IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re: BOOMERANG TUBE, LLC, a Delaware limited liability company, et al., Debtors.	Chapter 11 Case No. 15-11247 (Jointly Administered) **Hearing Held: October 5, 2015 at 9:30 a.m.** **Related D.I. Nos.: 470, 497, 528**

POST-CONFIRMATION-HEARING BRIEF OF SB BOOMERANG TUBULAR, LLC

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NATURE AND STAGE OF PROCEEDING

1. The Debtors' filed their Amended Joint Prearranged Chapter 11 Plan Dated September 4, 2015 [D.I. 470] (the "**Plan**"). On September 14, 2015, SB Boomerang Tubular, LLC ("**SBBT**") filed its objection to the Plan [D.I. 497] (the "**Objection**"). On September 18, 2015, the Debtors filed their response to Plan objections [D.I. 528] (the "**Response**"). On October 5, 2015, the Court held a hearing on the foregoing and directed the parties to submit post-hearing briefs no later than October 16, 2015. SBBT, by and through its undersigned counsel, submits this post-confirmation-hearing brief in opposition to the Plan. In support, SBBT respectfully states as follows:

SUMMARY OF ARGUMENT

2. SBBT's objection to the Plan is about fundamental fairness. The Debtors and Black Diamond are quarrelling with the Creditors Committee over Boomerang's enterprise valuation, which is somewhere between $200 million and $330 million. At the same time, in their dispute with SBBT the Debtors and Black Diamond are aggressively advocating for an unjustifiably low valuation of a heat treat line in an effort to secure an $8 million windfall by retaining income-generating equipment at a steep discount—at SBBT's expense. If the opportunity arose, SBBT would take back the Equipment and use it in its own operations. At the same time, SBBT would not oppose the Debtors' retention of the Equipment as long as SBBT were adequately compensated in accordance with the Bankruptcy Code's protections for lessors[1] or secured creditors. The Plan unfairly undermines those protections, and thus should not be confirmed unless amended to provide for either (i) assumption of the Lease or (ii) the full payment of SBBT's secured claim over the next seven years.

[1] SBBT asserts that the Lease is a true lease; as such, the Debtors must assume or reject the Lease under § 365 of the Bankruptcy Code.

3. Specifically, SBBT objects to the Debtors' Plan because (i) the Plan improperly seeks to recharacterize a true lease as a secured financing; (ii) upon such recharacterization, the Plan uses an unreasonably low value for the collateral securing the Debtors' obligations, thereby unfairly diminishing the amount of SBBT's secured claim; (iii) the Plan does not satisfy the Bankruptcy Code's provisions for creditors such as SBBT that have taken the election under § 1111(b) because the proposed payment terms are neither "fair and equitable" nor feasible; and (iv) the Plan improperly places SBBT in line for payment behind an invalid claim manufactured by the Debtors and not asserted by the supposed creditor. The evidence adduced at the confirmation hearing held on October 5, 2015 establishes conclusively that the Debtors' Plan is not confirmable as presently formulated.

ARGUMENT

I. The Law and Evidence Do Not Support the Debtors' Proposed Recharacterization of the Lease.

4. The Debtors seek by their proposed Plan to recharacterize the Lease[2] as a financing agreement. But the terms of the Lease and the economic realities of the transaction between SBBT and Boomerang belie Debtors' proposed treatment. The Lease is a true lease under the law, and the Court should reject the Debtors' proposed recharacterization.

5. As explained in greater detail in SBBT's Objection, the Uniform Commercial Code establishes a two-part test to determine whether a purported lease should be recharacterized as a disguised financing, often referred to as the "bright-line test." If a party seeking to recharacterize a lease cannot satisfy the bright-line test, then courts will examine the "economic realities" of the transaction to determine whether recharacterization is

[2] Capitalized terms not otherwise defined herein have the meaning ascribed in SBBT's Objection.

appropriate. In this case, the facts and evidence do not justify recharacterization under either the bright-line test or economic realities test.

6. Section 1.203(b) of the Texas UCC provides:

> (b) A transaction in the form of a lease creates a security interest if the consideration that the lessee is to pay the lessor for the right to possession and use of the goods is an obligation for the term of the lease and is not subject to termination by the lessee, and:
>
> (1) the original term of the lease is equal to or greater than the remaining economic life of the goods;
>
> (2) the lessee is bound to renew the lease for the remaining economic life of the goods or is bound to become the owner of the goods;
>
> (3) the lessee has an option to renew the lease for the remaining economic life of the goods for no additional consideration or for nominal additional consideration upon compliance with the lease agreement; or
>
> (4) the lessee has an option to become the owner of the goods for no additional consideration or for nominal additional consideration upon compliance with the lease agreement.

Tex, Bus. & Com. Code Ann. § 1.203(b) (West 2009).

7. Under the two-part bright-line test, the Lease can only be found to be a security agreement as a matter of law if Boomerang did not have the right to terminate its payment obligations under the Lease prior to the end of its term ***and*** one of the other four factors set forth in UCC section 1.203(b) is present. *See, e.g., In re Newsome,* 2003 Bankr. LEXIS 514 at *12-13 (Bankr. N.D. Tex. May 8, 2003) (applying former section 1.201(37) of the Texas UCC); *see also Duke Royal Energy, LLC v. Pillowtex Corp. (In re Pillowtex)*, 349 F.3d 711, 717 (3d Cir. 2003) (applying former section 1.201(37) under the New York UCC).

A. None of the Four Elements of the Second Part of the Bright-Line Test Are Satisfied.

8. The parties do not dispute that the first element of the two-part test is satisfied: Boomerang did not have the right to terminate its obligations under the Lease. But because

none of the other four elements in the second part of the test are satisfied, as a matter of law the Lease cannot be recharacterized under the bright-line test.

(i) The Lease Term Does Not Exceed the Life of the Equipment.

9. The Lease term is seven years. Lease (Ex. 139), ¶ 6(a). The parties have stipulated that their "experts agree the useful life of the Equipment, based on the Manufacturer's specifications, is 15 years." Joint Stipulation of Undisputed Facts Related to SB Boomerang Tubular, LLC's Objection to Debtors' Amended Plan of Reorganization (the "**Stipulation**") (Ex. 189), ¶ 37.

10. Moreover, the Final Purchase Option alone, exceeding $7 million, evidences SBBT's and Boomerang's mutual belief that the Equipment would have substantial remaining value at the end of the Lease term. *See In re Integrated Health Services, Inc.*, 260 B.R. 71, 76 (Bankr. D. Del. 2001) (the useful life of the leased property should be determined as it existed at the time of the transaction).

11. Accordingly, the evidentiary record indisputably shows that this element of the second part of the bright-line test is not satisfied and cannot serve as a basis for recharacterization of the Lease.

(ii) Boomerang Is Not Bound Under the Lease to Purchase the Equipment.

12. In their Response to SBBT's Objection, the Debtors argue that the bright-line test for treating a lease as a financing is met because, under ¶ 7 of the Lease (Ex. 139), "Boomerang is bound to become the owner of the goods at the conclusion of the agreement's term." Response 68, ¶ 130. This is simply wrong, and the Debtors cite no authority for their novel argument that a purchase ***option*** can properly be termed a purchase ***obligation*** simply because it is advantageous for a debtor in bankruptcy to so characterize it in hindsight.

13. The Debtors acknowledge that under the plain language of the Lease, the Lessor "may" exercise an option to require the Lessee to purchase the Equipment at a pre-determined, negotiated purchase price. *Id.* But there is nothing in the Lease itself, and nothing in the law, that requires the Lessor to exercise that option—it is completely voluntary. If SBBT does not exercise the option, then Boomerang will not, under the express terms of the Lease, become the owner of the Equipment. So while it is ***possible*** that Boomerang would become the owner of the Equipment at the end of the Lease, it is by no means ***certain***. That SBBT may have anticipated exercising the option does not transform the option into an unconditional obligation. No amount of linguistic gymnastics can change this simple fact: Boomerang is not "bound" to become the owner of the Equipment.

