



ABI Winter Meeting
***Asset Sale/Secured Credit/
Unsecured Trade Creditors Committees --
Polaroid and Beyond: Differing Perspectives on
What is the Highest and Best Bid, and Other
Selected Sale Issues***

**by Douglas E. Deutsch and Young Yoo
Chadbourne & Parke LLP**

CHADBOURNE
& PARKE LLP

Panelist Information

- Honorable Donald Steckroth
 - United States Bankruptcy Court (Newark, New Jersey)
- Ronald E. Gold
 - Frost Brown Todd LLC (Cincinnati, Ohio)
 - Bankruptcy and Financial Restructuring Group, Co-Chair
- Rafael Klotz
 - Gordon Brothers Group (Boston, MA)
 - Managing Director
- Douglas E. Deutsch
 - Chadbourne & Parke LLP (New York City)
 - Bankruptcy and Financial Restructuring Group Partner

Introduction to 363 Sales

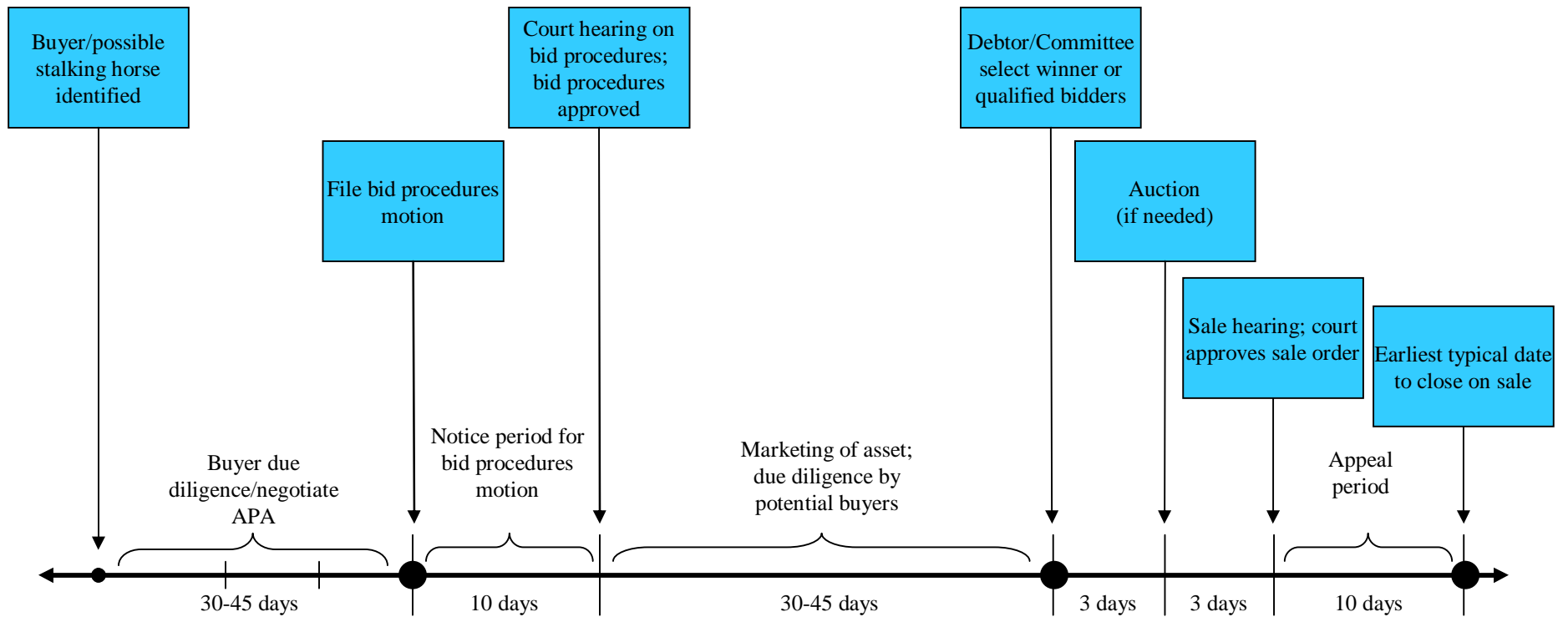
- Plan of Reorganization

- Process
 - disclosure
 - solicitation
 - confirmation
- Advantages
 - best successor liability protections available
- Disadvantages
 - multiple parties must approve
 - complexity and speed

