IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re: KiOR, Inc.,[1] Debtor.	Chapter 11 Case No. 14-12514 (CSS) Hearing Date: June 3, 2015 at 10:00 a.m. Objections Due: May 20, 2105 at 4:00 p.m. Re: Docket No. 470

OBJECTION OF THE MISSISSIPPI DEVELOPMENT AUTHORITY TO THE DEBTOR'S SECOND AMENDED CHAPTER 11 PLAN OF REORGANIZATION, AS REVISED DATED APRIL 7, 2015

The Mississippi Development Authority (the "MDA") votes against and files this objection (the "Objection") to *KiOR Inc.'s Second Amended Chapter 11 Plan of Reorganization* [Docket No. 470] (the "Plan") proposed by the KiOR, Inc. ("KiOR," or the "Debtor") in this case, and respectfully states as follows:

I. PRELIMINARY STATEMENT[2]

No true reorganization is being pursued. The Debtor's proposals amount to nothing more than empty packaging. The Plan does not propose to rehabilitate the Debtor or preserve the estate for the benefit of *all* creditors and parties in interest. The Plan is not proposed in good faith and serves no legitimate bankruptcy purpose. Instead, the Plan is primarily designed to provide inappropriate releases, protections and benefits to the Debtor's controlling shareholders, insiders, and professionals. The Plan is not feasible and otherwise does not meet the requirements of the Bankruptcy Code for confirmation. The Plan is inequitable and unfairly discriminates against arms-length creditors and parties in interest. The Plan violates the absolute

1 The Debtor and the last four digits of its taxpayer identification number are: KiOR, Inc. (2233). The Debtor's mailing address is 13001 Bay Park Road, Pasadena, Texas 77507.

2 Capitalized terms not otherwise defined in this Objection shall have meanings ascribed thereto in the Plan.

priority rule and would transfer all equity interests in the Reorganized Debtor to the prepetition controlling shareholders of KiOR, without any effort to value the equity and with inadequate exposure to the market.

The Debtor, in concert with the Khosla Parties,[3] could have pursued a transfer of the Debtor's assets through a 363 sale. They actually had a sale process noticed up earlier in the case. However, they have instead chosen to attempt to confirm a chapter 11 plan. This requires that the Debtor comply with the higher burden of 11 U.S.C. § 1129 and all of its provisions. Based on the facts and status of this case, this is a burden the Debtor cannot attain.

1. The Plan is Not Proposed in Good Faith and Serves No Legitimate Bankruptcy Purpose.

As noted by the Court at hearings held during the course of this case, confirming a plan is not the sole objective of chapter 11. Confirmation of a plan is only appropriate if the proposed plan, at a minimum, has a reasonable prospect of efficiently and fairly accomplishing some legitimate purpose of chapter 11.

The Court should ask why KiOR's prepetition controlling shareholders (*i.e.,* the Khosla Parties) are spending millions upon millions of dollars in professional fees and other administrative costs to accomplish nothing that could not have been accomplished more efficiently and more equitably via a sale of the Debtor's assets under Section 363 of the Bankruptcy Code (or, even more to the point, via a foreclosure sale without the need for a filing at all).

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[3] Vinod Khosla, Pasadena Investments, LLC, VNK Management, LLC, Khosla Ventures III, LP, and KFT Trust, Vinod Khosla Trustee are collectively referred to herein and in other pleadings filed by the parties (including the Khosla Parties) as the "Khosla Parties". The Khosla Parties compose the Debtor's supermajority controlling principal shareholders, the DIP Lender, holders of the vast majority of all prepetition secured claims, proposed recipients of all post reorganization equity in the Debtor, and the proposed providers of exit funding of the Debtor.

There is no viable business enterprise which the Plan will preserve or create. In fact, the Debtor has yet to achieve experimental benchmarks in its laboratory to justify any further attempts to commercialize its speculative technology. This fact is driven home by the as yet unachievable experimental benchmarks upon which further funding by the Khosla Parties under the DIP and the proposed exit funding are conditioned. Even if attained, there is no certainty that achieving these benchmarks transforms the Debtor's business into one that is viable, either operationally (the technology works) or commercially (the business is profitable).

As such, the purpose of the Plan can only be to provide insiders with protections against liability to third parties and, perhaps, preserve potential net operating loss tax attributes for the benefit of the Khosla Parties. These are not legitimate reasons to confirm a plan.

2. <u>The Plan Does Not Provide for Rehabilitation of the Debtor and Contemplates Only Inadequate, Short Term Exit Funding on a Discretionary Basis.</u>

There is nothing in the Plan which suggests that its implementation will cause the Debtor to achieve financial viability. Among other things, no revenues are projected for the foreseeable future. The Plan does not set forth a business plan, contemplate any concrete mechanism, or provide for funding by which the Debtor could reasonably hope to achieve commercial success. Rather, the primary aim of the Plan appears to be stripping arms-length creditors and investors of claims and rights, while, in exchange for inadequate and improper consideration, awarding insiders of KiOR new, controlling post-confirmation equity in a still foundering "reorganized" debtor.

The proposed exit funding appears to be largely discretionary. As noted above, if the Debtor does not soon reach speculative experimental benchmarks required by the Khosla Parties pursuant to the DIP facility and the proposed exit funding, the Debtor will not receive funding necessary for the Plan to become effective, much less to continue with its experiments thereafter. Further, even if all such funding is ultimately provided, the same would not be adequate to continue the Debtor's speculative experiments with its undeveloped technology beyond 12 months, at which point the Debtor admittedly still will not have revenues or a viable business. There is no funding in place for the Debtor to continue thereafter and there will be no business from which to generate revenue to pay continuing expenses.

Moreover, the funding contemplated is unlikely to sustain the Debtor for 12 months. Among other things, the proposed exit funding fails to take into account numerous likely administrative costs and expenses, such as indemnification claims of certain directors and officers and the cost of complying with the pending investigation of KiOR by the Securities and Exchange Commission (the "SEC"). The Plan is not feasible, and it appears almost certain further financial restructuring will shortly be required.

3. The Plan is Proposed for an Improper Purpose—Inappropriate Releases and Other Protections for Insiders.

As a result of their prepetition conduct, KiOR's insiders are defending litigation on multiple fronts, including, without limitation, a class action for violation of the federal securities laws, a shareholder derivative suit, whistleblower claims, and a civil action by the Attorney General of the State of Mississippi. Such actions and the associated underlying claims are based in part on assertions that KiOR's insiders engaged in misrepresentations concerning, without limitation, KiOR's finances and technology. In addition, KiOR and its insiders are subject to an ongoing formal investigation by the SEC for violations of the federal securities laws. Such investigation may result in claims against the Debtor by the SEC--claims that do not appear to be taken into account by the Plan.[4]

Meanwhile, in exchange for little or no consideration, the Plan seeks to implement improper and overly broad releases and erect other improper protections for insiders (as well as their counsel and other prepetition professionals). Consistent with the Debtor's intent and course of action throughout these proceedings, these provisions appear to be aimed at providing protection against the non-bankruptcy proceedings described above, as well as against bankruptcy avoidance actions and existing challenges to the alleged prepetition claims and liens of insiders.

4. The Plan Violates the Absolute Priority Rule.

Under the proposals of the Khosla Parties, which are adopted in the proposed Plan, the Khosla Parties would be awarded new equity in the Reorganized Debtor in exchange for approximately $15 million in purported prepetition insider secured indebtedness. As set out in the proposed adversary complaint submitted by the MDA,[5] this purported insider prepetition indebtedness is subject to recharacterization as equity or equitable subordination. The Court has found that such challenges to the Khosla prepetition claims are colorable and should be further investigated and pursued.[6] Issuing new equity to the Khosla Parties on account of their disputed prepetition claims as proposed in the Plan would be void of valid consideration, provide no benefit to the estate, and violate the absolute priority rule. Accordingly, the Plan cannot be confirmed under a "cram down" scenario.

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4 The SEC has filed a generalized proof of claim in the case, while pursuing its investigation. *See* POC No. 26, filed on January 16, 2015.

5 *See* Docket No. 433-1.

6 Transcript of April 29, 2015 hearing.

5. The Khosla Parties are Improperly Manipulating the Perceived Value of the Proposed New Equity.

It has been established at multiple hearings in this case that the Khosla Parties' DIP funding has added no measurable value to the estate. In fact, much of the DIP funding has been used to fund legal fees incurred in failed pursuit of inappropriate releases and improper protections for the Khosla Parties and other insiders. The most that can be said is that the DIP has preserved the operational status quo of the Debtor, while enabling the Debtor to incur millions of dollars in additional losses.

In April 2015, the Khosla Parties were willing to convert as much as $29 million in DIP Financing to acquire proposed new equity in the Reorganized Debtor. Now, the Khosla Parties are – under the Plan – only converting $20 million in DIP Financing to acquire the proposed equity. All the while, the proposed new equity has not been exposed to the marketplace, as required by controlling Supreme Court precedent. These and other manipulations by the Khosla Parties make it impossible to properly expose the Debtor and its assets to the marketplace or reliably determine their value. As a result, among other things, the Debtor cannot establish the value of its equity or assets and cannot carry its burden of establishing that the Plan is in the best interests of creditors as required, *inter alia*, by 11 U.S.C. § 1129(a)(7).

6. The Proposed Exit Funding Provides Little or No Value to the Bankruptcy Estate.

The vast majority of the proposed exit funding to be provided by the Khosla Parties is to be used for post-confirmation operating expenses and provides little or no benefit to the bankruptcy estate or its creditors. It cannot serve as consideration for acquiring as yet unvalued new equity in a reorganized debtor. Of the first tranche $19 million in proposed exit funding which may be provided on the effective date of the Plan, less than $2 million of this amount could even arguably serve as consideration for the proposed new equity, *i.e.*, those minimal amounts which may be paid towards satisfaction of priority tax claims and convenience class claims and to provide a relatively small $100,000 in seed money for a proposed post-confirmation liquidation trust. The balance of the exit funding would be provided solely to pay expenses of the Reorganized Debtor and pre-effective date administration of the plan for the benefit of the Reorganized Debtor. These funds are of no benefit to the bankruptcy estate or its creditors as the Reorganized Debtor would have no further obligation or liability to such arms-length creditors.