14. Indeed, Mr. Nystrom admitted at the confirmation hearing that at this moment Boomerang is ***not*** required to purchase the Equipment from SBBT. Hr'g Tr. 28:23-25, Oct. 5, 2015. Mr. Nystrom also acknowledged that at the end of the Lease, if neither party exercises the final sale option, the Equipment would be returned to SBBT:

> Q: Let's assume for a moment that the end of the lease term occurs. Let's assume, if we could, that no new lease is entered into and SBBT does not require Boomerang to purchase the equipment.
>
> A. Yes.
>
> Q. Let's assume further that … you, Boomerang do not demand that SBBT sell to you. What happens under the lease?
>
> A. Then it just expires. So if—in the scenario that I can't reach an agreement on lease payments to extend the lease, and SBBT does not force us to buy it and we choose, for whatever reason, not to buy it, then the lease will expire.
>
> Q. Okay. And under the lease, where does the property—where would the leased property go?
>
> **A. Back to SBBT.**

Hr'g Tr. 29:8-18 (emphasis added).

15. Mr. Nystrom's testimony on this point was corroborated by the testimony of Arish Gupta, President of SBBT:

> Q. If we were at the end of the lease today and all payments had been made, we were at the end of the seven years, and economic conditions were the same as they are today, what would SBBT do with the heat treatment equipment at the end of that seven-year period?
>
> A. Under current conditions, we would take back the equipment.

Hr'g Tr. 33:14-19 (emphasis added).

16. Mr. Gupta's testimony is supported by the fact that, well before Boomerang filed for bankruptcy, SBBT sought a quote from the manufacturer of the Equipment, which is now known as Primetals, for the potential purchase of a heat treat line similar to the Equipment at issue here:

> Q. Now isn't—in fact, isn't SBBT currently planning to upgrade one of its facilities with a heat treatment [line]. Is that correct?
>
> A. Yes.
>
> Q. When did those discussions begin? When did you start thinking about that?
>
> A. Those discussions started about a year and a half ago.

Hr'g Tr. 33:23-34:-6.

17. Mr. Gupta further testified that Primetals provided a bid on Equipment "almost identical to what we had set up at Boomerang." Hr'g Tr. 36:11-12. In response to SBBT's request, Primetals provided a quote for the installation of a heat treat line nearly identical to the Boomerang Equipment—at a price of $15 million. *See* Primetals Proposal (Ex. 174), at 3.

18. Mr. Gupta's testimony that SBBT would take back the Equipment at the end of the Lease term if Boomerang should choose not to exercise its option is both sincere and reasonable, as the undisputed evidentiary record shows that SBBT is in the market for a heat

treat line, and the cost to obtain a new one would be far greater than the cost of merely allowing the Lease to expire. Accordingly, this element of the second part of the bright-line test is not satisfied and cannot serve as a basis for recharacterization of the Lease.

(iii) Boomerang Does Not Have the Option to Renew the Lease of the Equipment for No or Nominal Consideration.

19. The Lease provides certain options to the parties during and at the end of the Lease, but does not provide Boomerang with the option to renew the Lease for no or nominal consideration. Rather, paragraph 7(d) of the Lease provides that at the end of the Lease, the parties may renew the Lease under its current terms (which are more than nominal consideration) or enter into a new lease. Lease (Ex. 139), ¶ 7(d). The evidentiary record shows that Boomerang has no option to renew the Lease at no or nominal consideration. Accordingly, this element of the second part of the bright-line test is not satisfied and cannot serve as a basis for recharacterization of the Lease.

(iv) Boomerang Does Not Have the Option to Purchase the Equipment for No or Nominal Consideration.

20. Under the Lease, if Boomerang does not choose to renew the Lease on its current terms, and if the parties do not agree to a new lease, Boomerang has the option to purchase the Equipment at the end of the Lease's term. Lease (Ex. 139), ¶ 7(d)[3] for 50% of the Total Cost of the Equipment. The express terms of the Lease are thus clear: Boomerang enjoys a purchase option, but not for anything close to no or nominal consideration.

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[3] Paragraph 7(d) provides that provides that "(a) Lessor may require Lessee to purchase the Equipment for a purchase price equal to 50% of Total Cost (the "Sale Option") or (b) Lessee may require the Lessor to sell the Equipment for a purchase price equal to 50% of Total Cost (the "Final Purchase Option" and, together with the First Purchase Option, the Second Purchase Option and the Third Purchase Option, the "Purchase Options")."

21. The uncontroverted facts show that to exercise its purchase option, Boomerang would be required to pay SBBT over $7 million (based on a Total Cost of $14,217,486, as reflected in the Lease Payment Schedule attached to the Lease (Ex. 139). As Mr. Gupta testified regarding the total cost under the Lease:

> A. So we assumed that if we were to go through the full lease term that at the end of the lease, if Boomerang—if we were to force Boomerang to buy the equipment, that the value would be 50 percent of the initial—initial value, which came out to be 7.1. That's about 50 percent of $14.2 million.

Hr'g Tr. 39:11-16.

22. Because Boomerang enjoys no option to purchase the Equipment for zero or nominal consideration, this element of the second part of the bright-line test is not satisfied and cannot serve as a basis for recharacterization of the Lease. Accordingly, none of the four elements under the second part of the bright-line test are satisfied, so there is no basis under the UCC's bright-line test to recharacterize the Lease as a financing.

B. The Economic Realities Do Not Support Recharacterization.

23. Nor do the "economic realities" support recharacterization. In their Response and in cross-examining Mr. Gupta, the Debtors spent an inordinate amount of time on what the parties may have called the Lease on their accounting books and an affiliate's website.[4] But what the parties may have called the Lease is not outcome determinative of the economic realities of the transaction. Indeed, if the wording used by the parties in referring to the transaction were controlling, no lease would or could ever be recharacterized—the fact that the parties deemed it a "lease" would be the beginning and end of the inquiry.

[4] The Debtors observe that an affiliate of SBBT on its website referred to the Lease transaction as a "financing." But in that same statement said SBBT had "***purchased*** a new, state-of-the-art heat treatment line from F&D Furnaces and ***leased the equipment*** to Boomerang Tube." Webpage Printout (Ex. 182). So even Boomerang's own evidence shows that the parties treated the transaction as a lease of the Equipment.

24. Here, the Lease itself has language—negotiated by both parties at arm's length—clearly indicating that both parties considered the transaction a true lease and not a financing. For example, the Lease states unequivocally that "[t]he Equipment is and at all times during the term of this Lease will remain Lessor's sole and exclusive personal property. Lessee will have no right, title or interest in the Equipment, other than the right to maintain, possess and use the Equipment during the Lease Term … ." Lease (Ex. 139), ¶ 10. The Lease also states that "[t]he parties intend to create a lease on the Equipment, and not a conditional sale." *Id.* ¶ 11(a). And, of course, paragraph 7 of the Lease provides several purchase options, none of which would make any sense if Boomerang were already the owner and not merely the lessee of the Equipment.

25. If how the parties themselves characterized the transaction is relevant to the inquiry, then the Court also should consider the October 12, 2012 correspondence between Michael Fielding, General Counsel for SBBT, and Bob Horsfield, then-CFO of Boomerang, in which Mr. Fielding stated that "SBI owns the 'Equipment' leased to Boomerang under and as defined in the Lease (the 'SBI Equipment') and, accordingly, SBI shall retain all right, title and interest in and to the SBI Equipment." Stipulation (Ex. 189), ¶ 30.

26. The Debtors assert that in its Objection SBBT "attempts to downplay" the "indicia of ownership on the part of Boomerang" that the Debtors allege are "not normally found in a lease agreement." Response 72, ¶ 142. But SBBT is not alone—this Court in past cases has downplayed indicia of ownership as meaningful. In the *Edison* case, cited in SBBT's Objection and ignored by the Debtors, the Court stated that it "place[s] little weight on the fact that debtor assumed many of the obligations associated with outright ownership of the equipment, namely, obligations to pay taxes, to pay insurances, to pay maintenance

expense, to indemnify the lessor, and to assume all risks. These factors are necessarily borne by one party or the other and therefore they reflect less the true character of the transaction than the strength of the parties' respective bargaining positions." *In re Edison Brothers Stores, Inc.,* 207 B.R. 801, 818 (Bankr. D. Del. 1997) (finding the agreement at issue to be a true lease) (internal quotations omitted).

27. Additionally, the Debtors argue without any supporting authority that SBBT's purchase of the Equipment from a third party for Boomerang's use "strongly weighs in favor of finding a disguised financing." Response 73, ¶ 143. But this Court held the exact opposite in *Edison Brothers*, 207 B.R. at 821-22, and the Debtors cite no countervailing authority in support of their sweeping assertion that a lessor cannot purchase equipment from one party and then lease it to another under a true lease.

