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**UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK**

In re:	:	Chapter 11 Case
MOTORS LIQUIDATION COMPANY, <i>et al.</i> ,	:	Case No. 09-50026 (MG)
Debtors.	:	(Jointly Administered)
<hr/>		
MOTORS LIQUIDATION COMPANY AVOIDANCE ACTION TRUST, by and through the Wilmington Trust Company, solely in its capacity as Trust Administrator and Trustee,	:	Adversary Proceeding
Plaintiff,	:	Case No. 09-00504 (MG)
vs.	:	
JPMORGAN CHASE BANK, N.A., individually and as Administrative Agent for Various Lenders Party to the Term Loan Agreement described herein, <i>et al.</i> ,	:	
Defendants.	:	

**TERM LENDERS' SUPPLEMENTAL BRIEF ADDRESSING
REGIONAL RAIL REORGANIZATION ACT DECISION**

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The Term Lenders respectfully submit this memorandum pursuant to this Court's April 17, 2017 Order directing that the parties submit supplemental briefs addressing the Special Court's decision in *Matter of Valuation Proceedings Under Sections 303(c) and 306 of Regional Rail Reorganization Act of 1973*, 445 F. Supp. 994 (Sp.Ct.R.R.R.A. 1977) ("Regional Rail").

INTRODUCTION

Regional Rail is similar to this case in some respects, and dissimilar in others. As here, *Regional Rail* involved a government-sponsored entity established to help ensure the continued viable operation of an industry deemed vital to the national economy. And as here, a court was charged with determining the value of assets transferred during a period of turmoil.

Regional Rail, however, applied a different statute to a different factual situation. In *Regional Rail*, the statute required the court to determine the "Net Liquidation Value" of the relevant assets, and the Special Court, in the portion of the opinion quoted in this Court's April 17, 2017 Order, addressed the "Constitutional Minimum Value" that the Government would have to pay in the "exercise of eminent domain." *Id.* at 1001, 1031, 1044-45. Here, in contrast, under Section 506(a)(1) of the Bankruptcy Code, property is to be valued based on its "proposed disposition" — in this case, the sale of Old GM assets to New GM so that the assets could continue to be used to manufacture automobiles for what continues to be the most valuable automobile manufacturer in the United States producing a full range of vehicles.

In *Regional Rail*, moreover, the Government took property from railroad companies with aging assets that "want[ed] to exit from the railroad business." *Id.* at 1017; *accord id.* at 1032. In that context, where the transferors wished to cease operations, the Special Court suggested that a "figure related to original cost" may be a useful valuation metric, because the "transferors" would have "no just grievance" if they received the book value of their assets less depreciation. *Id.* at 1030-31.

Here, on the other hand, GM very much sought to remain in the auto manufacturing business. The Section 363 sale achieved that objective. Thus, the issue here is

not what the Government would have to pay to take Old GM's assets — the Government *already* paid for the assets: it provided financing to Old GM, and then it used that financing to purchase GM's assets so that the firm's going-concern value would be preserved and enhanced. All of Old GM's stakeholders, *including unsecured creditors*, benefited tremendously from the consideration paid by the Government. As a result of the Government-supported purchase, the unsecured creditors were distributed 10% of New GM's equity, plus warrants for 15% of the equity. The unsecured creditors, therefore, captured a healthy slice of the going-concern value of GM's assembled assets. And yet, in this litigation, their representative (the Avoidance Trust) is trying to limit Old GM's secured lenders to the liquidation value of those very same assets.

