IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re: WELDED CONSTRUCTION, L.P., *et al.*,[1] Debtors.	Chapter 11 Case No. 18-12378 (KG) (Jointly Administered) **Re: Dkt. Nos. 17, 44, 246** **Hearing Date: November 30, 2018 at 10:00 a.m. (ET)** **Objection Deadline: November 27, 2018 at 12:00 p.m. (ET)**

OBJECTION OF OFFICIAL COMMITTEE OF UNSECURED CREDITORS TO DEBTORS' MOTION FOR FINAL ORDER (I) AUTHORIZING THE DEBTORS TO OBTAIN POSTPETITION FINANCING, (II) AUTHORIZING THE USE OF CASH COLLATERAL, (III) GRANTING LIENS AND SUPERPRIORITY ADMINISTRATIVE EXPENSE STATUS, AND (IV) GRANTING ADEQUATE PROTECTION

The Official Committee of Unsecured Creditors (the "Committee") of Welded Construction, L.P. and its affiliated debtor (together, the "Debtors"), by and through its undersigned proposed counsel, hereby submits this objection (the "Objection") to the *Debtors' Motion for Interim and Final Orders (I) Authorizing the Debtors to Obtain Postpetition Secured Financing, (II) Authorizing the Use of Cash Collateral, (III) Granting Liens and Superpriority Administrative Expense Status, (IV) Granting Adequate Protection, (V) Modifying the Automatic Stay, and (VI) Scheduling a Final Hearing* [Docket No. 17] (the "Motion").

PRELIMINARY STATEMENT[2]

1. The Debtors, a business on an apparently clear course to a near term wind down and likely liquidation, are owned directly and indirectly by Bechtel Gas and Chemicals, Inc.

[1] The Debtors in these chapter 11 cases, along with the last four digits of each Debtor's federal tax identification number, are: Welded Construction, L.P. (5008) and Welded Construction Michigan, LLC (9830). The mailing address for each of the Debtors is 26933 Eckel Road, Perrysburg, OH 43551.

[2] Capitalized terms used but not otherwise defined in the Objection shall have the meanings ascribed to such terms in the Motion, the Second Interim DIP Order (as defined below), and the DIP Credit Agreement.

("BGC") and McCaig US Holdings, Inc. ("McCaig US"). McCaig Welded GP, LLC ("McCaig GP"), an affiliate of McCaig US, is one of the general partners of Debtor, Welded Construction, L.P. ("Welded Construction"). The Debtors are governed by a board of managers. BGC has appointed three managers; McCaig US has a single appointee. BGC owns 75% of the equity of Welded Construction; McCaig US has the remaining 25%.

2. The DIP Lender, North American Pipeline Equipment Company, LLC, is likewise owned by affiliates of each of BGC and McCaig US and in the same percentages (the Bechtel entity owning 75% of the equity in the DIP Lender and the McCaig entity owning 25% of the DIP Lender). The DIP Facility, therefore, is an insider transaction, where the DIP Facility precisely mirrors BGC's and McCaig US' investments in the Debtors.

3. Thus far, the DIP Facility has been partially drawn to bridge the Debtors' liquidity in the immediate post-petition aftermath to project completion with respect to only the Columbia Gas Project. This has been its immediate and only positive function. Beyond that project, the DIP Facility's further purposes and timeline – along with the Debtors' ultimate financing needs – are ill-defined at present. The Debtors' general idea is that the remainder of the DIP Facility[3] will be used to fund receivables reconciliation and litigation, some asset sale activity (given required loan to value covenant maintenance, it is unclear whether such activity will involve marketing of the Debtors' equipment, a substantial source apparently of unencumbered value to the estate) and perhaps a plan process – all within the ambit of six months from the Petition Date.

[3] The DIP Facility's Initial Budget assumptions of failure to reach completion on most contracts and a high level of demobilization cost were appropriately conservative but incorrect. On November 10, the Committee received a revised Budget for the interim period that reduces the draws over the initial 13 week period and has received further supplemental information thereafter which the Committee continues to study and discuss with the Debtors concerning its impact on the overall DIP Facility.

4. While Debtor and Committee professionals have been actively engaged in discussions about the DIP Facility and other critical case issues as of the date of this Objection, the Committee has not received sufficient detail on the Debtors' case strategy and therefore the rights and liens of the DIP Facility. The Committee has received no extended forecast for the thirteen weeks following proposed final DIP approval that would pinpoint (or even frame) expenses needed beyond the current revised forecast, and no projections or model to get the Debtors to a plan and an exit. All that $212 million of unsecured creditors[4] have before them is a DIP Facility negotiated with equity in the exigent run up to bankruptcy when cash supporting an enterprise with over $1 billion of revenue dwindled to down to a mere $900,000 as of the Petition Date, and based on limited emergency marketing to other financing sources. Notwithstanding the significantly reduced draw amount in the Debtors' recently revised Budget, the DIP Facility places liens on all unencumbered asset value, significant value in real property, accounts, intangibles, equipment and actions, to support an ill-defined reorganization strategy and existing headquarters overhead. At a minimum, appropriate value or assets must be excluded and/or carved out for the benefit of unsecured creditors with respect to these valuable unencumbered assets ahead of any liens of the insider DIP Lender. Without such provisioning, the cost of the Debtors' initiatives may exceed the value created, especially when the unsecured creditors presently have access to unencumbered value that could provide for a meaningful recovery.

