

## Insolvency and Restructuring Update

### Significant Decision in Six Flags Chapter 11 Case Declining to Apply Disclosure Requirements of Bankruptcy Rule 2019 to an Informal Committee of Noteholders

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In an opinion issued on January 20, 2010 in the chapter 11 case of Premier International Holdings, Inc.,<sup>1</sup> an affiliate of theme park owner and operator Six Flags, Inc., Judge Christopher S. Sontchi of the Bankruptcy Court for the District of Delaware ruled that Rule 2019 of the Federal Rules of Bankruptcy Procedures (“Rule 2019”), which requires covered parties to disclose certain details regarding their claims against and interests in a debtor, does not apply to an informal committee of noteholders that appeared in the case. In so doing, Judge Sontchi disagreed with two recent decisions: *In re Northwest Airlines Corp.*<sup>2</sup> (“*Northwest*”), which ruled that an *ad hoc* committee of shareholders was required to comply with Rule 2019, and *In re Washington Mutual, Inc.*<sup>3</sup> (“*WaMu*”), which ruled that a group of noteholders was required to comply with Rule 2019.

This ruling comes in the midst of a heated debate over amendments to Rule 2019 that have been proposed by the Committee on Rules of Practice and Procedure of the Judicial Conference of the United States. The proposed amendments would broaden the rule’s disclosure requirements by, among other things, (i) expanding the covered parties to include the members of, and the parties represented by, “every entity, group or committee that consists of or represents more than one creditor or equity security holder”, every indenture trustee (unless otherwise ordered by the court) and, at the court’s discretion, *any single entity* that seeks or opposes the granting of any relief and (ii) expanding the types of disclosable economic interests for which a covered party must reveal the nature thereof, amounts held, dates acquired and, at the discretion of the court, prices paid, to include all claims, interests, pledges, liens, options, participations, derivative instruments, and any other rights or derivative rights that grant the holder an economic interest that is affected by the value, acquisition or disposition of a claim or interest.

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#### Rule 2019

Rule 2019(a) currently requires that “every entity or committee representing more than one creditor or equity security holder” (other than an official committee) and, unless otherwise directed by the court, every indenture trustee in a chapter 11 case file a verified statement disclosing: (i) “the name and address of the creditor or equity security holder”; (ii) “the nature and amount of the claim or interest and the time of acquisition thereof unless it is alleged to have been acquired more than one year prior to the filing of the petition”; (iii) “the pertinent facts and circumstances in connection with the employment of the entity or committee”; and (iv) “the amounts of claims or interests owned by the entity [or] the members of the committee . . . the times when acquired, the amounts paid therefor, and any sales or other disposition thereof.”

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<sup>1</sup> *In re Premier International Holdings, Inc.*, Case No. 09-12019 (CSS) [Dkt. No. 1423], (Bankr. D. Del. Jan. 20, 2010).

<sup>2</sup> *In re Northwest Airlines Corp.*, 363 B.R. 701 (Bankr. S.D.N.Y. Feb. 26, 2007).

<sup>3</sup> *In re Washington Mutual, Inc.*, 419 B.R. 271 (Bankr. D. Del. Dec. 2, 2009).

## Recent Case Law Interpreting Rule 2019

Historically, *ad hoc* (or informal) committees of creditors have rarely strictly complied with Rule 2019. In fact, Bankruptcy Judge Robert E. Gerber of the Southern District of New York recently wrote that he has “never seen a purported Rule 2019 submission . . . where all of the information Rule 2019 requires was actually provided.”<sup>4</sup> Typically, an *ad hoc* committee reveals the ownership of its members’ claims in the aggregate, but does not disclose the dates acquired, the prices paid or any dispositions of claims.

In 2007 in the *Northwest* bankruptcy case, the *ad hoc* committee of equityholders filed such a 2019 statement. The debtors filed a motion for an order compelling the *ad hoc* committee, which, according to the debtors’ motion, was “determined to try to disrupt and delay the reorganization process,” to strictly comply with Rule 2019.<sup>5</sup> Judge Allan L. Gropper of the Bankruptcy Court for the Southern District of New York held that the *ad hoc* committee of equityholders was a “committee representing more than one creditor or equity security holder” and was therefore governed by Rule 2019 and required to strictly comply with the rule’s disclosure requirements.<sup>6</sup>

Shortly thereafter Judge Richard S. Schmidt of the Bankruptcy Court for the Southern District of Texas issued a ruling in *In re Scotia Development LLC* denying a similar motion, holding that an *ad hoc* noteholder group was not a “committee” within the meaning of Bankruptcy Rule 2019 and declining to require the committee to make the Rule 2019 disclosures.<sup>7</sup>