Nevertheless, although *Regional Rail* involved a different statutory scheme and different facts, the Special Court's guidance in that case may be useful to this Court. The Special Court, faced with valuing assets of distressed railroad companies, pointed to net book value as "a figure which can be ascertained, with relative ease and without much guesswork, from records whose maintenance has long been required." *Id.* at 1045. The court further explained: "It should be clear that we are not suggesting that a figure related to original cost is the best indication of [Constitutional Minimum Value]. Instead, we propose it only as a possible check on shortcomings we fear may develop in the usual valuation method focusing on market values." *Id.* at 1031. Accordingly, the Special Court "place[d] the parties on notice that [it] may feel obliged to resort to some kind of analysis related to original cost and that they should present evidence accordingly." *Id.*

With that admonition in mind, the Term Lenders are providing a supplemental exhibit drawn from GM's books and records that will be submitted in evidence that will enable the Court to use net book value as a useful "check" on valuation or, if it chooses, as the value of the assets themselves. That evidence (summarized below) will further confirm the reliability of KPMG's individual RCNLD asset valuations and the appraisals of Carl C. Chrappa. For unlike *Regional Rail*, where the claimed RCNLD values were many multiples of the relevant book values (*see id.* at 1032), both the RCNLD values determined by KPMG and the values

determined by Mr. Chrappa here are similar to — and in many cases lower than — the net book values of the assets. In contrast, it is the liquidation values proffered by the Avoidance Trust’s experts (and the TIC-adjusted KPMG values) that diverge from the *Regional Rail* checkpoint.

POINT I

THE RELATIONSHIP BETWEEN THE REGIONAL RAIL DECISION AND THIS CASE.

A. The statutory schemes

In considering *Regional Rail* in the context of this case, the necessary starting point is the statutory schemes involved.

The Special Court was focused on determining the minimum amount the Government was required to pay for railroad assets to avoid a Constitutional violation, under a statute that provided a “Net Liquidation Value” standard. In considering that issue, the court addressed the valuation principles that govern in the eminent domain context. *Id.* at 1015-16. In particular, the Special Court stated that, for purposes of an eminent-domain valuation, the U.S. Government was required to be wholly ignored as a possible purchaser: “inclusion of the taker in the market, in the sense of here attempting to reconstruct a bargaining process between the transferors and the United States, is inconsistent with the basic principle of eminent domain.” *Id.* at 1015.

Here, in contrast, the required valuation standard is set forth in Section 506(a)(1) of the Bankruptcy Code, which requires valuation to be based upon the “proposed disposition” of the property:

Such value shall be determined in light of the purpose of the valuation and of *the proposed disposition or use of such property*, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor’s interest. (Emphasis added).

As the Supreme Court has made clear, Section 506(a)(1) — which was enacted after the *Regional Rail* decision — “expressly addresses how ‘value shall be determined’” when,

as here, a bankruptcy court is required to value a lender's collateral. *Assocs. Commercial Corp. v. Rash*, 520 U.S. 953, 962 (1997) (quoting 11 U.S.C. § 506(a)(1)). Under the statute, "the 'proposed disposition or use' of the collateral is of paramount importance." *Id.* Per the Supreme Court, "[t]hat *actual* use, rather than a foreclosure sale" or some other event "that *will not take place*, is the proper guide" in valuing collateral. *Id.* at 963 (emphasis added). The statute's "governing instruction" to focus on what the debtor actually proposes to do with its assets, and to ignore hypothetical alternatives, supplies a "simple rule of valuation" that fosters "predictability and uniformity." *Id.* at 965. Nothing in Section 506(a)(1) remotely suggests that the Government is to be ignored in this context or that eminent domain standards should be imported into the Bankruptcy Code.

In *Rash*, therefore, the Supreme Court concluded that a truck pledged as collateral by a chapter 13 debtor should be given its "replacement value," not its liquidation or "foreclosure value," where the truck would continue to be used by the business conducted by the debtor. *Id.* at 963-64. Similarly, in *ResCap*, this Court concluded that, where a debtor filed for bankruptcy intending "to market and sell" lenders' collateral "as a going concern," the valuation of the collateral had to be "based on the proposed disposition of the collateral" — namely, its value as a going concern, not foreclosure or liquidation value. *In re Residential Capital, LLC*, 501 B.R. 549, 594-95 (Bankr. S.D.N.Y. 2013).

