BANKRUPTCY COURT COMPELS WASHINGTON MUTUAL NOTEHOLDER GROUP TO DISCLOSE THE AMOUNTS OF THEIR CLAIMS AND PRICES PAID FOR SUCH CLAIMS

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To Our Clients and Friends:

On December 2, 2009, the United States Bankruptcy Court for the District of Delaware issued an opinion in the Chapter 11 proceeding of Washington Mutual, Inc. ("WMI"), holding that Rule 2019 of the Federal Rules of Bankruptcy Procedure requires that a group of holders of notes issued by WMI (the "Noteholder Group") disclose, among other things, the amounts of claims or interests owned by the members of the Noteholder Group, the time of acquisition of their claims and interests and the prices paid for such claims or interests. In finding that the Noteholder Group was an entity or committee representing more than one creditor within the meaning of Rule 2019, the court followed the controversial decision of the United States Bankruptcy Court for the Southern District of New York in *In re Northwest Airlines Corporation*, Case No. 05-17930 (Bankr. S.D.N.Y. Feb. 26, 2007), strictly applying Rule 2019 to *ad hoc* committees or groups of creditors. However, the Delaware Bankruptcy Court also broke new ground in suggesting that the Noteholder Group may owe fiduciary duties to other similarly situated creditors.

BACKGROUND

Rule 2019 requires any entity or committee, other than an official committee, representing more than one creditor or equity security holder, to disclose: (i) the names and addresses of those creditors and equity security holders represented, (ii) the nature and amount of their claims and interests, (iii) the time of acquisition of their claims and interests and the amounts paid therefore and (iv) the terms of any sales or other dispositions of any claims and interests. Courts have adopted inconsistent approaches in applying Rule 2019 to *ad hoc* committees or informal groups of creditors and equity security holders. In *Northwest Airlines*, Judge Allan L. Gropper of the United States Bankruptcy Court for the Southern District of New York compelled an *ad hoc* committee of equity security holders to comply with the disclosure requirements of Rule 2019 based on the finding that it was a group of shareholders holding similar claims who had elected to consolidate their efforts. In contrast, Judge Richard S. Schmidt of the United States Bankruptcy Court for the Southern District of Texas in *In re Scotia Development, LLC*, Case No. 07-20027 (Bankr. S.D. Tex. Apr. 18, 2007), denied a motion to compel an *ad hoc* noteholder group to comply with Rule 2019, finding that the noteholder group was not a committee within the meaning of Rule 2019.

Since the *Northwest* decision, certain industry groups, including the Loan Syndications and Trading Association and the Securities Industry and Financial Markets Association, have advocated the repeal of Rule 2019, arguing that it has the potential to affect the debtor's reorganization negatively by encouraging satellite disputes and discouraging active, efficient participation by certain investors.

DECISION

In compelling the Noteholder Group to comply with Rule 2019, Judge Mary F. Walrath rejected the Group's argument that it was not an entity or committee representing more than one creditor because it was only a loose affiliation of creditors who came together on an at-will basis to share the cost of advisory services and did not have the right to speak for or bind individual noteholders without their consent. Judge Walrath held that, in fact, the at-will nature of committee membership was one of the defining characteristics of *ad hoc* committees. Judge Walrath went on to find that the Noteholder Group possessed virtually all the characteristics typically found in an *ad hoc* committee, including that the Group consisted of multiple creditors holding similar claims that had filed pleadings and appeared in the case collectively, not individually. Moreover, the court noted that the Noteholder Group's counsel took its instructions from the Group as a whole. The Judge emphasized that it was the collective $1.1 billion in holdings of the members of the Noteholder Group that counsel used to argue in favor of the Noteholder Group's positions in the case. Judge Walrath argued that the case law supported her conclusion that the Noteholder Group was required to comply with Rule 2019, citing Judge Gropper's decision in the *Northwest* case while declining to follow the *Scotia Development* decision because it lacked legal reasoning.

Finally, of potentially broader consequence was Judge Walrath's response to the Noteholder Group's contention that Rule 2019 was not intended to apply because the Group did not speak on behalf of other noteholders in a fiduciary capacity. Judge Walrath suggested that creditor or shareholder groups may owe fiduciary duties to other members in the same class. While Judge Walrath declined to delineate the precise extent of fiduciary duties owed by such groups, she stated that collective action by creditors in a class implied some obligation to other members of that class.

IMPLICATIONS

With this decision, the bankruptcy courts in the two most popular venues for corporate bankruptcy filing have interpreted Rule 2019 to apply to *ad hoc* committees and groups of creditors or equity security holders.

In addition, this decision raises a new potentially troubling issue by suggesting that creditors or equity security holders acting as a group in a bankruptcy case may be assuming fiduciary duties to other similarly situated creditors or equity security holders. The scope of these

fiduciary duties will only become clear as other courts determine whether and how to apply the holdings in this case.

This is not likely the last word regarding Rule 2019 inasmuch as an amendment to Rule 2019 has been proposed by the Judicial Conference Advisory Committee on Bankruptcy Rules, which in its current form generally contemplates expanding the scope of disclosure required under Rule 2019. Public comments on the proposed amendment are due by February 16, 2010 when the Advisory Committee will determine whether to submit the proposed amendment to the Standing Committee on Rules of Practice and Procedure.

Please feel free to contact us with any questions.

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