UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re	:	Chapter 11
Chrysler LLC, et al.,	:	Case No. 09.50002 (AJG)
Debtors.	:	
	:	

MOVANTS' MEMORANDUM IN SUPPORT OF MOTION TO RECONSIDER THE COURT'S JUNE 9, 2009 REJECTION ORDER AND JUNE 19, 2009 REJECTION OPINION.

Pursuant to Federal Rules Of Civil Procedure 60(b)(1), and 60(d)(3), Movants respectfully request that the Court reconsider and reverse its Order, findings of facts, and application of law with regard to the Court's prior approval of Debtor's rejection of Movants' automobile dealership agreements.

STIPULATIONS

In order to avoid confusion and in recognition of the limitations put upon Movants in petitioning the Court to reconsider its prior ruling, Movants stipulate - *for the strict limited purpose of the present motion only* - as follows:

- The Debtor's methodology in choosing which dealers to reject and which to assume and assign is not contested by this motion.

- There was no prejudice to Movants by the Court's consideration of all 789

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

rejected dealership agreements in one motion (as discussed in the Court's Rejection Opinion, *In re Old Carco LLC* 406 B.R. 180 at 207 (S.D.N.Y. 2009). Movants further stipulate on this point that they do not contest the Court's failure to analyze each individual dealership agreement in determining whether the Debtor's decision to reject dealership agreements met the business judgment test.

- While Movants will be relying upon facts indicating bad faith of the Debtor overlooked by the Court in both its Rejection Opinion and its Rejection Order, Movants further stipulate that the Court's prior findings concerning bad faith, whim or caprice discussed by the Court in its Rejection Opinion and Rejection Order were proper and we do not challenge them again in the present Motion.

- No "heightened standard" or "public interest standard" (as discussed in the Court's Rejection Opinion, *Id*. 189-191) was required to be applied by the Court in its analysis of whether the dealership rejections met the business judgment test.

- While Movants will rely upon facts and authorities overlooked by the Court in its application of the business judgment standard, Movants further stipulate that the business judgment standard was the correct standard to apply and that the Court was not required to apply the "fairness" standard (as discussed by the Court in its Rejection Opinion, *Id*. 191).

- Federal law preempted state law as to the rejection of dealership agreements (as discussed by the Court's Rejection Opinion, 406 B.R. at 199 - 206).

FRCP RULE 60

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

Statute of Limitations

Rule 60(b)(1) allows movants to file motions to reconsider within one year of an Order being entered. The Rejection Order was entered on June 9, 2009 and so this motion is well within the one year limitation. Additionally, the statute does not limit the time within which motions made under 60(d)(3) can be made.

Requirements For Reconsideration

In, *Hoffenberg v. Hoffman & Pollok*, 296 F. Supp. 2d 504, 505 (S.D.N.Y. 2003), the Court discussed the necessary requirements for reconsideration:

> "A motion for reconsideration 'is appropriate where a court overlooks *controlling decisions or factual matters that were put before it on the underlying motion . . . and which, had they been considered, might have reasonably altered the result before the court*.' Banco de Seguros del *Estado v. Mut. Marine Offices, Inc.*, 230 F. Supp. 2d 427, 428 (S.D.N.Y. 2002) (*quoting Range Rd. Music, Inc. v. Music Sales Corp.*, 90 F. Supp. 2d 390, 392 (S.D.N.Y. 2000)). 'The standard for granting . . . a motion [for reconsideration] is strict, and reconsideration will generally be denied unless the moving party can point to controlling decisions or data that the court overlooked -- matters, in other words, that might reasonably be expected to alter the conclusion reached by the court.' *Shrader v. CSX Transp., Inc.*, 70 F.3d 255, 257 (2d Cir. 1995). "[A] motion for reconsideration may be granted to 'correct a clear error or prevent manifest injustice.'" *Banco*, 230 F. Supp. 2d at 428 (*quoting Griffin Indus., Inc. v. Petrojam, Ltd.*, 72 F. Supp. 2d 365, 368 (S.D.N.Y. 1999)).

Movants respectfully submit that this Court's June 9th Rejection Order and June 19th Rejection Opinion (*In Re Old Car Co*., 406 B.R. 180 (S.D.N.Y. 2009) overlooked important factual matters entered into the record and that such matters could reasonably be expected to alter the Court's original conclusions. Furthermore, we also respectfully submit that the Court overlooked controlling decisions and statutes which could also be reasonably expected to alter

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

the Court's original holding. Moreover, some of the controlling decisions overlooked by the court were cited in the Court's Rejection Opinion for other grounds. While we recognize that Rule 60(b) motions must be "*narrowly construed and strictly applied so as to avoid repetitive arguments on issues that have been considered fully by the Court*," Hoffenberg at 505, citing *DelleFave v. Access Temporaries, Inc.*, 2001 U.S. Dist. LEXIS 3165, No. 99 Civ. 6098, 2001 U.S. Dist. LEXIS 3165 (S.D.N.Y. Mar. 21, 2001)), the Rejection Opinion failed to consider other separate and distinct controlling points of authority flowing from those cases which we rely upon below. We respectfully submit that in overlooking the facts and authorities presented herein, the Court misapplied the law, committed clear error and has caused a manifest injustice by approving the rejection of 789 dealership agreements.

ARGUMENT

PRELIMINARY STATEMENT

The legal issue controlling Debtor's Omnibus Motion to reject 789 dealership agreements was considered in the Sale Hearing, Order and Opinion as well as the Rejection Hearing, Order and Opinion. Since the Court's approval of the 789 dealership rejections was specifically granted in the Rejection Order, Movants only seek relief from the Rejection Order and not the actual Sale Order. However, due to the Court having addressed the legal issues concerning whether Court approval was proper - as per Section 365(a) and relevant precedent - in both the Sale and Rejection Opinions, we therefore address our arguments to the entire record.

The paramount issue before the Court as to the Rejection Motion concerned whether rejection of the dealership agreements met the "business judgment standard". To that issue, an affirmative

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

conclusion as to whether rejection of the dealership agreements was required by Fiat as a condition precedent to the sale closing was the most important finding necessary to the Court approving rejection of the 789 dealership agreements, because had the purchaser been willing - under the same terms - to accept an assignment of the entire dealership network including the 789 rejected dealerships, then no benefit to the Debtor's estate was even remotely possible. And as to this issue, a close examination of the record indicates that the Court's factual finding in the second sentence of Footnote 21 of the Rejection Opinion (see *In re Old Carco LLC* 406 B.R. at 197) affects a fraud upon the court as per FRCP Rule 60(d)(3) by exhibiting a reckless disregard for the truth.