Here, the proposed (and actual) disposition of the vast majority of the Term Lenders' collateral was a going-concern sale. The Government took action to facilitate that sale, and it is pointless to debate what would have happened had it not done so. In approving the Section 363 sale, the Court expressly found that the sale transaction "was the product of intense arms'-length negotiations" and that the Court was "equally satisfied" with the "purchase price." *In re General Motors Corp.*, 407 B.R. 463, 494 (Bankr. S.D.N.Y. 2009). The Court observed that "the GM Board even secured a fairness opinion from reputable advisors, expressing the opinion that the consideration was, indeed, fair." *Id.*

The price paid by the Government included a credit bid of the Government's secured debt position. Old GM's other existing secured creditors were repaid in full. And, as noted, Old GM's unsecured creditors massively benefitted from what they now characterize as the Government's largesse: Old GM received fully 10% of New GM's equity for the benefit of unsecured creditors, plus warrants to purchase up to 15% more. GM's financial advisor, Evercore, valued this consideration at between \$7.4 billion and \$9.8 billion. It would be perverse indeed if unsecured creditors garnered this significant recovery based on a going-concern sale that was proposed and then effectuated with the benefit of Government assistance, but secured lenders were relegated to a valuation measure predicated upon a liquidation that was neither proposed nor effectuated.

B. Application of Section 506(a)(1) to this case

Given that, under Section 506(a)(1), the assets sold to New GM should be ascribed their going-concern value — and not some lower value that could be obtained through a piecemeal liquidation — the trial will show that the RCNLD values determined by KPMG, as well as the values resulting from the asset appraisals conducted by Mr. Chrappa, are the best evidence of that going-concern value. Those values accurately reflect the reality that Old GM sold its assets to a buyer that would use the assets to manufacture automobiles, and they take account of physical depreciation and obsolescence. As will be shown at trial, the complementary valuation approaches used by KPMG and Mr. Chrappa are widely accepted and — unlike a liquidation standard — are specifically designed to value assets in place and in use as part of a going concern.

In addition, contrary to the Avoidance Trust's repeated assertions (KPMG Motion in Limine at 4, 5), the evidence at trial will show that it is simply not true that KPMG only valued *categories* of assets and not individual assets themselves. As will be demonstrated at trial, KPMG assigned specific RCNLD values to over 430,000 individual assets based on a “ground-up” valuation method that involved a huge effort by dozens of individuals over many months. *See* DX-0346 (spreadsheet calculating individual asset values for Personal Property);

DX-0345 (spreadsheet calculating individual asset values for Real Property and Leaseholds). It was only the TIC adjustment that was imposed on a categorical basis from the “top-down,” with the same percentage reduction being applied to each asset within select categories.

Once again, the Supreme Court’s decision in *Rash* is illuminating. The Supreme Court — applying its holding that collateral must be valued based on its “actual” disposition or use — concluded that a truck pledged as collateral by a chapter 13 debtor should be afforded its “replacement value,” not its liquidation or “foreclosure value,” because the truck would continue to be used by the debtor to generate income. *Rash*, 520 U.S. at 963-64. Subsequent cases have likewise held that where, as here, collateral is proposed to be used on a going concern basis, replacement value is an appropriate valuation standard. *See, e.g., In re Castleton Plaza, LP*, 2011 WL 4621123, at *3 (Bankr. S.D. Ind. Sept. 30, 2011) (noting that “*Rash* expressly forbids use of a foreclosure or distressed-sale standard for purposes of § 506(a)” and applying replacement value standard to shopping center assets).¹

C. The discussion of RCNLD in *Regional Rail*

In setting forth its views concerning Constitutional Minimum Value in *Regional Rail*, the Special Court stated that it would not consider reproduction cost, RCNLD or similar valuation metrics because those values would not be realized and indeed the transferors “want[ed] to exit from the railroad business.” *Regional Rail*, 445 F. Supp. at 1017. The court suggested that RCNLD and reproduction cost could only be applicable for an enterprise that wanted to continue to operate in business and was anticipated to be profitable. *Id.* at 1017, 1032, 1036. The court also observed that reproduction cost and RCNLD simply could not be calculated in the circumstances presented, stating that applying such a “measure of value in a case like this would lead into a never-never land where this court and the parties would perforce spend long years in the quest of a goal that is unattainable and not worth attaining.” *Id.* at 1032.