On December 2, 2009, in the *WaMu* bankruptcy case, Judge Mary F. Walrath of the Bankruptcy Court for the District of Delaware considered whether Rule 2019 applied to a group of noteholders organized as a self-described “loose affiliation of creditors” for the purpose of sharing the cost of advisors. The *WaMu* Court held that under the plain language of Rule 2019, although the noteholders call themselves a group and not a committee, “they are in fact acting as an *ad hoc* committee or entity representing more than one creditor.”<sup>8</sup> The Court observed that they possessed “virtually all the characteristics typically found in an *ad hoc* committee, save the name.”<sup>9</sup> The Court ruled that Rule 2019 applies to *ad hoc* committees and required the committee to file the requisite disclosures.

### In re Premier International Holdings, Inc.

Premier International Holdings, Inc. and several of its affiliates, including Six Flags, Inc. (“SFI”), filed petitions for relief under chapter 11 of the Bankruptcy Code on June 13, 2009. SFI owns Six Flags Operations Inc. (“SFO”), which in turn owns Six Flags Theme Parks, Inc. (“SFTP”). SFI is a holding company, and the debtors conduct virtually all of their operations through SFO. SFTP owns, either directly or indirectly, all of the debtors’ theme parks. There were three committees involved in the case — the Official Committee of Unsecured Creditors (the “Official Committee”), the Informal Committee of SFO Noteholders (the “Informal Committee”) and the Ad Hoc Committee of SFI Noteholders (the “Ad Hoc Committee”). After failing to gain the support of any of the three committees for its initial plan of

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<sup>4</sup> Letter from Judge Robert E. Gerber to Advisory Committee on Bankruptcy Rules at 5 (Jan. 9, 2009).

<sup>5</sup> *In re Northwest Airlines Corp.*, Case No. 05-17930 at 3 (ALG) [Dkt. No. 4817] (Bankr. S.D.N.Y. Feb. 9, 2007).

<sup>6</sup> In a subsequent related decision Judge Gropper denied the *ad hoc* committee of equityholders’ request to file this information under seal. See *In re Northwest Airlines Corp.*, 363 B.R. 704 (Bankr. S.D.N.Y. Mar. 9, 2007).

<sup>7</sup> *In re Scotia Dev. LLC*, 2007 Bankr. LEXIS 4731 (Bankr. S.D. Tex. Apr. 18, 2007).

<sup>8</sup> *In re Washington Mutual, Inc.*, 2009 Bankr. LEXIS 3836 at \*10 (Bankr. D. Del. Dec. 2, 2009).

<sup>9</sup> *Id.* at \*9.

reorganization, the debtors proposed a revised plan that garnered the support of the Informal Committee, but such plan was opposed by the Official Committee and the Ad Hoc Committee.

On December 29, 2009, the Official Committee filed a motion to compel the Informal Committee to comply with Rule 2019 by disclosing the amount of each noteholder's respective claims (currently and previously held) against each debtor, the dates such claims were acquired, the amounts paid for the claims, and the dates and circumstances of any subsequent dispositions of the claims. The Official Committee further requested that, unless and until the disclosures were made, the Court bar the Informal Committee from participating in the case.

On January 20, 2010, the *Six Flags* Court issued an opinion holding that, under the plain meaning of Rule 2019, the Informal Committee was not a "committee representing more than one creditor." Judge Sontchi noted that the Oxford English Dictionary defines a "committee" as a "body of two or more people appointed for some special function by, and usually out of a (usually larger) body", and therefore "a self-appointed subset of a larger group — whether it calls itself an informal committee, an *ad hoc* committee, or by some other name — simply does not constitute a committee under the plain meaning of the word."<sup>10</sup> Judge Sontchi then examined the meaning of the word "represent" and determined that it contemplates "an active appointment of an agent to assert deputed rights."<sup>11</sup> Thus, the Court ruled that "under the plain meaning of the phrase 'a committee representing more than one creditor,' a committee must consist of a group representing the interests of a larger group with that larger group's consent or by operation of law."<sup>12</sup> The Informal Committee did not fit that description.