5. Further, the price of the insider DIP Facility to the Debtors and their creditors is high compared to other similar financings, which are designed to push through completion of a project or sell a key asset or are offered by insiders to settle claims against them. In essence, through the proposed DIP Facility, equity shifts risks associated with their structurally

[4] *See* First Day Declaration, ¶29.

subordinated position to general unsecured creditors, while liening substantial unencumbered assets (equipment, real property, proceeds of actions under chapter 5 of the Bankruptcy Code and tort claims) on a priming basis. And by priming possible incumbent security interests or liens, "equity" for the benefit of unsecured creditors in formerly unencumbered assets could be buried further behind these secured creditors (if any) and their purported secured claims.[5]

6. Inconsistent with the requirements of fairness pertinent to insider transactions of this type, the DIP Lender prices this deal to take profit, not simply to recover its protective lending on a present value basis. It structures the DIP Facility so that it can enforce its rights and remedies within 45 days of the Petition Date or some other DIP Lender approved timeframe if it refuses to reach agreement with its own affiliates, BGC, McCaig US and McCaig GP, and the Debtors, on yet to be determined case milestones. And the DIP Credit Agreement contains a host of provisions that relate to risks controlled by the Debtors (and their equity owners and, thus, their DIP Lender), which can generate artificial defaults and provides the DIP Lender with unfair leverage against the Debtors' estates.

7. The Committee is working hard with the Debtors to understand their plan for the next phase of these cases and the Debtors' position that there is a significant benefit of keeping these cases in chapter 11 past the point of project completion.[6] But absent a clear plan for driving value to creditors, supported by proper budgeting, the Committee must act to conserve the unsecured creditors' absolute rights in unencumbered assets. Accordingly, at present and as conformed, the Motion should be denied.

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[5] Adequate protection claims resulting from this priming are cross-collateralized against all of the Collateral.

[6] The Committee questions whether unsecured creditors may be better served through a structured conversion to chapter 7 due to the current winding up of the Consumers 2018 Project and the Williams/ASR Project. Nevertheless, the Committee is open to giving the Debtors the benefit of the doubt, at least in the early stages of these cases, and to allow their perceived vision of a chapter 11 solution to be properly defined and articulated to the Committee for consideration.

BACKGROUND

8. The Debtors filed their voluntary petitions on October 22, 2018 (the "Petition Date").

9. On the Petition Date, the Debtors filed the Motion. The Motion is supported by the First Day Declaration and a supplemental Pometti declaration.

10. On October 23, 2018, the Court entered the *Interim Order (I) Authorizing the Debtors to Obtain Postpetition Secured Financing, (II) Authorizing the Use of Cash Collateral, (III) Granting Liens and Superpriority Administrative Expense Status, (IV) Granting Adequate Protection, (V) Modifying the Automatic Stay, and (VI) Scheduling a Final Hearing* [Docket No. 44] (the "Interim DIP Order").

11. On October 30, 2018, the Office of the United States Trustee for the District of Delaware appointed the Committee pursuant to section 1102(a)(1) of the Bankruptcy Code. The Committee consists of (i) Ohio Machinery Co; (ii) Cleveland Brothers Equipment Co., Inc.; (iii) United Piping, Inc.; (iv) PipeLine Machinery International, L.P.; (v) Earth Pipeline Services, Inc.; (vi) IUOE and Pipe Line Employers Health and Welfare Fund; and (vii) Schmid Pipeline. *See* Docket No. 128.

12. That same day, the Committee selected Blank Rome LLP to serve as counsel to the Committee. The Committee also selected Teneo Capital LLC to serve as its financial advisor.

13. On October 23, 2018, the Court entered the *Second Interim Order (I) Authorizing the Debtors to Obtain Postpetition Secured Financing, (II) Authorizing the Use of Cash Collateral, (III) Granting Liens and Superpriority Administrative Expense Status, (IV) Granting Adequate Protection, (V) Modifying the Automatic Stay, and (VI) Scheduling a Final Hearing* [Docket No. 246] (the "Second Interim DIP Order" and together with the First Interim Order, collectively, the "Prior Interim Orders"). Among other things, the Second Interim DIP Order amended the

proposed DIP Facility to limit the releases and indemnities that previously extended to the equity owners (BCG, McCaig US and McCaig GP), affiliates and subsidiaries of the DIP Lenders. *See* Second Interim DIP Order ¶ 15; Ex. A to Second Interim Order (Amendments to the DIP Credit Agreement).

14. Through the Motion, the Debtors seek approval of a final order approving post-petition financing from the DIP Lender, an entity that is "under the common ownership with the partners of Welded Construction, L.P." (BGC, McCaig US, and McCaig GP) and is, therefore, an insider. Motion at ¶ 3, 22. Upon information and belief, the Debtors did not engage in a robust process with any reasonable timeline to identify financing; they focused their negotiations on BGC, McCaig US, McCaig GP and the DIP Lender. It appears that the Debtors did not have an independent board manager involved in the negotiations; rather all governance process involved managers affiliated with equity and the DIP Lender.

15. The proposed $20 million multiple-draw DIP Facility seeks to encumber substantially all the Debtors' assets, and to prime any existing liens in all such assets in exchange for a junior blanket lien granted to existing lienholders. Most of the Debtors' assets are presently unencumbered, including, upon information, $116 million of accounts receivable and related payment intangibles,[7] over $30 million of equipment,[8] and over $1 million of real property. Through the DIP Credit Agreement, the Debtors grant the DIP Lender *priming* liens under Bankruptcy Code section 364(d) on substantially all the Debtors' assets, including real property, accounts receivable and related payment intangibles, equipment, the goodwill/residual going concern value of the business, commercial tort claims, avoidance and similar actions, including

[7] *See* First Day Declaration at ¶16.