¹ *Accord, e.g., In re Nuts & Boltzs, LLC*, 2010 WL 5128961, at *3-4 (Bankr. D.S.C. July 2, 2010) (valuing inventory collateral on replacement cost basis); *In re TennOhio Transp. Co.*, 247 B.R. 715, 720 (Bankr. S.D. Ohio 2000) (replacement value appropriate standard under § 506(a)).

The court went on to observe that “no one knows what RCNLD means” and that determining each of the relevant inputs of RCNLD — from RCN to functional and capacity-based obsolescence — would result in great “uncertainties” and “difficulties.” *Id.* at 1032-33. The court was also troubled by the notion that, if the replacement value of land owned by the railroads were based on “the current value of adjoining real estate,” the transferors would get the benefit of major “public improvements” undertaken by state and local governments. *Id.* at 1034.

These rationales for declining to consider RCNLD as a measure of value — the nature of the transaction and the difficulties in using RCNLD as a measure of value — are decidedly *not* present here. *First*, the Section 363 sale enabled GM to remain in the auto manufacturing business under new ownership with a new capital structure. The same management team continued to operate the most valuable assets under the same name with the same employees and selling the same products. And Old GM’s unsecured creditors obtained a major equity stake in the recapitalized company, realizing significant going-concern value.

Second, RCNLD and reproduction cost here are readily identifiable and are not, as was the case in *Regional Rail*, mere “fantasies of ‘experts.’” *Id.* at 1045. Rather, as the evidence at trial will show, KPMG conducted a contemporaneous from-the-ground-up valuation of hundreds of thousands of individual assets, using pre-existing and highly reliable replacement cost information from GM itself. KPMG devoted tremendous resources to the RCNLD valuations and did so outside a litigation context.

Moreover, while the *Regional Rail* court expressed concern about determining RCNLD or reproduction cost for old railroads in a situation where there had been “practically no construction of new lines” for years (*id.* at 1033), that is not the case here. In the five years leading up to its bankruptcy, GM invested \$37.7 billion in plants, facilities and equipment. DX-0016-0078 and DX-0017-0111. In light of GM’s continued investments in its facilities, the manufacturing assets were well maintained and in good condition. Thus, unlike in *Regional Rail*, where the Special Court was confronted with the utterly fantastical replacement of, among other things, the land and rights of way underlying decades-old rail lines across numerous states, the task here is a straightforward

valuation of properly-cared-for manufacturing equipment. And unlike in *Regional Rail*, the value of that equipment does not depend on large-scale “public improvements” to related assets or land.

In addition, the evidence shows that both KPMG and Mr. Chrappa applied the very deductions that the *Regional Rail* court deemed would be necessary and did so in reliable ways — ways that even the Avoidance Trust cannot reasonably dispute here because its own expert, Mr. Goesling, used essentially the same methodology in valuing assets on a cost basis. In particular, to the extent that the relevant assets were subject to “functional depreciation,” which the Special Court described as “[p]erhaps the most difficult question” (*id.* at 1033), the evidence will show that both KPMG and Mr. Chrappa included adjustments. Both KPMG and Mr. Chrappa also applied substantial discounts based on physical deterioration and limits in utilization.

Finally, unlike in *Regional Rail*, where adopting RCNLD measures would have “doomed” the court to “spend years in an enterprise as unsatisfying as it will be interminable” (*id.* at 1044), the opposite is true here. As noted, KPMG assigned individual values to virtually all of the assets GM acquired in the Section 363 sale. It is the Avoidance Trust’s liquidation value approach — an approach that is, in any event, legally flawed — that would doom this Court to interminable disputes. *See* Defendants’ Amended Pre-Trial Brief at 50.

