

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE**

In re:)	Chapter 11
)	
Medley LLC,)	Case No. 21-10526-KBO
)	
Debtor.)	Hearing Date: Aug. 12, 2021 at 1:00 p.m.
)	Objection Deadline: Aug. 9, 2021 at 4:00 p.m.
)	(Extended by consent of the Debtor)
)	
)	Re: Docket Nos. 255, 284, 295, 299

LIMITED OBJECTION AND RESERVATION OF RIGHTS OF THE U.S. SECURITIES AND EXCHANGE COMMISSION TO MOTION OF THE DEBTOR FOR AN ORDER (I) APPROVING ON AN INTERIM BASIS THE ADEQUACY OF DISCLOSURES IN THE COMBINED DISCLOSURE STATEMENT AND PLAN (II) SCHEDULING THE CONFIRMATION HEARING AND DEADLINE FOR FILING OBJECTIONS, (III) ESTABLISHING PROCEDURES FOR SOLICITATION AND TABULATION OF VOTES TO ACCEPT OR REJECT THE COMBINED DISCLOSURE STATEMENT AND PLAN, AND APPROVING THE FORM OF BALLOT AND SOLICITATION PACKAGE, AND (IV) APPROVING THE NOTICE PROVISIONS

The U.S. Securities and Exchange Commission (the “SEC”) files this limited objection and reservation of rights to *Motion Of The Debtor For An Order (I) Approving On An Interim Basis The Adequacy Of Disclosures In The Combined Disclosure Statement And Plan (II) Scheduling The Confirmation Hearing And Deadline For Filing Objections, (III) Establishing Procedures For Solicitation And Tabulation Of Votes To Accept Or Reject The Combined Disclosure Statement And Plan, And Approving The Form Of Ballot And Solicitation Package, And (IV) Approving The Notice Provisions* [Docket No. 255] (“**Solicitation Motion**”) because the combined plan and disclosure statement (“**Amended Plan**”) fails to include support for key assumptions underlying the Amended Plan and lacks adequate information, as required under



Section 1125(b) of 11 U.S.C. §§ 101, *et seq.* (“**Bankruptcy Code**”). In addition, the Amended Plan includes overbroad release, exculpation, and injunction provisions.

1. The SEC is the federal agency responsible for regulating the U.S. securities markets, protecting investors, and enforcing the federal securities laws. In that capacity, the SEC is formally investigating whether Medley LLC (“**Medley**” or, the “**Debtor**”), and others, violated the anti-fraud and other provisions of the federal securities laws. The SEC has filed a proof of claim [Claim No. 11] in this case in connection with its contingent unliquidated claim against Medley for penalties and disgorgement.

2. On August 2, 2021, the Debtor filed the Amended Plan [Docket No. 284], which is jointly proposed by the Debtor, the Official Committee of Unsecured Creditors (“**Committee**”), and Medley Capital LLC (“**Medley Capital**”), a wholly-owned non-Debtor subsidiary. The clear beneficiaries of the Amended Plan are Medley Capital and Sierra Income Corporation (“**Sierra**”),¹ as Medley Capital’s officers and employees are recipients of a \$5.7 million employee compensation plan, Sierra is being provided with an extended off-ramp to find a new advisor, and both entities are receiving a release and exculpation.² Amended Plan, Articles I, V. However, the Amended Plan fails to provide critical information that the Debtor’s creditors, including the SEC, need to determine if the Amended Plan is in their best interests, including whether creditors would do better in an immediate liquidation.

¹ Richard T. Allorto, Jr. is Chief Financial Officer of Sierra, Medley Capital, and the Debtor.

² In addition, the Amended Plan accords certain professionals who were not retained in the bankruptcy case with administrative expense priority by allowing them to be paid in cash as soon as reasonably practicable after the claims are allowed. For example, although the retention applications for professionals of Peter Kravitz, as independent director of Medley Management Inc., were withdrawn [Docket Nos. 185, 186], certain of those professionals would be paid without any court oversight pursuant to the Amended Plan. Amended Plan, Article IV(B). Similarly, the Notes Indenture Trustee’s approximately \$716k claim would be paid in cash on the effective date. Amended Plan, Article I.