Furthermore, the Court's Rejection Opinion relied heavily upon its finding that the Debtor entered into prepetition obligations which - after Bankruptcy was filed - required the Debtor to reject the dealership agreements. As discussed below, Movants rely upon multiple facts overlooked in the Court's Opinions and Orders which illustrate that rejection of the dealership agreements was not insisted upon by any party to this transaction and was never a condition precedent to the sale closing. Moreover, the Court overlooked longstanding authorities indicating that prepetition obligations to waive protections of the Bankruptcy Code are against public policy and are therefore unenforceable. While the Court's Rejection Opinion (*Id*., 406 B.R. at 190) relied upon *In re Trans World Airlines, Inc.,* 261 B.R. 103 (Bankr. D. Del. 2001) on separate grounds, the Court overlooked that part of the TWA holding which held that "*...a debtor may not agree to assume or reject an executory contract until after the bankruptcy case is commenced and the*

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

debtor is acting in the capacity of debtor-in-possession." *Id*. at 115.[1] Therefore, and as fully discussed in more detail below, based upon the Court's failure to consider this important aspect of TWA, the Court's Rejection Order should be vacated.

The Court also stated in the Sale Opinion, *In re Chrysler LLC,* 405 B.R. 84, 97 (S.D.N.Y. 2009) that, "*Not one penny of value of the Debtors' assets is going to anyone other than the First-Lien Lenders*." The Court did not address this fact in the Rejection Opinion. As discussed below, while the Court did rely on the controlling 2d Circuit precedent of *In re Minges*, 602 F.2d 38 (2d Cir. 1979), with regard to defining requirements for Court approval of Debtor's rejection of the dealership agreements under the business judgment test, the Court overlooked that part of *Minges* which requires that "general creditors" - defined as encompassing both secured and unsecured creditors - must benefit from the rejection of an executory contract for the business judgment test to be satisfied. The Court failed to state in its Opinion how the "general creditors" - as opposed to just the "first lien lenders" - benefitted in any way from rejection of the dealership agreements since the Court admits "not one penny" of the value paid to the Debtor for its assets went to anyone other than first lien lenders. The Court also failed to discuss the fact that rejection of the dealership contracts would add 789 unsecured creditors to the Debtor's estate**.** [2]

---

[1] Debtor's Counsel, Corrine Ball also overlooked this aspect of the TWA holding when she discussed the TWA case in her closing statement at the Sale Hearing. See June 29, 2009 Hearing Transcript at 339-340.]

[2] The Court overlooked in its Rejection Opinion and Sale Opinion that it was not disputed during the hearings that rejection damage claims - broadly defined by the Debtor in its Rejection Motion at Paragraph 63 - could add up to 1 billion dollars. See, for example, the May 29, 2009 Hearing Transcript at 284.]

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

Proposed relief is discussed in the final section of this brief and is predicated upon the Court vacating its Rejection Order. During closing arguments to the Sale Hearing on May 29, 2009, Judge Gonzalez indicated (see May 29, 2009 Hearing Transcript at pg. 298-299) that his power - with regard to the dealership Rejections - was limited to approving the Sale to New Co or not approving it in the following discourse between his Honor and Eric Snyder, Esq. (Counsel for a group of rejected dealers):

> "All right, let me ask you one -- you propose something, but what authority do I have? I mean, the only real authority here that I think I have, I either approve the sale or I don't approve the sale. I don't have the authority -- I have the authority to say to New Chrysler I'm not approving the sale, but I don't have the authority to say to New Chrysler I'm approving the sale and I'm making you change it."

And to that conclusion, the Court overlooked legal authority respecting its power to withhold approval of the rejections pursuant to Section 365(a) of the Bankrutpcy Code. To wit, the Court had the power to authorize the sale and to also refuse approval of the rejections. The Sale authorization would not have been invalidated had the Court failed to approve the dealership rejections. Appropriate and equitable relief was (and still is) available against the Debtor's estate.

RULE 60(d)(3); FRAUD ON THE COURT

Statement of Facts.

In Footnote 21 of The Rejection Opinion, Judge Gonzalez's assertion regarding the testimony of Fiat executive, Alfredo Altavilla ("Altavilla"), exhibits such a reckless disregard for the truth that it constitutes a fraud on the court. The second sentence of Footnote 21 states:

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

> "Altavilla also responded affirmatively to a question regarding whether a dealership network needed to be restructured for the Fiat Transaction to close, stating that a "restructuring needs to occur."

The record indicates by clear and convincing evidence that this assertion by Judge Gonzalez is unequivocally false. It gives the appearance of judicial ventriloquism concerning the most important issue related to the Rejection Motion. Without this alleged affirmative response, the record of the case lacks any evidence whatsoever suggesting rejection of the dealership agreements was ever requested by Fiat, the US Government or the United Auto Workers as a condition precedent to the deal closing. Footnote 21 parses, "restructuring needs to occur" by ignoring the very next sentence of the very same answer given by Altavilla. And the complete answer made it perfectly clear that restructuring did *not* need to occur *before* the sale closed. Altavilla was being cross-examined by dealer counsel, Russel McRory, Esq. Here is the exact testimony Judge Gonzalez makes reference to in Footnote 21 from the May 27, 2009 Sale Hearing Transcript at pg. 352:

> Q. If this transaction closes without an absolute requirement of a particular number of dealers that are being terminated, would Chrysler still go through with this deal -- I mean, rather, would Fiat still go through with this deal?
>
> A. The answer is that a restructure needs to occur. Whether it occurs before or after the closing of the deal is not a material difference.

There's no excuse for Judge Gonzalez having parsed "restructuring needs to occur" from that straightforward answer. Having done so, Judge Gonzalez made it appear as if Altavilla's testimony stood for the exact opposite of what the witness actually said.

Judge Gonzalez's creative constuction therefore invalidated the true testimony.

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

Cavalier construction as this would never be tolerated by the Court if undertaken by Counsel.

Furthermore, even the answer as parsed by Judge Gonzalez doesn't equal an "affirmative" response to the question as posed by the Court in Footnote 21. The question Judge Gonzalez made reference to required a time sensitive answer. The purposeful inquisition by Counsellor McCrory was whether restructuring needed to occur as a condition precedent for the deal to close. Yet, the answer as parsed by Judge Gonzalez - "restructuring needs to occur" - is not time sensitive. The parsed response doesn't indicate whether "restructuring needs to occur" before or after the sale closed. The answer as parsed by Judge Gonzalez is technically non-responsive, but certainly misleading. And there is no justification for the Court having spliced an unintended response into the record.

Altavilla's testimony on this point was central to the arguments made by the various attorneys in their closing statements. Counsel for the dealers rightfully zeroed in on this testimony in support of their accurate position that no party requested dealers be stripped of their franchises before the the sale could close. For example, Eric Snyder stated during his closing at the Sale Hearing (see May 29, 2009 Hearing transcript at pg. 294):

> And I believe, as Mr. Lerner stated, Fiat doesn't care. It wasn't a factor in Fiat's decision to purchase the assets of Chrysler that 789 dealers be left behind. Whether they agreed with the methodology or not, it wasn't important enough for them to take a position, making it a condition precedent to the deal.

Even Counsel for the Debtor, Kevyn Orr, stated during his closing statement at the Rejection Hearing (see June 9, 2009 Hearing Transcript at pg. 156) that Altavilla testified dealer restructuring didn't have to occur before the sale closed. Orr cited directly to the page containing this key testimony:

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

> "To the extent counsel has tried to mischaracterize Mr. Altavilla's testimony, his testimony was that if rationalization did not occur before the sale, it would have to occur after the sale and that's at page 352."