7. <u>The Plan Unfairly Discriminates Among Creditors and Improperly Favors the Debtor's and Khosla Parties' Professionals.</u>

At the same time, the Plan as proposed unfairly discriminates among creditors having the same distribution priority under Bankruptcy Code. Among other things, the Plan proposes to group certain "continuing trade creditors" into a separate class (Class 7 under the Plan) and to pay those creditors 50% of their prepetition claims on the Effective Date. Such preferred general unsecured creditors will also participate in distributions, if any, made to other unsecured creditors under Class 9. To top it all off, the Plan proposes to release Class 7 creditors from Avoidance Actions (which could result in value being provided to Class 7 creditors in excess of their claim amounts). Class 7 appears to be made up largely, if not entirely, of KiOR's ongoing professionals. For example, the dominant claim in Class 7 belongs to the law firm of WilmerHale, which serves as special counsel to the Debtor, as well as counsel to the Khosla Parties in matters such as litigation with the State of Mississippi and the SEC investigation. By comparison, Class 9 arms-length unsecured creditors are to receive distributions, if any, solely from a post-confirmation trust, the assets of which consist of Avoidance Actions not released under the Plan (*i.e.* Avoidance Actions against the Class 9 creditors themselves) and other estate causes of action.

The Debtor has not demonstrated a legitimate need to provide such favorable treatment to its ongoing professionals. In addition, the Debtor's attempt to create a convenience class in Class 8 is inappropriate. Among other things, the unsecured claims against the Debtor do not appear to be so numerous as to justify creation of a convenience class. The apparent reason for the Class 7 and Class 8 constructs is to conjure consenting impaired classes for purposes of attempting inappropriately to confirm a plan over the objection of arms-length general unsecured creditors in Class 9. The MDA holds a large Class 9 claim that dominates the class, and the MDA has voted to reject the Plan as proposed. The Debtor's improper gerrymandering in attempt to achieve a "cram down" should not be countenanced by the Court and confirmation should be denied.

8. The Plan Is Fundamentally Unfair, Inequitable, and Not Feasible Because the Proposed Post-Confirmation Trust Is Not Adequately Funded and Not Designed to Serve Its Beneficiaries.

Importantly, the post-confirmation trust proposed in the Plan is to be funded with a mere $100,000 in seed money. This amount is woefully inadequate to administer the remaining bankruptcy estate. By way of comparison, the professional fees incurred by the Debtor have run as high as $3 million per month. The Reorganized Debtor has a proposed budget for professional fees in the amount of $3 million annually.

In addition to administration of the estate and pursuit of remaining estate causes of action (*i.e.*, those not given away under the Plan), the underfunded post-confirmation trustee will also be charged with pursuing the estate's challenges to the Khosla Parties' prepetition secured claims and any associated insider deficiency claims. Under the Plan as proposed, such insider claims could otherwise largely dilute and diminish any meaningful distribution to arms-length unsecured creditors. It is abundantly clear that the proposed gross underfunding of the post-confirmation trustee would impermissibly compromise the adversary system and leave the trustee unable to perform his duties – yet another improper attempt to use the bankruptcy/plan process to shield the Khosla Parties.

9. The Plan Would Serve Only the Prepetition Controlling Shareholders.

Among the aims of chapter 11 is to maximize the value of bankruptcy estates for the benefit of *all* creditors and parties in interest. A chapter 11 case cannot properly be conducted for the sole benefit of insiders, or even for the benefit of a limited number of parties in interest. The terms of the proposed Plan make clear that the goal of the Debtor and its insiders in this case is not to rehabilitate the Debtor or to maximize the estate for the benefit for *all* creditors, but to defeat the rights and claims of arms-length creditors and investors, while improperly shielding the Debtor's insiders with inappropriate protections from liability. This is not a proper bankruptcy purpose and the Plan should not be confirmed. Rather, as set forth in the MDA's Motion to Convert or Dismiss [Docket No. 168], a trustee should be appointed and/or the case converted or dismissed.

For the reasons set forth above and those discussed in greater detail below, the Court should sustain this Objection and deny confirmation of the Plan. Discovery concerning confirmation issues is ongoing, and therefore, the MDA reserves all rights to supplement this objection with additional facts and arguments, whether in subsequent filings or at the confirmation hearing.

II. OBJECTION AND ARGUMENT[7]

A. The Debtor Bears The Burden Of Proof Concerning Confirmation

The Debtor bears the burden of proving each of the requirements of the Bankruptcy Code, including, without limitation, those set forth in Section 1129(a), by a preponderance of the evidence. *In re Washington Mut., Inc.*, 442 B.R. 314, 328 (Bankr. D. Del. 2011); *see also Heartland Fed. Sav. & Loan Ass'n Enters. v. Briscoe Enters., Ltd. II (In re Biscoe Enters., Ltd., II)*, 994 F. 2d 1160, 1163 (5th Cir. 1993). If, as here, a plan proponent seeks nonconsensual confirmation of a plan pursuant to Section 1129(b) of the Bankruptcy Code, then the proponent must prove by a preponderance of evidence that the proposed plan meets all of the requirements of Section 1129(a), except for consent of all impaired classes under 1129(a)(8). In addition, the proponent must also prove that the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under the plan and has not accepted the plan. *See* 11 U.S.C. § 1129(b).

As set forth herein, the Court should deny confirmation of the Plan because the Debtor has not and cannot carry its burden of proof with respect to satisfying the requirements of the Bankruptcy Code.

B. The Plan Is Not Feasible.

Section 1129(a)(11) of the Bankruptcy Code requires that a plan may only be confirmed if it is "not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor . . ." 11 U.S.C. § 1129(a)(11). As such, a bankruptcy court must "assure itself that reorganization will succeed . . . . ," *United States v. Energy Resources Co.*, 495 U.S. 545, 549 (1990), and the Debtor must establish feasibility by a "preponderance of the

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[7] The MDA incorporates by reference, as if fully set forth herein in full, the facts and arguments set forth in its Motion to Convert or Dismiss [Docket No. 168].

evidence." *In re W.R. Grace & Co.*, 475 B.R. 34, 114 (D. Del. 2012); *In re T-H New Orleans Ltd. Partnership*, 116 F.3d 790, 801 (5th Cir. 1997). Here, the Plan is not feasible because it does not offer "a reasonable probability of success." *Id.*

The Debtor's proposed Plan is merely for short term additional funding by the Khosla Parties. The Plan is speculative in that it requires the Debtor attain research benchmarks prior to additional funding. These benchmarks have heretofore not been achieved by the Debtor, and even if the benchmarks were achieved, the proposed funding still runs out in 12 months or less. At that time the Reorganized Debtor is still an entity with no prospects for revenue and not financeable. There is no credible likelihood that the next 12 months of research will be any more effective than the previous 12 months. The Debtor has already burned through over $600 million to develop its technology. It lacks credibility that $22 million[8] over the next 12 months is sufficient to bring the Reorganized Debtor to commercial viability when KiOR has been unable to achieve anything close to that by spending $600 million.

However, this is even more problematic as there is initially only $12 million available[9] if the Reorganized Debtor does not achieve its required research goals.

Furthermore, the exit funding is also discretionary. On March 17, 2015, the Debtor and the Khosla Parties filed a Plan Supplement [Doc. No. 404]. Attached to the Plan Supplement is what the Debtor and the Khosla Parties characterize as an "Exit Financing Letter". The Exit Financing Letter provides that the Khosla Parties may, in their sole discretion, provide "equity

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[8] The Debtor's projections provide for a spend of $28,896,028; however, $7,182, 232 is earmarked for payment of administrative and other plan confirmation costs, leaving $21,713,796 for the 12 months following the Effective Date.

[9] The same $7,182,232 will be used for confirmation costs, leaving approximately $12 million.

financing" commencing on the effective date of a confirmed plan, in amount between $12 million and $22 million.[10]

The Exit Financing Letter contains numerous subjective conditions and, at the end of the day, leaves any decision to provide exit funding to the complete discretion of the Khosla Parties. For example, the Exit Financing Letter provides, without limitation, the following conditions:

> "<u>2. Conditions.</u> The **obligation of the Investor to invest**, or cause the investment of, the Commitment Amount **shall be subject to** (i) KiOR achieving the applicable production benchmark set forth on Annex A to Exhibit A **to the satisfaction of the Investor in its sole and absolute discretion**, (ii) the negotiation and execution of definitive documentation with respect to the Financing containing the terms and conditions set forth in Exhibit A and other terms and conditions **acceptable to the Investor in its sole and absolute discretion**, (iii) the satisfaction in full (or waiver with the prior written consent of the Investor) of the conditions to the Effective Date set forth in the Plan, (iv) the entry by the Bankruptcy Court of the Confirmation Order no later than May 31, 2015, in form and substance reasonably satisfactory to the Debtor and the Plan Support Parties, (v) the Effective Date of the Plan shall have occurred no later than September 30, 2015, (vi) none of Fred Cannon, Chris Artzer, or John Kasbaum has resigned, has been terminated or is otherwise unable to continue his employment with KiOR or reorganized KiOR; however, if one of the three of them were to resign, be terminated or unable to continue their employment and within ten (10) days after such resignation, termination or inability to continue employment, KiOR or Reorganized KiOR has not retained a replacement or otherwise reallocated duties among existing personnel in a manner, in each case, that **the Investor has consented to in writing in its reasonable discretion**, (vii) the absence of any filing of a formal action or claim by the SEC against KiOR or any of its respective officers, employees or directors, other than a protective proof of claim filed in the KiOR bankruptcy case, and (vii) the absence of any other event or development, which, **in the determination of the Investor**, could be expected to have a Material Adverse Effect (as defined in the DIP Credit Agreement) or an Additional Material Adverse Effect (as described in Section 9(k) of the DIP Credit Agreement)."
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> "Additional Equity Financing After the Effective Date - $10,300,000 on or prior to the date that is 6 months from the Initial Equity Financing if the specified benchmark set forth on Annex A is achieved by KiOR as determined **to the satisfaction of the Investor in its sole and absolute discretion**".