[8] The Debtors own equipment that is allegedly unencumbered by prepetition liens or security interests and that, according to ¶16 of the First Day Declaration, has an "appraised liquidation value of over $30 million."

potential actions against equity, and the proceeds of the foregoing. *See, e.g.*, DIP Credit Agreement, §10(u); Docket No. 92-3 (hereinafter the "Proposed Final DIP Order"), ¶1(d). Because of this priming, the Debtors also provide secured creditors that purportedly have incumbent first liens on certain Collateral with compensatory adequate protection liens on *all* DIP Collateral.[9] *See* Proposed Final DIP Order at ¶5.

16. While the DIP Facility is intended to provide committed working capital and a reliable source of liquidity for these estates in chapter 11, the DIP Lender can freely modify the DIP budget following the entry of the Final Order, in its sole discretion. *See* DIP Credit Agreement, §11.1(a)(i). Neither the Initial Budget nor the supplements explain satisfactorily the intended uses of the DIP Facility in the next phase of these cases post-project completion/contract termination, presumably because the Debtors have not yet formulated their plan, as mentioned above.

17. Given this budget fluidity, it is unclear how and when the DIP Facility will be repaid. And yet, the DIP Facility matures 180 days after the Petition Date (DIP Credit Agreement, §1.1); provided however, it could terminate as early as 45 days from the Petition Date if the DIP Lender and the Debtors are not able to agree on yet-to-be-disclosed "Bankruptcy Milestones" proposed in the sole discretion of the DIP Lender, which gives the DIP Lender a free option to declare a default since the Debtor and the DIP Lender are controlled by the same entities. *See* DIP Credit Agreement, §11(k); Proposed Final Order at ¶ 14.

18. Despite its broad DIP Collateral grant, the DIP Lender is willing to only lend against 75% of the fair market value of unencumbered equipment, as evidenced by the covenants

[9] Any such secured creditors are likely to have interests in equipment and the Debtors have identified a substantial equity in the equipment in excess of the DIP Facility if fully drawn. There is little risk to the DIP Lender for proceeding on a junior lien basis as to incumbent security interests and liens (particularly since the Debtors cannot identify relevant holders).

in the DIP Credit Agreement relating to the Loan to Collateral Value Ratio. *See* DIP Credit Agreement, §§9.2(f) & 10(bb).

19. The DIP Facility proposes a 10% interest rate. *See* DIP Credit Agreement, §4.1.

OBJECTION

A. The Committee Cannot Support the DIP Facility Without Clarity as to Budget and Case Strategy

20. Given recent developments in these cases, namely the (near) completion and the termination of certain projects and the funding of related costs, coupled with the simultaneous decrease in the need for certain operating capital by the Debtors at present, the Debtors do not need any portion of the DIP funding until January. Further, the Committee has not been provided with a clear model relating to DIP Facility usage and budgeting tied to a specific exit strategy.

21. Notwithstanding this state of affairs, the Debtors press forward with final approval of the DIP Facility and seek to encumber significant unencumbered assets, all prior to identifying how the DIP Facility will be repaid and how the DIP Facility will be used to increase creditor recoveries. This is unacceptable to the Committee. The Committee requires the Debtors to articulate to the Court, to creditors and to all stakeholders how the Debtors intend to size and use the DIP Facility to drive recoveries. The Debtors must do so with detail and pursuant to a concrete budget and strategic model that, among other things, shows how the DIP Facility will be repaid and from what sources of estimated achievable recovery, all in order to make the case that liquidating in chapter 11 provides a superior recovery than in chapter 7.

B. The Court Should Evaluate the DIP Facility Under the Entire Fairness Standard

22. Bankruptcy Code section 101(31)(C), in pertinent part, defines insiders among partnerships as "(i) [the] general partner in the debtor; (ii) relative of a general partner in, general partner of, or person in control of the debtor; (iii) partnership in which the debtor is a general

partner; (iv) general partner of the debtor; or (v) person in control of the debtor." 11 U.S.C. § 101(31)(C). Importantly, the Bankruptcy Code extends the definition of insider to any affiliate or insiders of affiliates "as if such affiliate[s] were the debtor." 11 U.S.C. § 101(31)(E).[10] The Debtors do not contest that the DIP Lender is an affiliate of Welded. *See* Motion at ¶¶ 3, 22 (noting that the DIP Lender is "an entity under common ownership with the partners of Debtor Welded Construction, L.P."). These partners include BGC, McCaig US and McCaig GP.

23. In determining whether to approve post-petition financing, courts typically will not substitute their own views regarding a proposed transaction as long as it is supported by a reasonable exercise of the debtor's business judgment.[11] *In re L.A. Dodgers LLC*, 457 B.R. 308,

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[10] The Bankruptcy Code defines "affiliate" as: "(A)entity that directly or indirectly owns, controls, or holds with power to vote, 20 percent or more of the outstanding voting securities of the debtor, other than an entity that holds such securities— (i)in a fiduciary or agency capacity without sole discretionary power to vote such securities; or (ii)solely to secure a debt, if such entity has not in fact exercised such power to vote; (B)corporation 20 percent or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by the debtor, or by an entity that directly or indirectly owns, controls, or holds with power to vote, 20 percent or more of the outstanding voting securities of the debtor, other than an entity that holds such securities— (i)in a fiduciary or agency capacity without sole discretionary power to vote such securities; or (ii)solely to secure a debt, if such entity has not in fact exercised such power to vote; (C)person whose business is operated under a lease or operating agreement by a debtor, or person substantially all of whose property is operated under an operating agreement with the debtor; or (D)entity that operates the business or substantially all of the property of the debtor under a lease or operating agreement." 11 U.S.C. §101(2).