28. The Debtors argue that the total payments due from Boomerang exceed the original cost of the Equipment. Response 71-72, ¶ 140. As the party seeking to recharacterize the Lease, the Debtors bear the burden on this issue. *Edison Brothers,* 207 B.R. at 812 n.14 (collecting cases). In their Response, the Debtors argue that the potential purchase price of the Equipment at the end of the Lease term should be added on to the lease payments to determine if they exceed the Total Cost. Response 72, ¶ 140. The Debtors cite no support for this novel theory because it has no support in the law. In fact, in *Edison Brothers*, the court found that the present value of the aggregate lease payments was substantially less than the purchase price of the equipment at issue, and at no point included in its calculation or even discussed the "fair market value purchase option" the debtor had at the end of the lease. *Edison Brothers*, 207 B.R. at 814. Likewise, the purchase price at the end of the Lease term is irrelevant to whether the total Lease payments exceed the Total Cost of the Equipment.

29. Even if this Court were to determine that the aggregate Lease payments exceed the Total Cost of the Equipment, this one factor would not establish that the Lease is a disguised secured financing. Texas UCC § 1-203(c)(1) ("A transaction in the form of a lease does not create a security interest merely because: (1) the present value of the consideration the lessee is obligated to pay the lessor for the right to possession and use of the goods is substantially equal to or is greater than the fair market value of the goods at the time the lease is entered into … ."); *In re HP Distribution, LLP,* 436 B.R. 679, 689 (Bankr. D. Kan. 2010) (applying the Texas UCC in finding the agreements at issue to be true leases even though the present value of the lease payments was substantially equal to or greater than the fair market value of the goods because the lessor retained a meaningful reversionary interest in the goods); *In re Gateway Ethanol, L.L.C.,* 415 B.R. 486, 505-06 (Bankr. D. Kan. 2009) (finding that even if the agreement at issue provided for the full price of the equipment to be paid by the lease payments, this would not conclusively establish a sale under former section 1-201(37), and noting the official comment's interpretation that under this provision "a full payout lease does not *per se* create a security agreement").

30. Rather, this Court still must look to the various factors articulated in *Edison Brothers* and *Integrated Health* to evaluate the economic realities of the Lease transaction. Among the "economic realities" supporting the conclusion that this is a true lease is the undisputed fact that if the parties do not renew the Lease, and neither party elects to consummate a sale of the Equipment, the Equipment will be returned to SBBT. Hr'g Tr. 29:1-29:18. It is also undisputed that the Equipment is very large, Hr'g Tr. 96:14-97:3, and as Mr. Ray testified, if it is returned to SBBT it would require a complicated removal and transport process. Hr'g Tr. 161:4-161:12. If the Equipment reverts to SBBT, SBBT will bear

the substantial costs associated with that removal. In analyzing the economic realities that support a finding that the Lease is a true lease, this Court should consider SBBT's responsibility for the great expense that would be incurred in repossessing the Equipment at the end of the lease term and SBBT's need to account for those potential expenses through the Lease payments.

31. For the many reasons articulated in the Objection—and unrefuted by the Debtors in their Response, by the documents in evidence, or by the testimony at the hearing—the economic realities of the transaction demonstrate that it was a true lease and not a disguised financing.

II. The Debtors Undervalue the Equipment.

A. Valuation is Determined in Light of the Proposed Use of the Property.

32. Even if the Court were to find that the Lease was not a true lease but, rather, a disguised financing arrangement (which it was not), SBBT would have a perfected security interest in the Equipment. The Debtors' proposed Plan is unjustifiably designed to pare down SBBT's secured claim by, among other things, assigning an unreasonably low value to the Equipment in which SBBT has a security interest and improperly impairing SBBT's rights as a secured creditor that has exercised its § 1111(b) election rights.

33. Section 506(a) of the Bankruptcy Code provides that:

> An allowed claim of a creditor secured by a lien on property in which the estate has an interest … is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property … and is an unsecured claim to the extent that the value of such creditor's interest … is less than the amount of such claim. **Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property.**

11 U.S.C. § 506(a) (emphasis added).

34. Courts have acknowledged that "Congress envisioned a flexible approach to valuation whereby bankruptcy courts would choose the standard that best fits the circumstances of a particular case." *In re Heritage Highgate, Inc.*, 679 F.3d 132, 141 (3d Cir. 2012). Although bankruptcy courts have some latitude in applying valuation standards, the Supreme Court of the United States has made it clear that "the 'proposed distribution or use' of the collateral is of paramount importance to the valuation question." *Assocs. Commercial Corp. v. Rash*, 520 U.S. 953, 962 (1997). In other words, "the appropriate standard for valuing collateral must depend upon what is to be done with the property—whether it is to be liquidated, surrendered, or retained by the debtor." *Heritage Highgate*, 679 F.3d at 141.

35. The parties agree that the Supreme Court's decision in *Rash* and the Third Circuit's opinion in *Heritage Highgate* are instructive. But the Debtors misapply these precedents to the facts of this case. Unlike what the subordinated secured creditors in *Heritage Highgate* argued, SBBT does not seek to value the Equipment based on improvements the Debtors may make to it in the future that will enhance its value. Instead, SBBT urges the Court to look at how the Debtors are using the Equipment now, and how they will continue to use it going forward, to arrive at a reasonable value for the Equipment ***at the present time***, which is exactly what the court in *Heritage Highgate* did. Because the Debtors intend to continue to use the Equipment for the manufacture of goods in the course of operating their business, the Equipment's value must be considered in light of that intended use.

36. In *Heritage Highgate*, the complaining creditors had stipulated to the value under an appraisal that was accepted by the bankruptcy court in connection with a cash collateral motion—an appraisal that took into account the intended use of the property as a real-estate

development but had valued it as of the petition date. *Heritage Highgate*, 679 F.3d at 137-38. At confirmation, the complaining creditors again did not contend that the appraisal's valuation was wrong per se. Indeed, they "agreed that the appraisal depicted the Project's fair market value" and "did not dispute the accuracy of the fair market value set forth in the appraisal." *Id.* at 138. Instead, the creditors argued that the value at the time of confirmation should not be used to determine whether their claims were secured. They asked the court to ignore the appraisal of the property's fair market value at the time of confirmation (which value they did not dispute), and use the debtor's forecasted budgets from its proposed plan as the basis for finding that they enjoyed secured status. *Id.*

37. It was this "wait and see" approach advocated by the subordinated secured creditors in *Heritage Highgate* that the Third Circuit in that case rejected. Here, SBBT is not asking the Court to ignore an appraisal's fair-market valuation at the time of confirmation and rely instead on projections from the Debtors' Plan, as the complaining creditors in *Heritage Highgate* did. SBBT simply wants any appraisal relied upon by the Court to recognize the fact that the Equipment is being used and will continue to be used to generate revenues for the Debtors, and to take that use into account in accordance with § 506(a), as SBBT's expert appraisal does.

38. Other differences between this case and *Heritage Highgate* are apparent. For example, in this case there has been no appraisal accepted by the bankruptcy court and agreed to by the parties. There are competing valuation appraisals using different methodologies. The parties in this case do not dispute that the Equipment has a useful life of 15 years. Stipulation (Ex. 189), ¶ 37. Boomerang acknowledges that it intends to keep the Equipment and use it in manufacturing, as it has done in the past. *Id.* ¶ 38. It is undisputed

that Boomerang does not intend to sell the Equipment. *Id.* ¶ 39. SBBT's expert appraisal appropriately takes these facts into account in determining the Equipment's current value. Boomerang's does not. The Court should adopt SBBT's valuation and reject Boomerang's.

B. SBBT's "Continued Use" Valuation of the Equipment is the Appropriate Standard Because it Accounts for the Debtors' Proposed Use of the Equipment.

39. Boomerang indisputably will retain and continue to use the Equipment post-confirmation. If the Plan is confirmed, Boomerang will not sell the Equipment but will retain and use it in its manufacturing operations. *See* Stipulation, ¶¶38-39. The Debtors' financial projections attached to the Disclosure Statement show that Boomerang will retain the Equipment to support its future sales. *See* Disclosure Statement (Ex. 28), 352. Consistent with § 506's mandate, this Court should apply a valuation standard based on and accounting for the ***actual proposed use*** of the Equipment, *i.e.*, its continued use at Boomerang's facility.

40. Duff & Phelps, SBBT's valuation expert, employed a valuation standard that reflects the Debtors' actual proposed use of the Equipment. Duff & Phelps utilized a "fair market value – continued use" valuation, which values the Equipment based on Boomerang's continued use of the Equipment at its facility as the Plan contemplates. Hr'g Tr. 160:25-161:8. This standard upholds § 506's directive that the value of a secured creditor's claim be determined in light of the proposed use of the property.

