UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF LOUISIANA
LAFAYETTE DIVISION

In re:	§	**Case No. 12-51127**
	§	
Piccadilly Restaurants, LLC, *et al*.,	§	**(Joint Administration)**[1]
	§	
	§	**Chapter 11**
Debtors	§	
	§	**Judge Robert Summerhays**

ATALAYA'S SUPPLEMENTAL MEMORANDUM OF LAW IN SUPPORT OF CONFIRMATION OF THE FIRST AMENDED JOINT CHAPTER 11 PLAN AND RESPONSE TO CONFLICTS OF INTEREST INHERENT IN THE TERMS OF IMPERIAL CAPITAL LLC'S ENGAGEMENT

Atalaya Administrative, LLC, Atalaya Funding II, LP, Atalaya Special Opportunities Fund IV, LP (Tranche B), and Atalaya Special Opportunities Fund (Cayman) IV, LP (Tranche B) (collectively, "Atalaya") submit this supplemental memorandum in support of plan confirmation in order to highlight significant conflicts of interest stemming from contingent valuation compensation payable to Imperial Capital LLC ("Imperial Capital") -- the sole valuation expert designated by the only party that has opposed plan confirmation, Yucaipa Corporate Initiatives Fund I, L.P. ("Yucaipa"). In further support of plan confirmation, Atalaya respectfully states as follows:

1. The Court has scheduled a hearing, to be conducted on January 13 and 14, 2014, to consider confirmation of the *First Amended Joint Chapter 11 Plan of Piccadilly Investments, LLC, Piccadilly Restaurants, LLC and Piccadilly Food Service, LLC* (the "Plan," Docket No. 1241),[2] which has been jointly proposed by Atalaya and the Official Committee of Unsecured Creditors (the "Committee"). As Atalaya explained in its prior memorandum of law (the "Plan

[1] Jointly administered with *In re Piccadilly Food Service, LLC*, 12-51128 (Bankr. W.D. La. 2012), and *In re Piccadilly Investments, LLC*, 12-51129 (Bankr. W.D. La. 2012).

[2] Capitalized terms not otherwise defined herein shall have the meaning ascribed to them in the Plan.

Brief," Docket No. 1342), the sole source of opposition to the Plan comes from the Debtors' prepetition equity holders, Yucaipa, who allege that their equity interests in the Debtors are "in the money" and cannot be extinguished pursuant to the Plan.

2. Yucaipa's sole evidentiary source for such allegations is a valuation report prepared by Imperial Capital, for Yucaipa's benefit, which alleges that the enterprise value of the Debtors falls between $48 million and $59 million. As set forth in the Plan Brief, Imperial Capital's valuation report relies on stale, outdated financial projections and is replete with mathematical and methodological errors.

3. Yet, even more troubling than the methodology flaws inherent in the Imperial Capital report, Atalaya has recently discovered[3] that Imperial Capital agreed to furnish the valuation report to Yucaipa in exchange for a contingent fee. Specifically, instead of receiving a set fee for valuation services (as is customary for valuation experts), the engagement letter between Yucaipa and Imperial Capital provides that Yucaipa has the sole discretion to set Imperial Capital's compensation for valuation services at any amount within a broad range. The upper end of that range is almost *60% higher* than the lower end of the range.

4. Courts around the nation have consistently held that the views of valuation experts engaged pursuant to contingent compensation arrangements are highly suspect, generally discrediting the views of such "contingent fee" experts. The bankruptcy court in the *TOUSA* bankruptcy case found that:

> The [expert's] solvency opinion is unpersuasive for several reasons - first, because of the circumstances of its creation. … The [expert's] solvency opinion was a contingent fee arrangement . . . .

[3] The contingent nature of Imperial Capital's compensation was not revealed to Atalaya until it received supplemental discovery responses from Yucaipa after 5:00 p.m. on Friday, January 10, 2013. Because Atalaya did not discover this information until after it submitted its Plan Brief, Atalaya was not able to incorporate analysis of this issue within its Plan Brief.