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[10] It appears such "equity financing", if any, would be provided solely in exchange for issuance of additional shares of stock in the Reorganized Debtor. These numbers take into account the Debtor’s budget, which provides approximately $7 million for confirmation costs.

(emphasis added.)

Moreover, the Plan and accompanying Second Amended Disclosure Statement set forth no business plan by which the Reorganized Debtor could hope to rehabilitate its business or achieve commercial viability. Rather, the Debtor admits that it is not commercially viable and there is no evidence to suggest it ever will be. *See*, *generally*, Second Amended Disclosure Statement.

It is important to note that, among other things, the proposed exit funding fails to take into account numerous likely administrative costs and expenses, such as indemnification claims of certain directors and officers and the cost of the SEC investigation. The Plan is not feasible, and it appears almost certain further financial restructuring will shortly be required if the Debtor is actually somehow to continue its experiments.

A "[d]ebtor's prior performance is probative of the feasibility of any plan of reorganization . . . . Speculative, conjectural or unrealistic projections by Debtor cannot support Debtor's predictions of future performance." *Canal Place Ltd. Partnership v. Aetna Life Insurance Co.*, 921 F.2d 569, 579 (5th Cir. 1991); *In re W.R. Grace & Co.*, 446 B.R. 96, 142 (Bankr. D. Del 2011) (chapter 11 plan found to be feasible where debtor in possession demonstrated "a strong financial track record by its growth in sales and Core EBITDA during its Chapter 11 reorganization"); *Matter of Sound Radio, Inc.*, 93 B.R. 849, 856 (Bankr. D.N.J. 1988) (the debtor's projections "must not be speculative, conjectural or unrealistic").

In this case, where the Debtor hopes to fund its plan exclusively through the limited equity exit funding, there is no reasonable probability of success based on the Debtor's past performance (operating at a loss since inception), future projections and the staggering amounts of additional capital the Debtor apparently will require to attempt to develop a commercially viable product, build expensive production facilities and, perhaps one day, begin generating revenue.

As the Court appropriately found at the conclusion of the final hearing on the DIP Financing, (x) the Debtor is a pre-revenue developmental research and development company with no immediate prospects of revenue and no immediate prospect of profitability, and (y) the Debtor's technology is not commercially viable as it exists, and further research, development and money will be required to get that technology to a place where even more money needs to be spent to take it to the next step. Indeed, the Debtor may require hundreds of millions of dollars in further investment to attempt to commercialize a saleable product and has no commitment from any party to fund its operations beyond the proposed Effective Date, if at all.

The Debtor readily admits in its Second Amended Disclosure Statement that "[t]he Reorganized Debtor does not expect to generate any material amount of revenues for the first twenty four (24) months following the Effective Date of the Plan." Second Amended Disclosure Statement § V. In addition, the Debtor further states in its Second Amended Disclosure Statement that:

> As set forth in the one-year budget attached hereto as Exhibit D, the Reorganized Debtor intends to continue its research and development activities but will not generate substantial revenues during the 12-24 months following the Effective Date of the Plan.
>
> In the absence of material revenues during the 12-month period following the Effective Date of the Plan, the Reorganized Debtor will be funded entirely by the Exit Facility. The Debtor believes that the Plan Support Parties have the desire and the ability to fund the Exit Facility, as required by the Plan.

Second Amended Disclosure Statement § VIII.A.

The Debtor wholly fails to address what will happen upon expiration of the twelve (12) month period if no additional funding is obtained. Currently, no additional funding beyond the initial twelve (12) month period has been obtained, let alone a commitment to fund. As the Debtor concedes, the Reorganized Debtor does not expect to generate *any* material amount of revenues for the first twenty-four (24) months following the Effective Date, *i.e.*, well after the initial twelve (12) month period ends. Thus, it is unclear as to how the Reorganized Debtor will be able to operate after it burns through the limited Exit Financing obtained by the Debtor. Accordingly, there is a material risk that the Debtor will require further financial reorganization if the Reorganized Debtor is unable to secure additional financing beyond the limited Exit Financing.

In addition, the limited Exit Financing is insufficient to pay, among other things, administrative indemnification claims of certain directors and officers and the cost of the SEC investigation. To be sure, a condition precedent to the Effective Date of the Plan is that Administrative and Priority Claims anticipated to be Allowed in the Chapter 11 Case cannot exceed $250,000 over the aggregate budgeted amounts for such claims pursuant to the DIP Orders. Plan Art. IX.B.1. If the administrative class is expanded to include indemnification claims of certain directors and officers and the cost of the SEC investigation, administrative claims will easily exceed the Plan's cap on such claims and the Plan will not go effective. Moreover, the limited Exit Financing is insufficient to fund such administrative claims, and the Reorganized Debtor will not have any material revenues to pay such claims.

The Debtor offers no basis for establishing that it will be able to pay all administrative claims and continue its research and development activities beyond the first year post-Effective Date when the Exit Financing has been spent. The Debtor's financial performance prior to the Petition Date and following commencement of this case, as well as the Debtor's own admissions and projections, demonstrate that the Reorganized Debtor will be unable to fund all administrative claims and continue its research and development activities following the first twelve (12) months after the Effective Date (when the Exit Financing is exhausted) until such time as it begins generating material revenues, which the Debtor readily admits won't happen until at least two (2) years after the Effective Date. As such, the Debtor will be forced to obtain additional financing, if even possible without a commercially viable product and no material revenues, to avoid another restructuring. Consequently, this Court is left to speculate as to whether and how the Reorganized Debtor will fund administrative claims and continue its research and development activities once the limited Exit Financing is exhausted. Mere speculation, however, is insufficient in determining whether a plan is feasible. *In re Briscoe Enters., Ltd.*, 138 B.R. 795, 807 (N.D. Tex. 1992) (holding "the debtor must offer more than speculation about the source of funding for the plan.").

In short, the Debtor fails to offer any evidence to demonstrate that the Plan is feasible and that the Reorganized Debtor will not have to undergo another financial restructuring. Because the Debtor has fallen far short of its burden of proving by a preponderance of the evidence that the Plan is feasible, the Court should sustain this Objection and deny confirmation of the Plan. Denying confirmation of the Plan for the lack of evidence on this point would be in keeping with other bankruptcy courts' decisions to deny confirmation where there is an inadequate showing that further restructuring is not likely to occur. *See In re Vaderveer Estates Holding, LLC*, 293 B.R. 560 (Bankr. E.D.N.Y. 2003); *Crestar Bank v. Walker (In re Walker)*, 165 B.R. 994, 1005 (E.D. Va. 1994); *In re Hoffman*, 52 B.R. 212, 215 (Bankr. D. N.D. 1985).

C. The Debtor's Plan Is Not In The Best Interests Of Creditors And Does Not Comply With Section 1129(A)(7) Of The Bankruptcy Code

1. There is no Credible and Accurate Valuation of the Debtor's Assets.

The Debtor has not supplied a valuation of the proposed new equity in the Reorganized Debtor. In addition the Debtor has not provided a credible and accurate valuation of its assets. Courts have held that a plan proponent cannot satisfy 11 U.S.C. §1129(a)(7) without providing an accurate and reliable valuation of the debtor's assets. *See, e.g., In re Multiut Corp.,* 449 B.R. 323 (Bankr. E.D. Ill. 2011).

The Debtor's initial attempt at valuation was to subject its assets to the market using investment bankers prior to case being filed. This attempt at valuation was flawed because (a) only the assets were exposed to the market in the context of a 363 sale and not the equity in the Reorganized Debtor as proposed in the Plan and (b) the assets were exposed against a backdrop of the likely credit bid of in excess of $100 million of insider secured debt.[11] The black cloud of a possible insider credit bid would deter parties from spending funds to conduct appropriate due diligence.

2. The Debtor Fails to Account for all of its Assets.

Even if the Court assumes that an appropriate valuation of the equity occurred, then the consideration would be what the insiders are seeking to pay to acquire the new equity. It is unclear what the Khosla Parties propose to acquire the new equity. We know that they seek to apply credit of $15 million of the First Lien Debt, the DIP (which is moving target between $15 and $20 million) and a portion of the exit funding (according to the budget attached to the disclosure statement, approximately $7 million) to acquire the new equity. For purposes of

[11] The process of exposing the assets to the market occurred prior to the issues of debt recharacterization and equitable subordination being raised regarding the insider secured claims.

illustration, assume that the total is $42 million.[12] That is the value currently assigned by the Khosla Parties to the new equity. However, if the Plan is not confirmed, then the equitable subordination and debt recharacterization adversary proceeding clearly goes forward with respect to the First Lien Debt. The Court has already held that claims are colorable and should be investigated and pursued by the estate. A meritorious outcome in the adversary proceeding would free up $15 million of value in addition to all of the items that are already assigned to the liquidation trust.

Issues concerning these challenges to the insider claims should not be decided in a summary fashion at plan confirmation. It should be noted that the Court has put off consideration of the recharacterization and equitable subordination challenges until after confirmation at the request of the Debtor and the Khosla Parties.

But there is more. There are certain additional claims that would be available in a chapter 7 that the Debtor is proposing to release. These include Avoidance Actions against the fifteen Class 7 creditors, totaling $1,740,181. At least two of these creditors are professionals of the Debtor, WilmerHale and Price Waterhouse. These two creditors alone total $1,332,597, or 76.5% of the proposed Class 7 claims. According to the Second Amended Disclosure Statement, WilmerHale received $364,294 in potential preferential payments within the 90 days prior to the Petition Date and Price Waterhouse received $60,040.

