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Hearing Date: November 26, 2013
Hearing Time: 9:45 a.m.

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

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In re:

261 EAST 78 REALTY CORPORATION, Chapter 11
Case No. 11-15624 (REG)

Debtor.

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261 EAST 78 REALTY CORPORATION,

Adv. Pro. No. 13-01000 (REG)

Plaintiff,

-against-

MB FINANCIAL BANK, N.A.,

Defendant.

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**DEBTOR'S MOTION IN SUPPORT OF APPROVAL OF SETTLEMENT
AGREEMENT BETWEEN DEBTOR AND MB FINANCIAL BANK, N.A.
REGARDING ADVERSARY PROCEEDING
AND CHAPTER 11 CASE *IN TOTO***

**TO: THE HONORABLE ROBERT E. GERBER,
UNITED STATES BANKRUPTCY JUDGE:**

261 East 78 Realty Corporation, the above captioned debtor and debtor-in-possession (the "Debtor"), by its undersigned attorneys, DelBello Donnellan Weingarten Wise & Wiederkehr, LLP, hereby files this ("Motion") pursuant to Rule 9019 of the Federal Rules of Bankruptcy Procedure ("FRBP") for entry of the Settlement Agreement, an executed copy of which is annexed hereto, (the "MB Settlement Agreement") by and between, inter alia, the Debtor and

MB Financial Bank, N.A., (“MB”), which MB Settlement Agreement, inter alia, effectively resolves all pending disputes between the respective parties in the pending above captioned Adversary Proceeding and the Debtor’s Chapter 11 case *in toto*. In support of this Motion, the Debtor respectfully states as follows:

JURISDICTION AND VENUE

1. The Court has jurisdiction over this Motion pursuant to 28 U.S.C. §§ 157 and 1334. Consideration of the Motion is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A).
2. Venue is proper in this District pursuant to 28 U.S.C. §§ 1408 and 1409.
3. The statutory bases for the relief requested herein are §§ 105(a) and 363 of Title 11 of the United States Code, 11 U.S.C. §§101, et seq. (the “Bankruptcy Code”) and FRBP Rule 9019.

BACKGROUND

4. On December 6, 2011, (the “Filing Date”), the Debtor filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code.
5. The Debtor has continued in possession of his property and management of his business affairs as debtor-in-possession pursuant to §§1107(a) and 1108 of the Bankruptcy Code. No trustee, examiner or statutory committee has been appointed.
6. The Debtor owns a commercial rental professional building located at 261 East 78th Street, New York, New York (the “Property”).

MB’s Claims Against The Debtor.

7. MB has filed in the Debtor’s Chapter 11 Case a secured claim in the amount of \$17,674,827.28 plus continuing default rate interest, advances, costs and legal fees thereon.

The Debtor's Objection to MB's Standing

8. The first issue that arose in the Bankruptcy was MB's standing to assert a claim against the Debtor. MB has admitted that it does not possess certain of the original notes. The Debtor argued that without possession or legal ownership of the notes, MB has no standing to assert a claim, secured, unsecured or otherwise, against the Debtor or its estate under well settled principles of New York statutory and case law. The Debtor accordingly filed an adversary proceeding under Adv. Pro. No. 12-01118 (the "Standing Lawsuit") seeking a determination and/or declaration from the Bankruptcy Court that MB neither has standing nor a claim against the Debtor or its estate.

9. The Bankruptcy Court ultimately came to the conclusion that MB had standing despite the fact it did not have the original notes or a lost note affidavit from someone with personal knowledge. Accordingly, on December 10, 2012, the Bankruptcy Court ruled that MB would have standing as a creditor in the Chapter 11 case conditioned upon posting a bond or other financial equivalent, including a stand by letter of credit, in the amount of \$35,349,654.56 (the "Bond"), that being twice the amount of MB's claim filed in the Chapter 11 Case.

10. Upon reconsideration by motion of MB, the Bankruptcy Court in July, 2013 modified its ruling by removing the condition that MB post any form of security and instead directed the establishment of an supplemental claims bar date for any third party to come forward and claim an interest in or ownership of the Broadway notes. The Court set October 21, 2013 as the supplemental claims bar date. To date, no party has filed a claim and, therefore, MB is deemed to have standing to assert its claims against the Debtor.

