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and Trace Technologies, LLC, Debtors

7 IN THE UNITED STATES BANKRUPTCY COURT
8 FOR THE NORTHERN DISTRICT OF CALIFORNIA
9 SAN FRANCISCO DIVISION

10 In re

11 GABRIEL TECHNOLOGIES CORP. et al.,

12 Debtors.

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17 E.I.N.s 22-3062052; 20-1711149

Case No. 13-30340 - DM
(Case no. 13-30341)

Chapter 11

(Jointly Administered)

Date: July 30, 2013
Time: 1:30 p.m.
Court: Courtroom No. 22
235 Pine Street, 22nd Floor
San Francisco, CA
Judge: Honorable Dennis Montali

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20 **DEBTORS' REPLY TO OBJECTION OF UNITED STATES TRUSTEE TO DEBTORS'
MOTION FOR APPROVAL OF DISCLOSURE STATEMENT AND RELATED RELIEF**

21 GABRIEL TECHNOLOGIES CORPORATION ("Gabriel") and TRACE TECHNOLOGIES,
22 LLC ("Trace"), as debtors-in-possession herein (collectively, the "Debtors"), submit this
23 memorandum in reply to the *United States Trustee's Objection To Debtors' Proposed Disclosure*
24 *Statement* (the "UST Objection," docket no. 182) filed by the United States Trustee (the "UST") on
25 July 26, 2013, and in further support of the Debtors' pending motion, the *Debtors' Motion For Entry*
26 *Of An Oder (I) Approving Debtors' Disclosure Statement; (II) Approving Solicitation Procedures,*
27 *Including Form Of Ballot And Manner Of Notice, And (III) Fixing Deadlines For Confirmation*
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1 *Objections And Discovery* (the “Debtors’ Motion” docket no. 140).¹

2 **I. INTRODUCTION**

3 The Debtors filed the Plan, docket no. 119, and the Proposed Disclosure Statement, docket no.
4 120, on June 7, 2013. On June 27, 2013, the Debtors filed the Debtors’ Motion, docket no. 140,
5 seeking approval of the Proposed Disclosure Statement and related relief regarding solicitation
6 procedures and deadlines for confirmation briefing and discovery. The hearing of the Debtors’
7 Motion is scheduled for July 30, 2013, at 1:30 p.m., pursuant to the *Amended Stipulated Scheduling*
8 *Order, etc.*, docket no. 157 (the “Scheduling Order”) entered on July 16, 2013.

9 On July 23, 2013, in accordance with the timing required under the Scheduling Order, the
10 Debtors responded (docket no. 172) to objections raised by Qualcomm Incorporated (“Qualcomm”)
11 and informal comments offered by the United States Securities and Exchange Commission (the
12 “SEC”). In this memorandum, the Debtors will respond to the UST’s objections, and will also
13 provide further language to address the SEC’s comments.

14 **II. UST OBJECTION**

15 The UST has raised several grounds for objection which are addressed in the order presented
16 by the UST Objection, as follows:

17 **A. More History Would Not Be Helpful.**

18 The UST argues that the Proposed Disclosure Statement contains insufficient information
19 regarding the history of the Debtors. In fact, the Proposed Disclosure Statement contains, at page 8,
20 all that is relevant to understanding the contents of the Plan – the Debtors’ relationship to each other,
21 their founding in the last decade, and the events that gave rise to the intellectual property claims that
22 are now at the heart of the Qualcomm Litigation. The Qualcomm Litigation, in turn, is described at
23 length, and even Qualcomm’s argument about claims against officers and directors is identified (see
24 pages 14-15). This, coupled with many pages describing the Debtors’ current assets and liabilities
25 and the components of the Plan, is sufficient for purposes of understanding the Plan and its risks and
26 rewards.

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28 ¹ All capitalized terms not otherwise defined herein are intended to have the meanings ascribed to them in the Debtors’
Motion.

1 The Plan only proposes a liquidation, and past operations and history are not relevant to that
2 liquidation. The liquidation is centered on prosecution of the Qualcomm Litigation, for which all
3 relevant history is in fact provided by the Proposed Disclosure Statement. More is not better in these
4 circumstances – most readers will absorb only so much information in reading a disclosure statement,
5 and the added time and expense needed to create more discussion of prior events and corporate
6 history that do not impact the Qualcomm Litigation or prospects for distributions under the Plan
7 would only result in a more densely packed disclosure statement that would be of less use to
8 creditors.