D. <u>The Plan Violates The Absolute Priority Rule</u>

The absolute priority rule requires that the holders of junior claims or interests not receive or retain under a plan on account of such junior claim or interest any property unless general unsecured creditors receive property of a value, as of the effective date of a plan, equal to the

[12] $15 million (First Lien) + $20 million (DIP) + $7 million (portion of exit financing used for confirmation expenses) = $42 million.

allowed amount of their general unsecured claims. *See* 11 U.S.C. § 1129(b)(2)(B)(ii). The Plan violates the absolute priority rule because it would allow the holders of First Lien Claims, which are the subject of a bona fide dispute concerning recharacterization of their alleged secured debt to equity, to receive equity when unsecured creditors are not paid in full, including interest, as required under the Bankruptcy Code. *See id.* Moreover, because the Plan provides the holders of First Lien Claims with exclusive opportunities free from competition and without the benefit of market valuation, to receive equity in the Reorganized Debtor, no new value corollary or exception to the absolute priority rule applies in this case.

The alleged secured debt held by holders of First Lien Claims has been challenged as mere equity disguised as "debt." MDA has sought standing to pursue its recharacterization action against the holders of First Lien Claims on behalf of the Estate. *See Motion of Mississippi Development Authority for Order Granting Leave, Standing and Authority to Commence and Prosecute Derivative Claims on Behalf of the Debtor's Estate* [Docket No. 223] (as amended or supplemented from time to time, the "Motion for Standing"). Attached as an exhibit to the Motion for Standing was a draft complaint to be filed by MDA once it is granted standing, which complaint includes, among other things, counts for recharacterization of the alleged secured debt held by the Debtor's insiders, including the holders of First Lien Claims, to equity. *See* Motion for Standing Ex. A. MDA has since filed an amended proposed complaint (under seal), which retains the recharacterization and equitable subordination counts and adds additional counts against the Debtor's insiders, including the holders of First Lien Claims. *See* Ex. A to *Amendment to Motion of Mississippi Development Authority for Order Granting Leave, Standing and Authority to Commence and Prosecute Derivative Claims on Behalf of the Debtor's Estate* [Docket No. 433].

The Debtor's proposed distribution of New Equity Interests in the Reorganized Debtor to holders of disputed First Lien Claims runs completely afoul of the United States Supreme Court's holding in *Bank of America National Trust and Savings Association v. 203 North LaSalle Street Partnership*, 526 U.S. 434 (1999) and causes the Plan to be unconfirmable.

In *La Salle*, the Supreme Court took up the issue of new value and the absolute priority rule. 526 U.S. 434. There, the primary secured creditor of a partnership, a bank, loaned $93 million to the partnership secured by a non-recourse first mortgage on the partnership's principal asset, fifteen (15) floors of a downtown Chicago office building. When the partnership defaulted and the bank began foreclosure proceedings, the partnership filed a petition for relief under Chapter 11. The debtor then attempted to cram down its plan over the objection of the bank. The plan contemplated that certain former equity holders would be given the exclusive right to contribute capital in exchange for ownership of the Reorganized Debtor. The bank objected to the cram down on the basis that the plan was not fair and equitable because it violated the absolute priority rule. Specifically, the bank argued that the plan could not be confirmed as a cram down because the debtor's old equity would receive property under the plan even though the bank's unsecured deficiency claim would not be paid in full.

Without deciding whether the Bankruptcy Code includes a new value corollary or exception, the Supreme Court determined that even if the exception was encompassed within the Bankruptcy Code, the debtor's proposed plan would still fail to satisfy § 1129(b)(2)(B)(ii). According to the Court, the debtor's proposed plan was doomed by its provision for vesting equity in the reorganized business in the debtor's partners without extending an opportunity for anyone else either to compete for that equity or to propose a competing reorganization plan. The Court held that

> [T]he exclusiveness of the opportunity, with its protection against the market's scrutiny of the purchase price by means of competing bids or even competing plan proposals, renders the partners' right a property interest extended "on account of" the old equity position and therefore subject to an unpaid senior creditor class's objection.

LaSalle, 526 U.S. at 456. The Supreme Court determined that, at a minimum, exposure to the market was necessary to ensure that old equity's retention of property under a plan was not "on account of" its equity position. Although the Supreme Court declined to decide the issue of what degree of exposure to the market was necessary, *i.e.*, whether an opportunity to offer a competing plan or a right to bid for the same interest sought by old equity was required, the Court noted "it is enough to say, assuming a new value corollary, that plans providing junior interest holders with exclusive opportunities free from competition and without benefit of market valuation fall within the prohibition of § 1129(b)(2)(B)(ii)." *Id.* at 458.

Here, the Plan fails to meet the rule established in *LaSalle* in that it does not provide that the New Equity Interests in the Reorganized Debtor will be marketed, auctioned or otherwise exposed to the market. Instead, the Plan provides for holders of First Lien Claims to convert a portion of their disputed, alleged secured debt to equity without any exposure of the New Equity Interests to the market.[13,14] Without exposing the Debtor's New Equity Interests to the free market and adequate disclosure regarding the value of the disputed, alleged secured debt being converted vis-à-vis the value of the New Equity Interests being issued, it is impossible to know whether the value of the New Equity Interests (and third party releases) is equivalent to the value of the disputed, alleged secured debt held by the Debtor's insiders, including holders of First Lien Claims. Any attempt by the Debtor to issue New Equity Interests in the Reorganized

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[13] Although the Debtor ran a marketing process approximately seven (7) months ago, the Debtor only marketed its assets, not its equity. Not only is the process stale at this point but also fails to provide any evidence whatsoever as to the value of the Debtor's reorganized equity. Thus, the Debtor's equity has not been market tested.

[14] In fact, some of these equity interest holders are receiving more than retention of their equity in the Debtor since they would also benefit from improper third party release provisions in the Plan, as discussed more fully herein.

Debtor on account of First Lien Claims, which for the reasons stated herein and the Motion for Standing are properly characterized as equity interests, is impermissible under the Bankruptcy Code and the Supreme Court's ruling in *La Salle*.

The Debtor's Plan, which permits properly recharacterized equity holders to receive New Equity Interests in the Reorganized Debtor on account of their existing equity interests in the Debtor, while not paying unsecured creditors in full, violates the absolute priority rule, with no new value exception applicable. To be sure, the holders of First Lien Claims are not providing any new value (other than conversion of their properly characterized equity) for the New Equity Interests being issued in the Reorganized Debtor. As such, the Plan cannot be confirmed.

E. <u>**The Funding Provided By The Khosla Parties Will Have Little Or No Benefit To Creditors Of The Bankruptcy Estate.**</u>

The disputed prepetition indebtedness which the Khosla Parties propose to use as consideration for their new equity is of no benefit to the bankruptcy estate or its creditors. Likewise, the DIP financing provided by the Khosla Parties (which has been used largely to fund legal fees incurred in pursuing inappropriate releases and protections for the Khosla Parties and other insiders) has failed to create any value for the bankruptcy estate and its creditors. The same holds true for the proposed exit funding. Approximately $19 million of the proposed equity exit funding would be provided, if at all, upon the effective date of the Plan. Of this amount, less than $7 million dollars[15] could arguably benefit arms-length creditors of the estate. The rest of the exit funding will be provided solely to pay post confirmation operational expenses of the Reorganized Debtor. These funds are of no benefit to the bankruptcy estate or its creditors. Thus, the true purchase price being paid to the estate for the proposed new equity is in the range of $2 to $7 million. (*See* f.n. 15.) This is not proper, fair or equitable, especially where

[15] This number is debatable, as the existing administrative claims should be paid from DIP financing, and, therefore, the actual amount may be closer to $2 million. The MDA is conducting discovery regarding this issue.

such new equity has not been exposed to the market or otherwise valued. As a result the Plan is unfair and inequitable.

F. The Proposed Trust Is Not Feasible And Its Proposed Funding Is Not Fair and Equitable.

3. The Proposed Funding of Liquidating Trust is Inadequate

The proposed funding for the Liquidating Trust is woefully inadequate. The Debtor proposes to fund the Liquidating Trust with $100,000. The Liquidating Trust, as proposed, is composed solely of causes of action. The largest of which are claims against directors, officers and other insiders of the Debtor. The Debtor also proposes that the trustee be charged with pursuing the debt recharacterization and equitable subordination of the prepetition claims of the insiders. The Debtor's paltry funding of the Liquidating Trust will undoubtedly handicap the Liquidating Trustee's efforts to pursue the valuable claims and causes of action being transferred to the Liquidating Trust and undermine the adversary process.

The Liquidating Trustee should have in excess of $3 million available solely to evaluate and pursue estate causes of action and administer the trust. This is approximately 10% of the exit funding suggested by the Khosla Parties. By way of example, the debtor's own budget provides that the Reorganized Debtor will spend $3,046,500 on professional fees over the 12 months following confirmation. Moreover, professional fees of the Debtor during the bankruptcy case have run as high as $3 million per month.

4. The Liquidating Trustee Should be Selected by General Unsecured Creditors, Who are the Beneficiaries of the Liquidating Trust

With respect to selection of the Liquidating Trustee, the Plan states that the Liquidating Trustee "shall be acceptable to the Debtor and approved by the Bankruptcy Court prior to the Effective Date." Plan Art. V.C.3. MDA asserts that the Debtor, who will have no interest in the

Liquidating Trust, cannot and should not select the Liquidating Trustee. Rather, MDA believes that the beneficiaries of the Liquidating Trust, *i.e.*, general unsecured creditors, should select the Liquidating Trustee. Otherwise, the Debtor essentially controls—through the selection of the Liquidating Trustee—the Liquidating Trust and the valuable claims and causes of action being transferred thereto. As the Liquidating Trust is being established for the benefit of general unsecured creditor beneficiaries thereof, the beneficiaries of the Liquidating Trust should select the Liquidating Trustee, which selection shall be approved by the Bankruptcy Court.

5. Liquidating Trust Assets Being Transferred to Liquidating Trust Have Not Been Identified with Particularity

The Plan provides that upon the Effective Date the Liquidating Trust Assets will be transferred to and vest in the Liquidating Trust. Plan Art. V.C.4. Importantly, however, the Debtor's definition of Liquidating Trust Assets in the Plan is entirely vague and fails to identify the specific assets being transferred to the Liquidating Trust.