3. A key assumption of the Amended Plan is that Medley Capital would receive at least \$7.1 million under remaining company contracts, up to \$1.3 million in “profit,” and up to \$1.75 million from investments in subsidiaries. Amended Plan, Introduction (B).³ However, those funds are apparently dependent on clients remaining and not terminating their agreements through March of 2022. Amended Plan, Introduction (B); Article II(R). Accordingly, the amount available for distribution to the Debtor’s creditors may be far less than the Debtor is projecting. *See* Docket No. 295-1. The Debtor has not provided backup to support its assertion that such funds would be received from Sierra and others, despite repeated requests from the SEC.

4. Moreover, the Amended Plan does not provide an adequate explanation as to why some or all of those funds would not be available to the Debtor in a Chapter 7 or an immediate liquidation under Chapter 11. *See* Docket No. 295-1. Indeed, if some of these funds would be available, the difference between an immediate liquidation and the extended wind-down proposed by the Debtor may be much closer than the Amended Plan suggests.⁴ And, while the Debtor is concerned that an immediate liquidation could result in breach of contract claims against Medley Capital or the advisors and potential claw-back actions against the Debtor, the

³ Specifically, the Amended Plan provides that Sierra would contribute \$2.1 million to Medley Capital’s employee compensation to facilitate the continued performance under the Sierra Investment Advisory Agreement. Amended Plan, Introduction (B). Medley Capital would pay approximately \$3.6 million to its employees. *Id.* As a result of this extended wind-down, Medley Capital would make an approximately \$3.5 million “plan contribution,” \$1.3 million in additional “profit” would ultimately be available to the Liquidating Trust, and up to \$1.75 million would be realized from investments in subsidiaries in the extended wind-down scenario. *Id.*; Docket No. 295-1, 3.

⁴ The liquidation analysis does not include the funds discussed in the preceding footnote in a Chapter 7 liquidation. However, pursuant to Medley Capital’s operating agreement, it appears that Medley Capital has an obligation to distribute funds to the Debtor once its expenses are paid. Accordingly, it is unclear why none of the \$3.5 million “plan contribution” would be available in an immediate liquidation. In addition, it is unclear whether Medley Capital is currently holding funds that should have been distributed to the Debtor on August 1, 2021, pursuant to the terms of its operating agreement.

Amended Plan does not quantify the amount of any such potential claims, or discuss the advisers' rights to terminate their advisory agreements without liability pursuant to the terms of their contracts. *See* Amended Plan, Introduction (B).

5. The SEC has made repeated requests for financial projections and backup from counsel to the Debtor and the Committee, but has not received them.⁵ On August 6, 2021, counsel to the Debtor, the Committee, and Medley Capital represented to the SEC that they may be amenable to producing some or all of the requested information. Counsel to the Debtor noted that they would be amenable as long as Richard T. Allorto, Jr. (Chief Financial Officer to the Debtor, Medley Capital, and Sierra), has no objection to doing so. The SEC intends to file a motion for 2004 discovery, if such information is not provided promptly, and reserves all rights to supplement this Objection and to object at confirmation, including based on information provided pursuant to such requests. The SEC further reserves the right to object to the exculpation of certain officers, directors, and estate professionals relating to the contemplated post-petition transactions involving Medley Capital, as the transactions contemplated by the Amended Plan may improperly limit recovery for creditors and result in violations of fiduciary duties owed to the Debtor. The exculpation provision is discussed further below.

6. The Amended Plan contains the following overbroad exculpation, release, and injunction, and other problematic provisions:

- In the SEC's view, the exculpation clause set forth in Article XI(D) of the Plan constitutes an impermissible non-debtor release and discharge since it limits the liability of various non-estate fiduciaries for conduct that occurred prior to the

⁵ The SEC has requested such information since the beginning of the case. On July 28, 2021, the SEC made specific requests to the Debtor, including for financial projections, Medley Capital's balance sheet, timing and amount of payment from Sierra to SIC Advisors LLC, and the amount and timing of any distributions owing to the Debtor from its subsidiaries that have not yet been paid or are required to be paid through March 2022.