41. By contrast, despite acknowledging that Boomerang will retain and continue to use the Equipment, the Debtors' valuation expert, Mr. Cook, used a "fair market value – removed" standard to value the Equipment. Hr'g Tr. 76:2-76:4. Counterfactually, this standard reflects an opinion of the amount at which the Equipment would change hands between a willing buyer and seller, neither being under any compulsion to buy or sell, and both having reasonable knowledge of the relevant facts, ***considering removal of the property***

to another location, as of a specific date. Hr'g Tr. 76:17-76:24 (emphasis added). Critically, the "fair market value – removed" standard is premised on the assumption that the Equipment would be removed to another location. Hr'g Tr. 96:10-96:13.

42. Of the many flaws to the valuation methodology and calculations Mr. Cook used, the most fatal flaw is that he used a valuation standard that assumes the sale and removal of the Equipment despite the Debtors' admission that they do not intend to sell or remove the Equipment. Mr. Cook never even considered a "fair market value – continued use" valuation approach—reflecting the Debtors' actual proposed use—because his mandate from the start was to use a "fair market value – removed" standard. Hr'g Tr. 97:16-97:24. This may explain why, in speaking with Boomerang personnel to perform his valuation, Mr. Cook never asked what the Debtors intended to do with the Equipment. Hr'g Tr. 98:25-99:10. Curiously, given that § 506 demands a valuation that accounts for the proposed use of the Equipment, Mr. Cook testified that it was of no concern to him in reaching his valuation whether the Debtors intended to sell or continue using the Equipment. Hr'g Tr. 99:11-99:14. When Mr. Cook issued his valuation report, he was not even aware of whether the Debtors planned to sell the Equipment or continue using it. Hr'g Tr. 98:6-98:14.

43. This Court should adopt the "fair market value – continued use" standard used by Duff & Phelps. Only Duff & Phelps' methodology, which properly reflects an Equipment value of approximately $12.6 million, accounts for the Debtors' proposed use of the Equipment as required by § 506. The Debtors' "fair market value – removed" standard, on the other hand, rests on an assumption that is directly at odds with the facts, ignoring the proposed use of the Equipment, in order to generate an artificially low valuation.

C. The Value of the Equipment under the Continued Use Methodology is $12,638,414.

44. To determine the value of the Equipment under the "fair market value – continued use" standard, Duff & Phelps used the cost approach to valuation, which both valuation experts agree is the most appropriate valuation approach for the Equipment under the circumstances. Hr'g Tr. 78:6-78:16; 163:9-163:10. Applying the cost approach model, Duff & Phelps concluded that the value of the Equipment is $12,638,414.

45. Duff & Phelps started with the "replacement cost new" of the Equipment, which reflects the estimated amount, at current market prices, required to replace the Equipment with a modern unit using modern technology and construction materials that will provide the production capacity and utility of the furnace at current market prices. To obtain the replacement cost new, Duff & Phelps relied upon a quote that SBBT received from Primetals, the successor to the Equipment's manufacturer.[5] Primetals provided a quote of $15,000,000 for a functionally identical replacement furnace. *See* Primetals Proposal (Ex. 174); Hr'g Tr. 164:6-165:23. This price represents the best starting point to determine the replacement cost new under the cost approach, and even Mr. Cook agrees that the best starting point is the actual price of equipment having the nearest utility to the equipment being appraised. Hr'g Tr. 123:9-123:14.[6] The experts did not differ significantly on their assessment of the cost to purchase a replacement heat-treat furnace, with the Debtors' own expert putting the replacement cost at $14.73 million. Hr'g Tr. 120:22-120:24.

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[5] SBBT requested this quote because they are planning to install heat treatment equipment at one of their Houston facilities. The request was not made in anticipation of the present litigation, and SBBT's desire to install heat treatment equipment at their Houston facility developed in 2014, well before the Debtors' bankruptcy proceeding. Hr'g Tr. 33:23-34:6.

[6] The quote from Primetals included certain "soft costs" such as project management, engineering and site advisory services, *see* Ex. 174, the value of which Duff & Phelps determined to be approximately $100,000, which would reduce the replacement cost new by a corresponding $100,000. Hr'g Tr. 224:2 to 224:17.

46. Duff & Phelps then added the expected installation costs of a new replacement heat-treat furnace. Hr'g Tr. 166:10-166:20. The addition of the installation costs is necessary to reflect the facts and circumstances as they exist, because the Equipment is currently installed at Boomerang's facility and will remain so, such that the valuation must include the costs of that installation. Hr'g Tr. 166:10-166:20. Importantly, Mr. Cook himself acknowledged that a fair market value – continued use valuation must include the installation cost. Hr'g Tr. 100:11-100:14. Moreover, the law supports inclusion of installation costs under a cost approach when deriving the "fair market value – continued use" value of an asset. *See Northern Natural Gas Co. v. United States*, 1972 U.S. Dist. LEXIS 15417 at *10-*13 (D. Neb. Jan. 25, 1972), aff'd, 470 F.2d 1107 (8th Cir. 1973) (finding that installation costs should be included in calculating replacement cost because they "add to the value and utility of the [asset] and … will necessarily be incurred anew in the replacement of the [asset] after the expiration of its useful life").

47. The Debtors' books and records reflect that Boomerang paid $4,820,063 to install the furnace in 2012. Hr'g Tr.167:2-167:7.[7] Duff & Phelps applied an inflation rate to that installation cost, using the multiplier of 1.09 called for under the Marshall & Swift/Boeckh index for the metal and mining industry, which index includes furnace manufacturers such as F&D Furnace. Hr'g Tr.167:13-168:11. The use of the 1.09 multiplier is also supported by the Bureau of Labor Statistics Producer Price Indices. Hr'g Tr. 167:13-168:11. Application of the 1.09 multiplier yields a total installation cost of $5,253,869. Hr'g Tr. 167:13-168:18.

[7] Mr. Nystrom, who was not employed by Boomerang when the Equipment was installed, testified that the installation costs were approximately $3.8 million (Hr'g Tr. 13:22-13:25), which is contrary to Boomerang's books and records (Hr'g Tr.167:2-167:7). Even if that were correct, however, and the installation costs in Duff & Phelps' calculations were correspondingly reduced, the "replacement cost new" would still equal over $19 million. Hr'g Tr. 197:23 to 198:3.

Adding the inflation-adjusted installation cost of $5,253,869 to the $15,000,000 Primetals quote for a new replacement furnace yields a "replacement cost new" total of $20,253,869. Hr'g Tr. 167:13-168:18.

48. Having calculated the total replacement cost new of the Equipment, Duff & Phelps then accounted for certain deductions to that cost—specifically: (i) physical deterioration; (ii) functional obsolescence; and (iii) economic obsolescence. Hr'g Tr. 168:19-169:1. To account for physical deterioration of the Equipment, Duff & Phelps deducted $2,700,516 from the replacement cost new of the Equipment. Hr'g Tr.168:24-169:5. The physical-deterioration deduction reflects the effective age of the Equipment divided by its average service life of 15 years. Hr'g Tr. 169:6-169:18. Duff & Phelps calculated the effective age of the Equipment to be two years after speaking with Boomerang personnel, who advised that the Equipment was placed into full production in the first quarter of 2013. Hr'g Tr. 169:6-169:18. At the hearing, the Debtors sought to discredit Duff & Phelps' physical-deterioration deduction as too low by asserting that the Equipment was actually placed in production in August 2012. Even if production began in August 2012, however, adding several months to the effective age would add only approximately $400,000 in physical depreciation to the Equipment. Hr'g Tr. 169:21-170:11. Moreover, Mr. Ray testified that because the manufacturer's calculation of average service life assumes that the Equipment will be run 24 hours a day, 7 days a week (though Boomerang is not actually running the Equipment around the clock), Duff & Phelps' overall calculation of physical deterioration would remain unchanged. Hr'g Tr. 171:15-172:3.

49. After deducting for physical deterioration, Duff & Phelps analyzed whether it was appropriate to deduct for any functional obsolescence of the Equipment, which is the

reduction in value attributable to something that is inherently wrong or impaired with the Equipment. Hr'g Tr. 172:11-172:13. Duff & Phelps concluded that a functional obsolescence deduction was inappropriate. Such a calculation would be impossible to perform with precision because Boomerang did not keep financial data for the Equipment on a stand-alone basis.[8] Hr'g Tr. 172:17-173:3.