[11] In evaluating whether proposed financing satisfies the business judgment standard, courts consider several factors, including:

(a) whether the proposed financing is an exercise of sound and reasonable business judgment;

(b) whether alternative financing is available on any other basis;

(c) whether the financing is in the best interests of the estate and its creditors;

(d) whether any better offers, bids, or timely proposals are before the court;

(e) whether the credit transaction is necessary to preserve the assets of the estate;

(f) whether the terms of the transaction are fair, reasonable, and adequate, given the circumstances of the debtor-borrower and the proposed lender;

(g) whether the financing is necessary, essential and appropriate for the continued operations of the Debtors' businesses and the preservation of their estates; and

(h) whether the financing agreement was negotiated in good faith and at arms' length between the Debtors, on the one hand, and the lenders, on the other hand.

See, e.g., *In re Farmland Indus., Inc.*, 294 B.R. 855, 879-80 (Bankr. W.D. Mo. 2003); *see also In re L.A. Dodgers LLC*, 457 B.R. at 312 (debtors have the burden of "proving that: (1) They are unable to obtain unsecured credit per 11

313 (Bankr. D. Del. 2011) ("[C]ourts will almost always defer to the business judgment of a debtor in the selection of the lender."). However, where, as here, the transaction involves an insider or insiders stand to benefit, the standard for approval is the much higher "entire fairness" review. *In re Zenith Elecs. Corp.*, 241 B.R. 92, 108 (Bankr. D. Del. 1999).

24. Under the "entire fairness" standard of judicial review, the Debtors must demonstrate that the challenged transaction is entirely fair to creditors both in terms of "fair dealing," which examines when the transaction was timed and how it was initiated, structured, negotiated and disclosed to the directors, and "fair price," which reviews the economics of and financial considerations in respect of the transaction. *Id*. (citing *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711 (Del. 1983)).

25. Other courts have held that transactions with insiders should be subject to a "strict scrutiny" standard of review. *See In re Keystone Surplus Metals, Inc.*, 445 B.R. 483, 488-90 (Bankr. E.D. Pa. 2010) (citing authorities and denying administrative expense status for postpetition loans from an insider without prior court approval); *WHBA Real Estate Ltd. P'ship v. Lafayette Hotel P'ship (In re Lafayette Hotel P'ship)*, 227 B.R. 445, 454 (S.D.N.Y. 1998) ("[S]ince there is an incentive and opportunity to take advantage . . . insiders' loans in a bankruptcy must be subject to rigorous scrutiny."), *aff'd*, 198 F.3d 234 (2d Cir. 1999); *Citicorp Venture Capital, Ltd. v. Comm. of Creditors Holdings Unsecured Claims (In re Papercraft Corp.)*, 211 B.R. 813, 823 (W.D. Pa. 1997) ("[I]nsider transactions are subjected to rigorous scrutiny and when challenged, the burden is on the insider not only to prove the good faith of a transaction but also to show the inherent fairness from the viewpoint of the corporation and those with interests therein.") (citing

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U.S.C. § 364(b), i.e., by allowing a lender only an administrative claim per 11 U.S.C. 503(b)(1)(A); (2) The credit transaction is necessary to preserve the assets of the estate; and (3) The terms of the transaction are fair, reasonable, and adequate, given the circumstances of the debtor-borrower and the proposed lender.").

Pepper v. Litton, 308 U.S. 295, 306 (1939)), *aff'd*, 160 F.3d 982 (3d Cir. 1998); *Stancill v. Harford Sands Inc. (In re Harford Sands Inc.)*, 372 F.3d 637, 641 (4th Cir. 2004) ("An insider's dealings with a bankrupt corporation are ordinarily subject to 'rigorous' or 'strict' scrutiny.") (citation omitted); *Norris Square Civic Ass'n v. St. Mary Hosp. (In re St. Mary Hosp.)*, 86 B.R. 393, 401-03 (Bankr. E.D. Pa. 1988) (denying debtor's proposed postpetition financing arrangement with its parent because the proposed financing gave the parent a superpriority lien on all unencumbered assets of the debtor, which the court found was not fair or reasonable considering the parties' relationship and the circumstances of the transaction).

26. Courts generally recognize that parties negotiating post-petition financing have unequal bargaining power. Accordingly, a debtor is often not the best party to ensure that the proposed terms of a DIP facility are fair to, and in the best interest of, all parties in interest, particularly a debtor's unsecured creditors. *See, e.g.*, *Otte v. Mfrs. Hanover Commercial Corp. (In re Texlon Corp.)*, 596 F.2d 1092, 1098 (2d Cir. 1979) ("The debtor in possession is hardly neutral. Its interest is in its own survival, even at the expense of equal treatment of creditors, and close relations with a lending institution tend to prevent the exploration of other available courses in which a more objective receiver or trustee would engage."). Post-petition financing should only be approved if "the financing agreement does not contain terms that leverage the bankruptcy process and powers or its purpose is not so much to benefit the estate as it is to benefit a party-in-interest." *In re Ames Dep't Stores*, 115 B.R. 34, 37-40 (Bankr. S.D.N.Y. 1990) (requiring onerous provisions to be modified before approving post-petition financing and noting that the court's discretion in determining whether to approve debtor-in-possession financing "is not unbridled").