Altavilla's testimony also contains the following from pg. 354 of the May 29 Hearing:

> Q. I'll just conclude, Mr. Altavilla, with one more question. Is the rejection of any certain number or any certain percentage of Chrysler dealers a condition for you closing on the contract with Chrysler?
>
> A. No, a number has never been a condition to close.

This relates back to the text that Footnote 21 is attached to, which states:

> "It is immaterial whether Fiat required the Debtors to reject the number of agreements it rejected. [21]"

The complete Footnote 21 reads as follows:

> 21 Altavilla testified that although Fiat did not indicate the size of the restructuring of the dealership network, the number of dealers involved in the restructuring came out of the application of the Debtors' selection methodology. Altavilla also responded affirmatively to a question regarding whether a dealership network needed to be restructured for the Fiat Transaction to close, stating that a "restructuring needs to occur."

The Court's reckless disregard for the truth in Footnote 21 becomes even more troubling in light of the first sentence of Footnote 18 which states:

> 18 Altavilla testified that it did not make a material difference whether the restructuring of the dealership network occurred before or after the closing of the Fiat Transaction.

Anyone not familiar with the May 29th Hearing Transcript would be left with the impression that Footnotes 18 and 21 refer to separate questions and answers, when in reality, all of this stems from the same question and answer. The fact it did not make a material difference to Fiat whether dealer restructuring happened before or after the sale closed was subverted. The crucial

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

testimony of this key witness therefore establishes that the Fiat transaction could have closed with the entire dealership network having been transferred which would have avoided the destruction of the rejected franchises, approximately 39,000 jobs and dealer reputations,

Before turning to our legal analysis of the elements necessary to establish fraud on the Court under FRCP Rule 60(d)(3), we should state that Movants do not allege Judge Gonzalez intentionally perpetrated a fraud on the Court. Regardless, we respectfully submit that the assertion wielded by Judge Gonzalez in Footnote 21 is fraudulent on its face and as such it exhibits a reckless disregard for the truth which is enough under controlling precedent to establish fraud on the court under Rule 60(d)(3).

Legal Discussion

> **Rule 60. Relief from Judgment or Order...(d)Other Powers to Grant Relief. This rule does not limit a court's power to...(3) set aside a judgment for fraud on the court.**

"The elements of a 'fraud upon the court' are numerous. Fraud on the court is conduct: 1) on the part of an officer of the court; 2) that is directed to the judicial machinery itself; 3) that is intentionally false, willfully blind to the truth, or is in reckless disregard for the truth; 4) that is a positive averment or a concealment when one is under a duty to disclose; 5) that deceives the court." *Workman v. Bell,* 245 F.3d 849, 852 (6th Cir. 2001). "[F]raud upon the court is limited to that species of fraud which does or attempts to, defile the court itself, or is a fraud perpetrated by officers of the court so that the judicial machinery cannot perform in the usual manner its impartial task of adjudging cases that are presented for adjudication." *Salsberg v. Trico Marine Servs. (In re Trico Marine Servs.),* 360 B.R. 53 (S.D.N.Y. 2006) (Citing *Serzysko v. Chase*

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

Manhattan Bank, 461 F.2d 699, 702 (2d Cir.), cert. denied, 409 U.S. 883, 93 S. Ct. 173, 34 L. Ed. 2d 139 (1972).

As noted by Chief Justice Bernstein in the Salsberg case, it is enough that the action taken "does" cause the judicial machinery to not perform in the usual manner. Establishing fraud on the court does not require that the court officer responsible "attempt" to defraud the court when the positive averment in question does, in fact, defraud the court. "The petitioner must show that an officer of the court '*whose judgment is under attack*' acted in a manner that is 'intentionally false, willfully blind to the truth, or is in reckless disregard for the truth.' " *James v. United States*, 603 F. Supp. 2d 472 (E.D.N.Y. 2009) (Citing *Alley v. Bell*, 392 F.3d 822, 831 (6th Cir. 2004)). In *In re M.T.G., Inc*. 366 B.R. 730 (E.D. Mich. 2009), it was held that, "The Court is unable to find, on the present record, that Taunt and his attorneys *intended* to deceive the Court or to commit a fraud on the court. But such intent is not required to find a fraud on the court, as that concept is defined in the case law."

We respectfully submit that the averment by Judge Gonzalez in Footnote 21 of the Rejection Opinion has caused the judicial machinery to work in an alien and wholly improper manner by subverting a clear response by a key witness as to the most important issue before the Court. Judge Gonzalez, in taking this action, has caused the appearance of impartiality to be disturbed by reckless disregard for the truth. The record of the case should not be allowed to remain so defiled. Accordingly, we request complete relief from the Rejection Order.

RULE 60(b)(1)

On motion and just terms, the court may relieve a party or its legal representative from a

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

final judgment, order, or proceeding for the following reasons:

(1) mistake, inadvertence, surprise, or excusable neglect;

Below, Movants incorporate all of the arguments and authorities in support of the foregoing as to FRCP Rule 60(d)(3) in that should the Court find that the actions therein described do not rise to the level of fraud on the court, we certainly allege the same to have been a mistake by the Court.

The Court's legal and factual analysis on the issue of whether the Debtor's rejection of 789 dealership agreements met the business judgment standard overlooked many important facts which could have reasonably altered the conclusions stated in the Rejection Order and discussed in the Rejection Opinion.

Business Judgment Test

Section 365(a) of the Bankruptcy Code requires that before a Debtor may assume or reject an executory contract, the bankruptcy court must approve the Trustee's (or Debtor In Possession's) decision thereto. In the Rejection Opinion issued by Judge Gonzalez, the Court failed to clearly identify the Debtor's burden under the business judgment test.

> "To meet the business judgment test, the debtor in possession must 'establish that rejection will benefit the estate. Once the debtor meets its burden, the non debtor party bears the burden of proving that the debtor's decision derives from bad faith, whim or caprice.' See In re Cent. Jersey Airport Servs., LLC, 282 B.R. 176, 183 (Bankr. D. N.J. 2002)."

In Re Helm 335 B.R. 528, 538 (S.D.N.Y. 2006),

Judge Gonzalez's decision failed to mention that Debtors had a burden here to "establish" that rejection would benefit the estate. Judge Gonzalez instead analyzed the issue as if the

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

the Debtor's judgment was not subject to judicial review absent a showing of bad faith:

> "'Generally, absent a showing of bad faith, or an abuse of business discretion, the debtor's business judgment will not be altered." *G Survivor*, 171 B.R. at 757. Moreover, the business judgment standard 'as applied to a bankrupt's decision to reject an executory contract because of perceived business advantage requires that the decision be accepted by courts unless it is shown that the bankrupt's decision was one taken in bad faith or in gross abuse of the bankruptcy retained business discretion.' *Id*. at 758 (quoting *In re Richmond Metal Finishers, Inc*., 756 F.2d 1043, 1047 (4th Cir. 1985))."