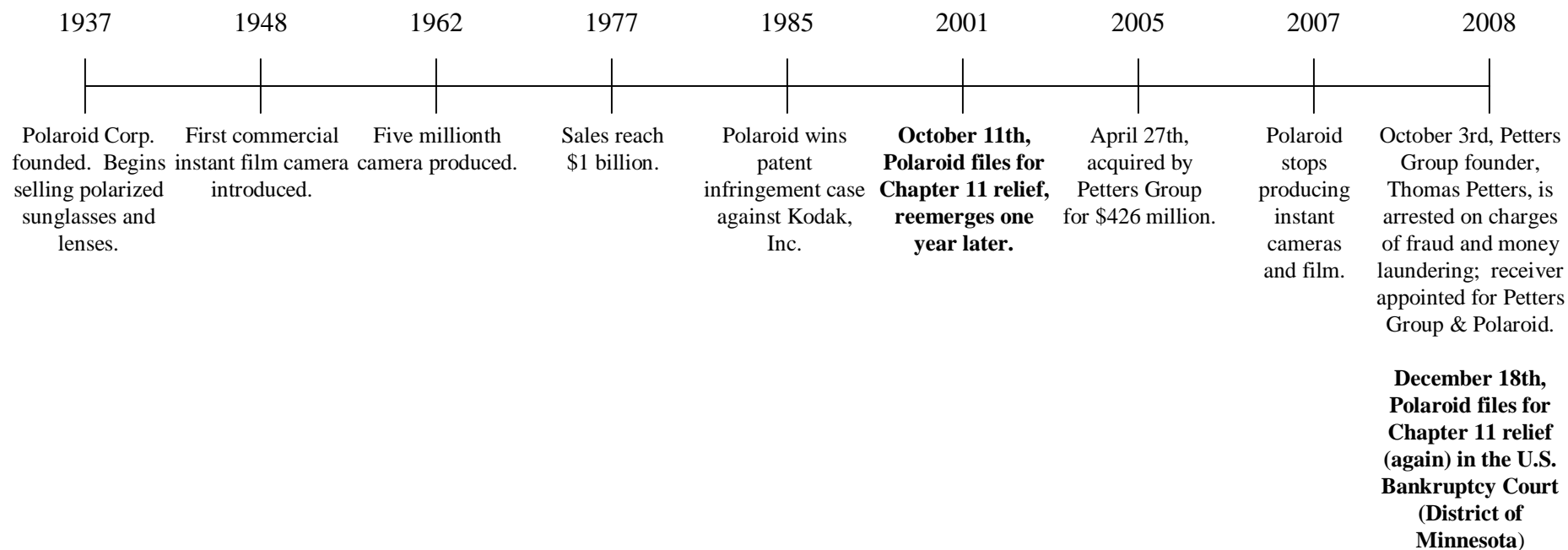
- 363 Sales

- Process
 - must obtain (a) bidding procedures order and (b) sale order
- Advantages
 - quick
 - free and clear/not subject to fraudulent conveyance claims
 - “no shop” protections
 - assign leases/contracts
 - easily understood (like M&A deal)
 - do not (usually) have to deal with resolution of claims
- Disadvantages
 - may be subject to attack as *sub rosa* plan
 - cannot generally deal with resolutions of claims or equity

Section 363 Sale Process



Background on Polaroid



Polaroid's Chapter 11 Filing

- Polaroid's bankruptcy cases are assigned to Hon. Gregory F. Kishel and jointly administered under Case No. 08-46617.
- Debtors:
 - Counsel - Lindquist & Vennum
 - Financial advisor – Houlihan Lokey Howard & Zukin Capital, Inc.
- Polaroid immediately proceeded to arrange for a sale of substantially all of their assets due to the following factors:
 - specter of Petters Group bankruptcy;
 - no reorganization plan due to lack of DIP financing;
 - the estate only had **\$21 million** in unencumbered proceeds to fund its business operations and the administration of the cases; and
 - was burning through that limited cash at a rate of **\$1 million** per week.

Polaroid's 363 Sale Motion

- On January 28, 2009, the Debtors filed a 363 Sale Motion Seeking Approval of Auction and Bidding Procedures.
 - Stalking Horse Bidder was chosen and a proposed Purchase Agreement was drawn up for **\$42 million**, with a break-up fee of **\$1.7 million**.
 - The Auction was scheduled for March 30, 2009 at Lindquist & Vennum's offices in Minneapolis, Minnesota.
 - The Sales Hearing is scheduled for March 31, 2009.

The Players

Judge

Hon. Gregory F. Kishel

United States Bankruptcy Judge
District of Minnesota

Auction Supervisors/Debtors

Houlihan Lokey

HOULIHAN LOKEY

Lindquist & Vennum

LINDQUIST & VENNUM

The Players – cont'd

Creditors' Committees

- Polaroid Unsecured Creditors' Committee
- represented by Paul Hastings



- Petters Group Unsecured Creditors' Committee
- represented by Fafinski Mark & Johnson



Creditor Constituency Parties

- Ritchie Special Capital Investments, Ltd.
- represented by Sidley Austin



- Acorn Capital Group, LLC
- represented by Winthrop & Weinstine



The Players - cont'd

Stalking Horse Bidder

Genii Capital S.A.

- by its affiliate, PCH Acquisitions, LLC
- represented by Wilkie Farr & Gallagher



Qualified Bidders

Patriarch Partners

- bid by its affiliate Lithograph Legends LLC
- Lynn Tilton, C.E.O.
- represented by Jones Day



Hilco/Gordon

- Private equity firms known for acquiring and liquidating distressed companies.
- represented by Dorsey & Whitney

Hilco Consumer Capital Corp.



DORSEY & WHITNEY LLP

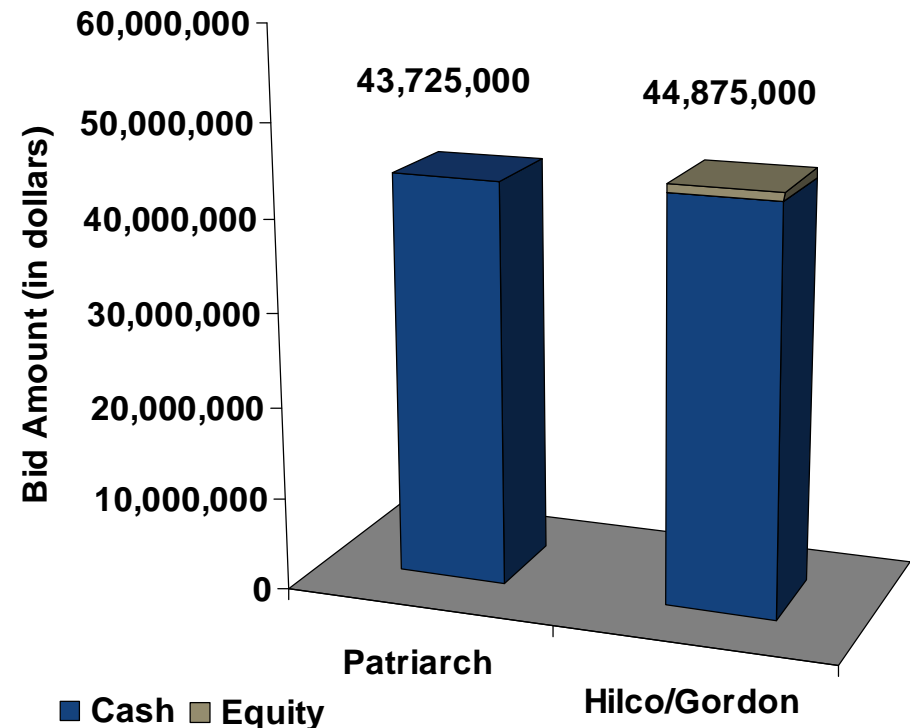
Phase One (March 30th – 31st)