The Plan defines Liquidating Trust Assets as "the Vested Causes of Action, and all proceeds thereof, and all rights of setoff and recoupment and other defenses that the Debtor and the Estate may have with respect to any Class 8 or Class 9 Claim, as well as cash in the amount of $100,000." Plan Art. I.B.67. The definition of "Vested Causes of Action" is similarly vague—"all Causes of Action other than the Excluded Actions which are transferred to the Liquidating Trust and become Liquidating Trust Assets pursuant to the Plan." Plan Art. I.B.104. The definition of "Excluded Actions" is likewise ambiguous and fails to specify what actions are being excluded.

MDA asserts that the Causes of Action being transferred to the Liquidating Trust should be specifically identified by the Debtor in the Plan. Without such information, it is unclear what assets are being transferred to the Liquidating Trust and the Plan should not be confirmed.

6. An Oversight Committee Should be Appointed

The Plan provides for the establishment of a Liquidating Trust, but it does not provide the appointment of an oversight committee (composed of certain beneficiaries of the Liquidating Trust) to oversee the Liquidating Trust and the Liquidating Trustee's actions or inactions. Without an oversight committee, the interests of the beneficiaries are not and will not be protected. This is especially worrisome in this case because the Debtor proposes to select the Liquidating Trustee and form the Liquidating Trust with insufficient funding. Thus, the Debtor (and the insiders who control the Debtor and the plan process) need only select a "potted plant," with no oversight in place to ensure that the rights and interests of the beneficiaries are protected at all times. In addition to requiring that an oversight committee be appointed, MDA asserts that it, as the Debtor's largest unsecured creditor, should be appointed to the committee, with other committee members selected by the Liquidating Trust beneficiaries, especially where the Plan proposes unilateral selection of the Liquidating Trustee by the Debtor and Khosla Parties.

7. Liquidating Trustee's Exculpation Should Not be Unfettered

The exculpation for the Liquidating Trustee should be limited and not unfettered, as currently proposed in the Plan. Pursuant to the Plan, "[t]he Liquidating Trustee, and its respective professionals, shall be exculpated and indemnified pursuant to and in accordance with the Liquidating Trust Agreement." Plan Art. V.C.10. The Liquidating Trustee's exculpation should be limited and include a carve-out for willful misconduct or gross negligence consistent with the exculpation provision approved by the Third Circuit in *PWS*. *PWS*, 228 F.3d at 246.

8. Transfer of Liquidating Trust Assets Should Include Attorney-Client Privilege

With respect to preservation of confidences and attorney-client privilege, the Debtor's Plan merely provides that "[t]o effectively investigate, defend or pursue the Liquidating Trust

Assets, the Debtor, the Liquidating Trust, the Liquidating Trustee and all counsel thereto, must be able to exchange information with each other on a confidential basis and cooperate in common interest efforts without waiving any applicable privilege." Plan Art.V.C.5. It is unclear, however, from this language if the Liquidating Trust Assets includes all attorney-client privileges associated therewith, which privileges should be transferred to and vest in the Liquidating Trust along with the Liquidating Trust Assets. *See In re Hechinger Inv. Co. of Delaware*, 285 B.R. 601 (D. Del. 2002) (liquidating trust, not debtors' former directors, officers and shareholders, controlled privilege where all estate assets were transferred to liquidating trust and no provision of plan addressed privilege issue). In addition, the language should expressly waive the Debtor's right and the right of any legal, financial or other advisors to assert such rights and privileges as a defense or otherwise.

In *In re Flag Telecom Holdings, Ltd.*, No. 02 CIV. 3400 (WCC), 2009 WL 5245734 (S.D.N.Y. Jan. 14, 2009), the district court held that a litigation trust – not a new, post-confirmation entity to which substantially all the debtor's assets were transferred – controlled the privilege relating to the causes of action transferred to the Trust where the plan expressly transferred such privilege to the Trustee. The *Flag Telecom Holdings* court reasoned that:

> the causes of action that [the debtor] could have brought against its former officers and directors are held exclusively by the trustee. Therefore, the trustee, and no one else, stands in the shoes of [the debtor] in bringing causes of action against former officers and directors. *The control over the attorney-client privilege, and the ability to waive that privilege where appropriate, is of paramount importance in a lawsuit against officers and directors.*

Id. at *9 (emphasis added). The district court further reasoned that:

> "[i]f we find that [the debtor] holds the attorney-client privilege, the practical result is that the trustee, the only entity to which the duty to bring causes of action against former officers and directors of [the debtor] is assigned, would be deprived of a key tool that would otherwise be

> available to a company bringing suit against its officers and directors. *Practically, the entity designated by [the debtor] in the Reorganization Plan with the responsibility of prosecuting officers and directors should control the ability to assert and waive the attorney-client privilege for communications related to those causes of action*."

Id. (emphasis added). The court concluded, "[w]e *find it improper to deprive an entity, in which the duty to sue officers and directors is assigned pursuant to the Reorganization Plan, of control over the attorney-client privilege*." *Id.* (emphasis added).

Without the attorney-client privileges being transferred to the Liquidating Trust, along with the Liquidating Trust Assets, the Liquidating Trust is not really receiving the claims and causes of action. As those claims and causes of action will form the basis for any recoveries for Liquidating Trust beneficiaries, it is imperative that the attorney-client privileges be transferred to the Liquidating Trust so that the Liquidating Trustee can meaningfully pursue those claims and causes of action. Otherwise, the Liquidating Trustee "would be deprived of a key tool that would otherwise be available to a company bringing suit against its officers and directors." *Id.*

9. Notice to Holders of Disputed Claims Should be Required if the Liquidating Trustee Seeks to Extend the Claims Objection Deadline

Pursuant to Article I.B.20 (which defines the "Claims Objection Deadline") of the Plan, the Claims Objection Deadline "may be extended one or more times upon motion by the Liquidating Trustee, *without notice to Holders of Disputed Claims in Class 8 or 9*." Plan Art. I.B.20 (emphasis added). MDA, as a holder of a Class 9 Claim, objects to this definition and believes that any motion filed by the Liquidating Trustee to extend the Claims Objection Deadline should be noticed to all creditors who are beneficiaries of the Liquidating Trust, whether or not such beneficiaries hold Disputed Claims.

10. Definition of Lapsed Challenge Period Claims Should be Modified to Include a Carve-Out for the Liquidating Trustee

The definition of "Lapsed Challenge Period Claims" should be modified to make it clear that such definition does not and shall not include any Challenges timely asserted by the Liquidating Trustee (or other estate fiduciary appointed) within sixty (60) days of appointment of the Liquidating Trustee (or other estate fiduciary). This modification is necessary so that the Plan accurately reflects the Final DIP Order previously entered by this Court, which expressly provides that:

> If a chapter 7 trustee or a chapter 11 trustee or post plan confirmation trustee or other estate fiduciary is appointed, then the Challenge Period [as defined in the Final DIP Order] with respect to such trustee or post plan confirmation trustee or other estate fiduciary only, shall be the date that is sixty (60) calendar days after the date on which such trustee or post plan confirmation trustee or other estate fiduciary is appointed.

Final DIP Order ¶ 6. Without this modification, the Plan should not be confirmed.

G. The Plan Unfairly Discriminates Among Creditors

Section 1129(b)(1) of the Bankruptcy Code requires that a plan proponent prove that its plan is fair and equitable and is not unfairly discriminatory as to the dissenting class. Section 1129(b)(1) also requires that a plan proponent meet all the requirements of Section 1129(a), other than Section 1129(a)(8). The requirement that a plan not discriminate unfairly is designed to "ensure[] that a dissenting class will receive value equal to the value given to all other similarly situated classes." *In re Armstrong World Industries, Inc.*, 348 B.R. 111, 121 (D. Del. 2006) (quoting *In re Matter of Johns-Manville Corp.*, 68 B.R. 618, 636 (Bankr. S.D.N.Y. 1986)).

A plan proponent bears the burden of proving by a preponderance of the evidence that its plan does not discriminate unfairly. *In re Lernout & Hauspie Speech Prods., N.V.*, 301 B.R. 651, 656 (Bankr. D. Del. 2003), *aff'd*, 308 B.R. 372 (D. Del. 2004) ("A nonconsensual plan requires the proponent to prove . . . that the plan does not unfairly discriminate."); *In re Genesis Health Ventures, Inc.*, 266 B.R. 591, 616 n.23 (Bankr. D. Del. 2001); *In re Colfer*, 159 B.R. 602, 608 (Bankr. D. Me. 1993) ("the burden rests on the debtors to persuade the court, by a preponderance of the evidence, that the classification and treatment they propose does not discriminate unfairly").

The Plan is neither fair nor equitable and plainly and unfairly discriminates against the holders of Class 9 General Unsecured Claims. For example, notwithstanding the fact that Classes 7 and 9 are each compromised of non-priority general unsecured claims, *i.e.*, of equal rank and priority, the treatment given to Class 7 Claims guarantees that claimants within that class will receive at least a 50% recovery on account of their allowed claims. On the other hand, the treatment proposed for Class 9 Claims is speculative and wholly dependent upon monetary recoveries, if any, from litigation claims and causes of action being transferred to the Liquidating Trust. Because the Liquidating Trust is so grossly underfunded, it is unlikely that the Liquidating Trustee will have the financial wherewithal to pursue those claims and causes of action to monetary recoveries, all but guaranteeing zero recoveries for Class 9 General Unsecured Creditors. Such disparate treatment is neither fair nor equitable and unfairly discriminates against Class 9 General Unsecured Claims.