Benefit To The Estate

Judge Gonzalez also failed to discuss how the controlling authorities define "benefit to the estate". The definition was established in the oft-quoted 2d Circuit precedent of *In re Minges*, 602 F.2d 38 (2d Cir. 1979) which held that "general creditors" must benefit from the debtor's rejection of an executory contract. In that case, there was a dispute between the parties as to whether the benefit received by rejection would favor the secured creditors over the unsecured creditors and whether the perceived benefit was substantial and significant enough to warrant rejection. The Court held that as long as both classes of creditors ("general creditors") received a "substantial and significant benefit", the business judgment test would be satisfied:

> "The parties thus lock horns on whether benefit to the secured creditors is enough, on these facts, to justify rejection of the lease covenants under the business judgment test. The disagreement, however, is irrelevant if there was a sound basis for the finding of the bankruptcy judge, quoted above, that the general creditors would benefit from the 'enhance(d) . . . value of the premises.' We are not satisfied that the record before us on the issue is adequate to decide this issue. We find only the most general estimate of increase in market value if the covenants involved here are rejected and no detailed support, by appraisal or otherwise, for this statement. Nor do we know the amount of the secured debt. Further relevant facts are whether the estate is likely to be adequate to cover administrative expenses and other priority claims, whether there are other properties beside Pro Park in the estate, and if there are,

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

> the extent of encumbrances on them. In short, we do not know whether a sound basis exists for a finding that there is a reasonable likelihood that general creditors will derive substantial or significant benefit from the proposed lease rejection. We therefore believe that the proceedings should be returned to the bankruptcy judge to make specific findings after giving the parties an opportunity to present further evidence. While we regret the further delay in the proceedings that a remand for this limited purpose will require, we believe that in the long run it will assist in a proper disposition of the remaining issues raised by the appeal."

Id. at 44.

While the Court was correct in stating that "fairness" was not the proper standard as was also held by the Court in *Minges*, Judge Gonzalez failed to address that part of *Minges* which requires that "general creditors will derive substantial or significant benefit" from the rejection. This is the required factor that wasn't addressed by Judge Gonzaalez. In *Minges*, even though the Court acknowledged there was a sound basis for finding that rejection of the lease in that case would convey some monetary benefit to the general creditors, the Court held that the record of the case did not contain enough evidence to find that this benefit was "substantial or significant" enough to meet the business judgment test. Accordingly, the Court remanded the case back to the bankruptcy judge to make specific findings thereto.

The concurring opinion by Justice Mansfield provides illumination to this analysis:

> Where rehabilitation of the debtor is contemplated, I agree that a Chapter XII trustee should be governed by the "business judgment" standard in determining whether burdensome executory lease provisions should be rejected. At the same time, as Judge Feinberg indicates, the standard governing the trustee should be whether there is a reasonable likelihood that general creditors will derive any substantial or significant benefit. If, for instance, the rejection would probably result in no benefit to general creditors or in recovery of only a few dollars for distribution to general creditors...the trustee should not have the power to reject... As a representative of the bankruptcy court, which is a court of equity, the trustee should not play favorites between the lessee and secured creditors by manipulating

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

> the obligations affecting them, absent some significant benefit to the creditors generally. To do so would be inequitable. Although rejection of onerous lease obligations would increase the value of the mortgagees' security, thereby reducing the size of any portion of their claims that could not be satisfied out of the security, it would simultaneously generate claims by the lessee against the estate for loss of his rejected executory rights.

Id. at 44-45.

It's important to note that Justice Mansfield properly weighed the rejection damage claims that result from rejection against any alleged monetary benefit to general creditors, whereas Judge Gonzalez failed to discuss the undisputed potential for rejection damage claims to reach as high as one billion dollars upon rejection of 789 dealership agreements. Furthermore, where the Court in *Minges* remanded the case because the record was insufficient as to whether the benefit to general creditors was substantial and significant enough to warrant rejection, Judge Gonzalez skipped over the issue entirely. So we must now turn our attention to that subject.

The proper analysis of the issue as controlled by *Minges* is that if the benefit to general creditors is "significant and substantial", then the Court need not weigh the harm to the rejected non-debtor party. Fairness is not an issue to be considered in that case. But proving the benefit to general creditors rises to the necessary level of being "significant and substantial" is the Debtor's burden. Judge Gonzalez didn't address the issue of whether unsecured creditors received any benefit in his Rejection Order/Opinion or the Sale Order/Opinion.

Regardless, it was not disputed that the entire 2 billion dollar purchase price went entirely to the 1st lien lenders in relation to their collateral. In fact, the Court stated in the Sale Opinion, *In re Chrysler LLC,* 405 B.R. 84, 97 (S.D.N.Y. 2009), that, "*Not one penny of value of the Debtors'*

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

assets is going to anyone other than the First-Lien Lenders." Judge Gonzalez failed to mention this fact with regard to the dealership rejection issue. Since "not one penny" of value paid by the purchaser went to the unsecured creditors, they didn't receive a monetary benefit from dealer rejections.

While jurisdictions have differed on other grounds such as the improper fairness standard (to which we stipulate agreement with Judge Gonzalez), there is no dispute that the 2d Circuit in *Minges* set binding precedent by holding that "general creditors" must benefit, and that determination has been universally interpreted to mean that the test of whether the rejection of executory contracts significantly benefits the estate revolves around whether the unsecured creditors get at least some benefit. This is because - assuming there is a benefit to be shared - secured creditors will always benefit. But in order to meet the business judgment test set by *Minges*, there must be something left over for the unsecured creditors. Hence, "The primary element of such a showing is the extent to which a rejection will benefit the general unsecured creditors of the estate." *In re Stable Mews Assocs., Inc*., 41 B.R. 594, 596 (Bankr. S.D.N.Y. 1984); "The primary issue when applying the "business judgment" test is whether rejection would benefit the general unsecured creditors..." *In re Meehan*, 46 B.R. 96, 101 (E.D.N.Y. 1985); "The primary element of [the business judgment test] is the extent to which a rejection will benefit the general unsecured creditors of the estate...*In re Sundial Asphalt*, 147 B.R. 72, 81 (S.D.N.Y. 1992); "'The business judgment standard... requires only a demonstration that rejection of the executory contract...will benefit the estate.'...(citing In re Minges), 602 F.2d 38, 43 (2d Cir. 1979). Central to this showing 'is the extent to which a rejection will benefit he general unsecured creditors of the estate...' Id." In re Kong, 162 B.R. 86, (E.D.N.Y. 1993).