Bidding Procedures and Rules

- Auction was scheduled to start at 9:00 A.M. and go until 3:00 P.M.
- Lindquist & Vennum's offices provided a conference room for the bidding and separate conference rooms for internal discussions amongst the bidder groups.
- The minimum amount for a counterbid to qualify was \$150,000 more than the previous bid.
- Bidders had 60 minutes to contemplate and submit a counterbid.

Phase One (March 30th Auction)

- Patriarch submits the opening bid at **\$43,725,000** (all cash).
- Hilco/Gordon counterbids **\$44,875,000**. \$1 million of bid consists of a **1% equity interest** in the new company (“NewCo”).
- Both Patriarch and Genii object: they claim not to have enough info to know whether \$1M for a 1% equity interest in proposed NewCo. is an appropriate valuation.
 - Patriarch demands an income statement, a balance sheet, or cash flow statement to value the equity.



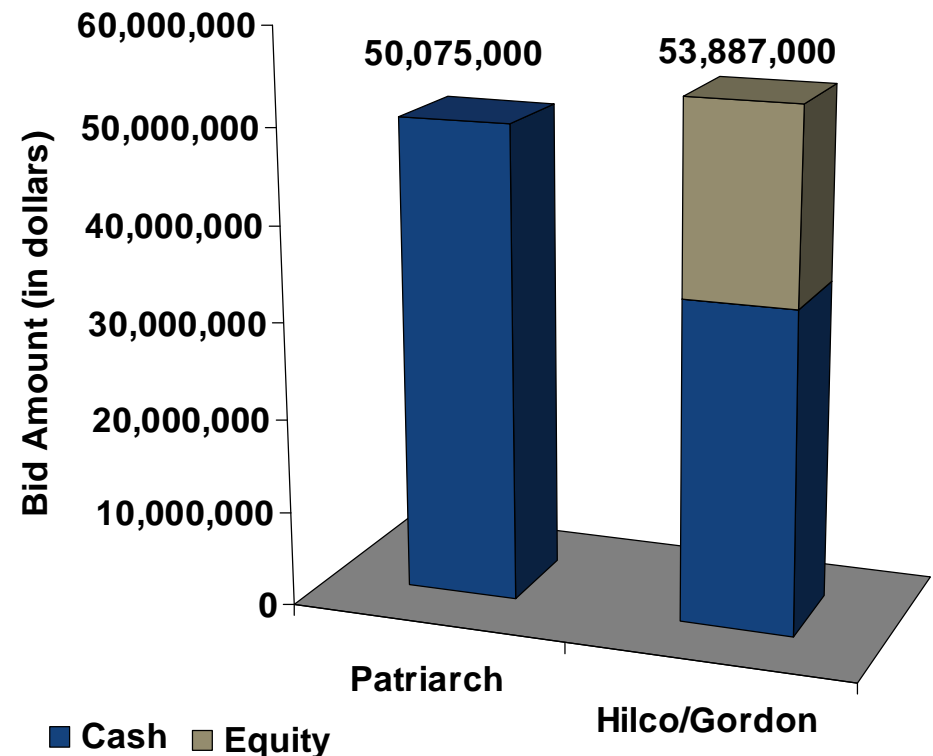
Phase One (March 30th Auction) - cont'd

Hilco/Gordon: “[Y]ou know, contrary to what Lynn says, she’s just wrong. Okay. Our game is different than her game, and it’s a fair game. . . . We are prepared to share [information] with the creditors’ committee, okay. But not with the other bidders, because that is proprietary information that we have. . . . We’re not giving our model to any other bidder.”

- After several back and forth's, Houlihan eventually deems the bid rejected and Hilco/Gordon asserts a revised counterbid of all cash valued at **\$43,887,000**.
- Patriarch counterbids and adds over \$6 million value to their bid for a total bid of **\$50,075,000**. At this point, Houlihan tries to accelerate the auction counterbid process.

Phase One (March 30th Auction) - cont'd

- Houlihan affirms Patriarch's counterbid of **\$50,075,000**.
- Hilco/Gordon responds with a revised counterbid of **\$53,887,000**, which consists of a **20% equity interest** in NewCo. They value the 20% at \$20 million and declined to provide information to the other bidders on how they quantified that valuation.
- Houlihan eventually agrees to (i) look over Hilco/Gordon's model and financials, and (ii) provide metrics on how the Debtors would value equity. The auction is adjourned for the day.