In addition to the disproportionate monetary recoveries afforded Class 7 Claims vis-à-vis Class 9 Claims, holders of Class 7 Continuing Trade Claims will also receive a full and complete release from any potential Avoidance Action by the Debtor, the Reorganized Debtor, the Estate or the Liquidating Trust. It is both unfair and inequitable to provide Class 7 claimants with a full release from liability without first understanding what is being given up (*i.e.*, the value of the Avoidance Action claims being released) in relation to the value of any continuing trade credit being provided to the Reorganized Debtor. Casting further doubt as to the validity of the proposed Class 7 treatment is the fact that (i) only 15 "trade" creditors are eligible for Class 7 treatment, six (6) of which appear to be professionals employed by the Debtor and (ii) the Debtor retains sole discretion as to whether the amount and terms of the continuing trade credit is satisfactory. In short, the Debtor is getting to pick and choose, in its sole discretion and without providing *any* disclosure of the value of the claims being released in relation to the value being provided to the Reorganized Debtor in exchange for those releases, which general unsecured creditors will receive the favorable treatment afforded Class 7 Claims. Because the proposed treatment of Class 9 General Unsecured Claims is materially worse than the treatment afforded all other similarly situated classes of non-priority general unsecured claims under the Plan, the Plan is not fair and equitable and unfairly discriminates against MDA and the other holders of Class 9 General Unsecured Claims.

The Debtor cannot demonstrate that the proposed discrimination against holders of Class 9 General Unsecured Claims is "fair." When determining whether discrimination under a proposed plan is "fair," courts in this district focus on two factors: (i) "whether there is a reasonable basis for the discrimination;" and (ii) "whether the debtor can confirm and consummate a plan without the proposed discrimination. *See In re Tribune Co.*, 476 B.R. 843, 865 (Bankr. D. Del. 2012), *aff'd as modified*, *Wilmington Trust Co. v. Tribune Co. (In re Tribune Co.)*, 2014 WL 2797042 (D. Del. June 18, 2014); *In re Exide Tech.*, 303 B.R. 48, 78 (D. Del. 2003); *Genesis Health Ventures, Inc.*, 266 B.R. at 611.

As stated above, it is the Debtor's burden to prove by a preponderance of the evidence that the Plan is fair and equitable and does not unfairly discriminate. The Debtor has not and cannot meet this burden. The Debtor has failed to offer any reasonable basis for the materially worse treatment afforded holders of Class 9 General Unsecured Claims under the Plan vis-à-vis holders of Class 7 Continuing Trade Claims. Nor has the Debtor provided any evidence that the separate classification of Class 9 General Unsecured Claims and the proposed treatment of holders of Class 9 General Unsecured Claims is reasonable and necessary to consummate its Plan.

The Debtor has provided no reasonable basis for, and MDA and the other holders of Class 9 General Unsecured Claims have not consented to, the disparate and unfair treatment afforded holders of Class 9 General Unsecured Claims under the Plan. The Debtor wholly fails to sustain its burden to prove by a preponderance of the evidence that its discrimination against the holders of Class 9 General Unsecured Claims is fair and reasonable. Accordingly, the Plan is neither fair nor equitable and unfairly discriminates against MDA and the other holders of Class 9 General Unsecured Claims and cannot be confirmed under section 1129(b) of the Bankruptcy Code.

H. <u>The Debtor Has Failed To Provide A Reasonable Basis For Separately Classifying General Unsecured Claims.</u>

Class 7 under the Plan is composed of fifteen creditors with claims totaling $1,740,181 and who are referred to as "continuing trade creditors". Yet at least two of these "trade creditors," WilmerHale and Price Waterhouse, are professionals of the Debtor with claims that total $1,332,597, representing 76.5% of the Class. The Class is called "trade creditors", but all members of the Class appear to be attorneys, accountants, and staffing services, and they have to "elect to provide trade credit to the Reorganized Debtor from and after the Effective Date, in the greatest amount and or the most favorable terms and conditions that such Trade Creditor was providing to the Debtor during the ninety (90) days before the Petition Date, for at least twelve (12) months after the Effective Date." Disclosure Statement, page 32.

Upon information and belief, the dominant claim in Class 7 belongs to the law firm of WilmerHale, which serves as special counsel to the Debtor, as well as counsel to the Khosla Parties in matters such as litigation with the State of Mississippi and the SEC investigation. WilmerHale holds $1,184,696 in prepetition claims or 68% of the Class and control the Class.

In addition, the Plan improperly attempts to create a convenience Class in Class 8. Among other things, based on the Debtor's schedules, the unsecured claims against the Debtor do not appear to be so numerous as to justify creation of a convenience class. The apparent reason for the Class 7 and Class 8 constructs is to gerrymander consenting impaired classes for purposes of attempting inappropriately to confirm a plan over the objection of arms-length general unsecured creditors in Class 9.

Pursuant to Bankruptcy Code section 1122(a) "a plan may place a claim or an interest in a particular class only if such claim or interest is substantially similar to the other claims or interests of such class." 11 U.S.C. § 1122(a). As noted by the Sixth Circuit in a seminal classification case, "[t]he statute [section 1122], by its express language, only addresses the problem of dissimilar claims being included in the same class. It does not address the correlative problem--the one we face here--of similar claims being put in different classes." *Teamsters Nat'l Freight Indus. Negotiating Comm. v. U.S. Truck Co., Inc. (In re U.S. Truck Co., Inc.)*, 800 F.2d 581, 585 (6th Cir. 1986).

As the Bankruptcy Code itself does not provide guidance on the issue of separate classification of similar claims, courts have developed tests to determine if a debtor's proposed classification scheme is permissible. Primary among such tests is that a debtor may not "gerrymander" classes in order to obtain an affirmative vote on its plan. *See*, *e.g.*, *Boston Post Rd. Ltd. P'ship v. FDIC (In re Boston Post Rd. Ltd. P'ship)*, 21 F.3d 477, 481 (2d Cir. 1994) cert. denied, 513 U.S. 1109 (1995) ("similar claims [may] not be placed in different classes solely to gerrymander a class that will assent to the plan"); *Phoenix Mut. Life Ins. Co. v. Greystone III Joint Venture (In re Greystone III Joint Venture)*, 995 F.2d 1274, 1279 (5th Cir. 1991) cert. denied, 506 U.S. 821 (1992) ("[T]hou shalt not classify similar claims differently in order to gerrymander an affirmative vote on a reorganization plan."). The supporting rationale has been explained by the Sixth Circuit:

> [T]here must be some limit on a debtor's power to classify creditors in such a manner. The potential for abuse would be significant otherwise. Unless there is some requirement of keeping similar claims together, nothing would stand in the way of a debtor seeking out a few impaired creditors (or even one such creditor) who will vote for the plan and placing them in their own class.

U.S. Truck, 800 F.2d at 586.

Moreover, courts have noted that allowing a debtor unlimited discretion to classify similar claims separately would render Bankruptcy Code section 1129(a)(10) meaningless. *See John Hancock Mut. Life Ins. Co. v. Route 37 Bus. Park Assocs.*, 987 F.2d 154, 158 (3d Cir. 1993) ("[I]t seems clear that the Code was not meant to allow a debtor complete freedom to place substantially similar claims in separate classes. The critical confirmation requirement[] set out in . . . Section 1129(a)(10) (acceptance by at least one impaired class in the event of a 'cram down') would be seriously undermined if a debtor could gerrymander classes."). Where, as here, a plan is devised for the purpose of manipulating the vote on such plan, that plan cannot be confirmed. *Id.* at 157 (holding plan of reorganization that contains "an impermissible classification scheme for unsecured claims [has] no reasonable prospect of confirmation.") *Id.*

Courts within the Third Circuit have considered whether a plan may classify similar claims in different classes without running afoul of section 1122(a) of the Bankruptcy Code. These courts have held that although section 1122(a) does not prohibit placing similar claims in separate classes, the debtor may not take advantage of this lack of prohibition to disenfranchise creditors. "[T]he Code was not meant to allow a debtor complete freedom to place substantially similar claims in separate classes. The critical confirmation requirements . . . would be seriously undermined if a debtor could gerrymander classes." *Route 37*, 987 F.2d at 158. Thus, the legal standard in the Third Circuit for separating similar claims is one of "reasonableness." *In re Coastal Broadcasting Systems, Inc., 570 Fed.Appx. 188, 193* (3d Cir. 2014) ("Although not explicit in § 1122, a corollary to that rule is that the 'grouping of similar claims in different classes' is permitted so long as the classification is 'reasonable.'"); *see Route 37*, 987 F.2d at 158; *see also In re Jersey City Med. Ctr.*, 817 F.2d 1055, 1061 (3d Cir. 1987) (noting that, although similar claims may be permitted to be classified separately, "the classification of the claims or interests must be reasonable.").

"[I]n determining whether a classification scheme is reasonable…this determination must be informed by the two purposes that classification serves under the Code: voting to determine whether a plan can be confirmed and treatment of claims under the plan." *Route 37*, 987 F.2d at 159 (internal citations omitted). However, the size of claim, the way in which the claim arises, and the subjective anticipation of payment alone cannot determine whether it is reasonable to separate similar claims into different classes. *See Fairfield Executive Assocs. v. Hyperion Credit Capital Partners, L.P. (In re Fairfield Executive Assocs.)*, 161 B.R. 595, 601-03 (D.N.J. 1993). In analyzing the classification of claims, the "primary analysis centers upon the legal attributes of the claims and not upon the status or circumstances of the claimant. Emphasis is not upon the holder so much as it is upon that which is held." *In re Coram Healthcare Corp.*, 315 B.R. 321, 349 (Bankr. D. Del. 2004) (quoting *In re FF Holdings Corp. & Farm Fresh, Inc.*, 1998 U.S. Dist. LEXIS 10741, at *13 (D. Del. Feb. 17, 1998)).

"Unsecured claims will, generally speaking, comprise one class, whether trade, tort, publicly held debt or a deficiency of a secured creditor." *In re Pine Lake Vill. Apartment Co.*, 19 B.R. 819, 830 (Bankr. S.D.N.Y. 1982) (Quoting 3 Norton Bankr. L. & Prac., § 60.05), *reh'g denied*, 21 B.R. 478 (Bankr. S.D.N.Y. 1982) (emphasis in original); *see also In re One Times Square Assocs. Ltd. P'ship*, 159 B.R. 695, 703 (Bankr. S.D.N.Y. 1993), *aff'd*, 165 B.R. 773 (S.D.N.Y. 1994) ("Generally, unsecured creditors are claimants of equal rank, entitled to share, pro rata, in the values remaining after the payment of secured and priority claims."); *In re 266 Wash. Assocs.*, 141 B.R. 275, 282 (Bankr. E.D.N.Y. 1992), *aff'd*, 147 B.R. 827 (E.D.N.Y. 1992) ("Generally, unsecured creditors hold substantially similar claims; they are claimants of equal legal rank entitled to share pro rata in values remaining after payment of secured and priority claims."). Separate classifications for unsecured creditors are only justified "where the legal character of their claims is such as to accord them a status different from the other unsecured creditors." *In re Lisanti Foods, Inc.*, 329 B.R. 491, 510 (D.N.J. 2005) *aff'd*, 241 Fed. Appx (3d Cir. 2007) (citing *Granada Wines, Inc. v. New England Teamsters & Trucking Indus. Pension Fund*, 748 F.2d 42, 46 (1st Cir. 1984)).