50. Finally, Duff & Phelps analyzed the deduction for the Equipment's economic obsolescence, which accounts for external forces that shape value. Hr'g Tr. 173:21-174:1. Recognizing that it impossible to account for economic forces that would contribute to the Equipment's obsolescence without examining the overall economic circumstances in which the Equipment is to be operated, Duff & Phelps sought to capture a full picture of Boomerang's business and the oil and gas industry. To do so, Duff & Phelps first determined the overall business enterprise value of Boomerang, using a discounted-cash-flow analysis for the entire business. Hr'g Tr. 174:21-174:25. That business-enterprise valuation resulted in a valuation of $200 million. Hr'g Tr. 175:17-175:18. Tellingly, Duff & Phelps' business-enterprise calculation of $200 million is consistent with the total-enterprise valuation of $200 to $220 million reached by the Debtors' own enterprise valuation expert. *See* Boomerang Valuation Report (Ex. 31), at 5. In fact, the Debtors tried to use the Duff & Phelps' business enterprise valuation against the Creditors' Committee in this case, thereby demonstrating their view that Duff & Phelps' conclusion as to the enterprise value of the Debtors is correct. *See* Response 34, ¶66 & 44, ¶ 85.

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[8] Boomerang's failure to maintain financial data on a stand-alone basis for the Equipment also prevented Duff & Phelps from analyzing the earnings attributable to the Equipment in connection with its economic-obsolescence analysis. Duff & Phelps therefore extrapolated the Equipment's earnings based on its detailed analysis of Boomerang's overall earnings. Hr'g Tr. 195:7-195:15.

51. Because the aggregate "continued use" values of a company's individual assets cannot exceed the total business-enterprise value of that company, Duff & Phelps engaged in a comprehensive and detailed analysis through which it valued all of Boomerang's underlying tangible and intangible assets, and compared the sum of those values to Boomerang's total business-enterprise value. Hr'g Tr. 175:24-177:2. The result of that asset-by-asset valuation resulted in the sum of the value of individual assets exceeding the $200 million business-enterprise value. As a result, Duff & Phelps discounted by 28% all personal-property asset classes that were valued on a cost approach to ensure that the sum of these parts did not exceed the whole. Hr'g Tr. 177:13-178:23. The reduction in the valuation of these personal-property assets to "fit" within the total enterprise value is necessary to avoid over-valuing any individual item of personal property. Application of the 28% discount to the $20,253,869 "replacement cost new" of the Equipment results in an economic obsolescence deduction of $4,914,939.

52. Not only was Duff & Phelps' valuation approach rigorous and detailed, it was also conservative. Had Duff & Phelps used a higher and less conservative business-enterprise valuation (such as that suggested by the Creditors' Committee or even the midpoint of the valuation range proposed by the Debtors), the economic obsolescence percentage would have been lower[9] and, hence, the valuation of the Equipment would have been higher.

53. After accounting for the Equipment's physical deterioration, functional obsolescence, and economic obsolescence, the "fair market value – continued use" of the Equipment is $12,638,414. Hr'g Tr. 180:5-180:11. Furthermore, even if one were to allow

[9] If, however, the total-enterprise value of Boomerang is greater than $200 million, as the Committee asserts in its $330 million valuation opinion, there would be a correspondingly lower economic obsolescence because there would be greater total-business-enterprise value to support the underlying tangible and intangible assets. Hr'g Tr. 178:14-178:23.

for slightly greater physical deterioration based on the Debtors' position that the Equipment was put into production several months earlier than their personnel advised Duff & Phelps, the value of the Equipment is only reduced to $12,238,414. Hr'g Tr. 180:12-180:15. This valuation reflects the facts and circumstances of the Equipment and its proposed use under the Debtors' plan, and is the appropriate value for the Court to adopt. Hr'g Tr. 221:19-222:9.

D. The Debtors' Valuation of $4,500,000 Under the Removal Methodology Is Invalid Both Because It Ignores the Proposed Use of the Equipment and Because It Is the Product of Incorrect Application of Valuation Principles.

54. The Debtors rely on an inappropriate valuation of the Equipment by Mr. Cook that wholly ignores its proposed use under the Debtors' plan. Mr. Cook's valuation of $4,500,000 is based on a false assumption that the Equipment is to be removed from Boomerang's facility and sold, despite it being undisputed that Boomerang will retain and continue to use the Equipment at its facility. As troubling as it is that Mr. Cook would ignore the economic realities relevant to the Equipment when determining its value, at the very least his opinion should have disclosed that his valuation assumes these facts so that this Court can view this opinion for what it is—a hypothetical valuation of property that runs directly contrary to the Debtors' proposed use.

55. Mr. Cook has taken coursework on the Uniform Standards of Professional Appraisal Practice ("**USPAP**"), and purports to have issued his valuation opinion in compliance with those standards. Hr'g Tr. 95:7-95:24. Mr. Cook acknowledged during his testimony that USPAP requires an appraisal to identify "extraordinary assumptions" and "hypothetical conditions" necessary to the assignment. Hr'g Tr. 112:7-112:12. An extraordinary assumption is defined under USPAP to be "an assumption, directly related to a specific assignment, as of the effective date of the assignment results, which, if found to be

false, could alter the appraiser's opinions or conclusions."[10] *See* Uniform Standards of Professional Appraisal (Ex. 175), at U-3. A hypothetical condition is defined under USPAP to be "a condition, directly related to a specific assignment, which is contrary to what is known by the appraiser to exist on the effective date of the assignment results, but is used for the purpose of the analysis." *See* Uniform Standards (Ex. 175), at U-3.[11] In employing a valuation standard that assumes the sale and removal of the Equipment, without any facts to support that assumption (rather, the facts directly contradict that assumption), Mr. Cook apparently determined that he was not required to disclose that the sale and removal of the Equipment on which his valuation was based reflected a hypothetical condition or extraordinary assumption. Hr'g Tr. 114:1-114:9. And notwithstanding Mr. Cook's conclusory testimony that he did not use any hypothetical conditions or extraordinary assumptions in his valuation, *see* Hr'g Tr. 153:8-153:14, he admitted that he did not bother to concern himself with whether the Debtors actually intended to sell the Equipment and have it removed from their facility. Hr'g Tr. 98:6-99:14. This approach by an appraiser is improper.

56. Mr. Cook also used a highly questionable sales-comparison approach, in addition to the cost approach, to support his $4.5 million valuation. Hr'g Tr. 115:7-115:9. This consisted of obtaining a single heat-treat-furnace broker's view of the market value of the Equipment, which was purportedly between $4,000,000 and $5,000,000. Hr'g Tr. 92:14-92:19; 116:7-117:7. The broker, however, never inspected the Equipment, Hr'g Tr. 116:10-

[10] The comment to the definition of extraordinary assumptions states that "Extraordinary assumptions presume as fact otherwise uncertain information about physical, legal or economic characteristics of the subject property; or about conditions external to the property, such as market conditions or trends; or about the integrity of data used in an analysis." Uniform Standards (Ex. 175), at U-3.

[11] The comment to the definition of hypothetical condition states that "Hypothetical conditions are contrary to known facts about physical, legal, or economic characteristics of the subject property; or about conditions external to the property, such as market conditions or trends; or about the integrity of data used in the analysis." *See* Uniform Standards (Ex. 175), at U-3.

116:11, and had no information about recent sales of similar heat-treat furnaces. Hr'g Tr. 116:12-116:18. Mr. Cook even acknowledged that under the sales-comparison approach it is not customary to rely on someone else's opinion about the price at which something might sell. Hr'g Tr. 117:8-117:18. Given the scarcity of the information the broker had about the Equipment, the absence of comparable sales of similar furnaces, and the lack of any information about how the broker arrived at his range, this Court should give short shrift to Mr. Cook's alleged "sales-comparison approach."