* * *

One other point bears noting: Apart from liquidation value, which should be rejected under Section 506(a)(1) for the reasons stated in Defendants’ Amended Pre-Trial Brief (Point III), the Avoidance Trust’s experts did not present any evidence, even in the alternative, valuing the Representative Assets based on a going-concern value. Whatever criticisms (however illegitimate) the Avoidance Trust’s experts level at KPMG’s RCNLD values and Mr. Chrappa, KPMG and Mr. Chrappa are measuring the right thing and are doing so with accepted methodologies.

As the Special Court cogently put it in a subsequent opinion four years later concerning the valuation of those rail properties that would remain in use under the Final System

Plan, “no amount of evidence, argument, deliberation and study can produce a single demonstrably right figure.” *Matter of Valuation Proceedings Under Sections 303(c) and 306 of Regional Rail Reorganization Act of 1973*, 531 F. Supp. 1191, 1201 (Sp.Ct.R.R.R.A. 1981). But that there is no single precise valuation figure that is indisputably correct to the penny is no excuse for throwing out the right measuring stick. And there is no support either in Section 506(a)(1) or in *Regional Rail* to apply liquidation value in the circumstances presented here.

POINT II

USING HISTORICAL NET BOOK VALUE AS A CHECK CONFIRMS THAT THE KPMG RCNLD AND CHRAPPA VALUES ARE SOUND

As in *Regional Rail*, historical net book value can serve as a “check” here. That “check,” easy to apply, will confirm the appropriateness of the KPMG RCNLD valuations and the appraisal values of Mr. Chrappa. 445 F. Supp. at 1031.

In *Regional Rail*, the Special Court observed that there was a wide disparity on the record between claimed replacement cost and net book value. For example, it observed that one of the transferors, Penn Central, claimed RCNLD of \$13 billion, but only had a book value of \$3.6 billion. *Id.* at 1032. Even more extreme was Erie Lackawanna, which claimed an RCNLD over *eleven times* higher than its book value (\$3.6 billion RCNLD as against \$318 million book value). *Id.* The Special Court thus stated that where such “a wide disparity . . . exist[s]” between depreciated original cost value and claimed fair market value, “we may not be able to accept as fair any valuation which does not reflect an adjustment related to original cost.” *Id.* at 1031.

These factors are not present here. Attached hereto as Exhibit 1 is a chart containing in the first three columns: (1) the KPMG RCNLD values; (2) the Chrappa appraised values; and (3) Old GM’s Net Book Value (*i.e.*, the depreciated historical cost as reflected in Old GM’s books and records as of the valuation date). Examining each row on an asset-by-asset

basis, the figures are generally similar and confirm the reliability and reasonableness of one another.

Conversely, as the last two columns of the same chart show, it is the post-TIC-adjustment figures and the liquidation values urged by the Avoidance Trust that yield the “wide disparity” from recorded net book value. Thus, to the extent net book value is used as a “check” as the *Regional Rail* court suggested, that “check” would only further confirm what the other evidence at trial will show: (1) that the TIC adjustment does not result in the fair value of the assets; and (2) that the liquidation values urged by the Avoidance Trust are, to borrow the words of the *Regional Rail* court, the mere “fantasies of ‘experts.’” *Id.* at 1045.

CONCLUSION

In short, although *Regional Rail* was different from this case in important ways, applying the Special Court’s guidance in *Regional Rail* would broadly support the Term Lenders’ valuation proof. In determining the value of the Representative Assets in light of their “proposed disposition,” as required by Section 506(a)(1), the Court should look to the RCNLD values calculated by KPMG and the appraisal values as determined by Carl C. Chrappa. But if historical net book value is used as a check on those asset values, or even in lieu of those values, the results are similar and complementary.