Here, the Plan impermissibly and unreasonably separately classifies general unsecured trade claims from all other general unsecured claims. MDA holds a non-priority general unsecured claim against the Debtor and its estate and has the same legal rights against the Debtor as all other holders of non-priority general unsecured claims. The fact that the holders of trade claims are trade creditors rather than another type of general unsecured claimant is not relevant in the context of classification. Rather, the focus is on the legal attributes of the underlying claims, which are substantially identical in this case (*i.e.*, general unsecured claims). In *In re Coram Healthcare Corp.*, the court held improper the separate classification of the following three classes of unsecured creditors: noteholders, general unsecured trade creditors, and general unsecured creditors that performed services for the debtor under one particular contract. 315 B.R. 321, 349-50 (Bankr. D. Del. 2004). In determining that the trade creditors could not be separately classified from the general unsecured creditors performing services pursuant to a particular contract, the court noted that "each class must represent a voting interest that is sufficiently . . . weighty to merit a separate voice in determining whether the proposed reorganization should proceed[.]" *Id.* at 349 (citing *Route 37*, 987 F.2d at 159). Since the claims of the trade creditors and the creditors under a contract for services were substantially similar in their legal attributes and priority status, *i.e.*, non-priority general unsecured claims, they were not entitled to separate classification. *Id.*

Similarly, in *In re Torgro Atl. City, LLC*, a bankruptcy court held that classifying the unsecured creditors of the estate into four classes was not reasonable under the circumstances. No. 08-13458 (GMB), 2009 WL 1288367, at *13 (Bankr. D.N.J. May 7, 2009). The proposed plan divided unsecured creditors into the following four classes: (i) trade creditors whose claims arose in the debtor's ordinary course of business and whom the debtor may continue to do business with in the future, (ii) trade creditors whose claims are not related to the debtor's ordinary business operations and that the debtor does not foresee doing business with in the future, (iii) creditors whose claims arose through litigation against the debtor, and (iv) insider creditors with intercompany loans with the debtor. *Id.* at *12. The court determined that any perceived distinctions among the first three of these classes were irrelevant and would not be considered because, for purposes of classification, what matters is their legal status as unsecured creditors of the debtor. *Id.* In so holding, the court cited to the Second Circuit's holding in *In re Boston Post Rd. Ltd. P'ship*, where the court noted that "approving a plan that aims to disenfranchise the overwhelmingly largest creditor through artificial classification is simply inconsistent with the principles underlying the Bankruptcy Code. A key premise of the Code is that creditors holding greater debt should have a comparably greater voice in reorganization." 21 F.3d at 483. The Debtor's classification scheme in this case disenfranchises MDA, the overwhelming largest unsecured creditor of the Debtor, and all but guarantees that MDA will not have a comparably greater voice in the proposed reorganization. This is neither reasonable nor proper.

In short, the Plan separates similarly situated general unsecured creditors into artificial classes for the purposes of gerrymandering plan voting and distributing the Debtors' assets unequally among unsecured creditors of equal priority and rank. The Debtor's classification scheme is nothing more than an attempt to silence MDA and artificially guarantee acceptance from at least one class of impaired claims. For these reasons, the separation classification of general unsecured trade claims is not reasonable and the Plan cannot be confirmed.

I. **The Plan Is Not Proposed In Good Faith─A Proper Bankruptcy Purpose Is Required**

Among the express requirements of Section 1129(a) is that the plan is proposed in good faith and not by any means forbidden by law. 11 U.S.C Section 1129(a)(3). In the plan confirmation context, good faith has been construed by the courts as requiring that a proposed plan have a reasonable likelihood of achieving a result consistent with the objectives and purposes of the Bankruptcy Code. *See, e.g., In re Madison Hotel Associates*, 749 F.2d. 410, 424-25 (7th Cir. 1984). The good faith requirement has also been construed as requiring fundamental fairness. *See, e.g., In re PWS Holding Corporation*, 228 F.3d 224 (3rd Cir. 2000); *In re Lernout & Hauspie Speech Products, N.V.*, 308 B.R. 672, 675 (D. Del. 2004).

As the bankruptcy court in *In re Brown*, 498 B.R. 486 (Bankr. E.D. Penn. 2013) explained:

> Recognizing that "**good faith**" under section 1129(a)(3) is not defined, the Third Circuit has adopted the Seventh Circuit's definition of this confirmation requirement. *In re Abbotts Dairies of Pennsylvania, Inc.,* 788 F.2d 143, 150 n. 5 (3d Cir.1986):
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>> "[F]or purposes of determining **good faith** under section 1129(a)(3) ... the important point of inquiry is the plan itself and whether such a plan will fairly achieve a result consistent with the objectives and purposes of the Bankruptcy ***494** Code." The purpose of requiring such a finding ... prevents a debtor-in-possession or trustee from effectively abrogating the creditor protections of Chapter 11.
>
> (quoting *In re Madison Hotel Assocs.,* 749 F.2d 410, 425 (7th Cir.1984)); *see In re Federal–Mogul Global Inc.,* 684 F.3d 355, 381 (3d Cir.2012); *In re Combustion Engineering, Inc.,* 391 F.3d 190, 247 (3d Cir.2004); *In re PWS Holding Corp.,* 228 F.3d 224, 242 (3d Cir. 2000)).
>
> The Court of Appeals has further explained the objectives and purposes that the **good faith** requirement of section 1129(a)(3) is intended to protect:
>
>> Specifically, under Chapter 11, the two "recognized" policies, or objectives, are "preserving going concerns and maximizing property available to satisfy creditors[.]" *Bank of Am. Nat.'l Trust and Sav. Ass'n v. 203 N. LaSalle St. P'ship,* 526 U.S. 434, 453, 119 S.Ct. 1411, 143 L.Ed.2d 607 (1999) (citing *Toibb v. Radloff,* 501 U.S. 157, 163, 111 S.Ct. 2197, 115 L.Ed.2d 145 (1991)). More generally, the Bankruptcy Code's objectives include: "giving debtors a fresh start in life," *Walters v. U.S. National Bank of Johnstown,* 879 F.2d 95, 98 (3d Cir.1989), "discourag[ing] debtor misconduct," *id.,* "the expeditious liquidation and distribution of the bankruptcy estate to its creditors," *Integrated Solutions, Inc. v. Service Support Specialties,* 124 F.3d 487, 489 (3d Cir.1997), and achieving fundamental fairness and justice. *In re Kaiser Aluminum Corp.,* 456 F.3d 328, 339–43 (3d Cir.2006).
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> *In re American Capital Equipment, LLC,* 688 F.3d 145, 157 (3d Cir.2012) (parallel citations omitted); *see, e.g., In re WR Grace & Co.,* 729 F.3d 332, 346–47 (3d Cir.2013).

Similarly, in the context of Section 1112 (*Conversion or Dismissal*), the Third Circuit has held that the proper purposes of chapter 11 reorganization include rehabilitation of the debtor's business, preservation of a viable enterprise, and maximizing value of the estate for the benefit of *all* creditors and parties in interest. *See, e.g.*, *In re 15375 Memorial Corp.*, 589 F.3d 605 (3d Cir. 2009); *.NMSBPCSLDHB, L.P. v. Integrated Telecom Express, Inc. (In re Integrated Telecom Express, Inc.)*, 384 F.3d 108 (3d Cir. 2004) (citing *Official Comm. of Unsecured Creditors v. Nucor Corp. (In re SGL Carbon Corp.),* 200 F.3d 154 (3d Cir. 1999)). While the timing of the inquiries may be different, good faith analysis under Section 1129(a)(3) is similar to and arguably dovetails with good faith analysis under 11 U.S.C. Section 1112. *See, for example*, *In re PPI Enterprises*, 324 F.3d 197, 210-11 (3rd. Cir. 2003); *In the Matter of Madison Hotel Associates*, 794 F.2d 410 (7th Cir. 1984). A more robust discussion of the legitimate aims of chapter 11 as articulated by the Third Circuit in cases under Section 1112 is included in the MDA's Motion to Convert or Dismiss [Docket No. 168], which is set to be heard at the same time as this Objection.

In the instant case, no true reorganization is being pursued. The Plan does not propose to rehabilitate the Debtor or preserve the estate for the benefit of creditors and parties in interest. There is no viable business enterprise which the Plan will preserve or create. There is nothing in the Plan which suggests that its implementation will cause the Debtor to achieve financial viability. There is no projection of any revenues at any time.

In fact, even by the reckoning of the Khosla Parties, the Debtor has not achieved so much as experimental benchmarks in the laboratory which would justify further investment to attempt to commercialize its speculative technology. This fact is driven home by the yet to be achieved threshold "experimental benchmarks" upon which further funding by the Khosla Parties under the DIP and the proposed exit funding are conditioned.

The Khosla Parties are spending millions upon millions of dollars in professional fees and other administrative costs to accomplish nothing that could not have been accomplished more efficiently and more equitably via a sale of the Debtor's assets under Section 363 of the Bankruptcy Code. This Plan makes no business sense.