As Judge Gonzalez stated, Old Co's unsecured creditor class received "not one penny" from the

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

value (2 billion dollars) paid to Old Car Co for its assetss by New Car Co. It is also undisputed that the dealership rejections added 789 unsecured creditor rejection damage claims to the Debtor's estate as per Section 365(g) of the Bankruptcy Code. Therefore, based upon monetary gain alone, the decision to reject the dealer contracts would not pass the business judgment test. A similar monetary analogy runs through the line of cases which hold that if the unsecured creditors will receive their full claims from proceeds of the estate, then rejection of an executory contract should not be approved: "If without regard to rejection of the contract, the estate is solvent and the unsecured creditors would receive 100 percent of their claims, rejection would then accomplish nothing for the general unsecured creditors." *In re CHI-FENG HUANG*, 23 B.R. 798, 803 (9th Circ. 1982)

These two major undisputed facts were overlooked by Judge Gonzalez:

- *Not one penny of monetary benefit went to unsecured creditors;*

- *Creditors became burdened by 789 potential rejection damage claims.*

The Court failed to properly discuss these facts anywhere in the Sale Opinion or the Rejection Opinion. These facts render as moot the issue of whether New Co. paid extra value (although no such value was ever tendered; see below) for the option of excluding executory contracts since "not one penny" of the two billion dollars went to anyone other than 1st lien lenders.

Benefits of Dealer Restructuring Went Exclusively To New Co.

To the extent that the methodology used to restructure the dealership network had any true benefit, it's important to note that while Judge Gonzalez acknowledged that New Co would

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

benefit from the rejections, his Rejection and Sale Opinions overlooked the fact that Old Co would receive no benefit whatsoever from a streamlined dealership network as Old Chrysler was not going to be selling automobiles anymore. This was candidly admitted by Old Co's Chairman and CEO, Robert Nardelli (see May 28, 2009 Hearing Transcript at 390-391):

> Q. What did Chrysler get in return for the acceleration of this rationalization?
>
> A. Chrysler didn't. It was really the value will be realized in NewCo.
>
> Q. But isn't your obligation to the debtors' estate?
>
> A. Yes.

Cost Allegations

In support of his finding that dealer rejections benefitted the Debtor's estate, Judge Gonzalez made references to various cost savings associated with the implementation of dealership rejections:

> "A smaller dealership network would also enable the Debtors to reduce expenses and inefficiencies in the distribution system, including reducing costs spent on training, new vehicle allocation personnel, processes, and procedures, dealership network oversight, auditing, and monitoring, and additional operational support functions. Consolidation of "partial line" dealerships would eliminate redundancies and inefficiencies in the dealership network. [13]
>
> 13 These cost-savings stand in contrast to the Affected Dealers' oft-repeated contention that the dealers cost the Debtors nothing. Nevertheless, cost-savings is not the relevant test under the business judgment standard, *see supra* fn.11 and accompanying text.

In re Old Carco LLC 406 B.R. at 194.

However, Judge Gonzalez overlooked the fact that Peter Grady, one of the leading Old Car Co. executives charged with the duty of implementing dealer rejections, testified quite

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

candidly that all cost savings thereto would be exclusively retained by New Co (see May 28, 2009 Hearing Transcript at 473):

> Q. To the extent there are any cost savings associated with rejecting these 789 dealers, those cost savings are going to be saved by New Chrysler, not the debtors, correct?
>
> A. Yeah, the savings of the new retained network going forward --
>
> Q. It's a yes or no. Yes or no?
>
> A. Yeah, they will be by New Chrysler.

Debtor In Possession Budget

On this issue, the Court stated:

> "Further, funding for the Affected Dealers under the Debtors' debtor-in-possession budget expired on June 9, 2009. Up to and including that date, the Debtors continued to pay all prepetition and post petition incentives and warranty obligations to the Affected Dealers. Following that date, the debtor-in-possession budget decreased by 25% for such obligations, reflecting the anticipated rejection of agreements constituting 25% of the Debtors' dealership network. [19] Therefore, if the dealership network were not reduced, the Debtors would be out of compliance with their budget. As a result, if the lenders did not authorize additional funds under the budget, funds set aside for the wind-down of the Debtors' estates would have to be used to cover such expenses."

However, the Court overlooked the fact that had the 789 dealership contracts been assumed on May 14th instead of rejected, the Debtor in Possession Budget would not have been affected at all. The Court has overlooked the fact that review of the Debtor's decision to reject the dealership agreements should be analyzed from the time the Rejection Motion was made, not the date it was returnable. To do otherwise strips the Court of any real power in approving rejections of executory contracts under 365(a). Come June 9, the DIP budget was free of dealers either way.

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

Fiduciary Duty For Debtor To Consider Effect Of Rejection On Unsecured Creditors.

Mr. Grady also testified candidly regarding the Debtor's failure to consider the amount of rejection damage claims to the Debtor's estate (see May 28, 2009 Hearing Transcript at 473):

> Q. In connection with the debtors' analysis of its business purpose in deciding which dealer agreements to seek to assume or reject, did the debtors consider the amount of the rejection damage claims that would be incurred?
>
> A. No, we did not.

The Debtor - as Debtor in Possession - had a fiduciary duty to consider the impact of rejection damage claims upon the Debtor's estate and to weigh such damages against any perceived benefit of rejection. Judge Gonzalez overlooked this breach of fiduciary duty. In turning a blind eye to the massive size of a potential rejection damage claim, the Court stated, "Whether the debtor is making the best or even a good business decision is not a material issue of fact under the business judgment test." *In re Wheeling-Pittsburgh Steel Corp*., 72 B.R. 845, 849 (Bankr. W.D. Pa. 1987). Regardless, it stands to reason that the Debtor's decision can't be obviously bad. Here, the record is clear that no party of interest ever requested dealers be rejected. The record is also undisputed that on April 29, the entire dealership network (with the 789 rejected dealers) would be continued if the Fiat alliance succeeded (see May 28 Hearing Transcript of Debtor CEO Nardelli at pg. 389). Instead of following that plan, the Debtor needlessly exposed the estate to a potential rejection damages claim of one billion dollars. Conversely, assigning the 789 dealers to New Chrysler would have cost the estate nothing at all.

To the extent the Court held that unsecured creditors did realize some ethereal benefit from the rejection of the dealership agreements, and we strongly urge that they didn't, the Court relied upon *In re G Survivor Corp*., 171 B.R. 755, 759 (Bankr. S.D.N.Y. 1994); "[T]*he ability to*

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

designate which contracts it wished to have rejected was a valuable right, for which [the purchaser] bargained." *In re Chrysler LLC,* 84 B.R. at 88-89 (citing *In re G Survivor Corp*.,171 B.R. at 759).

But the Debtor received no such relevant value here. Consider Peter Grady's testimony thereto:

> Q. Can you identify any benefit at all to Old Chrysler's estate as compared with New Chrysler, as a result of rejecting the 789 dealer agreements?
>
> A. I think the benefit of rejecting the contracts is to -- to the new company, who is -- that's part of the asset sale from the new companies -- from the old company to the new company. So part of the requirement is the transfer of the robust dealer network. And that's part of the, presumably, the sale price and the value that the new company is paying, if you will, for the assets.