27. Courts considering whether to approve post-petition financing "have focused their attention on proposed terms that would tilt the conduct of the bankruptcy case [and] prejudice, at

an early stage, the powers and rights that the Bankruptcy Code confers for the benefit of all creditors[.]" *See id.* at 37; *see also In re Mid-State Raceway*, 323 B.R. 40, 59 (Bankr. N.D.N.Y. 2005) ("[B]ankruptcy courts do not allow terms in financing arrangements that convert the bankruptcy process from one designed to benefit all creditors to one designed for the unwarranted benefit of the postpetition lender." (quoting *In re Def. Drug Stores, Inc.*, 145 B.R. 312, 317 (B.A.P. 9th Cir. 1992)); *In re FCX, Inc*, 54 B.R. 833, 838 (Bankr. E.D.N.C. 1985) ("[T]he court should not ignore the basic injustice of an agreement in which the debtor, acting out of desperation, has compromised the rights of unsecured creditors.").

28. In considering insider DIP financing, this Court has always been careful to balance the rights of unsecured creditors against case requirements and the demands of equity for Bankruptcy Code section 364(c) and (d) protections. The *Maxus Energy Corporation* case (No. 16-11501(CSS)) offers a good example of that balancing. There, the debtors sought to reorganize and propose a plan funded by their equity, which would release that equity from certain causes of action asserted by creditors against the debtor and also against equity. Recognizing that equity generally would have been expected to support the debtors' overhead and operating administration outside of bankruptcy, per this Court's final order approving same, the DIP facility was tranched and equity lent its debtor affiliate a Tranche B loan as a DIP to support overhead, etc., *but only on a subordinated basis* to the rights of unsecured creditors, while ensuring that the DIP could be treated in a plan if a monetization event had not occurred by DIP maturity to enable payoff. *See In re Maxus Energy Corp., et al.*, No. 16-11501 (CSS), Dkt. No. 268 at ¶2(i) (Bankr. D. Del., Aug. 19, 2016) (*Final Order Pursuant to Sections 362, 363 and 364 of the Bankruptcy Code and Rule 4001 of the Federal Rules of Bankruptcy Procedure (A) Authorizing the Debtors to Obtain Postpetition Financing and (B) Granting Related Relief*). Such an outcome is instructive here

considering the insider nature of the DIP Facility. Indeed, fairly, because of the existence of substantial unencumbered assets here, similar limitations or requirements need to be incorporated into the DIP Facility in these cases to respect the structurally senior rights of unsecured creditors as regards equity in these cases.

C. Fairness Requires the Establishment of a Creditor Fund as Part of the DIP

29. Because the proposed DIP Lender is an insider, it can influence (and may have influenced already) the Debtors' selection and structuring of its post-petition financing. This influence may manifest itself in various ways, such as the sizing of the DIP, the DIP's pricing and certain covenants therein, and the attendant risks the DIP shifts to unsecured creditors, whose recoveries may be compromised unfairly by the approval of the final DIP in its present iteration.

30. To counteract the burden placed on unencumbered assets by the DIP Facility in this uncertain next phase of these cases, this DIP Facility, in part, should be used to create a segregated fund for the benefit of holders of general unsecured creditors that is free and clear of rights, liens (including DIP Liens), and interests. The creditor fund would be part of a broad carve-out under the DIP Facility; a carve-out that would also include a proper winddown budget enabling an exit from chapter 11. This fund would provide an appropriate floor recovery for creditors in an amount that relates to the forced liquidation value of the Debtors' real property and equipment as of the Petition Date. The unsecured creditor fund could be used to platform a plan, but would be for the benefit of general unsecured creditors and its disposition in that context determined by the Committee.

D. Fairness Requires that the DIP Facility Be Structured under Bankruptcy Code Section 364(c) and Not on a Priming Basis

31. Even in a context where a creditor fund is created, the Committee questions the need for priming DIP Liens, which could transform unidentified incumbent secured claims with

limited prepetition lien rights into cross-collateralized obligations against all Debtor assets. This cross-collateralizing effect may further dilute unsecured creditor recoveries in these cases. Rather, the DIP Facility should be junior to any incumbent holder of a lien or security interest and the provision of adequate protection to such holders, if any, should be conditioned, expressly, on a demonstration that such holder's collateral has declined in value since the Petition Date.

E. Fairness Requires the Exclusion of Certain Assets from Collateral and from Sources of Recovery for the Proposed Super-Priority Administrative Claim

32. Avoidance Actions, commercial tort claims, actions relating to the relationship between the Debtors and affiliates and the Debtors' capitalization and generally in respect of insiders, including existing equity holders (BGC, McCaig US and McCaig GP), and personal property associated with the Debtors' residual going concern value, including, without limitation, rights to dispose of contracts with Consumers Energy Company ("CE") and certain pending bids, and the proceeds therefrom (collectively, "Excluded Property"), should be excluded from the DIP Collateral. Further, proceeds of Excluded Property should not be used to repay the DIP Superpriority Claim.[12]

33. The Excluded Property represents a source of recovery that should be reserved for the benefit of unsecured creditors. For example, the Committee has specifically negotiated for the preservation of the residual going concern value from the CE contract termination (certain phases of that contract remain salable post-termination for the estates' benefit). And if value is achieved from the sale of those remaining phases of the CE contract, that value will stem from the beneficial effect of the process of reorganization and not from direct support from the DIP Lender and the

[12] Whether the DIP Lender receives DIP Liens on avoidance actions or captures value from proceeds on account of the DIP Superpriority Claim under sections 364 and 507(b), the end result is the same: the DIP Lender is receiving a lien on a significant and financially controlling interest in the Avoidance Actions, including potential claims against the owners and affiliates of the DIP Lenders, who may be a target of the Avoidance Actions. Accordingly, both the Lien and the Super-Priority Claim must be subject to the proposed exclusion.