57. Even if Mr. Cook's "fair market value – removed" approach to valuation of the Equipment were not wholly inappropriate, which it is, his analysis also suffers from several critical mistakes. First, with respect to his determination of the replacement cost new of the Equipment, Mr. Cook's cost approach started with a replacement cost new of $14.73 million, which he calculated by multiplying Boomerang's original cost for the furnace, $14,300,000, by an inflationary multiplier of 1.03. Hr'g Tr. 120:5-121:5. Mr. Cook did so despite admitting during his testimony that the best way to determine replacement cost new is the actual cost of a new piece of replacement equipment. Hr'g Tr. 123:9-123:14.[12] Furthermore, Mr. Cook's 1.03 multiplier is the Marshall & Swift inflationary index for the petroleum industry. Hr'g Tr. 121:6-121:11. Despite using that index, however, Mr. Cook had no idea whether furnace manufacturers were included in that market segment, and made no attempt to investigate it. Hr'g Tr. 121:12-121:23. Rather, consistent with other unfounded assumptions he made in opining on the value of the Equipment, Mr. Cook simply assumed it was the correct multiplier. Hr'g Tr. 121:24-122:10. Recognizing the problem with this approach, Mr. Cook conceded at the hearing that if the 1.03 multiplier for the petroleum

[12] Mr. Cook admitted that if he had the Primetals quote at the time he arrived at his valuation, he would have considered it in his analysis. Hr'g Tr. 125:2-125:10.

industry is the wrong multiplier, the correct multiplier could be higher. Hr'g Tr. 122:11-123:4. As noted above, the 1.09 multiplier for the metal and mining industry that Duff & Phelps used in its analysis includes furnace manufacturers. Hr'g Tr. 167:16-168:8.

58. With respect to his physical-depreciation determination, Mr. Cook assumed physical deterioration of the Equipment to be 20%, for a deduction of $2,946,000, based on an effective age of three years divided by a useful life of 15 years. Mr. Cook's effective age of three years was based on information he received from a Boomerang employee that the Equipment went operational in July 2012 and that the average production was 25,000 tons a month. Hr'g Tr. 127:21-127:24. Even assuming, however, that the Equipment went online in July 2012, rather than in the first quarter of 2013 as Duff & Phelps was advised by the Debtors' personnel, Mr. Cook's effective age calculation is problematic because it evidently assumes that Boomerang has been producing 25,000 tons a month for the entire three years. Hr'g Tr. 128:13-128:21. Boomerang has not been running the Equipment full time, Hr'g Tr. 171:8-171:13, and in July 2015, the month on which Mr. Cook centered his valuation, the Equipment produced just 396 tons for the month. Hr'g Tr. 133:13-133:17; Production Report July 2015 (Ex. 171). Mr. Cook admitted during his testimony that the effective age of the Equipment is impacted by how heavily or lightly it has been used, whether it was shut down, and to what extent it has been maintained, Hr'g Tr. 126:21-127:13, yet he simply ignored the fact that Boomerang's production was far less than 25,000 tons in the month that he was taking his "snapshot" for valuation. This is another example of Mr. Cook selectively using data and information when it suited his valuation regardless of what reality reflected.

59. Mr. Cook's calculation of the functional obsolescence of the Equipment is also problematic. Mr. Cook used a functional obsolescence percentage of 3%, but admits he

performed no underlying calculations to support it. Hr'g Tr. 129:18-131:15. This is unsurprising, as Mr. Cook admitted he is not knowledgeable of the rules used in the appraisal profession for calculating functional obsolescence. Hr'g Tr. 131:16-132:5. The only basis Mr. Cook articulated for having chosen 3% functional obsolescence is a conversation he purportedly had with an employee of the Equipment's manufacturer, who advised that the current model of heat-treat furnace included software upgrades. Hr'g Tr. 129:18-129:24. The Equipment's manufacturer did not, however, tell Mr. Cook that the functional obsolescence was 3% as a result of those software upgrades. Hr'g Tr. 130:5-130:8. Mr. Cook's "analysis" of functional obsolescence constitutes nothing more than guesswork, and stands in stark contrast to Duff & Phelps' complete and thorough analysis, which looked at all of the relevant economic indicators to determine the appropriate deductions to be made.

60. But perhaps Mr. Cook's most glaring and problematic error is his economic-obsolescence determination. Mr. Cook calculated the economic obsolescence of the Equipment to be a whopping 60% based on a myopic inutility penalty that fails to account for projections of Boomerang's future sales and growth. Hr'g Tr. 138:12-138:19. Mr. Cook's stated basis for his inutility calculation is that Boomerang's drop in productivity is in direct correlation to the price of oil. Hr'g Tr. 133:22-134:7. Fully ignoring the Debtors' and industry projections that both the oil industry and OCTG production and sales are expected to rebound as soon as 2016, Mr. Cook simply divided Boomerang's production of 10,000 tons ***solely for the month of July 2015*** by Boomerang's historical average monthly production output of 25,000 tons, and concluded that the Equipment's inutility penalty should be 60%. Hr'g Tr. 133:13-133:21. Mr. Cook did not consider Boomerang's projections of its future production rates, nor did he consider the Debtors' future sale projections. Hr'g Tr. 134:23-

135:5; 136:9-137:13. Mr. Cook did not consider industry-wide OCTG growth rates, Hr’g Tr. 137:14-137:16, and could not even answer whether or not he agreed with Lazard’s assessment that the United States OCTG market troughed in July 2015. Hr’g Tr, 138:20 to 139:5. Rather, to calculate the inutility of the Equipment, he looked only at Boomerang’s production rate in a single month, July 2015, which represented a trough in the OCTG market. Hr’g Tr. 137:17-138:1. In other words, Mr. Cook carefully (and narrowly) cherry-picked the input data that he used to come up with his so-called inutility calculation.

61. As an initial matter, Mr. Cook’s application of an inutility penalty runs counter to accepted appraisal principles, which hold that an inutility calculation should only be employed when the impairment is going to last for some time. Hr’g Tr. 180:21-181:3. Debtors’ own enterprise valuation expert, Lazard, acknowledges that oil prices are expected to rebound through at least August 2019 from a near-low in July 2015. *See* Boomerang Valuation Report (Ex. 31), at 7. Mr. Cook’s use of a single month of production data, during the lowest point in production in years, to calculate the inutility of the Equipment also runs counter to the need for an inutility calculation to account for past performance, current performance and future performance. Hr’g Tr. 181:4-181:17. Simply put, Mr. Cook’s calculation of a 60% inutility penalty, and thus an alleged 60% economic obsolescence deduction, based on one month of data that reflects a trough in Boomerang’s industry (an industry that the Debtors’ own experts predict will substantially rebound), “puts the rabbit in the hat” to manufacture a low-ball valuation for the Equipment. In doing so, Mr. Cook ignored accepted principles of appraisal, not to mention the Debtors’ own financial projections showing an increase in production and sales. Having put these blinders on, Mr.

Cook's economic-obsolescence calculation is nothing more than a result-driven fiction based on grossly insufficient data, and should be wholly disregarded.

62. Moreover, even if one were to accept Mr. Cook's erroneous premise that an inutility calculation should be applied at all (and it should not), and that it should be determined by looking at a single month's production, Mr. Cook still used the wrong inutility calculation formula. He incorrectly calculated the inutility by performing his simple math equation on a linear basis rather than a logarithmic basis that applies a proper scaling factor to account for the cost of capacity. Hr'g Tr. 183:3-184:24. Where one is performing an inutility calculation to determine economic obsolescence, a formula that accounts for the cost of capacity must be used. Instead, Mr. Cook simply divided 10,000 by 25,000, and projected a linear inutility penalty based on that simple fraction. The result is a far higher economic obsolescence figure than the principles of equipment appraisal support.

63. Although not dispositive, it is remarkable that Mr. Ray, who has performed over a thousand appraisals of machinery and equipment in his career, Hr'g Tr. 158:11-158:13, has never seen an economic-obsolescence calculation in the 60% range. Hr'g Tr. 179:18-180:1. At Mr. Ray's deposition, and again at the hearing, the Debtors attempted to contort Duff & Phelps' economic obsolescence analysis to reach a similar 60% inutility figure. Hr'g Tr. 213:8-214:21. This, however, is another example of the Debtors selectively picking the most favorable inputs to suit their own desired valuation output, no matter how unrealistic and disingenuous those inputs are. Their flawed calculations using Duff & Phelps' analysis were based on an assumption that Boomerang's maximum OCTG output is 40,000 tons per month. Hr'g Tr. 213:24-214:21. The 40,000 tons per month figure that the Debtors touted at the hearing is the "nameplate capacity" of the facility that could be achieved only if Boomerang

ran just one product at the facility, which they do not. Hr'g Tr. 224:21-264:5. Rather, as Mr. Nystrom testified, Boomerang runs a mix of products at its facility, resulting in true output capacity of approximately 25,000 tons per month. Hr'g Tr. 14:20-15:18.