9 **B. More Discussion of Tax Returns and SEC Reports, While Not Needed, Will Be Added.**

10 The UST next argues that more information is needed as to the filing or non-filing of income
11 tax returns and SEC reports. Again, the Debtors submit that such information, while it may be
12 ultimately relevant to determining any tax claims, is not pertinent to the Plan itself. Nonetheless,
13 because it is not difficult to add, the Debtors propose to add the following language to the Proposed
14 Disclosure Statement to address the UST’s concern:

15 The Debtors have not filed income tax returns for the years 2005-2012, and have not
16 filed required annual reports with the Securities and Exchange Commission (“SEC”) since 2007, due to lack of funds. Section 7.6.8 of the Plan provides for the filing of
17 delinquent tax returns following the Effective Date, to the extent feasible and legally
18 required. The SEC reports will not be filed retroactively or going forward, as the
19 Debtors will stipulate with the SEC to end Gabriel’s registration for public trading.

19 **C. More Information Regarding Substantive Consolidation Is Not Necessary.**

20 The Plan provides for the substantive consolidation of the Debtors as of the Effective Date.
21 The Proposed Disclosure Statement describes the basis for consolidation as follows:

22 As of the Effective Date, all of the assets of Gabriel and Trace will be substantively
23 consolidated into Gabriel’s estate, and Gabriel will become the Reorganized Debtor.
24 The Debtors believe that the standards for consolidation of their two estates are
25 satisfied, as the Debtors’ creditors have historically dealt with the two Debtors as if
26 they were the same, and the affairs and obligations of the two Debtors are so integrally
27 mixed as to make it infeasible to separate them. *In re Bonham*, 229 F.3d 750, 764 (9th
28 Cir. 2000); *In re Augie/Restivo Baking Co.*, 860 F.2d 515 (2nd Cir. 1988). As a result
of such consolidation, all assets of both Debtors will be available for the satisfaction of
all Claims against either of the Debtors, in accordance with the terms of the Plan.

27 The UST argues that this is insufficient, and that more facts supportive of consolidation should be

1 identified. The Debtors disagree: Whereas the Debtors recognize their obligation to prove the basis
2 for consolidation at the time of the confirmation hearing, they do not believe that more is needed in
3 the Proposed Disclosure Statement. Nonetheless, the Debtors propose to add the following language
4 to address the UST's concern:

5 Facts supporting consolidation include the Debtors' historic sharing of all
6 administrative functions, their consistently collective corporate actions, their jointly
7 prosecuted litigation and persistent comingling of funds and other assets. Further,
virtually all of the Debtors' debts are owed jointly to creditors, making any distinction
between estates difficult and meaningless.

8 **D. Discussion of Chapter 7 Alternative Will Be Added.**

9 Even though the Plan provides for a liquidation of the Debtors' assets, the UST argues that a
10 chapter 7 liquidation analysis is needed in the Proposed Disclosure Statement. To that end, the
11 Debtors propose to add the following:

12 If the Plan is not confirmed and an alternative plan cannot be formulated and
13 confirmed, then the Debtors' cases are likely to be converted to chapter 7 liquidations.
14 The Debtors believe that such conversion, and liquidation through chapter 7, would
15 not be as beneficial to creditors as the Plan, for the following reasons: First,
16 liquidation in chapter 7 would necessitate the appointment of a trustee, in
17 displacement of the Debtors' current management. This would be disruptive and
18 harmful to the prosecution of the Qualcomm Litigation, as current management is
19 intimately familiar with the litigation and a new trustee would not be. Second, the
chapter 7 trustee would create greater expenses for the estate. The trustee would be
owed a statutory fee, and his or her counsel and other professionals, if retained, would
also earn fees and reimbursement of expenses, all as a burden to the Debtors' estates.
The Debtors' current management, both officers and directors, serve without
compensation from the Debtors or their estates.

20 Third, outside of the Plan, the important concessions made by secured creditors,
21 including Northwater and secured noteholders, would not be effective. As a result,
22 those creditors' claims and liens, to the extent allowed, would have full priority over
23 unsecured creditors, unlike under the terms of the Plan, and unsecured creditors'
24 prospects for recoveries would be significantly reduced. Fourth, without Plan
25 confirmation, Northwater's commitment under the Plan to loan funds to the
Reorganized Debtor in order to prosecute the Qualcomm Litigation and to pay certain
administrative costs, would be ineffective, leaving considerable risk that the trustee
would not be able to arrange funding of the litigation, and would not prosecute the
litigation accordingly.

26 **E. Statement Regarding No Future Operations Will Be Added.**

27 As discussed in the Debtors' earlier response to the SEC's informal comments, the Plan
28 requires the Reorganized Debtor to dissolve once it has completed its obligations under the Plan. In

1 order to address comments by the SEC in that regard, the Debtors have proposed language clarifying
2 the Reorganized Debtor's obligation to dissolve.

3 The UST has also requested additional language in order to clarify whether the Reorganized
4 Debtor will resume business operations in the event of success in the Qualcomm Litigation. To
5 address the UST's request, the Debtors propose to add the following sentence, in addition to the
6 language to be inserted in response to the SEC's comments:

7 Under no circumstances will the Reorganized Debtor resume business operations upon
8 the completion of the Qualcomm Litigation. Instead, upon the conclusion of the
9 Qualcomm Litigation and any other performance required under the Plan, the
10 Reorganized Debtor will be dissolved, as stated.