While the Court accepted this line of reasoning in its decision to approve dealer rejections, the Court completely overlooked the following statement by Old Chrysler's Chairman and CEO, Robert Nardelli, which thoroughly establishes that the value Mr. Grady "presumed" to have been tendered - really never was. The Debtor received no value for rejecting the dealership agreements (see May 28, 2009 Hearing Transcript at 392):

> Q. Okay. And I just want to reiterate -- ask another point to what we discussed before that did Chrysler receive any concession or value for accelerating the rationalization program by rejecting almost 800 dealers?
>
> A. Not to my knowledge.

Now consider that the Court's Opinion took notice of Debtor's assertion that prior dealer restructuring efforts cost 216 million dollars (*In re Old Carco LLC* 406 B.R at 195). Assuming that the cost of restructuring the dealership network down the road was going to be just as expensive for New Chrysler, and considering Nardelli's testimony that the Debtor received no value for rejecting 789 dealers, then the business judgment used in giving away 216 million dollars of

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

value is just awful. Had the Debtor offered to accept two hundred million dollars less for no added value, it would never pass the business judgment test or the smell test. The Court completely overlooked Nardelli's admission that the Debtor received no value for rejecting the dealer contracts.

No Faction Of New Co. Ever Requested Dealership Contracts Be Rejected.

The record is very clear on this issue. There is no evidence whatsoever in the record of the case indicating that Fiat, the US Government, the Canadian Government or the United Auto Workers ever requested dealers be rejected by the Debtor. Old Chrysler Chairman and CEO Robert Nardelli was very candid about this (see May 28, 2009 Hearing Transcript at 390):

> Q. Did the UAW ask for this dealer reduction?
>
> A. No.
>
> Q. Did the American government ask for this dealer reduction?
>
> A. No.
>
> Q. Did the Canadian government ask for this dealer reduction?
>
> A. No.
>
> Q. Did Fiat ask for this dealer reduction?
>
> A. No, I don't recall -- again, that -- I don't know if that was an item that was expressly indicated in the agreement or not.

The Court's Orders and Opinions completely overlooked this aspect of the CEO's testimony.

As to Nardelli's lack of recall pertaining to the master transaction agreement ("MTA"), the document does not include any request for rejection of the 789 dealers.

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

Fiat was not shy about excluding contracts in the MTA, and had they requested exclusions beyond those actually contained in the MTA, they were certainly business savvy enough to include more specific rejection provisions as a condition precedent to the deal closing. But they didn't. The record is undisputed that dealer rejections were the brainchild of the Debtor.

Mr. Grady's testimony adds more light to the issue. The following was also overlooked by the Court (see May 28, 2009 Hearing transcript at 477):

> Q. But Fiat did not require the rejection of the 789 agreements, did it?
>
> A. No. But Fiat did encourage and buys into a restructuring of the dealer network which includes rationalization.
>
> Q. And this was not done at their insistence, though, was it?
>
> A. It was not done at their insistence, but it was part of what we looked at as an opportunity --

Altavilla also weighed in on this issue as follows (see May 27, 2009 Hearing Transcript at 352):

> Q. To your knowledge, did the United Auto Workers or their VEBA request a reduction of the dealer network?
>
> A. This has never been part of any discussion between us and the UAW and VEBA.
>
> Q. To your knowledge, in any of your discussions with the United States Treasury, has the United States Treasury requested or demanded any reduction in the dealer network?
>
> A. U.S. Treasury has never demanded such a restructuring, at least in presence of Fiat.

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

> Q. Are you aware of any request by any government agency, including the Auto Task Force, that has demanded a reduction in Chrysler's dealer network?
>
> A. We have never been part of a discussion in which the Treasury has requested the restructuring.

Again, the Court overlooked this important evidence which indicates that nobody ever requested that Old Chrysler reject any dealer contracts.

Mark Manzo was the Chief Financial Advisor for the Debtor in this transaction. The Court relied extensively upon Mr. Manzo's testimony in the Sale Order. On the issue of whether Fiat ever requested dealership rejections, Manzo - who was in line to receive a ten million dollar fee if the sale closed - testified as follows (see May 27, 2009 Hearing Transcript at 267):

> Q. But as far as you know, Fiat never made it a condition to its transaction with Chrysler that the dealer network be reduced?
>
> A. Not that I recall.
>
> Q. Do you know of any party-in-interest that has made it a requirement for the sale transaction that the dealer network be reduced?
>
> A. Not that I'm aware of.

And yet again, the Court overlooked this important testimony that no party in interest ever requested that dealership contracts be rejected.

Prepetition Obligations

We will now address facts and authorities overlooked by the Court as to its holding that prepetition obligations compelled rejection of the dealership agreements. The main assertion adopted by the Court was that the Debtor had an obligation to accelerate dealership restructuring under a long running plan called Project Genesis which was allegedly going to be implemented

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

had the Alliance Viability Plan gone into effect instead of bankruptcy:

> "The Debtors determined, and New Chrysler agreed, [18] that rejection of the Rejected Agreements was necessary and appropriate for implementing the Alliance Viability Plan by enabling the Debtors to consummate the Fiat Transaction and transfer to New Chrysler a smaller, more effective, and more profitable dealer network without disruption while limiting the Debtors' potential post petition obligations to the Affected Dealers." Id. at 195.

But the Alliance Viability Plan was a failed and rejected business plan discussed by the parties prior to the Debtor having filed for bankruptcy protection. Neither the Bankrutpcy Code nor state law imposes obligations to such discussions. Subsequent failure of the parties to enter a contract has never given rise to a necessity in bankruptcy to implement such a failed plan. That is not the law. And the Court committed clear error by finding that prepetition discussions became binding postpetition, when in reality, no legal obligation to reject the dealers under the failed Alliance Viability plan existed. That the Court held such obligations did arise, it was is clear error.

Furthermore, as discussed below, an alleged obligation that calls for a party to waive protections of the Bankruptcy Code prepetition is unenforceable and against public policy.

In re Trans World Airlines, Inc.

While the Court's Rejection Opinion relied upon *In re Trans World Airlines, Inc.* 261 B.R. 103 (Bankr. D. Del. 2001) (see In re Old Carco LLC 406 B.R. at 190), the Court overlooked that part of the TWA holding which held that "*...a debtor may not agree to assume or reject an executory contract until after the bankruptcy case is commenced and the debtor is acting in the capacity of debtor-in-possession*." *Id*. at 115.

In TWA, the parties entered into a ticket vending agreement that contemplated TWA filing a

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

prepackaged chapter 11 petition. The agreement included a clause whereby TWA promised that in the event it should file for bankruptcy, TWA would not seek to reject the agreement pursuant to section 365(a) of the Bankruptcy Code. TWA did eventually enter bankruptcy and despite the clear terms of the contract, TWA sought Court approval to reject the ticket agreement. The Court held that the non-rejection clause was against public policy and therefore unenforceable:

> "I find that enforcing a prepetition agreement to waive the benefits of § 365 impermissibly violates the rights of third-party creditors. Accord In re South East Fin. Assoc., 212 B.R. 1003, 1005 (Bankr. M.D. Fla. 1997)(prepetition waivers are not self-executing and are not binding on third parties; if waiver adversely affects other creditors it is unlikely to be enforced). The interests of third party creditors is at the core of § 365."