64. In an attempt to make it appear as if Duff & Phelps somehow supports (or concurs with) the Debtors' inutility analysis (which it plainly does not), at the confirmation hearing the Debtors put Mr. Ray through paces of doing a hypothetical inutility calculation based on a formula that Mr. Ray stated was erroneous and using data inputs that that he clearly believed were improper. Hr'g Tr. 224:21 – 225:9. But it was not just Mr. Ray who believed that the data inputs suggested by the Debtors for the inutility calculation were incorrect. Both Duff & Phelps ***and the Debtors' expert Mr. Cook*** agreed that, in performing an inutility calculation, whether one used a straight-line or logarithmic approach, the correct number to be used for the denominator in this calculation was the actual plant capacity of 25,000 tons per month, ***not*** the 40,000 tons per month name-plate capacity of the plant's equipment. Hr'g Tr. 133:13-133:21. It is therefore both disingenuous and inconsistent with the analysis and opinion of the Debtors' ***own expert*** for the Debtors to use 40,000 tons per month capacity to allege that Duff & Phelps' analysis produces an inutility penalty of 60%.

65. In sum, Mr. Cook's proposed inutility deduction results from an analysis that should never have been performed, using cherry-picked data inputs that ignore the robust economic future for the Debtors predicted by the Debtors' own witnesses, which were then run through an inutility formula that is simply incorrect. As such, his entire inutility analysis is fatally flawed and should be disregarded.

E. Even if the Court were to Accept a "Fair Market Value – Removed" Valuation Premise, Correct Application Would Yield a Value of $9,360,000.

66. Mr. Cook's "fair market value – removed" standard of valuation is inappropriate because it does not account for the proposed use of the Equipment under the Debtors' plan. But even if the Court were to apply that standard, correcting the many errors made in his analysis would result in a valuation of $9,360,000 for the Equipment, nearly $5,000,000 higher than Mr. Cook's stated valuation. Hr'g Tr. 187:16-187:22.

67. Duff & Phelps would begin with a replacement cost new of $15,000,000, reflecting the quote received from Primetals, as compared to Mr. Cook's replacement cost new of $14,700,000, which represents the original cost of the Equipment, $14,300,000, multiplied by 1.03, *i.e.,* the Marshal & Swift inflation index for the petroleum industry that does not include furnace manufacturers. Hr'g Tr. 185:13-185:16.

68. Duff & Phelps would then deduct $2,000,0000 to account for physical depreciation of 13.33%, based on the Equipment's effective age of two years, as compared to Mr. Cook's deduction of $2,946,000 for physical depreciation of 20% based on an effective age of three years. Hr'g Tr. 185:19-186:8. Duff & Phelps would not make any deduction for functional obsolescence because Boomerang did not keep financial records that would permit a precise calculation, whereas Mr. Cook deducted $353,200 to reflect what Mr. Cook believes to be 3% functional obsolescence based on his single conversation with the Equipment manufacturer. Hr'g Tr. 186:9-187:1. Finally, Duff & Phelps would deduct $3,640,000 to account for 28% economic obsolescence based on the business enterprise value of Boomerang, as compared to Mr. Cook's deduction of $6,858,288 for a purported 60% economic obsolescence based on the trough in Boomerang's OCTG production experienced in the single month of July 2015. Hr'g Tr. 187:2-187:22.

69. Using Mr. Cook's flawed "fair market value – removed" standard of valuation but correcting the errors in his replacement value new and various deductions, the value of the Equipment would be $9,360,000, far in excess of the Debtors' $4,500,000 valuation. Hr'g Tr. 187:21-187:22.

III. The Plan Is Not Fair, Feasible, or Confirmable.

70. Bankruptcy Code § 1111(b) provides a secured creditor such as SBBT with the right to elect to have its claim treated as secured to the full extent its claim is allowed. 11 U.S.C. § 1111(b)(2). The Court should not be misled by the Debtors' attempts to complicate what is actually a straightforward analysis. In August 2015, SBBT timely filed a $12,590,518.64 proof of claim. SBBT also timely filed a notice of election under § 1111(b) in the event that the Court recharacterizes the Lease as a financing. Under § 1111(b), SBBT has a right to have its full $12,590,518.64 claim treated as secured, in exchange for surrendering the unsecured deficiency claim to which it would otherwise be entitled. Simply put, if the Equipment in which SBBT enjoys a perfected security interest has a value less than that of SBBT's claim, by taking the election SBBT is entitled to have the difference between the amount of its claim and the value of the Equipment treated as a secured claim.

71. The Court must decide whether the Plan complies with § 1111(b) by providing SBBT with one note paying $4.5 million over a seven-year period at an interest rate of 4.75%[13] and a second ***non-recourse*** note that would pay SBBT nothing for 12 years and then, on the twelfth anniversary of the effective date, pay SBBT the balance of its claim.

72. This proposed treatment fails on two levels. First, Debtor's treatment of SBBT's claim in this manner is not feasible. Second, the proposed treatment does not comply with the

[13] The parties have stipulated that the interest rate should be 4.75% in the event this Court recharacterizes the Lease as a financing. Stipulation (Ex. 189), ¶ 40.

Bankruptcy Code's requirements concerning creditors taking the § 1111(b) election. In that regard, the Debtors are effectively seeking to bifurcate the secured claim of SBBT into a secured and unsecured portion in violation of the express provisions of §§ 1111(b) and 1129.

A. The Debtors' Proposed Plan Is Not Feasible.

73. The Debtors bear the burden to prove that their proposed plan is feasible, 11 U.S.C. § 1129(a)(11), and they have produced ***no evidence whatsoever*** on their ability to make the balloon payment 12 years from now. *See Id.*, ¶¶ 57-64. Their failure to put on any evidence regarding feasibility is fatal.

74. The Debtors' financial projections included in the Disclosure Statement are silent on the source they will use to make the balloon payment 12 years from now. And the Debtors' financial projections included with their Disclosure Statement only go out to the end of 2018, some ***nine years*** before the balloon payment will be due. *See* Disclosure Statement (Dkt. 378), Ex. F. The Debtors' own witness, Timothy R. Pohl, testified that:

> 2018 is three—is three years from now. Right? This company is—the further—the further away you go, the more risk there is that you will achieve those numbers. That's sort of definitional, tautological. That's why analysts don't go out so far. So—because it's not reliable.

Hr'g Tr. 111:11-15, Sept. 22, 2015.

75. If this Court believes the Debtors' witness Mr. Cook that the Equipment is now three years into its effective life, then the Debtors' proposed note, payable to SBBT 12 years from now, will be secured by nothing of value because the equipment is projected to have a life of only 15 years total. In sum, the Debtors are proposing to make a payment, 12 years hence, from cash flows that neither they nor Lazard can demonstrate will be available—all while holding hostage SBBT's collateral as it depreciates. At the end of the 12 years, the

Equipment may be worth nothing because it will be at the end of its projected life. Debtors cannot reasonably argue that SBBT will be repaid from the collateral securing the note.

B. The Debtors' Proposed Treatment of SBBT Does Not Comply with the Bankruptcy Code.

76. The legal standard for confirmation of a "fair and equitable" plan of reorganization when a creditor takes the election under § 1111(b)(2) is clear:

> [E]ach holder of a claim of such class [must] receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property.

11 U.S.C. § 1129(b)(2)(A)(i)(II).

77. SBBT is entitled to receive: (1) (by virtue of § 1129(a)), payments in the aggregate that equal its total allowed claim under § 506; plus (2) payments in an amount that when added to the secured payments, add up to the total amount of its claim: (i.e., $12,590,518.64). In other words, the monthly payments on the allowed secured claim under § 506 must be supplemented with an amount equal to the allowed amount of SBBT's total unsecured claim.

78. The Plan's treatment of SBBT is not fair to SBBT because it improperly bifurcates the allowed secured claim from the unsecured portion of the claim and effectively shifts the entire risk of the Plan's success onto SBBT. *See* Objection, ¶¶ 57-64. The effective life of the Equipment according to the manufacturer is fifteen years, Stipulation (Ex. 189), ¶ 37, which means that the Equipment itself is insufficient to provide SBBT with any assurance that it will receive anything on account of the stub portion of its claim 12 years from now. *See also* Testimony of John Ray, Hearing Tr. (Oct. 5, 2015), at 181:12-17. SBBT is thus left without any recourse to recover on its claim.