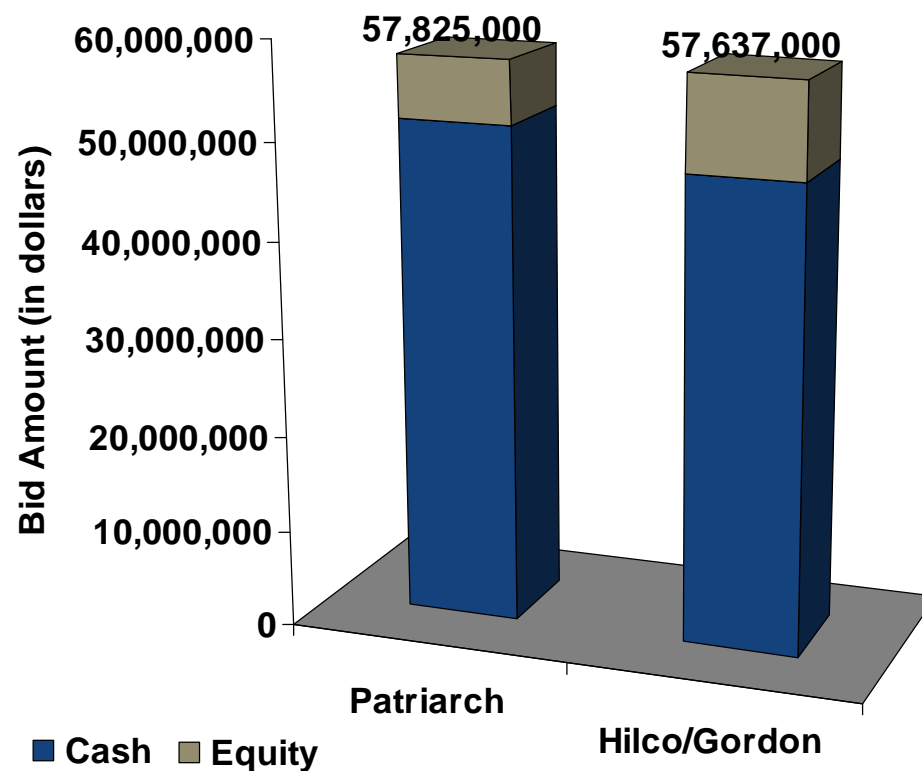


Phase One (March 31st) – The “Day After”

- The following morning before the auction resumes, Patriarch presents their own model and financials, also declining to provide information to the other bidders on how they quantified that valuation.
- Afterwards Houlihan announces that they will value each equity point at \$650,000. Both Patriarch and Hilco/Gordon object to the valuation, but Debtors nevertheless proceed on that basis.
- Upon reconvening, Houlihan announces that the revised Hilco/Gordon bid (with 20% equity) is deemed rejected for inadequate cash consideration.
- Hilco/Gordon revises their bid to a total value of \$57,637,000, which consists of:
 - increased cash component of \$4 million, and
 - 15% equity interest (using the \$650,000 per point value).

Phase One (March 31st) - “For shame!”

- Patriarch returns with a bid valued at **\$57,825,000**:
 - increased cash component of \$1 million,
 - 10% equity interest in their NewCo. (using the \$650,000 per point value).



Phase One (March 31st) - More equity...

- Both bidders begin adding percentage points of equity in rapid succession to outbid the other:

Patriarch - (+1% equity) = **\$57,825,000**,
topped by

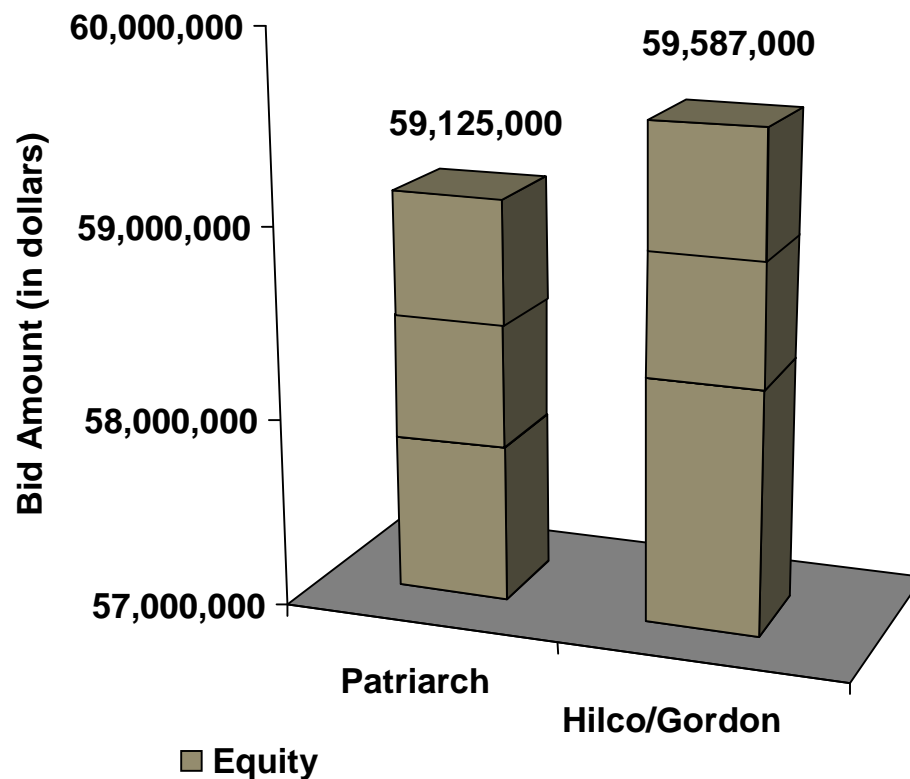
Hilco/Gordon - (+1% equity) = **\$58,287,000**,
topped by

Patriarch - (+1% equity) = **\$58,475,000**,
topped by

Hilco/Gordon - (+1% equity) = **\$58,937,000**,
topped by

Patriarch - (+1% equity) = **\$59,125,000**,
topped by

Hilco/Gordon - (+1% equity) = **\$59,587,000**.