Chapter 11 case, and hence falls squarely within the scope of Section 524(e).⁶ See 442 B.R. 314, 350 (Bankr. D. Del. 2011), citing *In re PWS Holding Corp.*, 228 F.3d 224, 246 (3d Cir. 2000) (exculpations are limited to actions by estate fiduciaries in the bankruptcy case); see also *In re Aegean Marine Petroleum Network Inc.*, 599 B.R. 717, 721 (Bankr. S.D.N.Y. 2019) (proper exculpation provision is a protection not only of court-supervised fiduciaries, but also of court-supervised and court-approved transactions) citing *In re Granite Broad. Corp.*, 369 B.R. 120, 139 (Bankr. S.D.N.Y. 2007) (approving exculpation provision that was limited to conduct during the bankruptcy case and noting that the effect of the provision is to require “that any claims in connection with the bankruptcy case be raised in the case and not be saved for future litigation.”). The exculpated parties are defined as “(a) the Independent Manager, (b) the Medley Capital Executives, (c) the Creditors’ Committee and the members of the Creditors’ Committee (in their capacity as such), (d) Sierra, (e) the Notes Trustee, and (f) the Related Parties of the foregoing.” Amended Plan, Article I. The “Related Parties” in turn are defined as “with respect to any Person or Entity, such Person’s or Entity’s current and former direct or indirect subsidiaries and Affiliates and each of their respective current and former stockholders, members, limited partners, general partners, equity holders, directors, managers, officers, employees, agents, designees, attorneys, financial advisors, investment bankers, accountants, consultants, and other professionals or representatives solely to the extent acting in such capacity for a Released Party or an Exculpated Party.” *Id.* The exculpation provision should be revised so that it is limited to estate fiduciaries for postpetition conduct, and include a carveout for gross negligence.

- The Debtor has also failed to provide an adequate justification for its release of claims against the “Released Parties”, which include (a) Medley Capital, (b) Crowe, (c) Liao, (d) Richards, (e) Sierra, and (f) the Related Parties of the foregoing. The Liquidating Trust will be funded, in part, by estate causes of action. The Debtor has disclosed that Wells Notices were received by certain current or former officers of the Debtor. Amended Plan, Article I. Yet, the Debtor is providing broad releases, which could release Debtor claims against current and former officers and others, without providing adequate justification for doing so, as the “Related Parties” include “such Person’s or Entity’s current and former direct or indirect subsidiaries and Affiliates and each of their respective current and former . . . officers.”
- Because the Debtor is liquidating it is not entitled to a discharge under 11 U.S.C. § 1141(d)(3). Although the Amended Plan does not include a discharge provision, it still contains a permanent injunction, including of claims against the Debtor. Amended Plan, Article XI(E). To address this issue, the SEC requests

⁶ The Debtor filed a motion to schedule a combined hearing on the Amended Plan under Local Rule 3017-2. Local Rule 3017-2 is only available if the “plan of liquidation does not seek non-consensual releases/injunctions with respect to claims creditors may hold against non-debtor parties.” Local Rule 3017-2(a)(iii). Here, Local Rule 3017-2 is unavailable because the Amended Plan includes an exculpation provision which would release prepetition claims against non-Debtor third parties without the consent of the affected parties.

that the reference to the Debtor be stricken from the permanent injunction provision, and the following provision be added to the Plan:

Notwithstanding any provision in the Plan or Confirmation Order to the contrary, the Debtor will not receive a discharge of any debts, in accordance with Section 1141(d)(3) of the Bankruptcy Code.

- In addition, the Amended Plan discloses that the SEC has requested the preservation of certain documents. Amended Plan, Article II(I). However, the Amended Plan does not require the Debtor or Liquidating Trustee to maintain its books and records. To address this issue, the SEC requests that the following provision be added to the Amended Plan:

The Debtor and Liquidating Trustee shall retain and preserve all financial books and records, emails, and other financial documents relating to the Debtor's business prior to the bankruptcy filing that are currently in their possession. Neither the Debtor nor the Liquidating Trustee shall destroy or otherwise abandon any such documents or records without seeking further authorization from this court.

Notwithstanding anything to the contrary in the Plan or this Confirmation Order, nothing in the Plan or this Confirmation Order shall affect the obligations of the Debtor, the Liquidating Trustee, and/or any transferee or custodian to maintain all books and records that are subject to any governmental subpoena, document preservation letter, or other investigative request.

RESERVATION OF RIGHTS

7. The SEC reserves all rights to supplement this Objection, including on grounds not raised in this Objection.

Dated: August 9, 2021

Respectfully Submitted,

**UNITED STATES SECURITIES AND
EXCHANGE COMMISSION**

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on this 9th day of August, 2021, a true and correct copy of the foregoing Objection was furnished to all ECF Participants via the CM/ECF system, and further, served by email upon the following:

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