DIP Facility, which Facility is now, as best the Committee can tell, designed to drive value from accounts receivable and equipment. Generally, courts in this District have expressed their hesitation to grant liens on previously unencumbered assets of a debtor's estate, where such assets would otherwise inure to the benefit of unsecured creditors. *See* Hr'g Tr. 21:17-20, 26:9-23, *In re SFX Entm't, Inc.*, No. 16-10238 (MFW), Dkt. No. 198 (Bankr. D. Del. Mar. 4, 2016) (refusing to grant liens to DIP lenders on unencumbered assets, but permitting DIP lenders to retain liens on commercial tort claims to the extent such lenders had existing, perfected interests in such claims).

34. Indeed, Avoidance Actions (and similar claims designed to benefit the estates generally like commercial tort claims) are uniquely for the benefit of unsecured creditors, the principal residual risk-takers in the estate. The intent behind avoidance powers and a debtor's power to bring general causes of action is to allow the debtor in possession to gain recoveries for the benefit of all unsecured creditors. *See Buncher Co. v. Official Comm. of Unsecured Creditors of GenFarm Ltd. Partn. IV*, 229 F.3d 245, 250 (3d Cir. 2000).

35. Accordingly, bankruptcy courts customarily restrict the ability of debtors in possession to pledge avoidance actions and their proceeds as security. *See, e.g.*, *In re Tribune Co.*, 464 B.R. 126, 171 (Bankr. D. Del. 2011) (noting "that case law permits all unsecured creditors to benefit from avoidance action recoveries"); *Official Comm. of Unsecured Creditors v. Goold Electronics Corp. (In re Goold Electronics Corp.)*, 1993 WL 408366 at *3-4 (N.D. Ill. Sept. 22, 1993) (vacating lien on preference actions granted under DIP Financing order); *In re Sapolin Paints, Inc.*, 11 B.R. 930, 937 (Bankr. E.D.N.Y. 1981) (reciting "the well-settled principle that neither a trustee . . . nor a debtor-in-possession, can assign, sell or otherwise transfer the right to maintain a suit to avoid a preference").

36. Likewise, assets like avoidance actions and the net proceeds thereof should remain available for the primary benefit of the unsecured creditors, requiring courts to limit recoveries from such actions to pay super-priority claims under Bankruptcy Code section 507(b). *See, e.g.*, *In re Excel Maritime Carriers, Ltd.*, No. 13-23060 (RDD), Dkt. No. 133 (Bankr. S.D.N.Y. Aug. 6, 2013) (granting the use of cash collateral and adequate protection but excluding avoidance actions and proceeds thereof from property that could be used to pay super-priority claims under § 507(b) and from the scope of adequate protection liens).

37. In these cases, there may be potentially valuable, unencumbered Avoidance Actions and similar claims belonging to the Debtors' estates in respect of old equity. Certainly, the Debtors arrived in bankruptcy undercapitalized. And so, it is possible that old equity (BGC, McCaig US and McCaig GP) affiliates of the DIP Lender took voidable transfers or that the Debtors and their estates may have claims against such entities relating to the Debtors' capitalization level pre-petition. Any such claims could have significant value and, if they exist, the claims against or in respect of equity should not be subjected to DIP Lender control, which will have an incentive to bury such actions to benefit their affiliates. Rather, claims like this must remain unencumbered for the benefit of all unsecured creditors in these cases.

38. For these reasons, the DIP Collateral must exclude all Excluded Property including Avoidance Actions under Sections 544 through 551 of the Bankruptcy Code, commercial tort claims, other claims and assets that generally benefit a bankruptcy estate, and the proceeds of the each of the foregoing. Similarly, the DIP Superpriority Claim must not be payable from the proceeds of this Excluded Property.

F. Fairness Requires Changes to Pricing, Representations and Warranties and Covenants.

39. The 10% Interest Rate (*see* DIP Credit Agreement at § 4.1) charged under the DIP Facility materially exceeds the fixed rate equivalents on recent protective advance or insider DIP facilities approved by this and other courts. *See, e.g*., *In re Molycorp Minerals, LLC, et al.*, No. 15-11371 (CSS), Dkt. No. 120) (Bankr. D. Del. Sept. 26, 2016) (zero interest and no fees with lender to bear its own costs in an unsecured post-petition provided by surety of certain debtor affiliates); *In re Navillus Tile, Inc., dba Navillus Contracting*, No. 17-13162 (SHL), Dkt. No. 156 (Bankr. S.D.N.Y. Dec. 21, 2017) (3% interest and no lender fees payable in secured insider DIP facility); *In re Maxus Energy Corporation, supra* (7% interest in secured, partially subordinated insider DIP facility). Pricing in these cases is driven by highly specific factual contexts (*e.g.*, the need to get a very unique asset sold by a cash-strapped trustee) and these contexts, in turn, define DIP pricing (as opposed to some external, efficient marketplace).

