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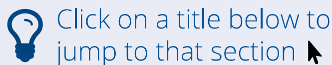

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Kamensky Forces More Scrutiny on Committee Process

by Stephanie Wickouski

No case in this century has riveted the attention of the restructuring community more than Daniel Kamensky's arrest and prosecution for his conduct while serving on the Neiman Marcus official committee of unsecured creditors (the "Committee").

Redefining the borders of creditors' entitlements in the pursuit of their own economic interests, the case raises the bar with respect to committee members' conduct. The case may portend the addition of layers of process to a bankruptcy system that is already laden with process.

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Garrett Motion Shareholders Applaud Exit Deal

by Christopher Patalinghug

Two shareholder factions in the bankruptcy case of Garrett Motion, Inc., recently agreed to resolve a dispute over the right to take the auto-parts maker out of Chapter 11 protection.

The first faction — dubbed the COH Group — is a consortium of stockholders led by Centerbridge Partners, L.P., and funds managed by Oaktree Capital Management, L.P., which partnered with Garrett's former parent Honeywell International Inc. and certain shareholders represented by a team of Jones Day lawyers. The COH Group sponsored a bankruptcy-exit plan to repay all creditors,

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Kamensky, *from page 1*

Neiman Marcus's pre-bankruptcy spinoff of its valuable MyTheresa business became a focal point of its Chapter 11 case, leading to an investigation of potential fraudulent conveyance claims arising from the spin-off. Those claims were ultimately settled in the Neiman Marcus plan of reorganization (the "Plan"). Under the settlement, certain Neiman Marcus sponsors would contribute their preferred stock in MyTheresa (the "MYT Stock") to the Plan, in exchange for the release of claims against them, including the fraudulent conveyance claims, and the unsecured creditors would receive the MYT Stock under the Plan.

The MYT Stock was not traded on any market and was illiquid, i.e., there was no easy way for unsecured creditors to liquidate it. Marble Ridge, a large bondholder on the Committee, intended to present a cash offer to the unsecured creditors for the MYT Stock, which would create a means by which those who did not wish to hold the MYT Stock could immediately receive cash.

Kamensky, Marble Ridge's representative on the Committee, learned from Committee counsel that investment bank Jefferies intended to present a materially higher competing offer for the MYT Stock. What ensued was a series of communications between Kamensky and Jefferies which ultimately led to Jefferies disengaging from presenting an offer.

The gravamen of the criminal charges is that Kamensky threatened Jefferies with withholding future Marble Ridge business if Jefferies did not withdraw its bid for the MYT Stock. The central count in the criminal complaint was 18 U.S.C. 152(6) (bankruptcy bid bribery), which states:

> … DANIEL KAMENSKY, the defendant, knowingly and fraudulently gave, offered, received, and attempted to obtain money and property, remuneration, compensation, reward, advantage, and promise thereof for acting or forbearing to act in any case under Title 11 of the United States Code, to wit, KAMENSKY pressured the Investment Bank [Jefferies] to withdraw its bid to purchase certain securities from the unsecured creditors by threatening to (i) use his position on the creditors' committee to ensure that the Investment Bank's bid would be rejected, and (ii) withhold Marble Ridge's future business from the Investment Bank, so that Marble Ridge could obtain those securities at a lower price (emphasis added).

Count Three (Extortion and Bid Bribery), *United States of America v. Daniel Kamensky* ("*Kamensky*").

Section 152(6) is most often applied in the context of a Section 363 sale of property of the estate in which one bidder attempts to bribe or coerce another bidder not to bid. Neiman Marcus did not involve a bankruptcy sale, but the disposition of illiquid stock distributed to creditors as part of a Plan settlement. This distinction, however, is irrelevant under Section 152(6), which is not limited to activities directly involving an asset of the bankruptcy estate, but simply actions "in a case."

Agreements between creditors to monetize non-cash distributions are not typically within the Bankruptcy Court's purview. Thus, offers to monetize such distributions — such as Marble Ridge's or Jefferies' offers — are arguably not "in a case" under title 11. However, in criminal cases, courts are not limited to civil bankruptcy law principles and tend to view facts from a broader, real world perspective. In the Neiman Marcus bankruptcy case, the MYT Stock was the product of settlement of estate claims, of which the unsecured creditors were the beneficiaries. Although not explicitly set out in the government's complaint, the creditors' avenue to monetize their distributions —which would be in the form of illiquid MYT Stock — was germane to their recovery and arguably central to the Neiman Marcus reorganization itself. Indeed, after the government filed its criminal complaint, Neiman Marcus filed a civil suit against Marble Ridge, which alleged that Kamensky's conduct eliminated a competitive bidding process and damaged the debtors and their stakeholders. The suit was settled, and Kamensky entered into a plea agreement with respect to the criminal charges against him, so the issues raised were never actually litigated.