Phase One (March 31st) - “Oh, btw...”

- At this point, Hilco/Gordon’s bid contains an 18% equity interest
- Patriarch asserts that the 20% cap on an equity component be put on the record.
 - Houlihan acknowledges the 20% cap.
- Hilco/Gordon’s team is bewildered; there is no 20% cap in the Bidding Procedures Order or the record.

Phase One (March 31st) - “Wait... what?”

Hilco/Gordon: “That’s never been told to us --
Ever.

And how do you do that after we’ve made nine bids?

. . . We retract the last three bids that we made, which were made --

No, we don’t. . . .

The last bid -- the last bid that we have on . . .

. . . she made it very clear earlier that if we’re going to bid on the same turf,
she just wants rules in the game.”

Patriarch: “Those were the rules of the game.”

Hilco/Gordon: “Right. But you got to tell the rules to the other side.”

Patriarch: “That’s not our responsibility.”

Hilco/Gordon: “I agree with that.”

Phase One (March 31st) - “2 hours later...”

- It is decided that the Patriarch bid of **\$59,125,000** is the last valid bid up to that point.
- Hilco/Gordon revises their last bid to increase it’s equity portion to 20.5%, a value they hold out as \$61,212,000.

Houlihan: “The offer is rejected by the estate.”

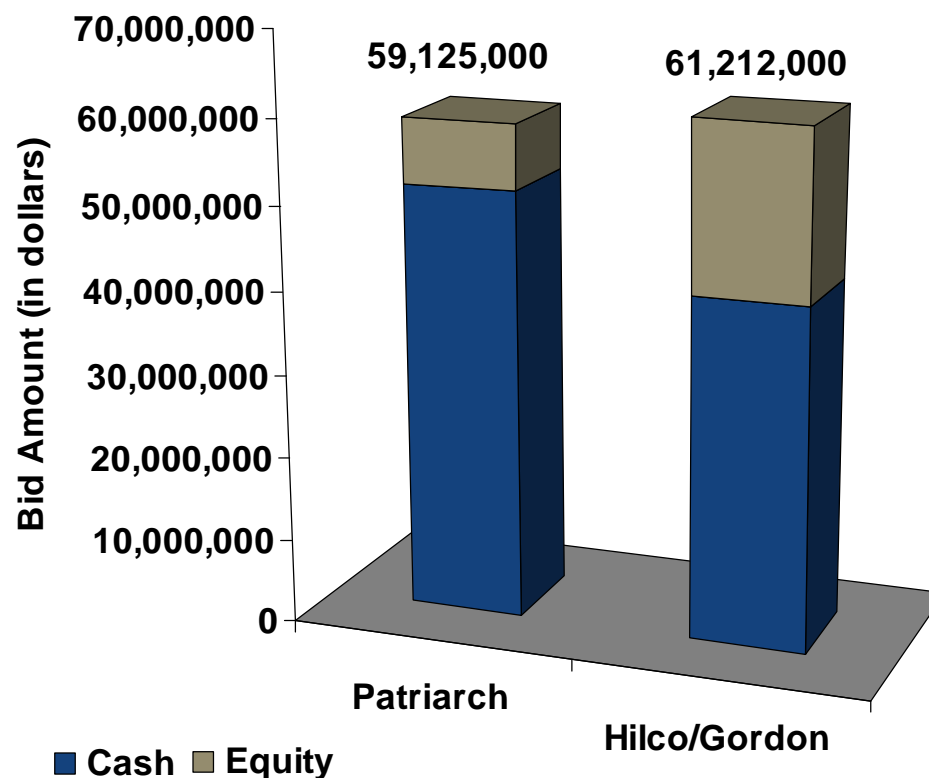
Hilco/Gordon: “Let the record reflect that that is a bid of -- with a value of \$61,212,000.”

Committee: “Let the record reflect that the committee did not support the debtor’s rejection of that bid. But the bid was premised upon the consent of both, so that bid has been withdrawn. So that is the highest and best bid.”

Houlihan: “Are there no further bids by either party? Let the record reflect that there are no further bids. The auction is hereby adjourned and we’re closed.”

Phase One - Aftermath

- Patriarch’s winning bid of **\$59,125,000** is accepted by the Debtors.
- Hilco/Gordon’s bid of \$61,212,000 is rejected.
- On April 3, 2009, Polaroid files a status report declaring Patriarch the winning bidder: “The Debtors firmly stand behind Patriarch as the prevailing bidder.”
- The Sale Hearing to approve the sale to Patriarch is scheduled for April 6th.



Phase Two (April 6th Hearing)

- Debtors' counsel immediately asks for a closed conference with the Judge. Only Committees' counsel both are invited to participate.
- Upon return to the courtroom, the Debtors propose to reopen the auction process and make use of a sealed final bid procedure with an equity cap of 25%.
- Patriarch objects on several bases:
 - the court is ignoring its prior orders;
 - which would endanger the integrity of the process; and
 - would be setting a precedent that would chill auction bidding.
- Hilco/Gordon agrees with the Debtors' proposal.
- Debtors assert that the open auction had "issues," and that they have a fiduciary duty to maximize value for the creditors.

Phase Two (April 6th Hearing) - “Fine print”

- Ultimately, the Debtors and the Judge relied on one of the last terms of paragraphs in the Bidding Procedures Order:

”The Debtors also reserve the right to reject, at any time before entry of an order of the Bankruptcy Court approving a Qualified Bid, any bid that is (i) inadequate or insufficient, (ii) not in conformity with the requirements of the Bankruptcy Code, the Bidding Procedures or the terms and conditions of sale, or (iii) contrary to the best interests of the Debtors or their estates.” Bidding Procedures Order, pp. 5-6.