The Debtor's Lender Liability Action Against MB

11. On January 2, 2013, the Debtor filed Adversary Proceeding No. 13-01000 (the

“Lender Liability Action”) against MB, alleging various claims against MB arising out of alleged lender liability related acts. MB initially moved to dismiss the complaint, after which the debtor amended its complaint. On July 17, 2013, MB filed an answer to the amended complaint, essentially denying all of the allegations contained therein. The matter was set down for discovery and is currently in the discovery stage.

Mediation and Settlement Between the Debtor and MB

12. As it became clear that the Debtor’s previously filed Plan of Reorganization and Chapter 11 case on the whole could not be resolved or proceed without a full adjudication of the Lender Liability Action, and in further light of escalating professional fees further jeopardizing the administrative solvency of the Debtor’s estate, and the Debtor’s attempts to reach a global settlement with MB having failed to date, the Debtor requested that the Court appoint a mediator.

13. On July 11, 2013, the Court signed an endorsed order directing the parties to go to mediation while permitting the continuation of the Lender Liability Action. The parties selected Hon. Melanie Cyganowski as mediator and the parties prepared for and attended mediation, including a ten (10) hour session on September 10, 2013, and substantial telephonic and written negotiations thereafter.

14. The mediation resulted in a global settlement between MB and the Debtor which resolves all outstanding litigation and paves the way for the Debtor to seek confirmation of its First Amended Plan.

THE MB SETTLEMENT AGREEMENT

15. The MB Settlement Agreement, a copy of which is annexed to the Motion as

Exhibit “A”, can be summarized as follows:

- i. *Satisfaction of Allowed Secured Claim of MB by Debtor.* As soon as practicable, the Debtor shall file its First Amended Plan pursuant to which MB shall have an Allowed Class 2 Secured Claim in the amount of \$10,700,000.00, and an Allowed Class 3 deficiency Unsecured Claim in the minimum amount of \$6,974,827.28, *provided that* MB’s Allowed Class 2 Secured Claim shall increase to \$11,000,000 (“Increased Allowed Class 2 Claim”) in the event that its Class 2 Claim is not satisfied by the Debtor (or the Plan Funder on behalf of the Debtor) within 120 days after the execution date of the MB Settlement Agreement (the “120-Day Deadline”), which Increased Allowed Class 2 Claim shall be paid in full from the proceeds of a public sale of the Property within 150 days (the “150-Day Deadline”) after the execution of the MB Settlement Agreement.
- ii. *Plan Confirmation Deadline and Conditional Stay Relief.* The Debtor shall obtain the entry of a Final Confirmation Order within 90 days after the execution of the Settlement Agreement. In the event that a Final Confirmation Order confirming this Plan is not entered by the Bankruptcy Court within 90 days after the execution of the MB Settlement Agreement, upon five-days’ notice served on the Debtor and creditors and filed with the Bankruptcy Court, MB shall be entitled to relief from the automatic stay, without further order of the Bankruptcy Court, to resume its foreclosure action with respect to the Property (the “Foreclosure Action”) in the Supreme Court of the State of New York State, County of New York (the “New York Court”).
- iii. *Public Sale Scenario.* In the event that the Debtor (or the Plan Funder on its behalf) fails to pay MB \$10.7 million in satisfaction of its Allowed Class 2 Secured Claim before the expiration of the 120-Day Deadline, the Debtor shall conduct a public auction of the Property (the “Public Sale”) on or before 140 days after the execution of the Settlement Agreement with a closing to occur on or before the 150-Day Deadline. Following the 120 Day Deadline and during the Public Sale process, MB’s Allowed Class 2 Secured Claim shall increase to \$11,000,000 and MB shall have an absolute right to credit bid its Allowed Class 2 Secured Claim up to the amount of \$11,000,000. Following the 120-Day Deadline, the Debtor may not terminate the Public Sale by satisfying MB’s Allowed Class 2 Secured Claim in cash through a refinancing. MB’s credit bid in the Public Sale shall be subject to higher and better cash bids made by bidders with the financial wherewithal to close by the 150-Day Deadline, provided that any such competing bids are subject to payment of a 10% deposit and a minimum overbid (above \$11,000,000) equal to the sum of (A) all outstanding real property taxes due with respect to the Property, if any (B) Allowed Administrative Expense Claims and (C) all sale closing costs, including any broker’s commission, if applicable, such that the net sale proceeds available to pay MB Financial shall be at least \$11,000,000. (“Qualifying Bids”). In the event that the Debtor is unable to consummate a refinancing and pay MB Financial \$10.7 million on or before the 120-Day Deadline or MB Financial does not receive \$11 million