79. In their Response, the Debtors ignore the bases for SBBT's objections and actually argue that § 1111(b) not only permits but requires the Debtors to structure payment of SBBT's claim to include a non-recourse balloon payment at the end of 12 years to avoid unfairly discriminating against other creditors. Response at 84, ¶ 164. But nothing in the text of § 1111(b) or in the case law in this Circuit interpreting it says anything of the sort.[14]

80. If the Debtors do not understand that § 1111(b) prevents bifurcation of both the secured and unsecured portion of a secured creditors claim, the Third Circuit most certainly does. In the *Heritage Highgate* case, the main issue before the Court was whether the Bankruptcy Code permitted a chapter 11 debtor to strip liens down to the value of the collateral. *See* 679 F.3d at 132. The subordinated secured creditors in that case objected to being treated as wholly unsecured creditors where the value of the collateral in the case was equal only to the amount of the senior lienholders' debt, thereby leaving them with nothing. In holding that chapter 11 debtors have both the ability and authority to strip liens down to the collaterals value, the Third Circuit noted that two other provisions of the Bankruptcy Code argued in favor of stripping down liens, the first of which was § 506(a):

> That the lien a plan must preserve need only collateralize a "secured claim," as defined in section 506(a), is indicative of Chapter 11 debtor's ability to strip liens down to the collateral value … . The second is section 1111(b) pursuant to which

[14] To support this remarkable proposition, the Debtors rely on the case of *In re Wandler* from the United States Bankruptcy Court for the District of North Dakota. In *Wandler*, the court compared the value of the secured creditor's lien to the amount of its total claim and said that the value was inconsequential for § 1111(b) purposes because "[t]he Debtors, within a reasonable life of a plan, could not make payments to [the secured party] totaling approximately $390,000.00 with a net present value of $15,000.00." *In re Wandler*, 77 B.R. 728, 733 (Bankr. N.D. 1987). But recently courts have rightly criticized *Wandler*. *See, e.g.*, *In re McGarey*, 529 B.R. 277 (Bankr. D. Ariz. 2015); *In re At-Net Services-Charlotte, Inc.*, Case No. 14-32047 (Bankr. W.D.N.C. Aug. 17, 2015). As explained in *At-Net Services*, "[h]ad Congress intended inconsequential value analysis to be determined by analyzing whether the debtor can satisfy the requirements of § 1129(b) in light of the secured creditor's section§ 1111(b) election, it would have said so in § 1111(b) or elsewhere in the Bankruptcy Code." *Id.* at 8. In fact, adoption of the holding in *Wandler* would destroy the purpose of § 1111(b), which is to prevent bifurcation of secured and unsecured claims.

> undersecured creditors may opt out of the lien stripping found in section 1129 and instead be treated as fully secured to the extent of their allowed claims.

Heritage Highgate, 679 F.3d at 145 n.10.

81. The Debtors are proposing to effectively strip down the lien that SBBT has on the Equipment by giving SBBT two separate notes and only paying on one of the notes for seven years. But this they cannot do because, in the words of the Third Circuit, a creditor may "opt out of the lien stripping found in Section 1129." *Id.* And that is precisely what SBBT has done by making its § 1111(b) election.

82. Having opted out of the provisions of the Bankruptcy Code allowing the stripping down of its lien, SBBT reiterates its request that the Plan be amended to provide for payment of the full stated amount of SBBT's claim in equal monthly installments beginning on the Effective Date and continuing over a period of no more than seven years from the Effective Date, in the event the Court recharacterizes the Lease as a financing.

IV. The Debtors Improperly Filed a Claim on Behalf of a Non-Creditor.

83. On September 25, 2015 the Debtors filed a proof of claim on behalf of Wells Fargo Equipment Finance ("**WFEF**"),[15] asserting a so-called secured claim on behalf of WFEF, which the Debtors say—without any factual, evidentiary, or legal basis—has priority over SBBT's secured claim. But WFEF never had, does not now have, and does not even allege that it has a valid perfected secured claim against the Debtors.

84. The agreement relating to the Equipment is either a true lease or a disguised financing. Under either scenario, WFEF does not hold a secured claim against Boomerang. If the Lease was and is a true lease (and not a disguised financing), then SBBT is simply the

[15] The Debtors refer to WFEF as the "SBI Lender" in the Plan and in the proof of claim.

Lessor under the Lease and is entitled to all the protections the Bankruptcy Code provides to claimants relating to unexpired leases under § 365 of the Bankruptcy Code. If the Lease is a true lease, then WFEF likewise could not possibly have a secured claim against the Debtors because the Debtors are not now, nor have they ever been, the owners of the Equipment.

85. If the Court finds that the Lease was a disguised financing, then as a matter of law Boomerang became the owner of the Equipment as of the date of execution of the agreement—February 18, 2011. If Boomerang became the owner of the Equipment, then SBBT holds a valid perfected security interest in the Equipment under the Lease and by virtue of having filed UCC financing statements, the first of which was filed a few days after execution of the Lease in February 2011. *See* Stipulation (Ex. 189), ¶¶ 17-20. The parties have stipulated that "[i]f the Equipment Agreement is recharacterized by the Court as a secured financing, then (a) Boomerang is the owner of the Equipment and (b) SBBT holds a valid perfected security interest in the Equipment to secure Boomerang's obligations to SBBT under the Equipment Agreement." *Id.* ¶ 28.[16]

86. If the Lease is recharacterized as a financing, WFEF has no secured claim because WFEF has no debtor/creditor relationship with Boomerang. WFEF has no security agreement with Boomerang. And WFEF did not file its UCC financing statement until long after SBBT had already filed its initial financing statement. It is hornbook secured-transactions law that for a creditor to enjoy an enforceable security interest in personal property, the creditor must

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[16] SBBT also has a junior lien on spare parts inventory. *See* Stipulation (Ex. 189), ¶ 35; SBBT Financing Statement (Ex. 151).

have (i) a security agreement with the owner of the property and (ii) a properly filed financing statement.[17]

87. The Debtors never executed any security agreement with WFEF. Nor was any value given by WFEF to the Debtors. There is no debtor/creditor relationship between WFEF and the Debtors (which is probably why WFEF did not file any claim in the Debtors' bankruptcy cases. The Debtors filed a proof of claim on WFEF's behalf, but such an act cannot create a claim out of thin air where, as here, there is no factual or legal basis for the claim). That SBBT and WFEF may have had their own separate and distinct debtor/creditor relationship is irrelevant to the debtor/creditor relationship between SBBT and Boomerang.

88. Moreover, if the Lease is recharacterized as a financing, then the date the lease payments commenced is irrelevant to the analysis.[18] If it was a financing, then Boomerang became the owner of the Equipment on the date the agreement was executed—February 18, 2011. It was on that date that the parties' mutual obligations commenced. Had either party breached any of those obligations at any time, even before lease payments began, the other party would have been legally entitled to enforce the agreement. The Debtors offer no legal authority for their novel argument that their rights as owner of the Equipment under the Lease sprang into existence only after they began making lease payments in August 2012.

[17] Section 9-203 of the Uniform Commercial Code provides that "a security interest is enforceable against the debtor and third parties with respect to the collateral only if: (1) value has been given; (2) the debtor has rights in the collateral or the power to transfer rights in the collateral to a secured party; and (3) one of the following conditions is met: (A) the debtor has authenticated a security agreement that provides a description of the property …; (B) the collateral is not a certificated security and is in the possession of the secured party …; (C) the collateral is a certificated security …; or (D) the collateral is deposit accounts, [etc.] … ." Tex. Bus. & Com. Code Ann. § 9.203(a) (West 2009).

[18] The Debtors arbitrarily focus on the lease commencement date of August 1, 2012 in a futile effort to give priority to WFEF because of the financing statement WFEF filed on September 14, 2011, some seven months after the Lease was executed and SBBT filed its financing statement. (Ex. 146).

89. The uncontroverted evidence shows that the parties had a number of obligations to one another that they had to fulfill under the Lease before payments commenced in August 2012. For example, Boomerang was obligated, among other things, (i) to make multiple advance payments under the Lease prior to the Lease Commencement Date, Lease (Ex. 139), ¶ 6(c) (which payments Boomerang made, Stipulation (Ex. 189), ¶ 8); and (ii) to properly install the Equipment according to Manufacturer specifications, *Id.*, ¶ 5(a). *See also* Testimony of Arish Gupta, Hr'g Tr. 31:24-33:4.

90. The Debtors' assertion that SBBT is "fully unsecured" lacks any foundation. SBBT is the ***only*** party with a perfected security interest in the Debtors' Equipment. As such, SBBT is secured to the full value of its claim. If the value of the Equipment exceeds the allowed amount of SBBT's claim, then SBBT is oversecured.

CONCLUSION

91. For the reasons stated herein, SBBT respectfully requests that the Court deny confirmation of the Debtors' Plan as currently drafted.

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Respectfully submitted,

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