Final Sealed Auction Procedures

- A sealed final bid w/ draft purchase agreement must be submitted by Patriarch and Hilco/Gordon by the next day, Tuesday, 4:00 P.M.
- Each equity point would be valued at \$650,000 and the cap is 25%.
- The Debtors have until 12 P.M. noon, Wednesday, to choose.
- The following day, Thursday, the court would reconvene the Sale Hearing at 8:00 A.M.

Phase Two (Sealed Bidding Process)

April 7

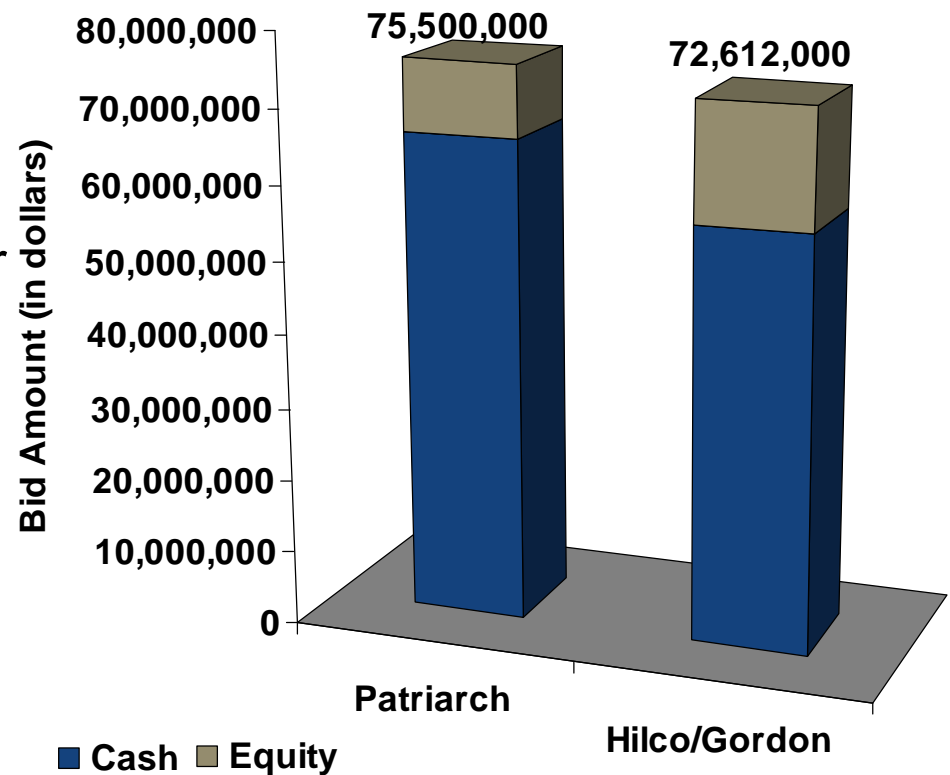
- Hilco/Gordon submits a sealed bid of **\$72,612,000** which is superior to Patriarch's sealed bid of **\$65,700,000**.

April 8

- Debtors file Notice of Filing of Prevailing Bidder, identifying Hilco/Gordon as the winning bidder.
- Patriarch calls the Debtors and discovers the outcome of the sealed bidding. Patriarch informs Debtors that it will make one more bid.

Phase Two (April 9th Hearing)

- In the morning hours before the scheduled Sale Hearing, Patriarch submits an objection, restating its original objections and submitting a revised bid after the deadline. Their bid now totals **\$75,500,000**.



Phase Two (April 9th Hearing) - cont'd

- Debtors switch positions and support Patriarch, noting the differences in the revised Patriarch bid that make it superior:
 - \$17 million more cash (depending on how calculate – could be \$9.5mm) and consequently, less equity,
 - retention of Polaroid headquarters in Minnetonka, MN (saving jobs of 70 Polaroid employees)
 - nearly \$3 million of additional value over Hilco/Gordon's bid, and
 - Patriarch assumes it will use Polaroid licenses within its companies
 - compared to Hilco/Gordon (Hilco/Gordon state that they will license the brand out to 3rd parties and liquidate the other assets)
- The Committees agree with the Debtors and several 8th Circuit cases are cited supporting the bankruptcy court's broad discretionary power:

In re Food Barn Stores, Inc., 107 F.3d 558, 565-66 (8th Cir. 1997); *In re Farmland Indus., Inc.*, 289 B.R. 122, 126 (8th Cir. B.A.P. 2002) (“Up to the point where the court actually enters an order confirming the sale, . . . a bankruptcy court has broad discretion to accept or reject bids and to conduct sales or auctions in the manner deemed most appropriate by the court.”).
- Ultimately, the Debtors and the Committees request the Court reopen the auction for further bidding and not be “in the situation again where, in essence, money is left on the table.”

Phase Two (April 9th Hearing) - “Déjà vu.”

- Hilco/Gordon is stunned, likening the situation as though the debtors were “bribed with a lot of cash at the last second,” and objects on several bases:
 - the court is ignoring its prior orders;
 - which would endanger the integrity of the process; and
 - would set a precedent that would not promote the highest value in auction bidding.
- Patriarch agrees with the Debtors now and notes that Hilco/Gordon was making virtually the same objections as Patriarch had previously. They ultimately assert the following premises in support of renewed bidding:
 - their revised bid is undeniably the best and highest bid there is;
 - the entire process was flawed, but that the 363 sale typically contemplates an open auction anyway (not sealed bidding); and
 - the court has broad discretionary power to order the requested relief.