The Court then examined the legislative history of Rule 2019 and noted that while at first blush the legislative history would appear to support the expansive reading of the rule advanced by the *Northwest* and *WaMu* Courts, "a careful review of the facts and circumstances leading to the rule's adoption as well as its intended purpose [makes] clear that the informal and *ad hoc* committees as they exist today are very different from the 'protective committees' that were the target of the reforms in the 1930's."<sup>13</sup> In fact, the Chandler Act of 1938 (which first imposed the requirements currently found in Rule 2019) was so effective in curbing the power of protective committees that such committees had virtually ceased to exist within a few years of the Act's passage and the predecessor to Rule 2019 was, for all intents and purposes, superfluous almost immediately after its passage.<sup>14</sup> Furthermore, the Court noted that the Bankruptcy Code contains numerous protections for minority creditors that would prevent informal committees from engaging in the sort of abuses historically engaged in by protective committees. Thus, Judge Sontchi ruled, "Rule 2019 is also, for all intents and purpose, superfluous — the problem it was designed to address by requiring certain disclosures simply no longer exists."<sup>15</sup>

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<sup>10</sup> *In re Premier International Holdings, Inc.*, Case No. 09-12019 at 11 (CSS) [Dkt. No. 1423], (Bankr. D. Del. Jan. 20, 2010) (internal quotes omitted).

<sup>11</sup> *Id.* at 12.

<sup>12</sup> *Id.*

<sup>13</sup> *Id.* at 13. Judge Sontchi described the protective committees that formed in the equity receivership practice that evolved in the 1890's in connection with railroad reorganizations, and noted that, in stark contrast to today's informal committees, those protective committees (which were the target of the predecessor to Rule 2019) (i) were able to control completely the entire reorganization; (ii) were granted the authority to negotiate on behalf of and to bind creditors who had deposited their bonds with the protective committees; (iii) were so intimately involved with management as to virtually control the business; (iv) could force disparate treatment of similarly situated creditors; and (v) were able to steal the company for an inadequate upset price at a foreclosure sale by credit bidding their debt.

<sup>14</sup> *Id.* at 27.

<sup>15</sup> *Id.*

Finally, the Court noted its disagreement with the *Northwest* and *WaMu* decisions, which in Judge Sontchi's view did not properly and specifically analyze the plain language of Rule 2019 or its legislative history. Judge Sontchi also expressed the view that it would be a mistake to focus on the conduct and role of informal committees or groups only deep into the case (when Rule 2019 can be used as a litigation tactic) to determine whether the committee or group is a "committee" covered by Rule 2019. Rather, the Court noted, Rule 2019 should either be applied from the inception of the case or not at all.<sup>16</sup> Finally, Judge Sontchi took issue with the *WaMu* Court's use of the proposed changes to Rule 2019 to support its decision requiring a group of noteholders to comply with Rule 2019 (because the proposed changes should be of "no moment with regard to whether the rule applies in the first place[]") and opined that "there is nothing neither nefarious nor problematic, in and of itself, in disparate parties banding together to increase their leverage."<sup>17</sup>

## Future Implications

The proposed amendments to Rule 2019 have stirred up significant controversy, with certain Judges and other parties arguing strongly in favor of increased disclosure<sup>18</sup> and certain distressed investors and their representatives arguing that such disclosure is unnecessary and in some cases inappropriate (particularly the disclosure of acquisition dates and prices, which such investors argue is irrelevant to their statutory rights under the Bankruptcy Code).<sup>19</sup> A hearing on the proposed amendments to Rule 2019 is scheduled to be held in New York City on February 5, 2010. Comments to the proposed amendments must be submitted to the Advisory Committee on Bankruptcy Rules by February 16, 2010. It will be interesting to see to what extent this strongly worded opinion from the Delaware Bankruptcy Court (particularly Judge Sontchi's reasoned view that the rule is no longer necessary) may influence the debate. One thing that is certain is that it has become increasingly difficult to predict how other Judges will interpret the existing rule in the (at least) twenty-two months until the proposed rule (or some variation thereof) may become effective.

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<sup>16</sup> It is perhaps telling that in both the *Northwest* and *WaMu* cases the committees at issue were allegedly frustrating the debtors' efforts, whereas in *Premier International Holdings* the committee at issue was *supporting* the debtors' plan of reorganization, and the proponent of the motion to compel disclosure was opposing the debtors' plan.

<sup>17</sup> *Premier International Holdings* at 33.

<sup>18</sup> See, e.g., Letter from Judge Robert E. Gerber to Advisory Committee on Bankruptcy Rules (Jan. 9, 2009) (recommending amendments to Rule 2019 that broaden its disclosure requirements); Letter from Judge Robert D. Drain to Advisory Committee on Bankruptcy Rules (Jan. 13, 2009) (same).

<sup>19</sup> See, e.g., Letter from Loan Syndications & Trading Association and the Securities Industry & Financial Markets Association to Advisory Committee on Bankruptcy Rules (Nov. 30, 2007) (recommending that Rule 2019 be repealed).

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If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact

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