40. Additionally, the DIP Credit Agreement provides that fees and expenses of the DIP Lender include "allocated costs of internal counsel." *See* (DIP Credit Agreement at § 24). The Committee expects this to be removed, as it would be inappropriate for a non-insider lender's salaried in-house counsel to be paid by the Debtor's estate, and is engaged in discussions on this point.

41. There are numerous representations and warranties, defaults and covenants under the DIP Credit Agreement that are not appropriate in this insider DIP Facility where the Debtor/Borrower is under common ownership and control of the DIP Lender and the DIP Lender is indirectly in control of the Debtors/Borrower's ability to comply with the covenants, representations and warranties in question.

42. Generally, the DIP Lender need not require representations regarding matters already known to it, including the Debtors' organizational status, equity ownership, authorization to enter into the transactions and prior financial condition. *See* DIP Credit Agreement, §10. Similarly, covenants and defaults requiring the Debtors to take or refrain from actions/events that are completely within the Debtors' control, and thereby within the DIP Lender's control, are not appropriate. *See* DIP Credit Agreement at §§ 11.1, 11.2 and 12. Perhaps most troubling is the proposed covenant in Section 11.1(k) of the DIP Credit Agreement, where the Debtors must cause the DIP Lender to agree, in the DIP Lender's sole discretion, on case milestones *after* final approval of the DIP Facility within 45 days of the Petition Date (i.e., on or prior to December 6, 2018, less than a week from the final DIP hearing) or some other date to be agreed to between the DIP Lender and the Debtors. *Id*. at 11.1(k)(ii). In sum, such provisions must be modified as the Committee requests.

G. Fairness Requires Modification of DIP Credit Agreement Provisions Relating to the Budget and Carve-Out.

43. The proposed DIP Facility provides a budgeting process that entirely replaces the estates' budget each week, in the sole and exclusive discretion of the DIP Lender without any input from the Committee. *See* DIP Credit Agreement at § 11.1. The Committee does not object to and in fact would require weekly compliance review and reporting in these cases. However, the concept of a continually rolling budget that gets extended on a week-by-week basis with no input from the Committee is not acceptable.

44. The DIP Credit Agreement requires modification to provide for: (i) a 13 week budget acceptable to the Committee running from the entry of the Final Order, which remains in effect (subject to the variance covenants) for such 13 week period absent any change thereto, and

(ii) at least 10 business days prior to the end of the last week of the budget, for the Debtors to propose, and for the Committee and the DIP Lender to review and approve, a new 13 week budget.

45. Further, the Budget needs to fund the Committee sufficiently and on a committed basis so that it can properly investigate causes of action that might benefit the estates, including in respect of equity. Likewise, the professional Carve-Out must be sufficiently topped off to enable Committee work.

46. Near absolute Budget control and limitations on reasonable Committee investigative work are inappropriate. The Committee's professionals must be able to assist their client to fulfill its duties under the Bankruptcy Code, which include investigating possible causes of actions against old equity. *Cf., In re Encore Healthcare Assocs.*, 312 B.R. 52, 56-58 (Bankr. E.D. Pa. 2004) (denying a Section 363 sale because such sale was solely for the benefit of the secured creditors and not the estate and further stating that courts approve such sales when they benefit all creditors, particularly unsecured creditors, or fund the debtor's ongoing business operations); *Comm. Of Equity Sec. Holders v. Lionel Corp. (In re Lionel Corp.)*, 722 F.2d 1063, 1071 (2d Cir. 1983); Hr'g Tr. 100:17-20, *In re NEC Holdings Corp.*, No. 10-11890 (PJW), Dkt. No. 224 (Bankr. D. Del. July 13, 2010) (stating that a DIP creditor must "pay the freight" of the bankruptcy case).

H. The Proposed Waiver of Section 506(c) Is Not Warranted Under These Facts

47. Absent an adequate budget for the full payment of all administrative claims to ensure the administrative solvency of these estates, including the timely payment of all normal course operating expenses, the advance waiver under section 506(c) of the Bankruptcy Code is inappropriate and must be denied. Specifically, the Second Interim Order provides that "[u]pon entry of the Final Order, no costs or expenses of administration which have been or may be incurred in the Chapter 11 Cases or any Successor Cases at any time may be charged against the

DIP Lender or any of its claims or the DIP Collateral pursuant to sections 105 or 506(c) of the Bankruptcy Code, or otherwise." Second Interim DIP Order, ¶10.

48. Section 506(c) of the Bankruptcy Code allows a debtor to charge the costs of preserving or disposing of a secured lender's collateral to the collateral itself. This provision ensures that the cost of liquidating a secured lender's collateral is not paid from unsecured creditor recoveries. *See Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 12 (2000). This section is designed to "prevent a windfall to the secured creditor . . . . [Section 506(c)] understandably shifts to the secured party . . . the costs of preserving or disposing of the secured party's collateral, which costs might otherwise be paid from the unencumbered assets of the bankruptcy estate . . . ." *Precision Steel Shearing, Inc. v. Fremont Fin. Corp. (In re Visual Indus., Inc.)*, 57 F.3d 321, 325 (3d Cir. 1995). Courts routinely reject the waiver of surcharge rights under Section 506(c) where the costs of the administration of the cases are not included in the budget. *See, e.g.*, *In re Colad Grp., Inc.*, 324 B.R. 208, 224 (Bankr. W.D.N.Y. 2005); *Hartford Fire Ins. Co. v. Norwest Bank Minn., N.A. (In re Lockwood Corp.)*, 223 B.R. 170, 176 (B.A.P. 8th Cir. 1998); *McAlpine v. Comerica Bank-Detroit (In re Brown Bros, Inc.)*, 136 B.R. 470, 473-4 (W.D. Mich. 1991). In this district, courts also refuse to enforce waivers of Section 506(c) surcharge rights when a creditors' committee objects to the waiver. *See, e.g.*, Hr'g Tr. 21:7-9, *In re Mortg. Lenders Network USA, Inc.*, No. 07-10146 (PJW), Dkt. No. 346 (Bankr. D. Del. Mar. 27, 2007) ("Well, let me tell you what the law in this Court's been for at least the last five years. If the Committee doesn't agree with the waiver, it doesn't happen."); *see also* Hr'g Tr. 212:12-22, *In re Energy Future Holdings Corp.*, No. 14-10979 (CSS), Dkt. No. 3927 (Bankr. D. Del. June 5, 2014) (declining to approve a 506(c) waiver over objection and stating that "Judge Walsh once told me that he'd never approve a 506(c) waiver on a non-consensual basis"); Hr'g Tr. 101:7-9, *In re NEC*