Phase Two (April 9th Hearing) - “Do-over”

Judge: “They have both regaled their own experience in participating in sales of assets in Chapter 11 cases under Section 363 throughout the country and yet on the other hand both of them claim to have been blind-sided, to have been taken for patsies, for suckers at one point or another in the course of the bidding process. There’s a little bit of disjunction there shall we say.”

- Judge makes his decision based on the wide discretion granted to bankruptcy judges and holds that:
 - he must place priority on “**maximization of realization over the more abstract goal and definitively subordinated goal of ‘integrity in the process,’** and parties reliance. . . .” and
 - “the measure that was pitched to me and that I ended up adopting [] for a last final closed bid was not appropriate. . . it was less than optimal for generating a last shot of value for the estate.”

Phase Two (April 9th Hearing) - “Final final”

- The Judge agrees to schedule a final open auction in the court:
 - Houlihan will still supervise the auction,
 - Judge agrees to preside as an “observer,”
 - and help resolve any legal disputes,
 - the \$150,000 requirement to counterbid is reinforced,
 - the \$650,000 per equity point is reinforced,
 - the 25% equity cap is reinforced, and
 - requests for recesses to contemplate bids would be discouraged.
- The Sale Hearing is scheduled to take place immediately thereafter:

Judge: “[F]rankly, you know, I don’t see that -- this bidding process is going to run more than about an hour, if that.”

Phase Three (April 16th Auction)

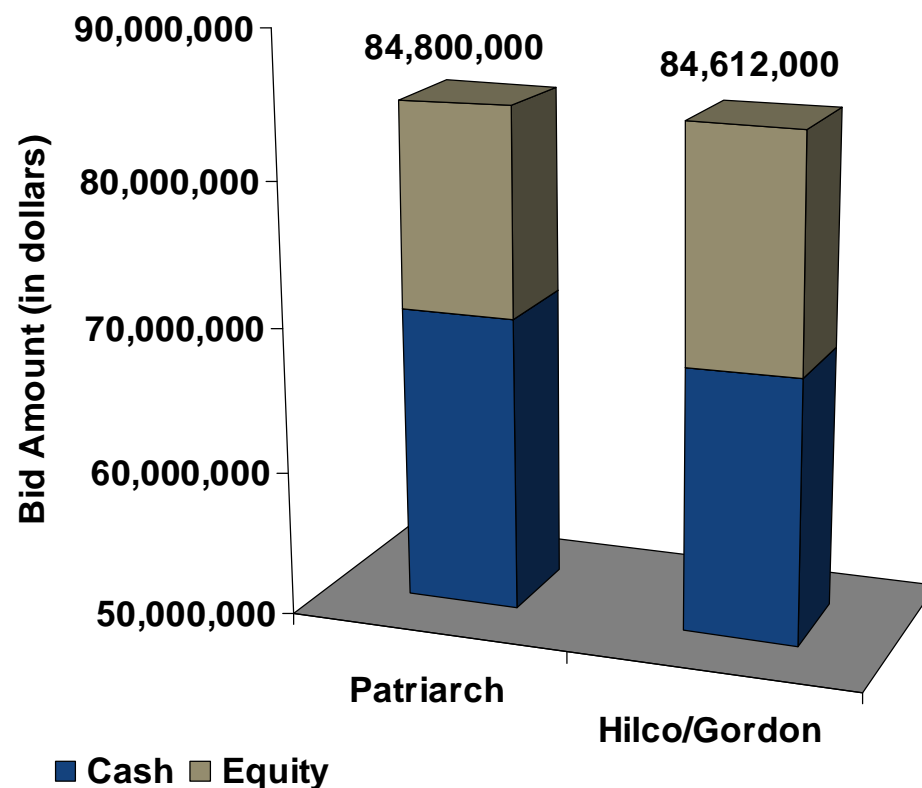
- Bidding process begins with a rapid exchange of bids
- At about the three-hour mark:

Patriarch

\$84,800,000 (at 22% equity)

Hilco/Gordon

\$84,612,000 (at 25% equity)



Phase Three (April 16th Auction) - “Oh btw.”

- At this point during the bidding, the Committee reserves its rights as to whether Patriarch’s bid is the highest bid or not. The reason proffered by Hilco/Gordon is that Patriarch’s LLC agreement has no provision that prevents the Debtors’ equity from being diluted (unlike Hilco/Gordon’s).

Patriarch: “[T]o me that means we were proceeding under false pretenses here today. That’s not what we signed up for today.”

Hilco/Gordon: “I’ll be brief, your Honor. It’s absurd for a bidder that submitted a bid after the sealed bid auction to complain about not following rules, absurd.”

- The Judge comments that the bidding process is designed to arrive at a proposed sale, which the Debtor then evaluates and at the Sale Hearing, the “best and highest bid” question can become an issue.