Id. at 117.

To the extent the Court considered Old Co was obligated to reject dealership agreements to further the failed Alliance Viability Plan, this important aspect of the TWA case makes clear that no such obligation is enforceable. This precedent was ignored by the Court. And just as in TWA, the MTA here contemplated bankruptcy filing as a future event. The Alliance Viability Plan wasn't even a contract; it was an idea that failed. Since the contract in TWA was unenforceable, obligations flowing from the Alliance Viability Plan were even more unenforceable.

The Court in TWA concluded, "I hold that TWA's prepetition agreement to waive its debtor-in-possession authority to assume or reject an executory contract under § 365 is contrary to the purpose of chapter 11 and unenforceable." *Trans World Airlines, Inc.,* 261 B.R. at 118.

TWA also cited *In re G Survivor* as follows:

> "Indeed, '[a] debtor may reject a contract to make itself more attractive to a buyer" thereby maximizing the benefit to the estate by obtaining the highest

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

> possible bid for the business.' In re G. Survivor Corp., 171 B.R. at 759 citing In re Maxwell Newspapers, Inc., 981 F.2d 85 (2d Cir. 1992)."

Judge Gonzalez also cited this passage in Footnote 10 of the Rejection Opinion. We can only hazard a guess as to whether Justice Walsh's opinion in TWA failed to take note that in the *G Survivor* case, the court upheld a *prepetition* agreement wherein the Debtor entered into a contract to reject executory contracts excluded by the purchaser. The facts are similar in *G Survivor* as they are here. The parties entered into contracts via prepackaged bankruptcy events with similar exclusion clauses approximately one day before the bankruptcy was filed. Regardless, the holding in TWA is aligned with public policy with respect to the bankruptcy code.

And while it's true that a seller is entitled to make itself more attractive to a buyer, to the extent that is accomplished via prepetition promises waiving the Debtor's right to choose which contracts it will assume post-bankrutpcy, such promises are unenforceable.

Additonally, G Survivor is easily distinguished from Chrysler. There, Fruit of the Loom - the purchaser - was set to do business in Canada with Wal-Mart after having bought the assets of Gitano in a 363 sale. Gitano was party to an executory contract with a company named Forsyth who was already doing business in Canada and was viewed by Fruit of the Loom as an impediment. Fruit of the Loom demanded *upon its own initiation* and due diligence that Gitano reject the Forsyth contract, whereas all of the evidence before the Court here indicates that Old Co initiated the dealership rejections, not Fiat.

G Survivor is further distinguished as in that case the Court was satisfied that the "general creditors" received a clear monetary benefit whereas no such showing was made by Old

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

Co here.

"Project Tiger."

One final point must be made concerning the alleged Project Genesis acceleration. There is a major difference between dealer *restructuring* as contemplated by Project Genesis and dealer *rejections*. Project Genesis involved "restructuring" via negotiations between dealers and Chrysler under protection of state and federal law in an orderly policy which respected the rights of each party. That was the essence of Project Genesis. And had the Debtor sought to truly accelerate Project Genesis, the Debtor, instead of pushing new inventory on the dealers without informing them of the potential rejection consequences, could have spent its time implementing *that* plan for the good of the company moving towards a new tomorrow.

However, that's not what happened. There was no acceleration of Project Genesis. Instead, the Debtor implemented a new plan, appropriately named Project Tiger. The Court overlooked the fact that Project Genesis was actually abandoned in favor of Project Tiger (see Deposition of Jim Press, May 26, 2009 at 202):

> Q. Mr. Press, earlier this morning you mentioned a project known as Project Tiger. Do you recall your testimony this morning mentioning project tiger?
>
> A. Yes.
>
> Q. And what is project tiger?
>
> A. It was a study on if it became necessary to go through the process of bankruptcy and to assess the alternatives for either rejecting or accepting dealers going forward in the new company.

Project Tiger destroyed 789 small businesses in its path and approximately 39,000 jobs

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

by circumventing state and federal franchise laws, while Project Genesis operated within the protection of those laws. The Court completely overlooked Project Tiger's existence.

PROPOSED RELIEF

Throughout the hearings, the Court made numerous comments to the effect that it was powerless to do anything - with regard to dealership rejections - other than approve the sale or not approve the sale (see May 29, 2009 Hearing Transcript at 298-299):

> THE COURT: All right, let me ask you one -- you propose something, but what authority do I have? I mean, the only real authority here that I think I have, I either approve the sale or I don't approve the sale. I don't have the authority -- I have the authority to say to New Chrysler I'm not approving the sale, but I don't have the authority to say to New Chrysler I'm approving the sale and I'm making you change it.

But the Court had the power to authorize the sale while refusing rejection approval as well. This was the course taken in *In re Lady H*, 193 B.R. 233 (Bankr. Ct. W.D. W.Va. 1996), a case overlooked by the Court's Opinion. In that case, the debtors moved the court to approve a 363 sale of assets free and clear of all liens and encumbrances. The debtors also sought to reject a collective bargaining agreement. The court granted the debtors' motion to sell property free and clear of all liens and encumbrances, holding that a sound business reason justified the sale, but the Court denied the debtors' motion to reject the CBA. It held that the balance of equities did not clearly favor rejection of the CBA. The Court then treated damages as a result of the CBA having been breached as a post petition administrative claim.

The issues surrounding what may become of an executory contract subjected to a rejection motion by a debtor facing a 363 sale of its assets when the rejection is not approved by

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

the Court are nebulous. Determining the exact effect of a Court's refusal to authorize rejection during a 363 sale appears to be an issue of first impression outside the collective bargaining arena. But a CBA is also governed by 365(a) as in Lady H. In Re Moline, 144 B.R. 75 (N.D. Ill., E.D. 1992) held, "...[M]ost collective bargaining agreements would be assumed by either inaction or denial of motions to reject...If the debtor elects to, or is forced to, assume the collective bargaining agreement under § 1113, the employees' claims, both prepetition and postpetition enjoy administrative priority." Id. at 88-89. And while the bankruptcy code provides no direct guidance, implied guidance can be discerned from Section 365(d)(1):

> In a case under chapter 7 of this title, if the trustee does not assume or reject an executory contract ...within such 60-day period...then such contract ...is deemed rejected.

Section 365(d)(4)(A) also includes an automatic rejection clause:

> Subject to subparagraph (B), an unexpired lease of nonresidential real property under which the debtor is the lessee shall be deemed rejected...

In a Chapter 11 proceeding, the Debtor will usually be reorganizing and the contract may "ride through" the bankruptcy, or the debtor may be selling assets in a 363 sale where the contract might be assigned. Both instances provide a non-debtor party with hope for a realization of the benefit of the contract, whereas in a Chapter 7, there really is no hope. The power granted a bankruptcy judge under 365(a) was thoroughly examined by the 1st Circuit in *In re Thinking Machines,* 67 F. 3d 1021 (1st Cir. 1995):

> "First and foremost, we think that the structure of the Bankruptcy Code and the nature of judicial oversight in the Chapter 11 milieu combine to make it highly likely that Congress intended judicial authorization to be a condition precedent to rejection. Bankruptcy is inherently a judicial process. From the moment that a

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

debtor's petition is filed in the bankruptcy court, the debtor's property is in custodial legis. See 1 William C. Norton, Jr., Norton Bankruptcy Law and Practice 2d Sec. 3:2 (1994). From that point forward, the bankruptcy court is charged with overseeing the trustee's management in order to ensure that the interests of the bankruptcy estate are served. See 4 Norton, supra, Sec. 77:4.