Holdings Corp., No. 10-11890 (CSS), Dkt. No. 224 (Bankr. D. Del. July 13, 2010) (stating that "you don't give a 506 waiver over an objection by the committee"). Given the uncertainty surrounding any chapter 11 case, the Debtors' creditors should not bear the risk of administrative insolvency.

49. Alternatively, and particularly because the DIP Lender is an insider seeking to lien unencumbered assets, if the Court is unwilling to strike the Debtors' waiver of their own section 506(c) rights, the Committee should be explicitly vested with standing to seek a surcharge against the DIP Lender's collateral if the facts ultimately prove that a surcharge is appropriate in these circumstances. Providing the Committee with standing to seek a 506(c) surcharge will preserve estate assets for the benefit of all unsecured creditors. Here, it is particularly appropriate because no party can seek to surcharge the Collateral and if the Debtors' waiver is approved, no other party will be able to assert this important right.

I. The Marshaling Doctrine Must be Preserved at this Early Juncture of these Cases.

50. The DIP Lender should not be exempted from its equitable duty to marshal its collateral in a liquidation. The Second Interim DIP Order provides as follows: "The DIP Lender shall not be subject to the equitable doctrine of 'marshaling' or any other similar doctrine with respect to any of the DIP Collateral." Second Interim DIP Order ¶ 17(e).

51. Such an exemption would enable the DIP Lender to cherry pick the collateral it could liquidate most expeditiously, without regard for the overall value realized by the estate. It would also allow the DIP Lender to liquidate collateral in a fashion calculated to maximize its recovery.

52. Although the common law doctrine of "marshaling" is generally an equitable remedy to be invoked by junior secured or lien creditors, sections 544(a) and 1107 of the

Bankruptcy Code confer upon the Debtors' estates the power to invoke marshaling to require a secured creditor to first satisfy its claims from previously encumbered assets, thus preserving unencumbered assets for the benefit of all creditors. *See Kittay v. Atl. Bank of N. Y. (In re Global Serv. Grp. LLC)*, 316 B.R. 451, 463 (Bankr. S.D.N.Y. 2004) ("The trustee has standing to invoke marshaling because he has the status of a hypothetical lien creditor."); *see also Berman v. Green (In re Jack Green's Fashions for Men Big & Tall)*, 597 F.2d 130, 133 (8th Cir. 1979) ("Federal courts of bankruptcy are courts of equity and may apply the doctrine of marshaling in proper cases. In this case it would be in the highest degree inequitable to allow the [secured lender] to exhaust the business assets of the corporate bankrupt without first looking to the real estate mortgaged to it. To permit such a course would leave the general creditors of the business with nothing.") (citation omitted).[13]

53. Importantly, given the uncertainties associated with the Debtors' strategy for these cases and the lack of clarity on how and when the DIP Facility will be repaid within its term, this may be a context where confining the DIP Lender to a particular source of recovery post-maturity may be necessary.

WHEREFORE, the Committee requests that the Court deny the Motion, and grant such other and further relief as is just and appropriate in the circumstances.

[13] If a debtor refuses to bring a colorable claim of marshaling, then an unsecured creditor may be granted derivative standing to do so. *See, e.g.*, *Official Comm. of Unsecured Creditors v. Hudson United Bank (In re America's Hobby Ctr., Inc.)*, 223 B.R. 275, 287 (Bankr. S.D.N.Y. 1998) ("[S]tanding in the shoes of the debtor in possession, the Committee can assert [marshaling] claim."); *In re Newcom Enters. Ltd.*, 287 B.R. 744, 750 (Bankr. E.D. Mo. 2002) (granting unsecured creditors' committee derivative standing to bring marshaling claim against secured lender, and thereby increase pay-out to unsecured creditors, where debtor refused to do so).

Dated: November 27, 2018
Wilmington, Delaware

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Proposed Counsel to the Official Committee of Unsecured Creditors of Welded Construction, L.P., et al.

CERTIFICATE OF SERVICE

I, Josef W. Mintz, hereby certify that on November 27, 2018, I served or caused to be served the foregoing *Objection of Official Committee of Unsecured Creditors to Debtors' Motion For Final Order (I) Authorizing the Debtors to Obtain Postpetition Financing, (II) Authorizing the Use of Cash Collateral, (III) Granting Liens and Superpriority Administrative Expense Status, and (IV) Granting Adequate Protection* upon the following persons via CM/ECF and the manner indicated below.

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