Phase Three (April 16th Auction) - cont'd

The Final Bids

Patriarch

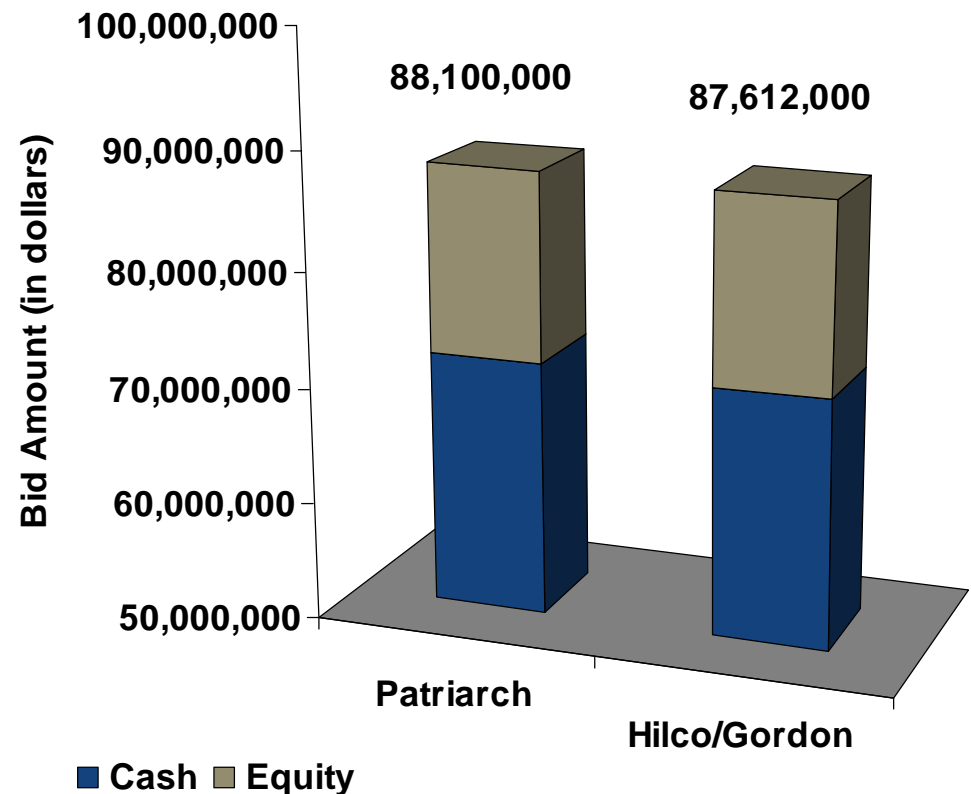
\$88,100,000 (at 25% equity)

Hilco/Gordon

\$87,612,000 (at 25% equity)

The Final Results

- Both Bidders had maxed out at 25% equity.
- Debtors return and assert that Patriarch's bid is the "best and highest bid" by nearly **\$500,000**.
- The auction is closed and the Sale Hearing begins.



Phase Three (April 16th Hearing) - “We’re best.”

- Debtors announce their support for the Patriarch bid:
 - it has a greater total value by nearly \$500,000;
 - it actually contains \$8.5 million more in cash;
 - because it buys more assets (which lowers the execution risk for the Debtors to liquidate them on their own); and
 - the Minnetonka lease for Polaroid’s headquarters will (it is asserted) be assumed and the 70 employees supposedly retained.

Phase Three (April 16th Hearing) - “No, we are.”

- One by one, the Committees and other creditor constituency parties call witnesses, and argue that the Hilco/Gordon bid is the “best and highest bid” because:
 - difference between Patriarch’s price for certain artwork (which is being excluded by Hilco/Gordon’s offer) and the independent appraisal price ranges between \$800,000 to \$4.8 million, thus overshadowing the nearly \$500,000 in Patriarch’s “greater total value;”
 - Hilco/Gordon decided to remove a 10% charged interest rate on a preferred instrument projecting savings of \$5 million per year for the Debtors;
 - the Debtors’ 25% equity in Hilco/Gordon is protected and can’t be diluted;
 - Hilco/Gordon provides more transparency to its equity holders; and
 - a waterfall provision provides definitive income distributions to equity holders (unlike Patriarch’s solely discretionary ability).

Phase Three (April 16th Hearing) - “Not really.”

- Patriarch’s rebuttal focuses on the following reasons:
 - they are offering nearly \$500,000 in additional total value;
 - the difference in artwork price does not account for the execution risks, i.e., actual liquidation costs and artwork preservation costs;
 - the elimination of the 10% interest rate is a red herring because Patriarch never had a concomitant 10% interest rate in place; and
 - if either the dilution protection or waterfall income distribution provisions were any real issue, the Committees never informed Patriarch.
- The Judge announces his final decision.

“Hilco/Gordon wins.”

Judge: “[A]s measured against the original stalking horse bid, the amount of dollar value to be attributed to either these bids is very close to or slightly more than on a net basis the original – twice the original amount of the original stalking horse bid. So the process was definitely work it going through.

Now when you’re talking about a pure liquidation, reduction solely to cash . . . that’s relatively easy. I’m going to hold that that’s not the sole consideration here in the calculus as to highest and best offer.

[T]he Court is to consider the paramount interests of creditors and their reasonable wishes under the circumstances.

I am content with deferring to the judgment of all of these creditor constituencies that the equivalent 25 percent at the outset shareholding to be given in the successor entity to be formed by Hilco Gordon has more attractiveness from the standpoint of the protections to be given to a minority shareholder up front legally speaking as set forth in the form of the LLC agreement. And I am content with giving deference to the ones whose money it is after all that we’re dealing with here. This is not going to be the Debtors’ money.”

Phase Three - Aftermath

- Patriarch attempts to interject one last time and offers that they will change their LLC agreement to grant the equity dilution protection provisions.
- The Judge flatly refuses, “I’m making my decision. It’s a little late to be forthcoming with that. I closed my record.”
- Hilco/Gordon’s last bid totaled **\$87,612,000**. Patriarch’s last bid totaled **\$88,100,000**. A difference of **\$488,000**.
- On April 23rd, Patriarch’s Motion for a Stay Pending Appeal was denied without prejudice to renew at the District Court level.
- On April 30th, U.S. District Court Judge Rosenbaum denied Patriarch’s renewed Motion, finding that the standard to set aside a Sale Order was not met, i.e., that either the purchase price was grossly inadequate, or that the sale proceeding was tainted by fraud.
- On May 7th, Hilco/Gordon announced that it would keep the headquarters in Minnetonka.

Polaroid 363 Auction, ...

- Was it a success?