the DIP Lender have not yet concluded that contingency fees would be preferable to Committee counsel's current

discounted hourly rates, given the $33 million in Potential Recoveries.[2] Such terms are comparable to or better than the terms received from other counsel who were solicited to make a proposal with respect to pursuit of the Preference Actions, all of which contemplated fees based on a percentage of recoveries. *See* Affidavit ¶¶ 11, 12 & 16; *see generally In re Dewey & Leboeuf, supra*, at *7 (noting that it was acceptable under the circumstances that fee arrangements had not yet been made in a situation where a "contingency, or combined contingency time charge basis," would be 'common").

UPDATE

17. As of the filing of this Motion, the majority of the Potential Defendants (in number and amount) who are not affiliates of Mr. Su have agreed to enter into tolling agreements, with the remainder still in discussions with the Debtors concerning same. Once all persons who have agreed to sign tolling agreements have formally done so, the Debtors will file a "Notice of Tolling Agreements" that (i) identifies who has signed a tolling agreement and (ii) who has declined to sign a tolling agreement. Unless otherwise stated in the Notice, the Debtors or the Committee (depending on disposition of the Standing Stipulation) will be filing complaints against those who have declined to sign.

WHEREFORE, the Debtors request that the Court approve the Standing Stipulation and deny the Motion to Convert.

Respectfully submitted,

BRACEWELL & GIULIANI LLP

By: */s/ Jason G. Cohen*
Jason G. Cohen

[2] If a contingency fee approach is ultimately considered appropriate, an application will be timely filed with the Court to approve such approach.

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COUNSEL FOR THE DEBTORS AND DEBTORS IN POSSESSION

CERTIFICATE OF CONFERENCE

I hereby certify that, although Local Rule 9013-1(g) does not require the Debtors to meet and confer with Mr. Su's counsel in connection with the Memorandum, and Mr. Su did not confer with the Debtors either before or after filing his Objection to the Standing Stipulation to which the Debtors are one of two parties, I attempted to resolve this matter on the basis suggested by the Court at the first day of the Hearing through a series of communications with Mr. Su's counsel on Saturday evening, June 13. As of the time of the filing of this Memorandum, the parties have been unable to resolve this matter.

/s/ Evan D. Flaschen
Evan D. Flaschen

CERTIFICATE OF SERVICE

I hereby certify that on June 16, 2015, a true and correct copy of this document was served by the Electronic Case Filing system for this Court, which gives notice to all parties who have requested ECF notification of this proceeding.

/s/ Jason G. Cohen
Jason G. Cohen