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Exhibit 1
Valuations of 40 Representative Assets

Representative Asset Number and Description	Final RCNLD Values (KPMG)	Appraised Value (Chrappa) ^(a)	Net Book Value	TIC -Adjusted Value (KPMG)	Liquidation Value
1 OP-150 Shims Station	207,000	345,000	REDACTED	REDACTED	3,000
2 Pits & Trenches	2,440,890	2,285,000			0
3 Power Zone Conveyor	553,000	825,000			3,000
4 Electro-Coat Paint Operations ("ELPO") Waste System	989,600	890,000			0
5 Paint Circulation Electrical System	1,482,270	1,745,000			152,000
6 ELPO Oven Conveyor	964,420	930,000			7,000
7 Top-Coat Software	61,400	145,000			0
8 Paint Mix Room	636,000	750,000			82,500
9 Top-Coat Bells	2,188,200	2,270,000			263,400
10 Opticell Robotic System	N/A	420,000			73,000
11 Central Utilities Complex	51,210,000	64,770,000			2,367,000 (b)
12 Overhead Body Shop Welding Robot	19,210	18,100			25,000
13 Weld Bus Ducts	3,220,000	3,750,000			681,000
14 Leak Test Machine	629,000	810,000			9,000
15 Soap, Mount and Inflate System	1,402,500	1,715,000			59,000
16 Skid Conveyor	2,172,600	2,290,000			15,000
17 Power and Free Conveyor	1,439,520	1,445,000			24,000
18 Vertical Adjusting Carriers	3,579,400	3,600,000			59,000
19 Full Body Coordinate Measurement Machine ("CMM")	274,000	285,000			39,000
20 Wheel & Tire Conveyor	1,000,100	970,000			5,000
21 Final Line Skillet Conveyor	1,287,000	1,235,000			1,000
22 Fanuc Gantry Robot	126,000	190,000			32,000
23 Aluminum Machining System	862,000	1,475,000			14,000
24 Base Shaping Machine	533,300	810,000			224,000

Representative Asset Number and Description	Final RCNLD Values (KPMG)	Appraised Value (Chrappa) ^(a)	Net Book Value	TIC -Adjusted Value (KPMG)	Liquidation Value
25 Liebherr Hobb Machine	591,000	965,000	REDACTED	REDACTED	244,000
26 Core Delivery Conveyor System	90,400	100,000			1,000
27 Emissions System	2,820,300	3,130,000			131,000
28 Holding Furnace	1,211,100	1,515,000			8,000
29 GG-1 Transfer Press (Grand Rapids)	N/A	930,000 (c)			261,000
30 TP-14 Transfer Press (Mansfield)	N/A	500,000 (c)			800,000
31 Danly Press	N/A	880,000			276,000
32 AA Transfer Press	N/A	27,860,000			3,675,000
33 B3-5 Transfer Press	N/A	22,455,000			2,400,000
34 Build Line w/ Foundation	142,000	100,000			45,000
35 Button Up Conveyor System	1,370,800	2,005,000			2,000
36 Helical Broach	653,430	1,080,000			150,000
37 Courtyard Enclosure	211,720	410,000			0 (b)
38 Gas Cleaning System	69,000	0			24,000
39 Core Box Robot	N/A	N/A			N/A (d)
40 Charger Crane	114,000	160,000			10,000

Notes:

- (a) The asset values in this column are from the written testimony of Carl C. Chrappa, submitted April 7, 2017.
- (b) Representative Assets No.11 and No.37 are partially Fixtures. To estimate the value of the Fixture portion of these two assets, their Final RCNLD Value, Net Book Value, and TIC-Adjusted Value are adjusted by the percentage of the total Replacement Cost that Mr. Chrappa has identified as the Replacement Cost of the Fixtures.
- (c) Mr. Chrappa appraised these assets based on Orderly Liquidation Value because they were not included in the bankruptcy sale.
- (d) The parties have mutually agreed that they will not present evidence on the value of Representative Asset 39, Core Box Robot, at trial.