on or before the 150-Day Deadline from the proceeds of a sale of the Property to a third party that submitted a Qualified Bid on or before the bid deadline (to be at least 2 business days before the date of the Public Sale), MB Financial shall receive title to the Property, free and clear of any claims, interests, liens or encumbrances, in consideration of its credit bid, on the 150-Day Deadline. If a Qualified Bid is not received before the bid deadline, the Debtor shall be obligated to execute and deliver all documents of assignment and transfer reasonably requested by MB to convey it title to the Property such that a closing can occur on the 150-Day Deadline and MB shall make a \$85,000 payment to the Debtor's estate on account of U.S. Trustee fees and Allowed Administrative Expense Claims. In the event that a Qualified Bid is received before the bid deadline, but the successful bidder fails to close by the 150-Day Deadline, then the Debtor shall be obligated to promptly proceed with a closing of a sale of the Property to MB as soon as possible after the 150-Day Deadline or earlier if the Debtor has prior notice that the successful bidder will not close on the sale by the 150-Day Deadline.

- iv. *Waiver of MB Deficiency Claim.* MB shall agree to vote its Allowed Class 3 deficiency Unsecured Claim in favor of the Plan but, subject to the terms and conditions of the MB Settlement Agreement, shall waive its right to receive any distribution on account of its Allowed Class 3 deficiency Unsecured Claim, provided, however, that MB shall retain all of its rights under its subordination agreement with Hermes Capital, LLC.
- v. *Release of Claims.* The parties shall mutually release each other and discontinue the Lender Liability Action with prejudice, subject to the terms and conditions of the MB Settlement Agreement.

The MB Settlement Agreement therefore permits the Debtor to satisfy MB's claim in a substantially reduced and compromised amount and, in the event the Debtor fails to satisfy said claim within the time frame imposed under the MB Settlement Agreement, a public auction sale shall ensue, with MB entitled to assert a credit bid in an amount (\$11 million) which is still substantially less than its total Claims of \$17,674,827.28.

16. Absent the settlement, the Debtor would be mired in endless and administratively crushing litigation with no certainty of success. The other Creditors of the estate would be in jeopardy of zero distribution in the event that MB's entire claim were Allowed as a Secured Claim.

17. The MB Settlement Agreement gives the Debtor an opportunity to satisfy MB's Secured Claim at a significant discount and make a meaningful distribution to its other creditors.

Even if the Debtor is unsuccessful in satisfying the MB Allowed Class 2 Secured Claim within the 120 Deadline, creditors will still have an opportunity to receive a distribution from a sale auction process and, should they wish, submit bids to purchase the Property. Absent the MB Settlement Agreement, it is likely that creditors would receive no distribution under any scenario. Accordingly, the Debtor submits that the MB Settlement Agreement is reasonable and necessary and in the best interests of all creditors.

**REQUEST FOR APPROVAL OF THE MB SETTLEMENT
AGREEMENT PURSUANT TO FRBP RULE 9019**

18. The Debtor submits that approval of the MB Settlement Agreement is in its best interest since the MB Settlement Agreement materially reduces MB's secured claim against the Property, waives its rights to distribution on its almost \$7 million deficiency unsecured claim and allows the Debtor a realistic opportunity to confirm a plan which will result in distributions to all of the Debtor's creditors.

19. Absent the settlement, MB's secured claim, if allowed in full, would materially diminish if not wholly eliminate any return to the Debtor's creditors or its estate or, at a minimum, the estate will incur additional risk, cost, time delay and expense of prosecuting the Lender Liability Action.

20. FRBP Rule 9019(a) permits this Court to approve a compromise or settlement.
The Rule provides:

- (a) *Compromise.* On motion by the trustee and after notice and a hearing the court may approve a compromise or settlement. Notice shall be given to creditors, the United States trustee, the debtor, and indenture trustees as provided in Rule 2002 and to any other entity as the court may direct.

21. Neither FRBP Rule 9019 nor any section of the Code explicitly sets forth the standards by which a court is to evaluate a proposed settlement for approval. However, the standards for approval of settlements in bankruptcy cases are well established in the case law, focusing upon whether the proposed settlement is reasonable and in the best interests of creditors. *See Protective Committee v. Anderson*, 390 U.S. 414 (1968), *reh'g denied*, 391 U.S. 909 (1968).