11 **F. Miscellaneous Points**

12 The UST has also raised various miscellaneous points, to which the Debtors respond as
13 follows:

14 **1. Priority Claims**

15 The UST complains that the Proposed Disclosure Statement states that Priority Claims are not
16 "significant," but fails to quantify those claims. The Debtors propose to add the following language:

17 Priority Tax Claims have been filed in the aggregate amount of \$7,843 by the
18 California Franchise Tax Board, and the Internal Revenue Service has filed a claim in
19 an undetermined amount. The Debtors believe that such claims may be subject to
20 challenge, but that in no event is any greater amount owed on account of Priority Tax
21 Claims.

22 In addition, the Debtors propose to delete the word "material" with reference to Class A Claims
23 (Priority Claims Other Than Nonclassified Priority Claims), to clarify that no priority claims, other
24 than Priority Tax Claims, are expected to be allowed.

25 **2. Executory Contracts**

26 The UST requests the addition of language to describe treatment of executory contracts, as set
27 forth in Article VI of the Plan. The Debtors propose to add the following language:

28 The Plan provides for treatment of executory contracts in Article VI, whereunder, all
such contracts will be deemed rejected unless affirmatively assumed by the
Reorganized Debtor pursuant to notice provided prior to the Effective Date of the
Plan. At present, the Debtors do not anticipate that any executory contracts will be
assumed, or that any cure amounts will be owed, other than to the extent that any
existing insurance policies are deemed to be executory contracts. Any such policies

1 will be deemed assumed as of the Effective Date, and the Debtors do not believe that
2 any cure amounts will be owing thereunder.

3 **3. Definition of Terms**

4 The UST complains that the Plan provides for definitions of terms that in some instances may
5 vary from definitions of similar terms under the Bankruptcy Code. The Debtors submit that there is
6 no requirement that defined terms adhere to Bankruptcy Code definitions, nor is any explanation of
7 differences in definitions needed or useful to creditors seeking to make an informed decision about
8 the Plan.

9 **4. Consultation with UST**

10 The UST objects to language that indicates that the Debtors have consulted with the UST in
11 the course of managing their chapter 11 cases. The UST does not appear to challenge the accuracy of
12 the language, but only any implication of endorsement by the UST. The Debtors will remove any
13 reference to the UST in that language.

14 **5. Monthly Operating Reports**

15 The UST states that no monthly operating reports have been filed by Trace, but that Gabriel is
16 current with respect to its reports. In fact, all reports filed by Gabriel have been intended as joint
17 reports by the two Debtors. The Debtors will consult with the UST in order to reconcile or amend the
18 reports to satisfy the UST's concerns, but the Debtors do not believe that further text is required in
19 the Proposed Disclosure Statement in this regard.

20 **III. ADDITIONAL LANGUAGE REGARDING SEC COMMENTS**

21 Based on further exchanges with the SEC's counsel, the Debtors propose to add the following
22 language with respect to Section 7.24 (Exculpation, Indemnification and Insurance) of the Plan:

23 Under the Plan, as of the Effective Date, each of the Debtors, the members of the
24 Committee (acting in such capacity) and their respective professionals, officers,
25 directors and representatives, will be deemed to have no liability to any person or
26 entity for any act taken or omitted to be taken, in connection with, or related to, the
27 formulation, preparation, dissemination, implementation, administration, confirmation
28 or consummation of the Plan or any contract, instrument, waiver, release or other
agreement or document created or entered into, in connection with the Plan, or any
other act taken or omitted to be taken in connection with the Chapter 11 Cases up to
and including the Effective Date, except to the extent arising an act or omission that is
determined to have constituted gross negligence or willful misconduct.

In addition, the Reorganized Debtor's, the Plan Committee's, and the Litigation

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Trust's members, professionals, officers and directors, including the Litigation Trustee, will be indemnified by the Reorganized Debtor with respect to their implementation of the Plan and their post-Effective Date activities in connection with the administration and implementation of the Plan, but not as to their own gross negligence or intentional misconduct. To the extent reasonably available, the Reorganized Debtor may purchase errors and omissions insurance coverage for the Reorganized Debtor, the Plan Committee, the Litigation Trust and their members, officers, directors and professionals, including the Litigation Trustee.

IV. CONCLUSION

Based on the foregoing, and in light of the additional language proposed by the Debtors as reflected above, the Debtors submit that the Debtors' Motion should be granted, and that the Proposed Disclosure Statement, as modified by the changes proposed by the Debtors above and in its earlier response, should be approved.

DATED: July 29, 2013

MEYERS LAW GROUP, P.C.

By /s/ Merle C. Meyers
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