Marble Ridge's membership on the Committee was inextricably tied to the criminal charges. As a Committee member, Marble Ridge's fiduciary duty ran not to Neiman Marcus, but to its unsecured creditors collectively. The unsecured creditors were the prospective sellers of the MYT Stock which Marble Ridge sought to buy — a clear conflict for Marble Ridge as a Committee member. But for the Committee seat, Kamensky may not have known of the competing offer

Kamensky, *from page 2*

or Jefferies' role in it — knowledge that led to Kamenksy's controversial communications with Jefferies and the resulting criminal charges. In a future case, committee professionals might exercise caution before providing information to a member with a conflict, such as informing Kamensky that Jefferies was about to make a competing offer. Predicaments such as this can also be avoided by bondholders being represented on a committee by their indenture trustee.

It is beyond peradventure that Kamensky's conduct, as a representative of a Committee member, was a breach of fiduciary duty to the unsecured creditors collectively. What is remarkable is the government's position that a breach of fiduciary duty in a bankruptcy case is criminally fraudulent.

Essential to a charge under 152(6) is that the conduct is "knowing and fraudulent." The government claimed that Kamensky's use of his position on the Committee, and his threat to withhold his future business from Jefferies, was knowing and fraudulent. The plain meaning of "fraudulent" is the use of lying or deception.

Kamensky was not literally lying or deceptive in his conversation with Jefferies, in which he demanded that Jefferies not proceed with a competing bid. Nevertheless, the characterization of this conversation as fraudulent is the core of the government's case. The government's construction of "fraudulent" is that intent to deprive creditors of a potential benefit constitutes fraudulent intent. Stated simply, fraud does not only mean lying, it also means stealing. Unless there is lying or stealing, there can be no crime.

If a committee member breaches his fiduciary duty to other unsecured creditors in a manner that is akin to stealing, that breach may be considered fraudulent. To conclude that an action was tantamount to stealing requires a determination of what was stolen and who it belonged to. These points were not fully explored in either the criminal case or in Neiman Marcus's civil suit.

Non-cash recoveries (for example, warrants, options, contingent value rights, restricted stock, or over-the-counter stock) are increasingly the currency of Chapter 11 plans. Most creditors lack the wherewithal to sell such assets themselves or the desire to hold them until they yield a cash return. The ability of a creditor to monetize such an asset immediately is often more important than the asset itself.

In many cases, creditors struggle to find ways to monetize non-cash recoveries such as illiquid securities. Neiman Marcus is a truly rare case: not only was there a party wanting to buy the illiquid MYT Stock, the opportunity to make an offer to buy the stock had real value.

Investors in distressed securities sometimes view investment opportunities that may accompany the ownership of distressed debt in a Chapter 11 case — such as providing litigation funding or exit financing, or monetizing non-cash recoveries — as soft entitlements of their investment. None of these are passive entitlements; all involve additional investment. On one hand, the exercise of these opportunities allows the investor to take a bigger piece of the reorganization pie. On the other hand, without investors willing to put new money at risk, there may be no pie. Indeed, the settlement which provided for the contribution of the MYT Stock to the Plan might not have occurred had it not been for Marble Ridge's initial funding and pursuit of fraudulent conveyance claims. Of course, this did not give Marble Ridge any exclusivity with respect to the purchase of the MYT Stock.

The *Kamensky* story is dramatic but seems familiar. Threats and boundary crossing in bankruptcy negotiations are not uncommon, although often more subtle and lacking repercussions. Notable here is that inter-creditor transactions were at the heart of the controversy. In future cases, transactions among creditors that were previously considered to be beyond the jurisdiction of the bankruptcy court may be subject to examination, particularly in the plan confirmation process.

The case is a warning sign that that creditor accoutrements — the opportunities that accompany a claim or a committee seat — do not necessarily belong to one creditor or committee member. Committee selection and process will now face closer scrutiny. *Kamensky* may force the restructuring industry to reexamine the way things are done, elevating the standard of care for professionals representing committees and for committee members. ¤

About the Author

Stephanie Wickouski is a partner in the New York Office of Locke Lord LLP. She is the author of Bankruptcy Crimes (Beard Books 3rd Ed.), Indenture Trustee Bankruptcy Powers & Duties (Beard Books 2015) and Mentor X: The Life-Changing Power of Extraordinary Mentors (Beard Books 2019).