22. In deciding whether a proposed compromise is fair and equitable, reasonable and in the best interests of creditors, courts in the Second Circuit follow the analysis first articulated by the Supreme Court in Anderson, as developed and applied by the case law. Thus, courts assess a proposed settlement based upon a consideration of some or all of the following factors:

- (i) the relative benefits to be received by creditors under the proposed settlement;
- (ii) the likelihood of success in the litigation compared to the present and future benefits offered by the proposed settlement;
- (iii) the prospect of complex and protracted litigation if settlement is not approved;
- (iv) the attendant expense, inconvenience and delay of litigation;
- (v) the probable difficulties of collecting on any judgment that might be obtained;
- (vi) the competency and experience of counsel who support the proposed settlement;
- (vii) the extent to which the settlement is the product of arm's-length bargaining, and not the product of fraud or collusion;
- (viii) the nature and breadth of any releases to be issued as a result of the proposed settlement; ;and
- (ix) the paramount interest of the creditors and proper deference to their reasonable views.

See City of Detroit v. Grinnell Corp., 495 F.2d 448, 463 (2d Cir. 1974); In re Ionosphere Clubs, Inc., 156 B.R. 414, 427 (S.D.N.Y. 1993); In re Purified Down Products Corp., 150 B.R. 519, 522 (S.D.N.Y. 1993); In re International Distribution Centers, Inc., 103 B.R. 420, 422 (S.D.N.Y. 1989); In re Fugazy, 150 B.R. 103,106 (Bankr. S.D.N.Y. 1993); In re Drexel Burnham Lambert Group, Inc., 134 B.R. 499, 506 (Bankr. S.D.N.Y. 1991); In re Crowthers McCall Pattern, Inc., 120 B.R. 279, 287 (Bankr. S.D.N.Y. 1990); In re Texaco, Inc., 84 B.R.893, 901 (Bankr. S.D.N.Y. 1988); In re Lion Capital Group, Inc., 49 B.R. 163, 175 (Bankr. S.D.N.Y. 1985); In re Carla Leather, Inc., 44 B.R.457, 466 (Bankr. S.D.N.Y. 1984), *aff'd* 50 B.R. 764 (S.D.N.Y. 1985); In re W.T. Grant Co., 4 B.R. 53,69 (Bankr. S.D.N.Y.). *aff'd*, 20 Bankr. 186 (S.D.N.Y.), *aff'd*, 699 F. 2d 599 (2d Cir. 1983), *cert. denied sub nom.* Cosoff v. Rodman, 464 U.S. 822 (1983). *See also* In re Jackson Brewing Co., 624 F. 2d 599, 602 (5th Cir. 1980).

23. In evaluating the propriety of a settlement in concert with the foregoing factors, the court need not conduct a trial, “mini-trial,” or “a rehearsal of the trial” on the merits to actually resolve the extant factual and legal issues, but must simply consider whether against the background of those issues, the settlement is reasonable. Newman v. Stein, 464 F. 2d 689, 692 (2d Cir. 1972), *cert. denied sub nom.* Benson v. Newman, 409 U.S. 1039 (1972). *See also*, International Distribution,103 B.R. at 423; Drexel Burnham, 134 B.R. at 496. In so doing, the court may consider the settlement in the context of its familiarity with the history of the case, the complexity of the claims alleged, the parties, and the context in which the claims and the settlement arose. *See* Anderson, 390 U.S. at 444; Purofied Down Products, 150 B.R. at 519, 524; International Distribution Centers, 103 B.R. at 423.

24. The settlement evaluation process is not designed to substitute the court’s judgment for that of a trustee. Carla Leather, 44 B.R. at 465. While the Court is not expected to

“rubber stamp” a proposed settlement, the Court should give considerable weight to the informed judgment of the Debtor that the compromise is fair and equitable and the support of the Committee to the settlement, *See Anderson*, 390 U.S. at 444; *Ionosphere*, 156 B.R. at 426; *International Distribution Centers*, 103 B.R. at 423; *Drexel*, 134 B.R. at 496; *Carla Leather*, 44 B.R. at 472. As articulated by the district court in *International Distribution Centers*, the Court should give weight to the support not only of the Debtor’s counsel but of other counsel to a settlement in determining the wisdom of the compromise. *International Distribution Centers*, 103 B.R. at 423.