In such circumstances, the purpose of the Plan can only be to provide insiders with protections against liability for their prepetition conduct, and, perhaps, preserve potential net operating loss tax attributes for the benefit of the Khosla Parties. These are not legitimate reasons to confirm a plan. *See, e.g., In re Maxim Industries, Inc.*, 22 B.R. 611 (Bankr. D. Mass. 1982); *Marsch v. Marsch*, 36 F.3d 825 (9th Cir. 1994)

A chapter 11 case cannot properly be conducted for the sole benefit of insiders, or even for the benefit of a limited number of parties in interest. The MDA submits, however, that the proposed Plan make clear that the aim of the Debtor and its insiders in this case is not to rehabilitate the Debtor or to maximize the estate for the benefit for *all* creditors, but to defeat the rights and claims of arms-length creditors and investors, while improperly shielding the Debtor's insiders with inappropriate protections from liability. This is not a proper bankruptcy purpose and the Plan should not be confirmed. Rather, as set forth in the MDA's Motion to Convert or Dismiss [Docket No. 168], a trustee should be appointed and/or the case converted or dismissed.

J. The Plan Includes Inappropriate Releases

The Plan is unconfirmable because, *inter alia,* it contains impermissible third party releases and purports to discharge and release, among others, the Debtor's directors and officers, insiders of the Debtor and other non-debtors without consideration, when colorable claims and other causes of action exist against them.

Article X.D of the Plan purports to release all claims against the Released Parties, which definition includes certain non-debtor parties.[16] This release provision covers claims of third-party creditors and, thus, is inappropriate and overly broad. The Debtor fails to specifically identify what persons and entities are being released under the Plan, nor is it even clear what

[16] Specifically, Article X.D of the Plan states:

> As of the Effective Date, for good and valuable consideration, unless otherwise noted on its ballot, each Holder of a Claim that has affirmatively voted to accept the Plan, shall be deemed to have unconditionally released and discharged the Released Parties from any and all Claims, obligations, rights, suits, damages, causes of action, remedies and liabilities whatsoever, including any Claims or Causes of Action that have been or could be asserted by or on behalf of the Debtor or the Estate or that are derivative or duplicative of any such Claims or Causes of Action, whether known or unknown, foreseen or unforeseen, existing or hereafter arising, in law, equity or otherwise, that such Holder of a Claim could have been legally entitled to assert in its own right (whether individually or collectively), based in whole or in part upon any act or omission, transaction, agreement, event or other occurrence taking place on or before the Effective Date, in any way relating or pertaining to (w) the purchase or sale, or the rescission of a purchase or sale, of any security of the Debtor, (x) the Debtor or the operation or conduct of the business of the Debtor, (y) the Chapter 11 Case and/or (z) the negotiation, formulation and preparation of the Plan, or any related agreements, instruments or other documents; provided that these releases will have no effect on the liability of any Released Party arising from any act, omission, transaction, agreement, event or other occurrence, constituting fraud, criminal conduct, gross negligence or willful misconduct. The releases set forth in this paragraph shall be binding upon and shall inure to the benefit of the Liquidating Trustee and any other successor to the Debtor or the Estate. Each ballot will have a place for a party to opt out of the release provided herein. Nothing in the foregoing or elsewhere in the Plan constitutes a waiver or release of (1) any claim, right, or causes of action that any Creditor or other Person or Entity owns and holds for its own account against KiOR Columbus; or (2) any right to receive distributions from the Liquidating Trust or of any portion of a Claim supporting such right.

Plan Art. X.D. Article I.B.92 defines the Released Party or Released Parties as:

> "Released Party" or "Released Parties" means the Debtor, the Estate, each of the Plan Support Parties, each of the DIP Lenders, the DIP Agent, each of the Prepetition Lenders, each of the Prepetition Agents, and each of their respective successors and predecessors and current and former control persons, trustees or beneficiaries, direct or indirect shareholders or members, officers, directors, employees, affiliates, principals and agents (and each of their respective attorneys, consultants, financial advisors, investment bankers, accountants, and other retained professionals), in each case solely in their capacities as such.

Plan Art. I.B.92.

claims are being released. Furthermore, there is no analysis whatsoever regarding the value of the claims being released vis-à-vis the consideration, if any, being provided for such releases.

In addition, Article X.C of the Plan purports to release all Avoidance Actions that have been or could be asserted against a vendor, supplier or other Trade Creditor that becomes a holder of a Class 7 Continuing Trade Claim.[17] As with the improper releases of non-debtor Released Parties, this release provision likewise fails to specifically state what, if any, consideration is being provided in exchange for the releases. Because the Plan provides no detailed analysis as to the value of the Avoidance Actions the estate is waiving against these parties in return, it is impossible to understand the economic effect of such releases on the recoveries for general unsecured creditors. There is no showing made that these releases are necessary to carry out or implement the terms of the Plan. Nor is there any analysis proffered that supports release of the Avoidance Actions as against holders of Class 7 Continuing Trade Claims. Finally, the release provision set forth in Article X.C of the Plan should not extend to professionals.

Accordingly, the release provisions set forth in the Plan are improper, thereby rendering the Plan unconfirmable.

K. <u>The Exculpation Provisions Are Impermissibly Broad</u>

The exculpation provisions in Article X.G of the Plan are likewise unconfirmable because they are too broad and are not supported by controlling case law. The Third Circuit in *In re PWS Holding Corp.* set the standard for exculpation-type release provisions such as the one

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[17] Article X.C of the Plan provides:

> All Avoidance Actions that have been or could be asserted against a vendor, supplier or other Trade Creditor that becomes a holder of a Class 7 Continuing Trade Claims shall be forever waived, released and extinguished under the Plan.

Plan Art. X.C.

set forth in Article X.G of the Plan. 228 F.3d 224 (3d Cir. 2000). In *PWS*, the Third Circuit approved an exculpation provision in a plan that provided for the debtors, the reorganized debtors, the official committee of unsecured creditors and each of their respective members, officers, directors, employees, advisors, professionals or agents would not incur any liability, except for willful misconduct or gross negligence, arising out of "the Chapter 11 Cases, the pursuit of confirmation of the Plan, the consummation of the Plan or the Administration of the Plan or the property to be distributed under the Plan." *Id.* at 246.

Here, the exculpation provision at issue fails to include a carve-out for willful misconduct or gross negligence, as required by *PWS*. Moreover, the exculpation provision in the Debtor's Plan purports to impermissibly extend the exculpation of liability to "any other prepetition or postpetition act taken or omitted to be taken in connection with, or in contemplation of, the restructuring of the Debtor or the Chapter 11 Case." Plan Art. X.G. As written, the Debtor's exculpation provision would extend the exculpation of liability to almost anything, whether prepetition or postpetition, in direct contravention of *PWS*, which limits exculpation to acts taken or not taken in connection with a plan and the chapter 11 case. *See PWS*, 228 F.3d at 246. Thus, the exculpation provision is too broad and goes well beyond the exculpation provision approved in *PWS*, and should not be approved as written.

L. <u>Proposed Treatment For Classes 1, 2 And 3 Could Lead To Double Recoveries</u>

It is a general rule of law and equity that a claimant is entitled to recovery once on account of a claim. Under this rule, often referred to as the "single satisfaction" rule, a claimant that is satisfied with respect to all of its losses cannot assert a second claim for those losses. This horn book rule has long-standing Supreme Court precedent.

In *Ivanhoe Bldg. & Loan Assn. v. Orr*, 295 U.S. 243 (1935), a debtor had previously executed a bond to a creditor, which was secured by a mortgage on real estate owned by a non-debtor. The creditor eventually purchased the real estate at a foreclosure sale. Notwithstanding the fact that the creditor held the collateral in partial payment for its debt, the creditor nonetheless filed a claim for the full amount of the debtor's obligation under the bond. The Supreme Court held that the claim was valid even though the creditor held property that partially satisfied the claim. Importantly, however, the Supreme Court expressly clarified that the creditor "may not collect and retain dividends which with the sum realized from the foreclosure will more than make up that amount." *Id.* at 246. Thus, *Ivanhoe* holds that while a creditor may file a proof of claim for the total amount it is owed by a debtor (notwithstanding the fact that it has recovered or may recover all or a portion of that amount from a non-debtor), the creditor may not collect more, in total, than the amount the creditor is owed. *Accord Board of Commissioners v. Hurley*, 169 F.92, 97 (8th Cir. 1909) ("[T]he holder of a claim, upon which several parties are personally liable, may prove his claim against the estates of those who become bankrupt and may at the same time pursue the others at law, and, notwithstanding partial payments after the bankruptcy by other [parties] or their estates, he may recover dividends from each estate in bankruptcy upon the full amount of his claim at the time the petition in bankruptcy was filed therein *until from all sources he has received full payment of his claim, but no longer*.") (emphasis added).

The Debtor's Plan runs afoul of this deeply rooted Supreme Court precedent. Under the Plan, the treatment and any distributions for holders of Class 1, 2 and 3 claims "shall not reduce, waive or diminish, or otherwise affect, KiOR Columbus' separate liability with respect to [Classes 1, 2 and 3], all of which claims, and any and all existing liens and security interests securing such claims in favor of holders of [Class 1 through 3] Claims remain outstanding and enforceable against KiOR Columbus and its assets after confirmation of the Plan." Plan Art.

III(B)(1 - 3). Importantly, the Plan is silent with respect to limiting recoveries for holders of Class 1, 2 and 3 Claims to a "single satisfaction."

Unless language is added to the Plan which expressly states that holders of Class 1, 2 and 3 Claims are entitled to only a "single satisfaction" on account of their claims, the Plan should not be confirmed. This is especially true in this case where the current proposed treatment could unfairly lead to double-recoveries for holders of Class 1, 2 and 3 Claims, all of whom control the Debtor and the plan process. In short, the Class 1, 2 and 3 insiders have devised a plan that unfairly benefits them to the detriment of other legitimate creditors who are not afforded such favorable treatment. The preferential treatment for those who control the plan process should not be condoned by this Court.

III. RESERVATION OF RIGHTS

The MDA reserves its rights to supplement or amend this Objection at any time and for any reason, or file additional Objections, as necessary or appropriate should the Debtor file a further amended chapter 11 plan of reorganization.

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IV. CONCLUSION

For the reasons stated herein, the MDA respectfully requests that the Court deny confirmation of the Debtor's Plan.

Respectfully submitted, this 20th day of May, 2015.

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