Creditors of TOUSA, Inc. v. Citicorp N. Am., Inc., 422 B.R. 783, 839-40 (Bankr. S.D. Fla. 2009). Likewise, a New York bankruptcy court, in assessing an expert's opinion, found that:

> [expert's] submission was seriously undermined by the fact that his compensation from [equity] is contingent . . . . a court is entitled to discredit anything said by an expert compensated by such an arrangement.

In re Granite Broadcasting Corp., 369 B.R. 120, 142 (Bankr. S.D.N.Y. 2007).

5. Notably, this case will not be the first time that Imperial Capital has agreed to a contingent compensation arrangement for valuation services, of which courts are universally suspect. Rather, Atalaya has discovered two other instances where courts have criticized Imperial Capital's decision to agree to such contingent compensation arrangements and have disregarded the validity of Imperial Capital's valuation testimony as a result of the conflict of interest inherent in such contingent compensation arrangements.

6. The first case occurred in March of 2006, in *Milfam II LP v. Am. Commercial Lines, LLC*, Case No. 4:05-cv-0030, 2006 WL 3247149 (S.D. Ind. Mar. 30, 2006)(a copy of the case is attached). In that case, much like this one, Imperial Capital agreed to provide valuation services to a group of dissident equity holders that were opposing plan confirmation. The contingent compensation structure incentivized Imperial Capital to arrive at an enterprise value substantially above the value arrived at by the two other expert witnesses retained in that case (who did not receive contingent fees for their valuation services). Due to the conflicts of interest inherent with contingent expert compensation, the bankruptcy court discredited Imperial Capital's valuation testimony. In affirming the bankruptcy court's ruling, on appeal the district held:

> This highly unusual contingent fee for an expert witness raises obvious questions of credibility. . . . [T]he Bankruptcy Court was entitled to discredit anything [Imperial Capital] said on the basis of this unusual arrangement.

Milfam II LP, 2006 WL3247149 at *2-3 (emphasis added).

7. Less than six months after the district court's admonishment of Imperial Capital's contingent fees in the *Milfam* case, another bankruptcy court found Imperial Capital's testimony lacked credibility due to its contingent fee arrangement. In *Oneida Ltd.*, equity holders again sought to employ Imperial Capital to establish a "high" enterprise value for the debtors' estate, in order to oppose confirmation of a plan that proposed to wipe out prepetition equity. *In re Oneida Ltd.*, 351 B.R. 79 (Bankr. S.D.N.Y. 2006). After the *Oneida* court discovered that Imperial Capital had entered into a contingent fee, Imperial Capital's valuation opinion in *Oneida* was again disregarded. Specifically, the Court held:

> In addition to problems with his valuation methodology, [expert's] credibility was successfully challenged by the Plan proponents. Most significantly, [expert's] employer, *Imperial Capital*, entered into a contingency agreement . . . This contingent fee, and the circumstances surrounding it, seriously undermine [Imperial Capital expert's] credibility.

Id. at 92 (emphasis added).

8. The combination of the methodological flaws inherent in Imperial Capital's valuation report, and the contingent, suspect nature of its compensation arrangement, confirm that this Court should give little to no weight to Imperial Capital's valuation analysis. Indeed, these two factors may be interrelated, as the contingent nature of Imperial Capital's valuation fee likely incentivized Imperial Capital to rely upon the heroic, unsupportable assumptions that appear throughout its valuation report, with the hopes of producing a "high" valuation that would please Yucaipa and increase Imperial Capital's chances of being compensated at the "high" end of the compensation spectrum controlled entirely by Yucaipa.

WHEREFORE, for the reasons set forth herein and in the Plan Brief, Atalaya respectfully requests that this Court (i) discredit any valuation analysis put forth by Imperial Capital; (ii)

confirm the Plan, (iii) enter the Confirmation Order, and (iv) grant Atalaya such other and further relief as the Court deems just and proper both at law and in equity.

Dated: January 13, 2014

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