25. The Debtor and its counsel have determined that the MB Settlement Agreement is fair and reasonable for several reasons. First, the MB Settlement Agreement provides for a substantial savings to the estate by reducing MB’s secured claim by more than \$6 million, accompanied by a waiver of its corresponding unsecured deficiency claim in such amount, which therefore allows for a return to the Debtor’s other creditors under the Debtor’s Amended Plan.

26. Furthermore, without the MB Settlement Agreement, the Debtor would have to proceed to trial on the Lender Liability Action, which would be extremely risky, costly (and has already cost the estate in excess of \$550,000 in post-petition legal fees) and consume the Debtor’s already limited cash flow and cash reserves. Proceeding to trial on the Lender Liability Action would not only pose costly financial constraints to the Debtor and its estate, but also pose a risk in the possibility of not succeeding at trial, in which case, all of the costs associated with proceeding with the trial would have provided no benefit to the Debtor’s estate and the MB secured claim would likely be allowed in a significantly higher amount than the \$10,700,000-\$11,000,000 settlement amount.

27. The Debtor submits that approval of the MB Settlement Agreement is in the best interests of the Debtor and its estate since the MB Settlement Agreement effectively resolves all disputed claims and issues between the parties with respect to the secured claims of MB in the Debtor's bankruptcy proceedings, the Debtor's estate will avoid the costs and time delay which would be associated with further protracted litigation and discovery, and the Debtor believes that the consideration given by both parties in the MB Settlement Agreement is fair and reasonable.

REQUEST FOR CONDITIONAL AUTOMATIC STAY RELIEF

28. The MB Settlement Agreement provides that the Debtor shall file its First Amended Plan as soon as practicable after the date of execution of the MB Settlement Agreement and that the Debtor shall obtain the entry of a final, non-appealable order confirming the First Amended Plan, consistent with the MB Settlement Agreement and in form and substance reasonably satisfactory to MB Financial, within 90 days after the execution of the MB Settlement Agreement. The MB Settlement Agreement provides further that in the event a final, non-appealable order confirming the First Amended Plan is not entered within 90 days after the execution of the MB Settlement Agreement, upon five-days' notice served on the Debtor and creditors and filed with the Court, MB Financial shall be entitled to relief from the automatic stay, without further order of the Bankruptcy Court, to resume the Foreclosure Action.

29. Accordingly, by this Motion, the Debtor seeks conditional relief from the automatic stay in favor of MB to effectuate the terms of the MB Settlement Agreement. The grant of stay relief in favor of MB is an essential component of the consideration MB bargained for in entering into the MB Settlement Agreement without which the parties would not have reached an agreement. The Debtor believes that 90 days is a reasonable period of time for it to achieve confirmation of its First Amended Plan. However, in the event that the Debtor is unable

to confirm its plan within that time frame, the Debtor has agreed that MB should be entitled to stay relief to resume the Foreclosure Action. Pursuant to section 362(d)(1), cause exists to lift the automatic stay in favor of MB in the event that the Debtor fails to obtain entry of a confirmation order within 90 days because MB's secured interest in the Debtor's property is not adequately protected. Among other reasons, the Debtor continues to use rents to fund operating and other expenses that are MB's cash collateral without providing meaningful adequate protection to MB in return. In addition, the Debtor has significant unpaid real property tax liabilities which by law are entitled to a priming lien on the property. Pursuant to section 362(d)(2), MB is also entitled to stay relief because, absent the reduction in MB's claim and MB's consent and support provided for in the MB Settlement Agreement, the Debtor lacks equity in its property and the cannot effectively reorganize. Therefore, there is ample basis to grant MB stay relief conditioned on the terms of the MB Settlement Agreement.

NOTICE

30. Notice of this Motion will be provided to (i) Office of the United States Trustee; (ii) parties who have filed notices of appearance; and (iii) all creditors. The Debtor submits that said notice is adequate and proper.

CONCLUSION

31. In light of the foregoing, the Debtor respectfully submits that the settlement embodied in the MB Settlement Agreement falls well above "the lowest point in the range of reasonableness" and is in the best interests of the estate at large and should therefore be approved. Accordingly, the Debtor respectfully requests the Court approve the MB Settlement Agreement in its entirety.

32. No previous application for the relief herein requested has been made to this or any other Court.

WHEREFORE, the Debtor respectfully requests that the Court approve and authorize the MB Settlement Agreement, together with such other and further relief as is just and proper under the circumstances.

Dated: White Plains, New York
November 4, 2013

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