Judicial oversight of the reorganization process takes two forms. Many routine decisions are made by the trustee without any specific clearance from the bankruptcy court, and are reviewed (if at all) only in the course of an examination of the trustee's overall stewardship (say, when a plan of reorganization is proposed or when an application for fees is filed). Other decisions are not effective unless they are specifically sanctioned by the court. In those instances, judicial approval is almost invariably a condition precedent to the trustee's action.5 Arranging matters in this sequence facilitates judicial oversight, minimizes false starts, and enhances the efficiency of the process. We can think of no convincing reason why Congress would abruptly depart from this tried-and-true formula. More importantly, we are confident that if Congress wished to inaugurate so radical a change, it would have taken pains to mark the trail brightly.

A second reason for reading section 365(a) to require judicial approval as a condition precedent to rejection of a nonresidential lease is rooted in history. Congress enacted section 365(a) as part of the Bankruptcy Code of 1978, making court approval of such rejections obligatory for the first time. The predecessor to section 365(a), section 70(b) of the Bankruptcy Act of 1898, 11 U.S.C. Sec. 110(b) (repealed 1978), and the applicable bankruptcy rule governing actions taken pursuant to section 70(b), Fed.R.Bankr.P. 607 (repealed 1978), did not explicitly require judicial approval of a trustee's rejection of a lease, and many courts held that the trustee, acting alone, could make a rejection stick. See, e.g., Vilas & Sommer, Inc. v. Mahony (In re Steelship Corp.), 576 F.2d 128, 132 (8th Cir.1978). The conclusion is irresistible that Congress, by changing the protocol in 1978, intended to involve bankruptcy courts more actively in the decisional process. We believe that this policy of increased involvement is better served by viewing judicial approval as a condition precedent to the effectiveness of a rejection instead of as a condition subsequent.

In a related vein, we note that several courts have found support for requiring court approval as a condition precedent to rejection in two extant rules of bankruptcy procedure, namely, Fed.R.Bankr.P. 6006 and 9014. See, e.g., Revco, 109 B.R. at 268. Read together, these rules require a trustee who desires to reject a lease to file a formal motion to that effect. This, too, constitutes an innovation for, previously, the rules did not provide a formal procedure for rejecting leases.

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

> We think this is another sign that Congress intended courts to become more involved in the decisional process, and, thus, reinforces our vision of court approval as a condition precedent to a valid rejection of a nonresidential lease.
>
> The third reason for our view is that reading the statute in the manner favored by the district court tends to reduce a bankruptcy court's order of approval to a bagatelle. So interpreted, the provision would trivialize judicial oversight of the rejection process. Court orders are customarily important events in the life of a judicial proceeding; they are the primary means through which courts speak, see, e.g., Advance Financial Corp. v. Isla Rica Sales, Inc., 747 F.2d 21, 26 (1st Cir.1984), and they should carry commensurate weight. We see no reason for allowing a trustee to substitute his voice for that of the court. The trustee may sing all he wants, but it is the court that must call the tune. Cf. W.A. Mozart, Le Nozze di Figaro, Act 1, sc. 2 (1786) (Figaro's Aria)." In reThinking Machines, 67 F. 3d 1021.

Considering all of the above, *In re G Survivor* provides guidance as to the necessity that contracts designated for rejection by a debtor facing a 363 sale should be so designated *prior to* Court approval of the sale:

> "I see no reason to distinguish between a rejection motion returnable prior to the sale and one returnable after, if the rejection passes the business judgment test and the contracts to be rejected are designated prior to court approval of the sale contract.

In re G Survivor, 171 B.R. at 759. Indeed, this was quoted by Judge Gonzalez as well (see *In re Old Carco LLC* 406 B.R. at 208). The requirement of designating the contracts to be rejected *prior to* the sale authorization must be considered a due process device which would appear to fix the non-debtor party's rights to a point in time before which the decision to assume or reject has become moot by the debtor having no other choice due to his assets having been transferred via approval of the 363 transaction.

We respectfully assert that when all of the above is considered, the most likely intended result of a Court's failure to approve rejection in 363 sale environment would be to grant the non-

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

debtor party with an administrative expense claim against the Debtor's estate for damages due to the breach of his contract should that contract not be assumed and assigned to the purchaser of the debtor's assets. We believe the same result should accrue when the debtor assumes the contract, assigns it to the purchaser and the contract is later excluded by the purchaser. Allowing an administrative claim under those circumstances would not ever invalidate a 363 sale since the administrative claim would only be good against the debtor's estate.

When a bankruptcy judge holds that there is no benefit to the estate by rejecting an executory contract in the context of a 363 sale, such a holding would strongly indicate that the contract has value and should be preserved by the estate via assumption. Once a contract is assumed, if it is later rejected, the contract is treated as an administrative claim. *In re Klein Sleep*, 78 F.3d 18 (2d Circuit 1996). Should a debtor refuse to assume the contract after the court refuses to approve rejection, the non-debtor party should be entitled to an administrative claim as per *Lady H.* Or, the Debtor should be forced to assume the contract as was suggested in Moline. This puts force of law behind the requirement of court approval via 365(a). Any other result would "reduce a bankruptcy court's order of approval to a bagatelle". This could not be the intent of Congress.

Section 105(a), Equitable Powers of the Court.

The Court overlooked its inherent power as a court of equity. Considering that approximately 39,000 jobs were in jeopardy, rejected dealer reputations would be stigmatized, and that it was not disputed that many rejected dealers purchased excessive inventory in order to help save Chrysler, the Court should have at least considered its equitable powers under Section 105(a):

(a) The court may issue any order, process, or judgment that is necessary or

PIDGEON & DONOFRIO GP
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774

> appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.

In *Pepper v. Litton*, 308 U.S. 295, 60 S.Ct. 238, 84 L.Ed. 281 (1939), the Supreme Court stated:

> "The bankruptcy courts have exercised these equitable powers in passing on a wide range of problems arising out of the administration of bankrupt estates. They have been invoked to the end that fraud will not prevail, that substance will not give way to form, that technical considerations will not prevent substantial justice from being done."

Respectfully submitted this 25th day of December, 2009.

/s/ LEO C. DONOFRIO

On The Brief, Leo C. Donofrio, Esq.
NJ#00440-1991
Stephen Pidgeon, WSBA#25265
The Law Offices of Pidgeon & Donofrio GP
Old Federal Building
3002 Colby Avenue, Suite 306
Everett, Washington 98201
(425)605-4774
Attorneys for Certain Affected Dealers